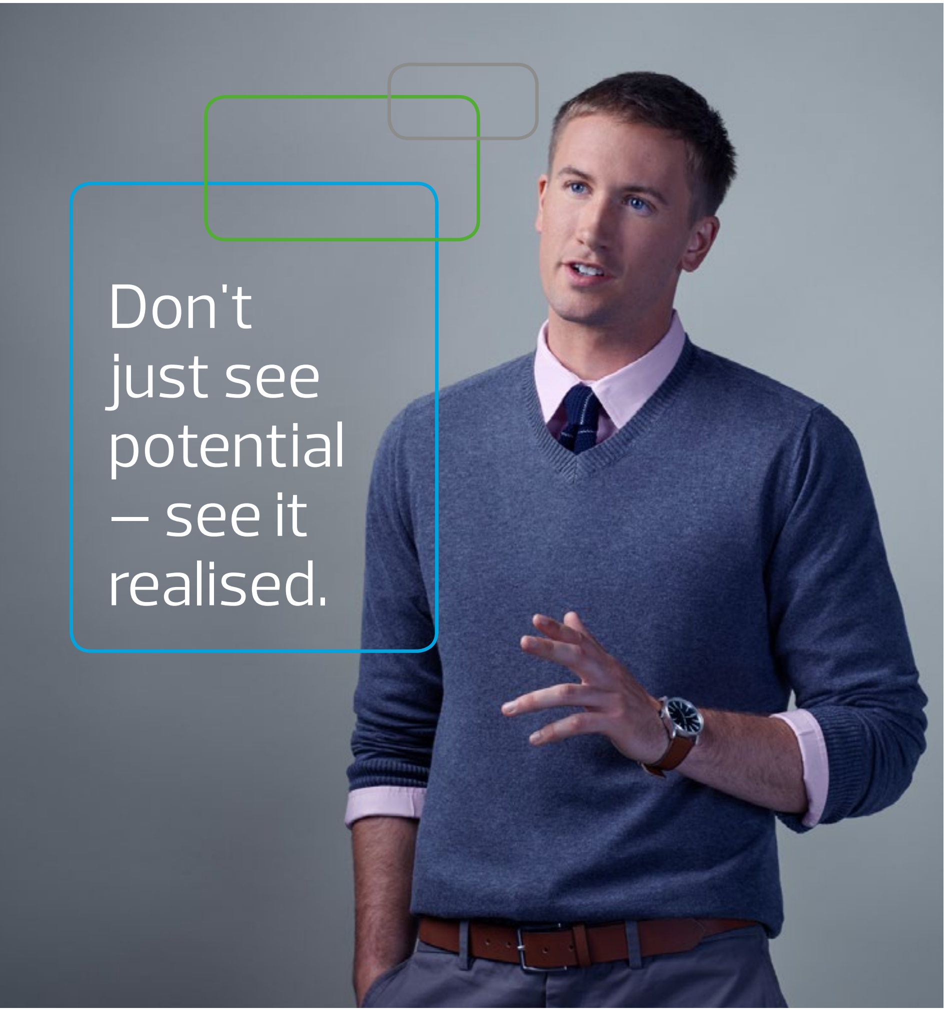
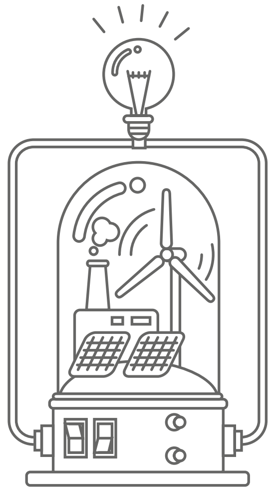
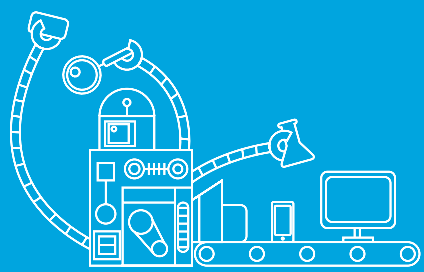


thinkBIG 2017





thinkBIG measures the pulse of the Australian SME, benchmarking business confidence and attitudes of business owners towards planning, growth, succession and the future of their SME.

BUSINESS GROWTH

THE POWER OF BEING UNDERSTOOD
AUDIT | TAX | CONSULTING

RSM

FOREWORD

This year's thinkBIG report reflects general positivity and optimism among SME owners, following on from similar sentiment last year. Over 200 business owners participated in this year's study. Business growth, both actual and anticipated, stayed relatively high. The key barrier to achieving this growth remains access to the right skills. So talent management should be high on the SME owner's agenda. Whilst access to capital was not far behind this issue, more businesses are using bank debt to fund that growth. Family loans are on the increase but care needs to be taken that the paperwork around this debt is put in place. And we've seen the first instance of a business gaining finance through crowdsourcing in this year's survey.

There is an overall sustained acceptance that technology is a critical and indispensable tool in today's business climate, and most businesses are investing in various types of technology. However, cybersecurity remains a significant area that is overlooked by SMEs, who put themselves and their partners, suppliers, customers, and other stakeholders at risk by not taking adequate measures to protect their networks.

Planning continues to be underdone in SMEs. Despite strong evidence that business plans contribute to success, more than 30% of respondents are still failing to complete a business plan.

When it comes to an exit strategy, the numbers are even lower. Just 36% of respondents had an exit plan in place this year. With every SME owner destined to leave the business at some point, whether voluntarily or otherwise, an exit strategy is a neglected but important part of business planning.

The areas of digital implementation, cyber security, business planning and exit strategy are all fields of expertise for RSM. We see that the promotion of these areas to SMEs is important because they are key success strategies for owners. We trust that by highlighting them, it might move owners to take action where needed to shore up their future sustainability and ultimately their financial future.

2017 is the twelfth year that RSM has conducted the thinkBIG study. It measures the pulse of the Australian SME sector, and has been structured around five key areas:

- **Superannuation**
- **Business growth**
- **Business planning**
- **Exit strategy**
- **SME of the future**

I hope you find it valuable.

Peter Saccasan
National Head of Business Advisory
RSM Australia

OBJECTIVES

The key objectives of the research were to:

- Identify the impact of financial conditions on business sentiment
- Report on the business outlook over the next 12 months from the perspective of SME owners
- Benchmark business planning and critical areas such as an exit strategy and superannuation planning
- Assess the utilisation of self-managed superannuation funds by SME owners
- Report on work/life balance of SME owners
- Assess the impact and uptake of technology

OTHERS IN THE SERIES...

Superannuation
Business planning
Exit strategy
SME of the future

BUSINESS GROWTH

Despite the current economic climate, SMEs continue to experience business growth and remain optimistic about future prospects. Most businesses expect to see growth over the next 12 months.

This optimism is reinforced by the results of this year's thinkBIG survey. Only 16% of respondents say that their revenue has declined over the past 12 months and 73% of respondents are saying that they believe their business profitability will improve over the next year.

However, optimism and reality do not always coincide so it's crucial for businesses to ensure they are in a position to take advantage of their recent revenue gains. Having a clear business plan, for example, will help businesses to understand what type of growth they want to achieve and, therefore, where the gaps are that need to be addressed.

Regardless of how good a company's value proposition is, without a clear plan to promote that value proposition, the business is unlikely to grow accordingly. Therefore, SME owners may see growth in the top line that isn't reflected in the bottom line. Of those companies that prepared a business plan, 53% experienced growth and only 15% experienced a decline in revenues. A business plan need not be a weighty tome. The best plans are those which are concise, clear in their targets and relevant to the owner and the team as they set about trying to achieve the goals.

We read often that a large proportion of small businesses fail in the first three years (some sources cite figures as high as 60%). SMEs that survive that danger period are likely to remain operational in the longer term[1]. Surviving the first three years and beyond requires strong management vision and practices.

[1] https://www.treasury.gov.au/~/media/Treasury/Publications%20and%20Media/Publications/2012/Australian%20Small%20Business%20-%20Key%20Statistics%20and%20Analysis/downloads/RTF/AustralianSmallBusinessKeyStatisticsAndAnalysis.ashx

General optimism

79% of SME owners see their business as successful to some extent and still remain optimistic about their business's medium-term prospects.

Future growth

Similar to previous years, nearly half of all respondents reported growth over the past 12 months, indicating four years of growth for Australian SMEs. Optimism is high, with an increased percentage of respondents believing their business will grow in the next 12 months.

New opportunities

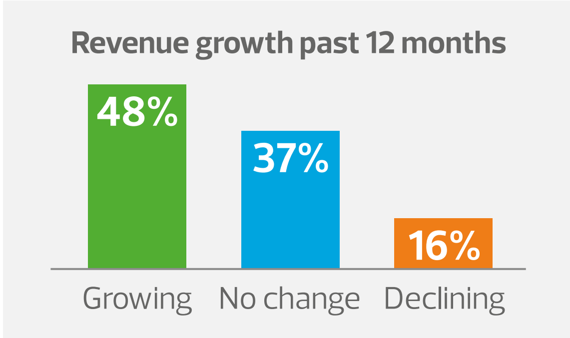
Most businesses indicate they will look to their current customers for growth opportunities. This approach has taken over from a reliance on marketing and advertising as the number one growth tactic. The skills gap has consistently been cited as the number one barrier to growth since 2011 and this year is no different. A lack of market opportunity has also consistently been cited as a significant barrier to growth though that does not stop SME owners in marketing and advertising activities. Interestingly, 2017 has seen a significant increase in the number of SME owners who plan to grow their business. This may reflect an increasing level of optimism due to the relatively stable local political and economic environment as well as the ongoing low level of interest rates which can only encourage investment in business as well as other assets.

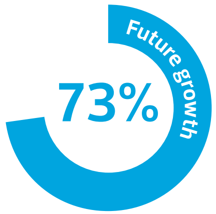
Business funding

A lack of access to capital was cited as the third-most common barrier to business growth but the proportion of SMEs funding their businesses through bank debt has grown to a new high in 2017. This indicates that SMEs are finding it easier than in previous years to access bank debt. However, the perception that there is a lack of access may be that they can't get enough in dollar terms from the banks. Family loans have also increased in 2017. We see this reflected in banking practices where the lenders want to know where the capital comes from and if there are any strings attached to such loans, or if there are in fact 'silent investors' who are benefiting from the business and who the bank thinks should be more visible.

Growth

50% of SME owners rated **8/10** for feeling their business is successful





believe their business will grow over the next 12 months

(An increase from last year's 69%)

Despite the hype around 'doing more with less', only 4% of businesses expect to achieve growth by reducing costs alone.

54%
will increase top line

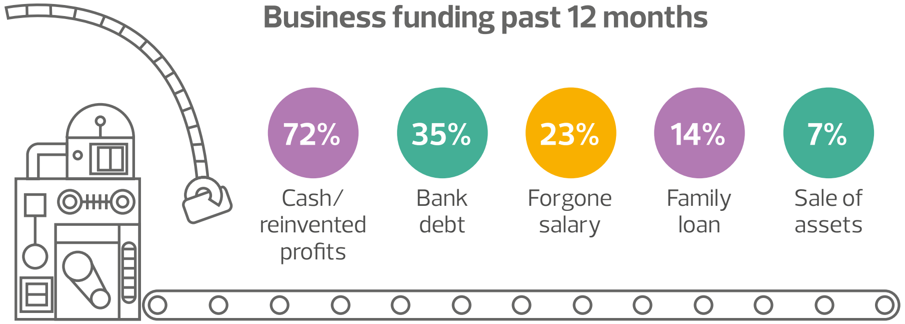
42%
will combine cost reductions with increased top line

Top growth priorities for the coming year

- **57%** Sales to existing customers
- **46%** Marketing and advertising
- **43%** New use of technology
- **41%** New product or service

13% are satisfied and don't plan to grow their business

Business funding past 12 months



- 72% Cash/ reinvented profits
- 35% Bank debt
- 23% Forgone salary
- 14% Family loan
- 7% Sale of assets

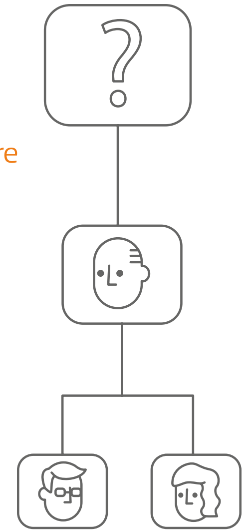
Despite alternative funding models, cash and reinvested profits remains king.

Top barriers to growth

1. Finding skilled people
2. Lack of management time
3. Access to capital
4. Lack of market opportunity
5. Government regulation

Family loans

The borrower and lender ought to have **appropriate documentation** to ensure there are no family disputes down the track should anything go wrong with the business or the health of either party suffers. To protect the family investment, all parties should give consideration to the **legal protection** that might be available for such lending. This could protect **valuable family wealth** from creditors.



Crowdfunding

For the first time in our thinkBIG survey, a new method of business funding emerged.

5 SOURCES FOR BUSINESS FUNDS BEYOND TRADITIONAL BANKS

1. APPLY FOR GRANTS OR GOVERNMENT FUNDING

There are a large number of government grants and funding opportunities available to businesses who fit specific criteria, both at a state and federal level. These funding "buckets" are subject to regular policy change, so it is useful to work with a mentor to ensure your application is strong and your business plan is solid.

2. SELL STOCK VIA AN INITIAL PUBLIC OFFERING (IPO)

By selling shares on a public exchange, companies can grow without having to borrow from traditional sources and pay interest to service the debt. Instead, they pay dividends to investors, which depends on profits. This also lets the company access other growth levers including providing shares and options to incentivise staff, and accessing other funding at a favourable rate based on share price performance. However, listed companies are subject to a raft of compliance requirements and restrictions, so business owners must consider the potential downsides before going public. The costs of both raising public capital and maintaining a public listing are also significant, and an IPO is only a realistic option if the business has market recognised scale.

3. ACCOUNTS RECEIVABLE FUNDING

This is a type of finance arrangement where the business typically uses its outstanding invoices or inventory as collateral. This can be an expensive way to access capital but it can help businesses free up funds that would otherwise be buried in working capital. The evolution of products available in this area has been significant in recent years, and the issue of the relative cost of funding may not be applicable ie – bricks and mortar backed mainstream funding may not be available, so the costs are not comparable.

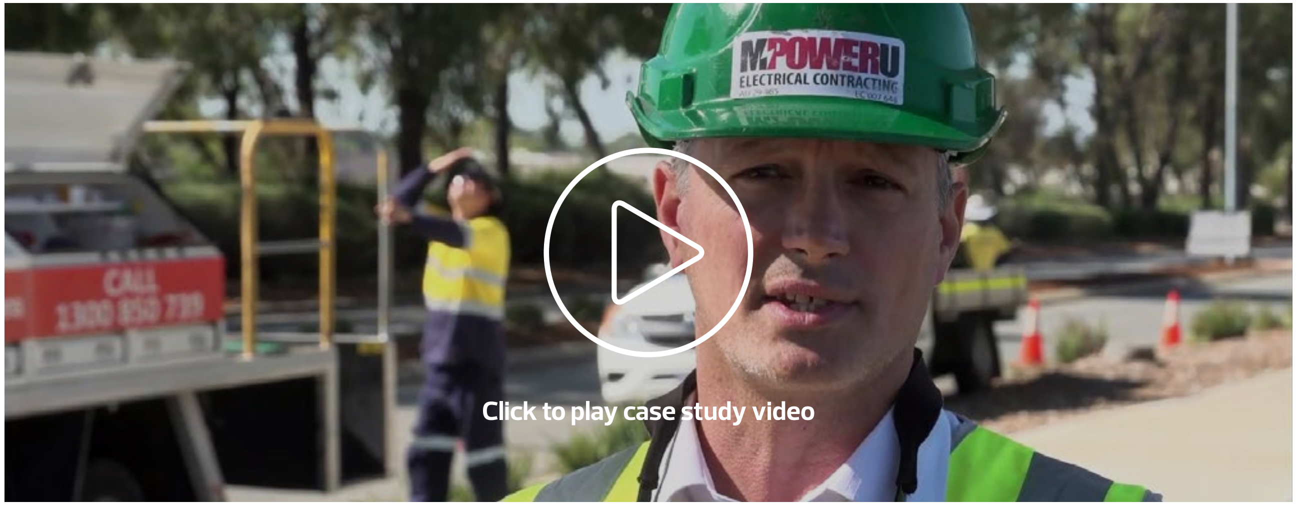
4. WORKING CAPITAL

Venture capitalists are professional business investors that inject funds into early stage business for long-term equity gain. They're not limited to a single round of funding and their business experience and contacts can be a valuable addition to the team. It's important to have a strong pitch and a clear understanding of how much capital the business needs, as well as the potential returns. Typically venture capitalists will demand a bigger slice of equity to reflect the relative risks of backing early stage businesses, many of whom have unproven business models.

5. ACCESS PRIVATE EQUITY

A private equity investor will typically invest in emerging or mature businesses with upside delivered throw growth, merger of restructuring. Private Equity investors often require a majority stake in return for providing funds, which may the SME owner with little control over the business. Private Equity firms will usually work to a defined exit timetable, often between 1 and 3 years.

CASE STUDY:
MPowerU Electrical – Western Australia



MPowerU Electrical provides electrical services across Perth with major emphasis on commercial breakdown and maintenance. Their clients consist of both state and local governments including police stations and schools – they also offer their services to residential customers. Established in 2006, Giulio Montini started MPowerU Electrical and has since grown his team, consisting now of 12 trade staff and three full time office staff. Being a reactive, breakdown and maintenance company, ensuring the smaller jobs are done well and on time is important to opening the door to bigger jobs, potentially with larger clients as well.

> "We wanted someone who could advise us on the company we want to be, not just the company we are."
>
> Giulio Montini
> Director

Improving labour efficiency

Giulio initially engaged a business coach to help guide his company which proved to be effective in the early stages of development however fast realised that there was a need to be more analytical and exercise certainty in decision making. Giulio started looking for an accountant who could provide business consulting advice and through a referral, was introduced to Matthew Robinson from RSM's Rockingham office. "Matthew showed us how we could make good financial forecasting decisions – he gave us clarity in this area."

Requiring more robust and financially sound advice that would help build their strategy, the team at RSM was able to help navigate MPowerU Electrical through effective financial management principals. A financial model was prepared that tracked both financial inputs and activity outputs producing results that allowed RSM to provide advice on the key areas for improvement. "We wanted someone who could advise us on the company we want to be, not just the company we are."

As a result, adjustments were made to improve labour efficiency which not only turned the business around but helped target new work. Giulio now has the confidence to make strategic decisions based on solid data including employing new staff, purchasing equipment and growth in targeted areas. MPowerU Electrical have achieved ISO 9001 accreditation.

Looking at the future, MPowerU Electrical's growth has enabled them to repay debt as well as take on new financial commitments improving resource capability. It was RSM's local position with access to national resources that made Giulio transition his accounting and strategic planning partner to RSM. "We wanted to engage with someone who has dealt with the bigger businesses but still has the small business mindset and approach towards their client."

Headquarters: Rockingham, Western Australia
Industry: Electrical services
Number of employees: 11-50
Year founded: 2006

www.mpoweruelectrical.com.au

SUMMARY

Key findings for business growth in 2017:

- Almost half of respondents reported business growth over the past 12 months. After a successful 2011, in which 73% of respondents reported business growth, 2013 saw this number drop to just 42%. Since then, around half of respondents have reported business growth each year.
- 73% of respondents expect to see growth over the next 12 months. This reflects an overall increase in optimism not seen since 2012 when 77% expected to see growth. By contrast, this fell to just 64% of respondents expected growth in 2013 , with this number rising to 69% in 2016.
- Cost-cutting alone will not achieve a sustainable business. Growth is a must on the business plan agenda. There is only so much cost-cutting that can be done before it actually starts to harm the business by removing resources necessary to take the business forward.
- Getting more business from current customers is the most popular way companies intend to grow their business. Organisations also intend to rely on marketing and advertising, or create new products or services. As in 2016, this is likely a priority as companies look to overcome the skills gap which remains a significant barrier to growth, along with finding time to spend on managing the business.
- If a business intends to place reliance on marketing and gain more revenue from their existing customers, businesses need to ensure they continue to remain relevant to their customer base. Often businesses can get blasé and take for granted just what it is their customers are looking for. So what was a loyal customer can easily turn into a former customer if service levels drop and product innovation falls away. Business owners should consider finding ways of finding out what their customers want as opposed to promoting to them what the business thinks their customers need.
- 72% plan to fund their business through cash flow. This is in on the back of bank debt having increased again, with 35% of businesses funding operations through debt this year compared with 29% in 2016. The family as a source of capital has risen significantly, with family loans increasing from eight% last year to 14% in 2017.

PROFILE OF PARTICIPANTS

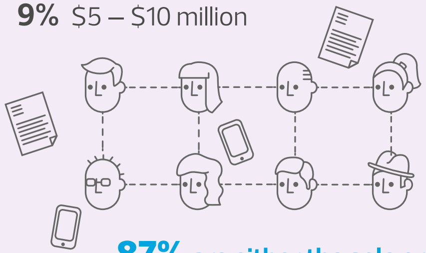
Location
51% capital cities
28% rural areas
21% regional areas

Size of team
11% sole trader
19% 1–2 employees
22% 3–5 employees
21% 6–19 employees
17% 20–49 employees
6% 50–99 employees

Age group
21% aged over 65
65% aged between 45 and 65
15% aged between 25 and 45

Top industries represented
23% Agriculture, forestry and fishing
19% Professional services
18% Other services
8% Construction
7% Retail
5% Technology

Turnover last year
34% Up to $1 million
17% $1 – $2 million
22% $2 – $5 million
9% $5 – $10 million



87% are either the sole or one of the owners of the business

NEXT IN THE SERIES...

- Business planning
- Exit strategy
- SME of the future

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