Management Accounting

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Economic Outlook Survey

3rd quarter executive summary

The CPA Outlook Index

The CPA Outlook Index (CPAOI) is a broad-based indicator of the strength of U.S. business activity and economic direction that reflects the views of CPAs who are AICPA members in Business & Industry holding executive positions in both public and privately-owned organizations of all sizes, and across a broad spectrum of industries.

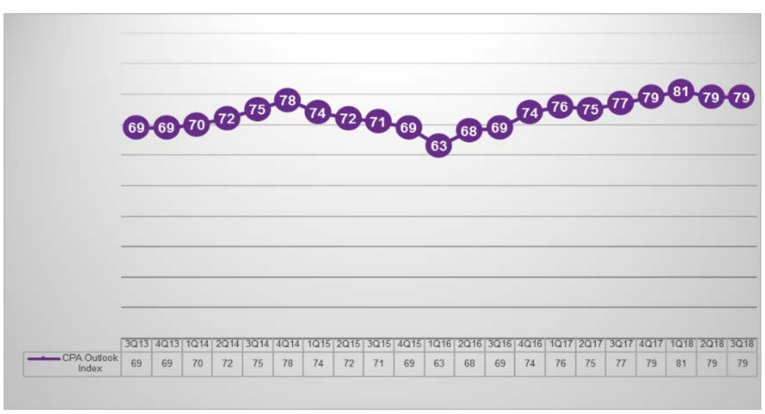
CPA Outlook Index

The CPA Outlook Index (CPAOI) remained constant at 79 in the third quarter of 2018.

The index component for optimism about the U.S. Economy dropped from 83 to 79, still up 2 from 77 in the second and third quarters of 2017.

Organization optimism and expansion plans, along with revenue and profit and employment plans all improved slightly. Spending plans for IT and other capital remained flat; training and development spending plans declined 2 points.

CPA Outlook Index (CPAOI)



A reading above 50 indicates a generally positive outlook with increasing activity.

A reading below 50 indicates a generally negative outlook with decreasing activity.

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CPA Outlook Index

Component	3Q17	4Q17	1Q18	2Q18	3Q18	ΔQ to Q	ΔY to Y
U.S. Economic Optimism	77	84	86	83	79	↓04	↑02
Organization Optimism	78	80	81	80	81	↑01	↑03
Expansion Plans	76	80	81	79	80	↑01	↑04
Revenue	83	85	86	83	85	↑02	↑02
Profits	77	78	80	77	79	↑02	↑02
Employment	72	71	74	75	76	↑01	↑04
IT Spending	81	82	83	82	82	→00	↑01
Other Capital Spending	77	76	79	78	78	→00	↑01
Training & Development	74	76	77	77	75	↓02	↑01
Total CPAOI	77	79	81	79	79	→00	↑02

The CPAOI is a robust measure of sentiment about the U.S. economy that is supported by the unique insight and knowledge that CEOs, CFOs, Controllers, and other CPA executives have about the prospects for their own organizations, their expectations for revenues and profits, and their plans for spending and employment.

The CPAOI is a broad-based composite index that captures the expectations of our members and their plans for a breadth of indicators of economic activity. It is a composite of the following nine measures at equal weights:

U.S. Economy Optimism	Respondent optimism about the US economy
Organization Optimism	Respondent optimism about prospects for their own organization
Business Expansion	Respondent expectations of whether their business will expand over the next 12 months
Revenues	Expectations for revenue over the next 12 months
Profits	Expectations for profits over the next 12 months
Employment	Expectations for headcount over the next 12 months
IT Spending	Plans for IT spending over the next 12 months
Other Capital Spending	Plans for capital spending over the next 12 months
Training & Development	Plans for spending on employee training and development over the next 12 months

Each individual component indicator is calculated by taking the percentage of respondents who indicated that their opinion or expectation for the metric is positive or increasing, and adding to that half of the percentage of respondents indicating a neutral or no-change response. A reading above 50 indicates a generally positive outlook with increasing activity. A reading below 50 indicates a generally negative outlook with decreasing activity.

Outlook for the U.S. Economy and Organizations

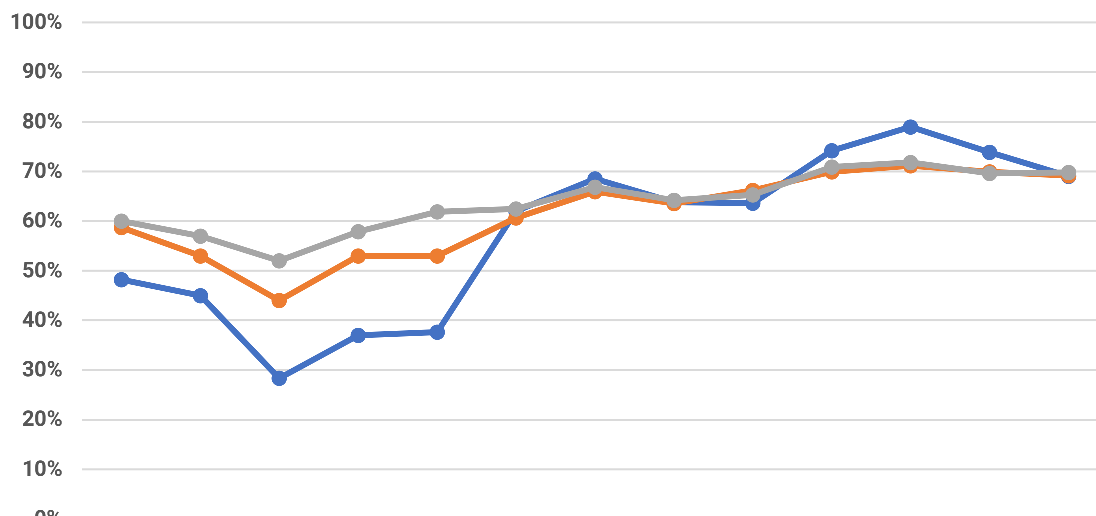
Optimism for the U.S. Economy remains strong but declines another 5 points

The percentage of CPA executives who are optimistic about the U.S. continues to be quite strong at 69%, although giving back another 5 points following the jump to the record high of 79% seen in the first quarter of 2018, followed by a 5 point decline in the second quarter.

Optimists site the benefits of corporate tax cuts and deregulation along with the general strength of many economic indicators. Concerns expressed by pessimists focused primarily on the impact of tariffs and trade war, interest rates and the yield curve, deficit and stock market levels, along with political divisiveness.

Organizational optimism continues to be strong at 69%, while giving back another point from its post-recession first quarter high of 71%. The percentage of companies with expansion plans remained flat with 70% of respondents having plans for expanding their business.

Outlook for the U.S. Economy, Organizations & Expansion



	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18
U.S.	48%	45%	28%	37%	38%	62%	69%	64%	64%	74%	79%	74%	69%
Organization	59%	53%	44%	53%	53%	61%	66%	64%	66%	70%	71%	70%	69%
Expansion	60%	57%	52%	58%	62%	62%	67%	64%	65%	71%	72%	70%	70%

The increased concern about inflation seen in the first quarter remained constant again in the third quarter with 49% of respondents expressing worry about inflation. While early in 2016 we saw some level of concern about deflation, now only 3% of respondents have that concern.

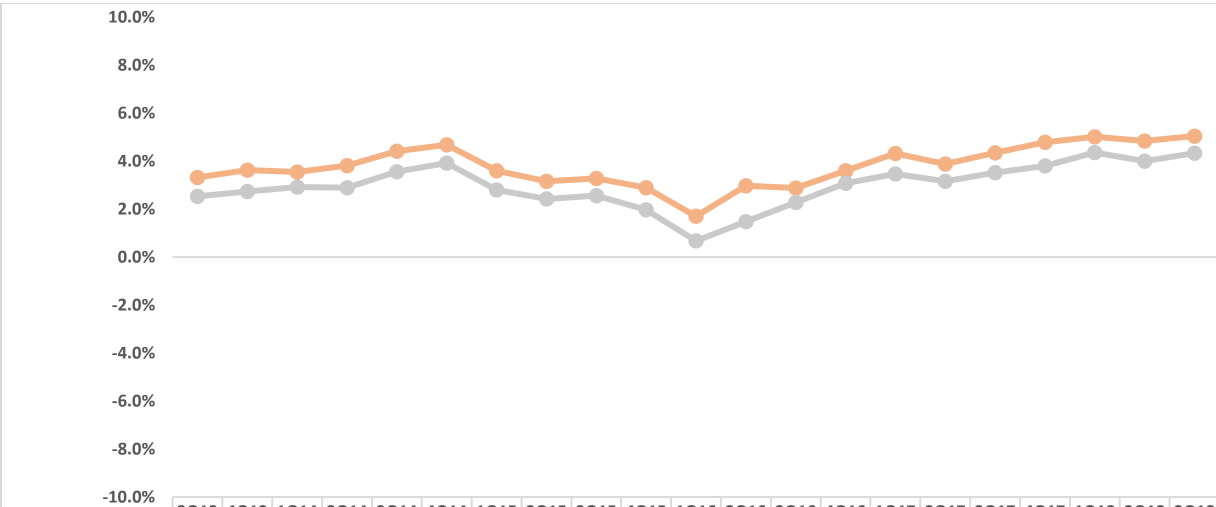
Labor costs continue to be the highest-ranking inflation concern for 36% of respondents. Raw materials cost concerns increased another point to 32%, along with interest rate concerns which increased from 18% to 20%. Energy cost concerns eased a point from 7% to 6%.

Key Performance Indicators

Revenue and profit projections recover second quarter givebacks

Revenues are now expected to grow at a rate of 5.0% back to the level expected in the first quarter. Profit expectations also recovered most of the second quarter easing, now expected to increase at a rate of 4.3%.

Expectations for Revenue and Profits



	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18
Revenue	3.3%	3.6%	3.6%	3.8%	4.4%	4.7%	3.6%	3.2%	3.3%	2.9%	1.7%	3.0%	2.9%	3.6%	4.3%	3.9%	4.3%	4.8%	5.0%	4.8%	5.0%
Profit	2.5%	2.7%	2.9%	2.9%	3.6%	3.9%	2.8%	2.4%	2.6%	2.0%	0.7%	1.5%	2.3%	3.1%	3.5%	3.2%	3.5%	3.8%	4.4%	4.0%	4.3%

Spending plans continue to be strong. While technology optimism and hiring plans both declined in the third quarter, expected spending for IT eased only a tenth of a point from 3.7% to 3.6%. Spending plans for other capital and for training and development also declined a tenth each, to 3.5% and 2.3%, respectively.

Marketing spending plans remained constant at 1.9%, while anticipated spending for R&D eased two tenths from its post-recession high, returning to the first quarter level of 2.0%.

Salary and benefits cost expectations remained constant at a 2.8% rate of increase. Expected healthcare cost increases which continue to be higher than other costs, eased to 5.7%, down from and expected rate of 5.9% in the second quarter.

Reflecting the level of concern about inflation, the expected increase in “other input prices” remained constant at a rate of 3.2%, a post-recession high. On the other side of the equation, the expected ability to increase “prices charged” also remained constant at 2.5%.

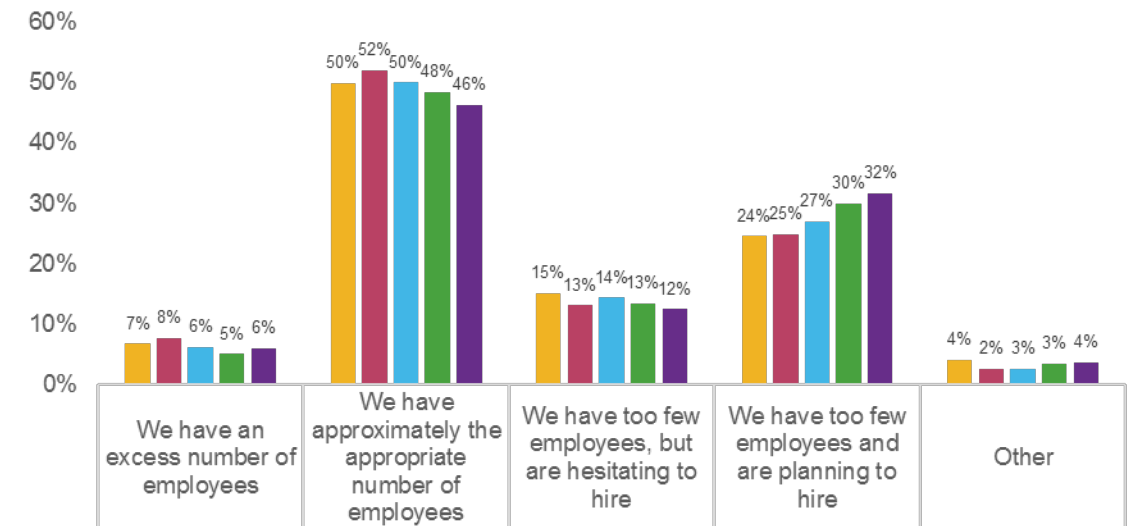
Hiring Plans

While some continue to have concerns, hiring plans continue to improve

In this quarter 46% of all companies say they have the appropriate number of employees. Those saying they have an excess number of employees increased slightly from 5% to 6% overall. The number of companies with revenues in excess of $1 billion having too many employees decreased another point to only 8%.

This quarter, 44% now indicate that they currently have too few employees, up from 43% last quarter. Of these, the percentage of companies that are planning to hire improved another two points to 32%. The percentage of those who are reluctant to hire decreased another point to 12%. This continues to show an easing from levels seen in 2016 and early 2017.

Staffing Relative to Needs



	We have an excess number of employees	We have approximately the appropriate number of employees	We have too few employees, but are hesitating to hire	We have too few employees and are planning to hire	Other
3Q17	7%	50%	15%	24%	4%
4Q17	8%	52%	13%	25%	2%
1Q18	6%	50%	14%	27%	3%
2Q18	5%	48%	13%	30%	3%
3Q18	6%	46%	12%	32%	4%

Employment plans by business size show a bit of a mixed picture:

- For employers with > $1 billion in revenues, 47% have the right number of employees and only 8% have an excess number, leaving 42% with too few employees. Of those, only 14% remain hesitant, while 28% are planning to hire.
- Of those in the $100 million to $1 billion category, 46% now say they have too few employees; 37% are hiring with only 9% being hesitant.
- In the $10 - $100 million range, of the total of 45% with too few employees, 35% have plans to hire; only 10% are hesitant.
- For employers with revenues < $10 million, again this quarter 52% say they have the right number, down from 61% in the first quarter; only 3% have an excess of employees; of the 40% having too few employees, 21% are planning to hire; while19% are hesitant.

Industry, Region and Business Size Outlook

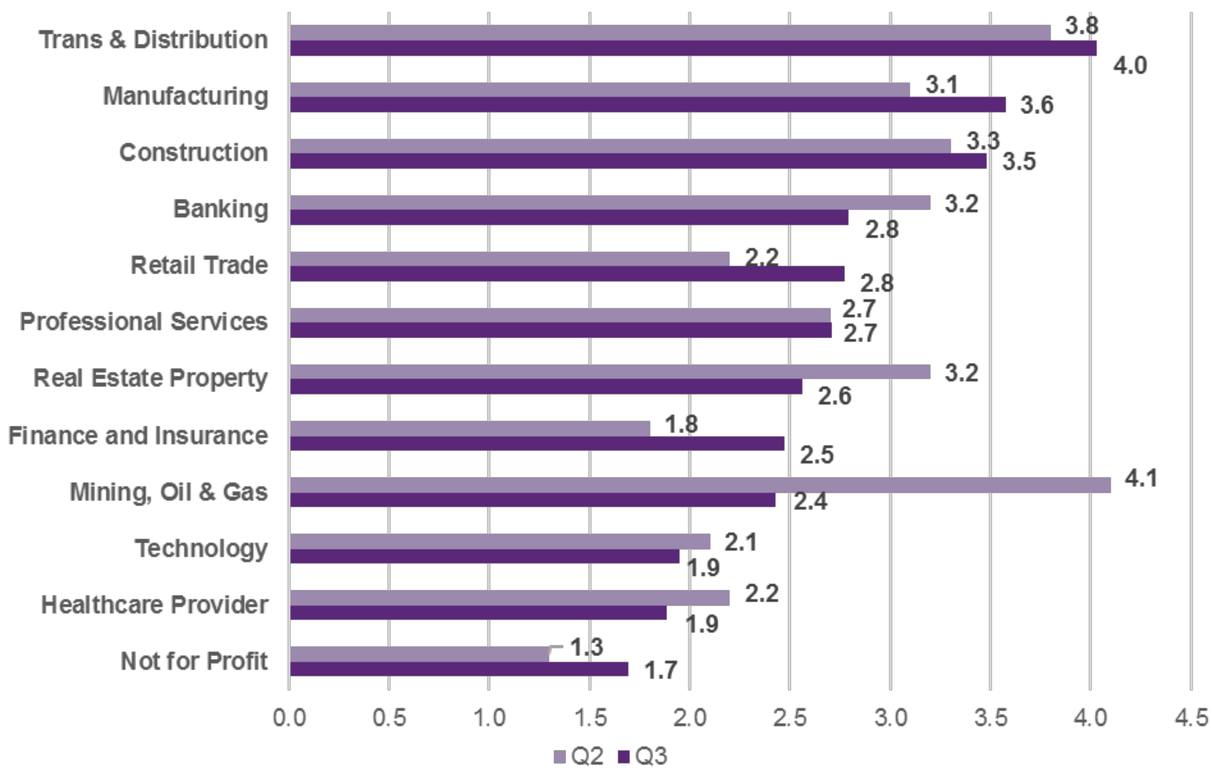
Optimism and hiring eases in some sectors, continues strong in others

Retail trade optimism remained constant at 61%, in the first quarter. Retail hiring plans improved from and expected rate of 2.2% to 2.8%. Wholesale trade optimism declined in the second quarter from 76% to only 63%.

Manufacturing optimism improved to a high of 78%, up from 75% in the second quarter. Manufacturing hiring is also expected to increase at a rate of 3.6%, up from 3.1% in the second quarter. While construction optimism eased from 76% in the second quarter to 69% in the third quarter, hiring in the construction sector strengthened from 3.3% to 3.5%

Finance and Insurance optimism also improved to 78%, up from only 69% in the second quarter, with hiring expected to improve from 1.8% to 2.5%. Professional services optimism also continues to be very strong, improving from 82% to 84% optimistic. Professional services hiring is expected to be flat at 2.7%.

Expected Employment Change by Industry



While IT spending is expected to continue to be strong, optimism in the tech sector continued its declined to 60%, down from 80% optimistic in the first quarter, and 69% in the second quarter. Hiring plans also eased from an expected rate of 2.1% to only 1.9%.

Real estate and property also dipped from its high level of optimism, declining twelve points from 78%, to only 66%. Hiring expectations also eased from 3.2%, to 2.6% in the third quarter.

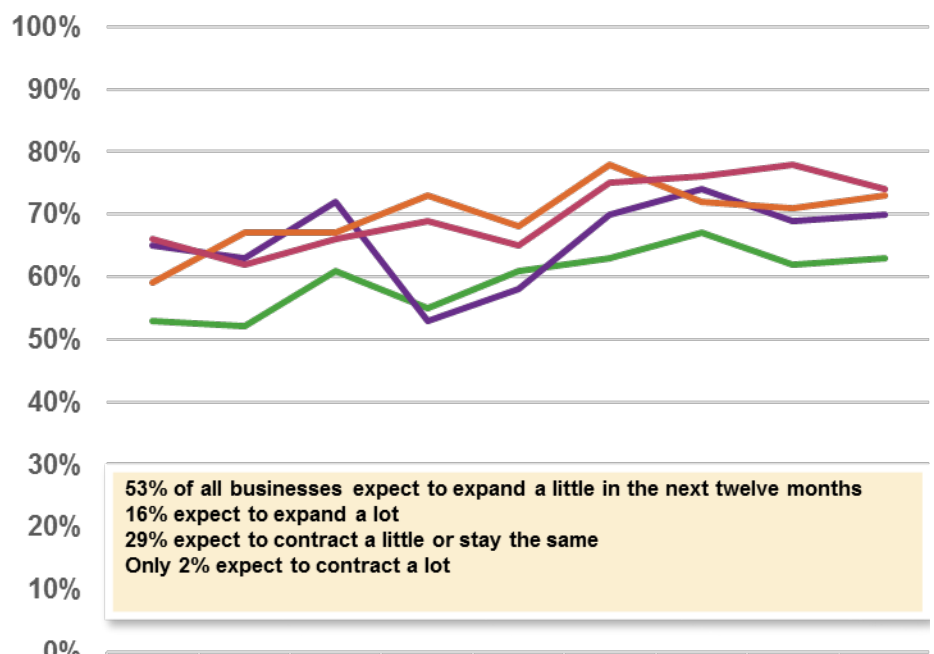
Healthcare optimism rebounded sharply back to the 61% level of optimism, after falling to only 44% optimistic in the second quarter. Planned healthcare hiring however declined slightly from 2.2% in the second quarter to 1.9% in the third quarter. On the other hand, optimism in the healthcare – other sector (pharma, devices, etc.) fell off from 88% optimistic in the second quarter to 67% optimistic in the third quarter.

Industry, Region and Business Size Outlook (cont'd)

Regional optimism evens out; expansion plans for small business continues to lag

In terms of regional perspective, the Northeast rebounded strongly to now 69% optimistic up from only 59% in the second quarter and a string of being the least optimistic region. The Midwest improved three points to 73% in the third quarter. Optimism in the West eased three points to 65% and optimism in the South gave up five points of early 2018 gains, with now 69% of respondents being optimistic.

Expansion Plans by Business Size



	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18
< $10 million	53%	52%	61%	55%	61%	63%	67%	62%	63%
$10 to <$100 million	65%	63%	72%	53%	58%	70%	74%	69%	70%
$100 million to <$1 billion	59%	67%	67%	73%	68%	78%	72%	71%	73%
> $1 billion	66%	62%	66%	69%	65%	75%	76%	78%	74%

Expansion plans:

- Expectations for expansion by businesses with revenues < $10 million improved a point to 63%;
- Plans for companies in the $10 - $100 million category also improved a point to 70%;
- Companies in the $100 million to $1 billion range improved from 71% to 73%;
- Those with revenues in excess of $1 billion fell from 78% to 74%.

Top Challenges

Availability of skilled personnel continues to be most challenging

- Availability of skilled personnel continues as the top challenge
- Regulatory requirements also maintains its second place spot
- Domestic competition moves up from 4th to 3rd, switching places with employee and benefit costs
- Materials/supplies/equipment costs maintains its 5th place ranking after jumping from the 10th spot in Q2
- Developing new products/services/markets, rose to 6th place in Q3 after falling to 9th place in Q2
- Staff turnover maintains its top ten ranking at #7
- Domestic economic conditions eased from #6 to #8, while domestic political leadership moved up from 10th to 9th place
- Financing (access/cost of capital) returned to the top ten ranking this quarter in the 10th spot

Top Challenges Facing Organizations

	3Q17	4Q17	1Q18	2Q18	3Q18
1	Availability of skilled personnel	Availability of skilled personnel	Availability of skilled personnel	Availability of skilled personnel	Availability of skilled personnel
2	Regulatory requirements/changes	Domestic competition	Domestic competition	Regulatory requirements/changes	Regulatory requirements/changes
3	Domestic competition	Regulatory requirements/changes	Employee and benefits costs	Employee and benefits costs	Domestic competition
4	Domestic economic conditions	Employee and benefits costs	Regulatory requirements/changes	Domestic competition	Employee and benefits costs
5	Employee and benefits costs	Developing new products/services/markets	Developing new products/services/markets	Materials/supplies/ equipment costs	Materials/supplies/ equipment costs
6	Developing new products/services/markets	Domestic economic conditions	Domestic economic conditions	Domestic economic conditions	Developing new products/services/markets
7	Stagnant/declining markets	Changing customer preferences	Staff Turnover	Staff Turnover	Staff Turnover
8	Changing customer preferences	Domestic political leadership	Changing customer preferences	Changing customer preferences	Domestic economic conditions
9	Domestic political leadership	Staff Turnover	Financing (access/cost of capital)	Developing new products/services/markets	Domestic political leadership
10	Staff Turnover	Materials/supplies/ equipment costs	Materials/supplies/ equipment costs	Domestic political leadership	Financing (access/cost of capital)

Survey within the Survey

Topical questions provide insight on a number of current issues

Our Survey within the Survey questions touched on several issues this quarter including tax reform, potential interest rate increases, and the impact of tariffs and potential retaliation on respondents' businesses.

Tax Reform and Interest Rates

With respect to the Tax Cuts and Jobs Act, slightly more than two-thirds (68%) of executives predicted that the impact on their business over the next twelve months would be favorable. Of the balance, 19% are expecting a neutral impact, and only 12% predict a negative impact while 1% remain unsure about the impact on their business.

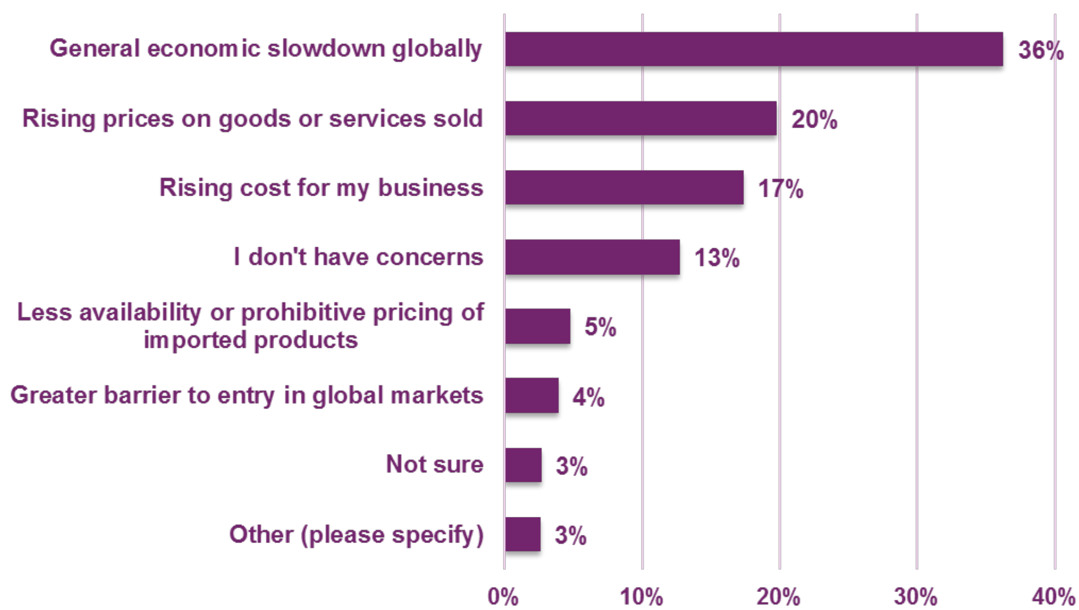
As a follow-on question we also asked whether the expected impact of tax reform has changed since the start of the year. Slightly less than two-thirds (63%) indicated their impression had not changed; 23% indicated their expectation had become more favorable, while 12% indicated their expectation had become less favorable; 3% indicated that they were unsure.

Potential hikes in interest rates are expected to have an unfavorable impact on 57% of respondents' businesses. Only 14% expect a favorable impact, while 29% expect the impact to be neutral, or minimal.

Tariffs and Trade Conflict

The likely impact on of recent tariff increases/trade quotas imposed by the U.S. is expected to be unfavorable by 49% of respondents. The vast majority of the remainder (44%) expect the impact to be neutral or minimal. Similarly, 48% expect the likely impact of retaliatory tariffs or trade quotas to be unfavorable, with 47% expecting neutral or minimal impact.

The greatest concerns about rising trade tensions are summarized as follows:



Survey Background

The survey was conducted of AICPA Business & Industry members between July 31, to August 22, 2018 and had 1242 qualified respondents.

CFOs comprised 41% of the respondents, 19% were Controllers, 10% were CEOs or Presidents, 10% were VP/SVPs, 8% were Directors, 2% were COOs, and 2% were CAOs; the remainder were other executives.

Sixty nine percent of respondents came from privately owned entities, 17% from publicly listed companies, and 12% from not-for-profits.

Fourteen percent came from organizations with annual revenues of $1 billion or more, 23% from organizations with $100 million to under $1 billion in annual revenues, 44% from organizations with $10 million to $100 million and 19% from organizations with under $10 million in revenues.

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