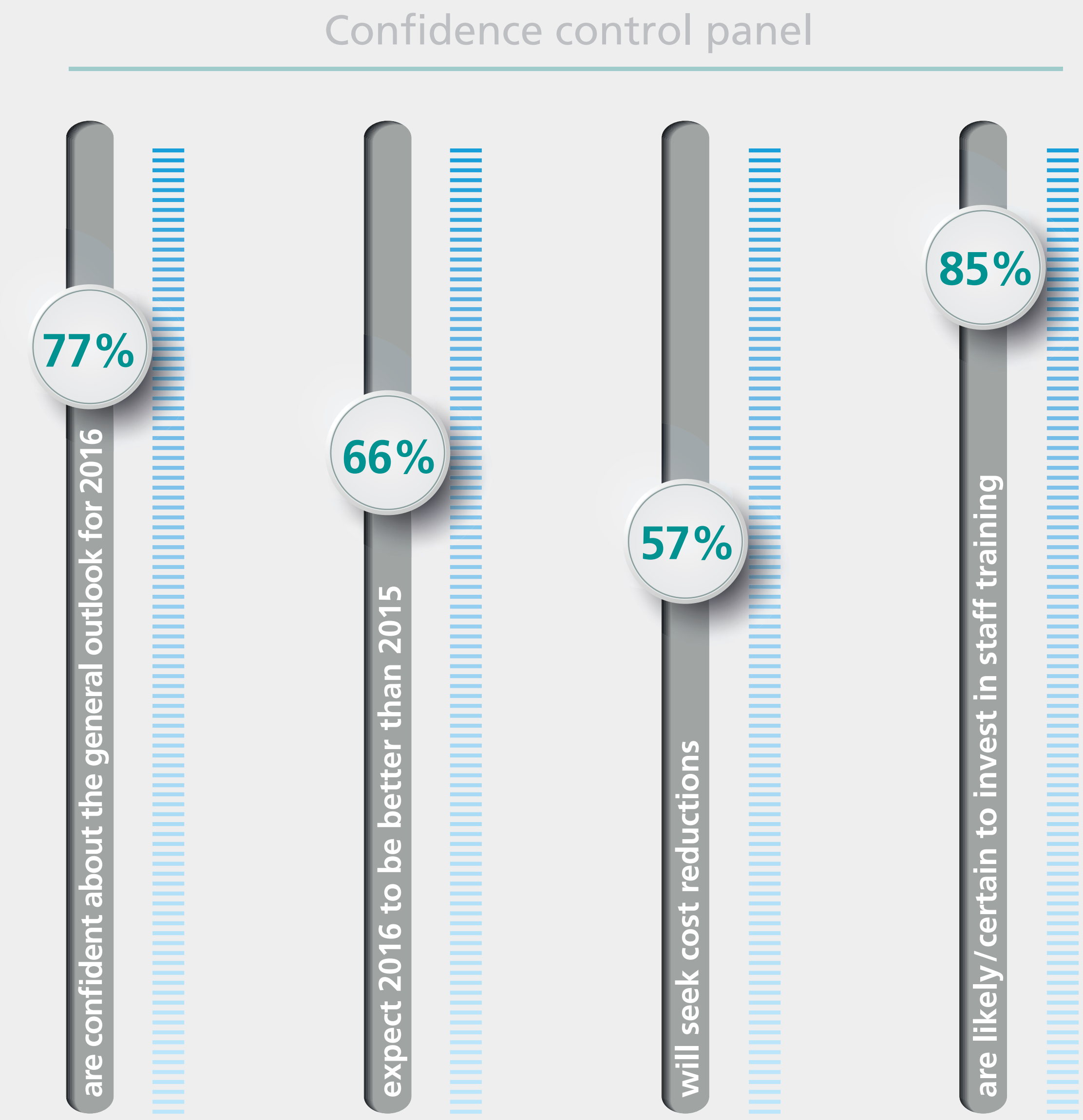
MOORE STEPHENS



Investing for success in 2016

The owner managed business view

Owner managed businesses

PRECISE. PROVEN. PERFORMANCE.

Contents

Survey details

We conducted an online survey of OMBs between 10 November and 18 December 2015. We analysed 466 responses, drawn from across all business sectors and from entities with headquarters in England, Scotland, Wales and Northern Ireland, as well as a few based offshore and further afield. Respondents were senior personnel within their businesses – primarily founders and owners, chief executives and managing directors, or other high-level directors. We then spoke in depth with the leaders of seven OMBs to find out more about their experiences in 2015, their expectations for 2016, the risks they foresee and the strategies they aim to apply in their businesses.

Foreword

Our latest annual survey among owner managed businesses (OMBs) finds cautious optimism based on strategic investment and tight cost control, despite uncertain economic indicators.

The International Monetary Fund recently warned that global economic growth will be disappointing in 2016. The prospect of rising interest rates in the US is feeding uncertainty and increasing the risk of economic vulnerability worldwide. Growth in global trade has slowed considerably and a decline in raw material prices is posing problems for economies reliant on commodities.

How will such uncertain conditions affect UK OMBs, whose continued health is so vital for the national economy? Our third OMB survey conducted across the whole of the UK brings some much needed positive news: OMBs are still confident about hitting profit and revenue targets in the medium term, with the majority expecting turnover and net profitability to increase in 2016.

As with last year, there is uncertainty too, however. OMBs have particular concerns about domestic competition, the strength of the UK economy and a UK skills shortage. Salary costs are rising, but paying staff more money is not necessarily sufficient to retain talent. Many employees now look for career development opportunities – a request harder to satisfy in an OMB than a major international corporate. Survey participants are responding by investing in training – an important activity if OMBs are to retain and develop their valued employees.

Most OMBs appear cautiously optimistic about 2016. Many are planning to expand their UK customer base, develop new products or services and increase marketing spend – while also seeking cost reductions. A smaller proportion have merger and acquisition activity high on the agenda, as well as selling their business or expanding overseas.

Last year we reported that many OMBs were concerned about the longevity of the tax incentives they value, particularly Entrepreneurs' Relief (ER). In December 2015, shortly before this year's survey closed, the Government issued a consultation document on company distributions. Its thrust is the long-awaited attack on the common practice of taking economic gains in capital rather than income form, i.e. arranging that returns are subject to capital gains tax (CGT) at 10% (assuming that ER applies), instead of being taxed at dividend rates of tax currently at 30.6% (going up to 38.1% from 6 April 2016 for additional rate taxpayers). These changes will significantly affect the ability of owners to extract money tax efficiently from their business. It seems that the OMBs who expressed concern about the tax environment in our survey did so with some justification!

On the global stage, 2016 will see presidential elections in the US and Taiwan, a summer Olympics in Brazil, and a new five-year plan in China. On the home front, the biggest event will surely be the UK referendum on whether to remain part of the European Union. In our survey, 60% of OMBs are against Britain leaving the EU, with 23% undecided. Almost half believe there would be a negative impact on their business if Britain left the EU – no doubt this will be the main subject for the Government as we fast approach 23 June 2016.

Many more detailed findings are set out in this report. I would like to thank all the businesses who completed this year's survey, and particularly those individuals who agreed to be interviewed. Your stories provide insight and inspiration.

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Survey highlights

Most OMBs have high expectations for 2016, building on a strong performance in 2015

- 38% of OMBs said their business performed better than expected in 2015.
- 77% are confident about the general outlook for 2016 (up seven percentage points from last year), while 73% are confident about meeting revenue targets and 68% are confident about hitting profit targets – results consistent with those of the last two years.
- 66% expect 2016 to be better than 2015, of which 21% expect it to be a much better year.

OMBs will continue to invest in their businesses in 2016, seeking growth at home and abroad

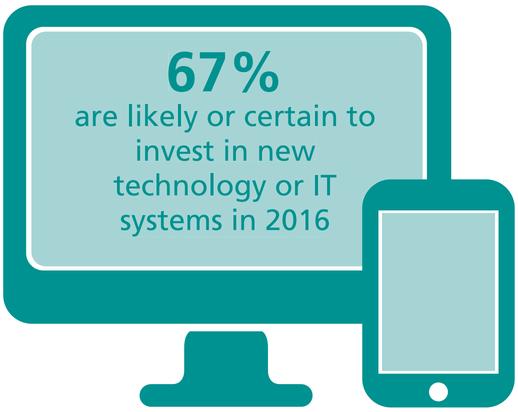
- 85% of OMBs are likely or certain to invest in staff training.
- 81% are likely or certain to try to expand their UK customer base, with 27% intending to open new sites or offices, or to expand into new territories in the UK.
- 67% of OMBs are likely or certain to invest in new technology or IT systems in 2016, while 66% intend to launch new products or services, and 55% expect to introduce new production techniques.
- 57% are likely or certain to seek cost reductions.
- 34% are likely or certain to expand overseas, compared to 27% who are considering expanding into new territories in the UK.

OMBs are most concerned about competitive and economic risks in 2016, but skills shortages are also a big worry

- Over half (53%) are concerned about the risk from domestic competition, while 27% see international competition as a risk to their business.
- 52% view the strength of UK economy as a risk and 33% have concerns about the strength of the global economy.
- Employee skills shortages are seen as a risk by 45% of OMBs.

Most OMBs do not want Britain to leave the EU

- 60% say Britain should not leave, with just 17% in favour of an exit. 23% have yet to make up their minds.
- 46% think that leaving the EU would have a negative impact on their business, and only 5% see any potential positive impact.
- 50% of OMBs employ at least some workers from mainland Europe.
- 24% say that over 20% of their workforce is from mainland Europe – and for over one in ten (13%), workers from mainland Europe make up over 75% of headcount.



2015 in perspective

Being a General Election year, 2015 was never going to be the easiest of trading periods for the UK's OMBs, but many still performed better than expected.

Over the past three years, the expectation that business performance will improve has decreased. Among this year's survey participants, just 38% of OMBs said their business performed better than expected in 2015 – compared to 45% in last year's report, and 49% two years ago.

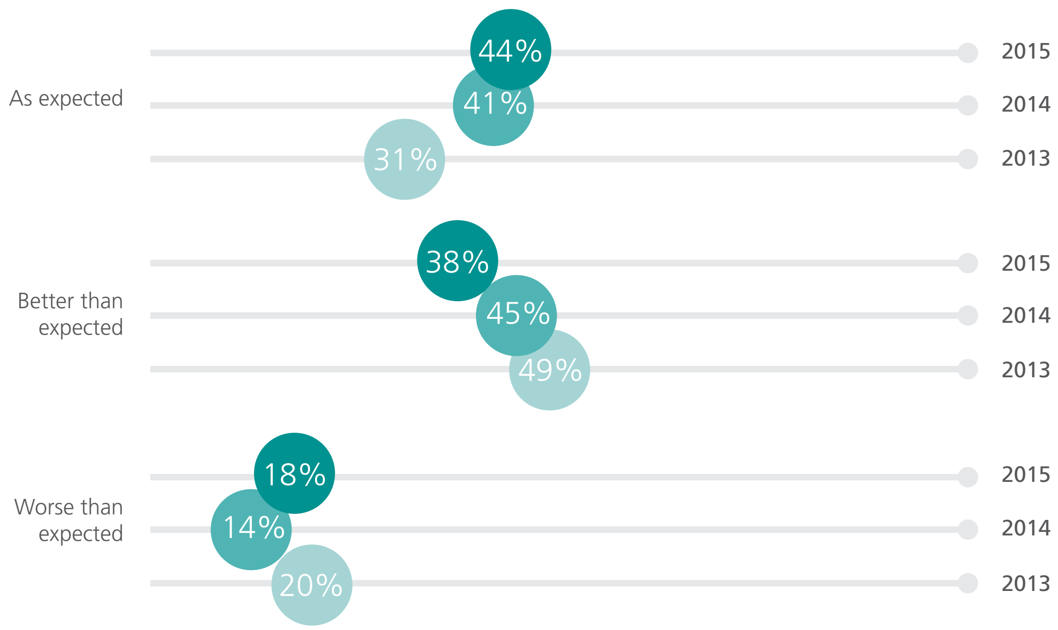
OMBs in Scotland were particularly likely to report a better year than expected (49% doing so), compared to 35% of OMBs headquartered in England. Of all regions in England, the East (not including London and the South East) came out on top, with 50% of OMBs stating their business performed better than expected in 2015.

From a sector perspective, OMBs most likely to have exceeded expectations in 2015 are professional practices (43% reporting a better year than expected) and real estate and construction businesses (42%).

OMBs gave a range of reasons for their better-than-expected performance, including:

- improving trading conditions and customer confidence;
- increased sales (e.g. through online platforms);
- the launch of new products, services and business lines;
- additional personnel driving increased revenues;
- overseas expansion or stronger than expected performance in overseas markets;
- higher pricing and more profitable contracts being negotiated;
- tighter cost control (e.g. by reviewing suppliers) and debt management;
- lower costs due to the strong pound against the Euro and low oil prices;
- past investments and restructuring now paying off;
- strong performance in the construction, property and IT sectors.

Fig 1. Business performance over a three year period



Not such good news for all

In this year's survey, 44% of OMBs (compared to 41% last year and 31% two years ago) said their business performed as expected, but 18% said their business performed worse than expected (14% last year, 20% two years ago).

Paul Fenner, Real Estate & Construction partner at Moore Stephens is surprised that only 18% had a disappointing year. "A lot of businesses have told me that, while they felt things were improving, they didn't actually see that happening around them," he says. "Growth wasn't as fast as expected. I see that, particularly in construction, where companies have lots of opportunities and potential new contracts in the pipeline, but they can't take them up because they haven't got the resources or the funding. They are nervous that if they go after too many, they will end up overtrading and suffer cashflow problems. So the market is still nervous."

Many OMBs indicate that their disappointing performance has been caused by factors beyond their control. Reasons for the worse-than-expected performance included:

- weak global demand and challenging US or European markets;
- increased competition (e.g. from cheap Chinese products);
- low oil and other commodity prices (affecting oil and energy-related industries);
- the strong pound affecting exports and increasing competition from imports;
- ongoing uncertainty about Scotland's future if another referendum is held;
- cost pressures (e.g. rising raw materials costs);
- staffing problems;
- 'unhelpful' weather (e.g. mild winter);
- delays in capital expenditure programmes and public spending cuts;
- retailers' price war driving down supplier prices;
- slower than expected uptake for new products or business streams;
- bookkeeper errors;
- increased bad debts;
- European conflict (Russia and Ukraine);
- UK regulations.

Shaylor Group: building growth in a competitive construction market

CASE STUDY

Although a second generation family-owned business formed in 1969, West Midlands construction firm Shaylor Group is "definitely in expansion phase and has been for the last couple of years," says CEO Stephen Shaylor. "Last year was a record for us – we grew 20%." This success has been built on a "back to basics policy" initiated a few years ago, when the business diversified its activities. It now has core business interests in general contracting, repair and maintenance works and specialist fit-outs, and has developed specialist sector expertise. The business plans to continue growing by winning more framework contracts, generating more relationship-led business (where projects aren't necessarily awarded on price) and competing for tenders using accurate market and price information.

Headcount increased by around 40 in the last 12 months to total 200. Skilled employees are in short supply in the construction sector, and Shaylor does identify this as a risk to his business in 2016. "We are constantly training," he says. "We have apprentices and management trainees. We have training programmes and management academies that we run every year." The business has also invested in a new "benefits platform" to help its recruitment and retention strategy. "We want to be seen as an attractive employer in the marketplace," Shaylor says. "Twice a year we effectively close the business down for a day for a staff conference. It's about making people feel part of one team."

The management team has developed a comprehensive approach to risk management. "We are focused on project risk management," Shaylor says. "All schemes have risk registers and we have a Risk Committee. As a board of directors, we are far more cognisant of risks than we were a couple of years ago."

Pushing ahead in 2016

OMBs show high levels of confidence about their ability to hit revenue and profit targets in 2016.

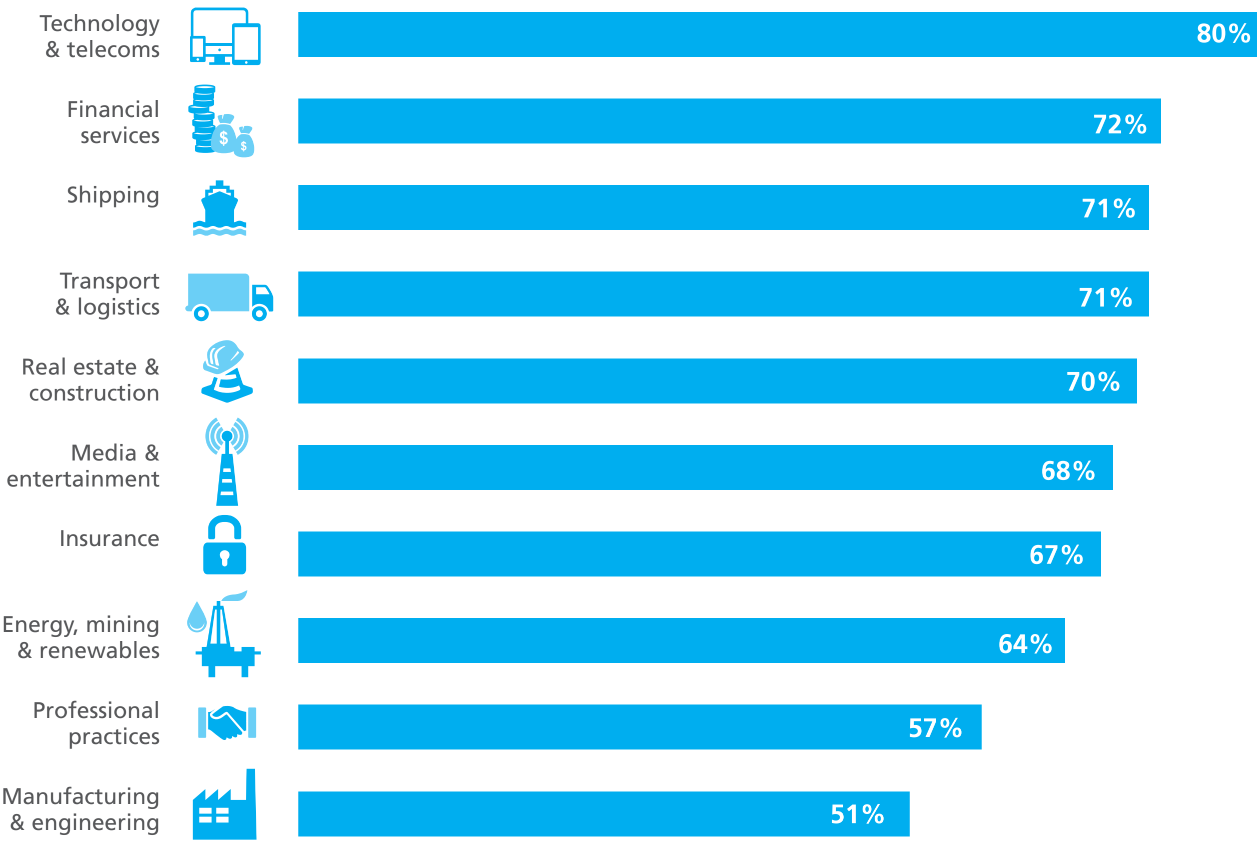
Over three-quarters (77%) of OMBs surveyed are confident about the general outlook for 2016, compared to 70% last year. Almost three-quarters (73%) are confident about meeting revenue targets and 68% are confident about hitting profit targets – results consistent with those of the last two years. (One OMB was anticipating 25% UK growth and 40% growth overseas, on average).

Two-thirds (66%) of OMBs surveyed expect 2016 to be a better year than 2015, of which 21% expect it to be a much better year – similar to those recorded in last year's survey. However, OMBs had substantially higher expectations two years ago, when 76% expected a better year (48% a much better year). It seems that OMBs have now adjusted to the gradual nature of the economic recovery, no longer expecting a dramatic upward rebound but instead accepting more steady growth.

From a regional perspective, OMBs headquartered in England are particularly optimistic, with 68% expecting 2016 to be a better year, followed by 56% of OMBs based in Scotland. Within England itself, OMBs in London top the positivity scale, with 82% expecting a better year in 2016, followed by 70% of OMBs in the South and 64% in the North.

Sector wise, technology and telecommunications OMBs appear most confident about 2016 – with 80% expecting a better year ahead, followed by financial services (72%).

Fig 2. Confidence amongst sectors on whether 2016 will be a better year than 2015



Pushing ahead in 2016/continued

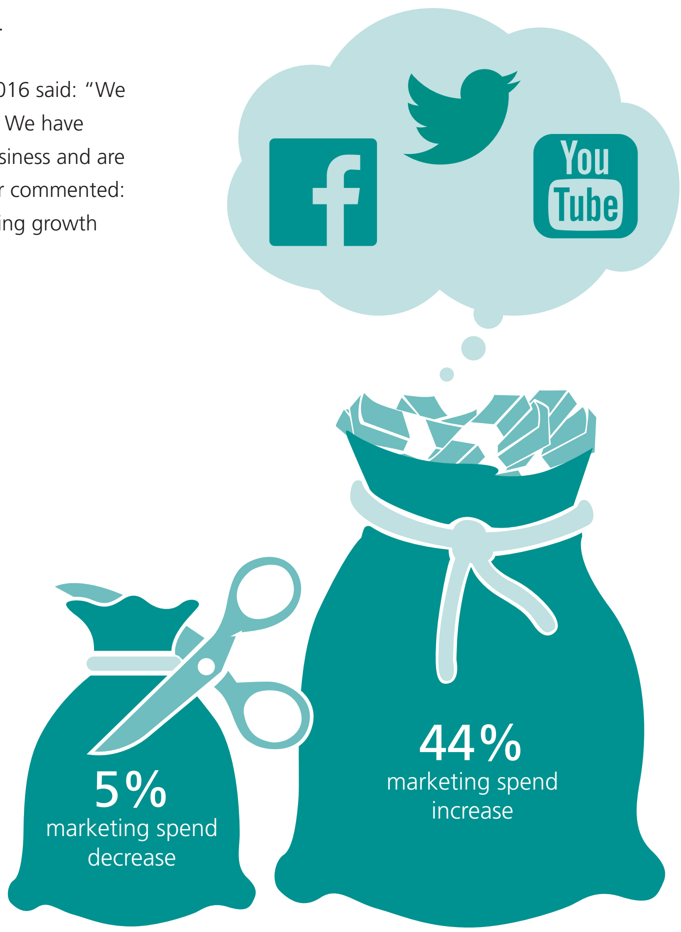
Causes for optimism

OMBs who expect 2016 to be a better year base their optimism on a range of factors, including:

- new products and services coming on stream;
- new or higher value contracts having been won;
- positive impact of investments in technology, equipment or additional staff;
- expansion into overseas markets;
- increased focus on sales and marketing activity (including websites);
- tight cost control and efficiency initiatives having an impact;
- the ability to access markets where growth is predicted, such as construction and aerospace;
- acquired businesses being integrated into the business;
- increased confidence in the economy.

One OMB anticipating a much better 2016 said: "We have worked hard at training our team. We have increased our fees, are winning new business and are carefully controlling our costs." Another commented: "We have a digital strategy and are seeing growth through this channel."

The dominant optimistic attitude among OMBs this year is confirmed by the finding that 44% expect to increase their marketing spend in 2016 – just 5% plan to cut it. Anecdotal evidence suggests that marketing budgets are being spent in more innovative ways, with more OMBs using digital marketing. "How an OMB manages its marketing is often affected by the age of the individuals in the business," notes Mervyn Dolan, a partner with Moore Stephens in Northern Ireland. "Younger generations use social media. For them, if a business isn't on Facebook or using Twitter, it's almost as though it doesn't exist. There are new channels now that people are prepared to try. So as economic conditions improve and new people come up through the business, OMBs will increasingly look at new and different ways of marketing."



Reasons for OMB pessimism

While just one in ten of the OMBs surveyed expect 2016 to be worse than 2015, this still compares unfavourably with previous surveys (8% and 6%). OMBs in the manufacturing and engineering sector are most likely to anticipate a worse year (16%), citing concerns about worsening economic conditions, reduced orders, competition from more automated competitors, the impact of the oil industry slump and delays to defence contracts.

Among OMBs expecting a worse year in 2016, key challenges include:

- concerns about the economic strength of international markets, particularly the Eurozone and China;
- uncertainty about the resilience of the UK economy;
- a gloomy UK retail outlook, with retailers being under pressure to reduce prices;
- the low oil price hitting investment in the energy sector;
- staff being poached or in short supply;
- local councils and other public bodies cutting spending.

Just under a quarter (24%) of OMBs expect 2016 to be about the same as 2015 (24% last year, 18% two years ago). OMBs in this group see opportunities, but also challenges in the year ahead. One OMB anticipated having to "work much harder to stand still" given weak international markets and increased compliance and labour costs (in terms of auto enrolment and the national living wage), although appreciating the benefits of low interest rates.

Some OMBs are factoring in a longer timeframe before they see a dramatic improvement in their business. One commented: "Whilst we would expect to grow in 2016, given we have opened an international office and we are expanding into the rest of the UK, we have lost a few key staff."

James Anderson Estate Agents: increasing spend on digital marketing

CASE STUDY
MOORE STEPHENS

Founded in 1991 by Paul Eperon and Peter Davey, James Anderson Estate Agents now has six offices in London, mainly in the Barnes and Putney areas. Around 60% of revenues are generated from property sales and 40% from lettings.

The business performed slightly worse than expected in 2015. "The principal part of our business is estate agency sales and this was affected by the unpredictable election at the start of the year," says co-founder Paul Eperon. "It was an excuse for people not to make a financial commitment." However, activity was stronger at the end of 2015 than at the end of 2014, raising expectations of improved performance in 2016.

Cost reduction and staff training are two priorities for this year, and the business is also investing in IT and marketing. "In the last couple of years we spent quite a lot of money on paper marketing – magazines and leaflets," Eperon says. "This year we will spend less on physical, hardcopy marketing and quite a lot more digitally. We have just employed someone to do digital marketing for us. Apart from the obvious social media, she is experimenting with Google ads, new websites and sending electronic newsletters to our database. There's a lot going on digitally."

Before the last recession Eperon admits, that quite separate to his principal business, he borrowed too much from the banks to finance various different development building projects. When recession hit and the banks wanted the money back, the business was left without any "wriggle room", leaving a bad taste in Eperon's mouth. "That taste will stay with business owners for some time," he says. "Right now the banks are willing to lend, but many businesses may well seek to find alternative forms of finance."

New strategies to support growth

This year staff training is the top priority for OMBs, but other forms of investment also underpin strategies for 2016.

Staff training tops the list of likely strategic actions that OMBs in our survey plan to undertake in 2016, with 85% saying they are likely or certain to invest in staff training.

Experience and gift cards business Acorne plc invests heavily in management training. "We have a young management team and we use the business schools at Cranfield, Henley and Ashridge for training our up-and-coming managers," says Managing Director Paul O'Brien. "We also focus on customer service, for which we have internal training programmes, and digital marketing, where we invest through external trainers."

Andrew Henshaw, a partner at Moore Stephens South, Chichester believes there has been a major shift over the last 15 years in terms of recognising the importance of people in business. "Most business objectives used to be 'hard' targets like turnover or gross profit, but 'softer' targets like people development have come into play," he says. "There's a recognition that if you get the right people and train them properly, get them to buy in and give them good leadership, then you will have a good business. The turnover and gross profit will come as a result of the people."

The second most popular strategy for 2016 is to expand the UK customer base, with 81% of survey participants likely or certain to do so. Most plan to achieve this without opening new sites (only 27% intend to open new sites or offices or to expand into new territories in the UK). Over a third (34%) are likely or certain to expand overseas.

OMBs that do decide to expand internationally need to choose their target markets carefully. "When OMBs consider international expansion they often look first at Western Europe or the US," says Kevin Phillips, a tax partner at Moore Stephens. "They may think the business culture in the US is more like that of the UK than France, Germany or Italy. But it's a brave step to try and break into the US, because it can be a tough market. Europe could actually be a lower risk option, despite the apparent language barriers."

Commitment to investment

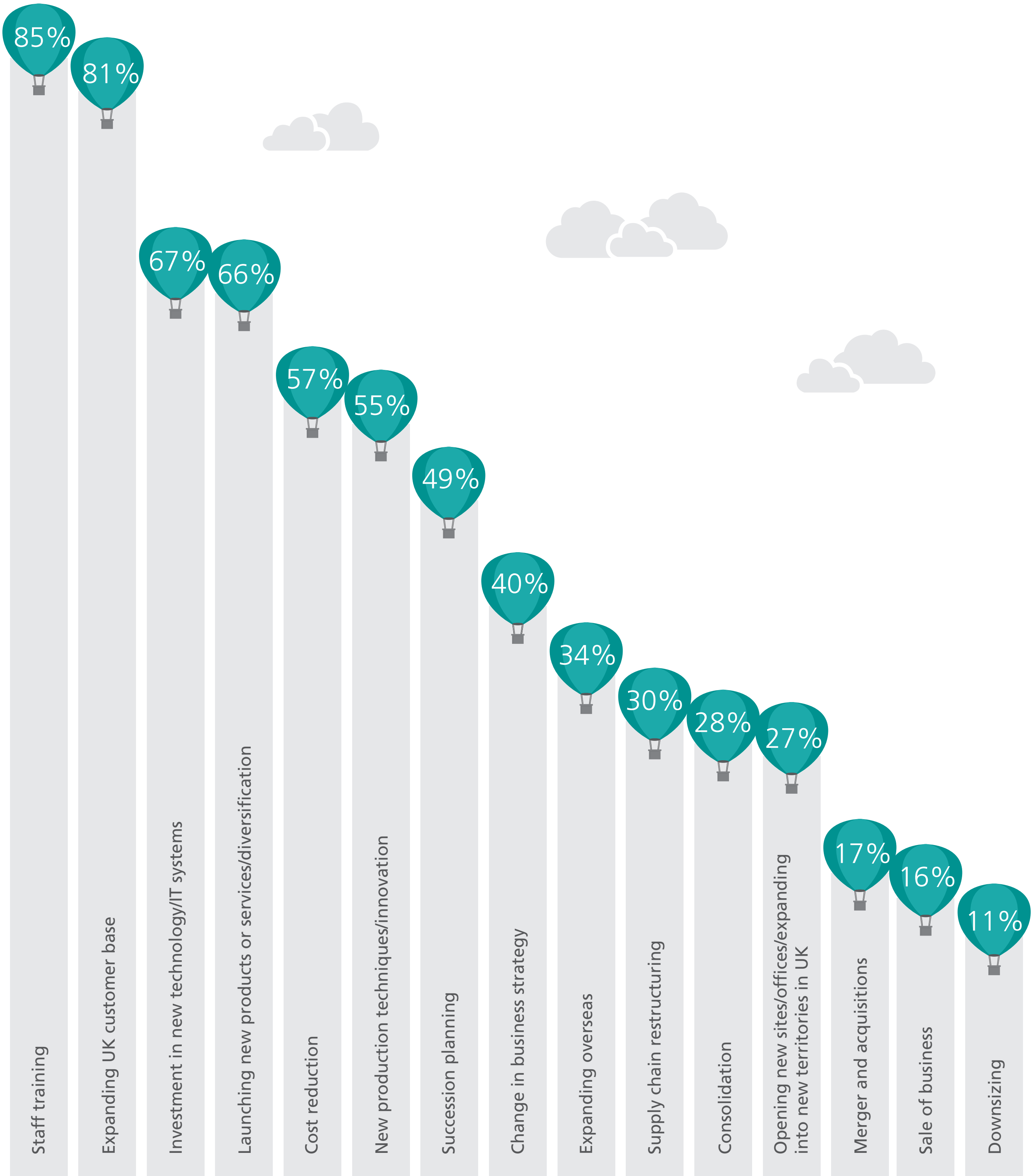
Previous surveys have highlighted OMBs' commitment to innovation and investment in their businesses, and this message comes through strongly again in this year's results. Two-thirds (67%) of OMBs are likely or certain to invest in new technology or IT systems in 2016, while 66% are certain or likely to launch new products or services, or diversify their businesses in some other way. Over half (55%) expect to introduce new production techniques or undertake some other form of innovation in their business operations.

Construction firm Shaylor Group continues to invest in innovation, new technology and techniques to improve buildings' energy efficiency, thermal performance and carbon footprint. The business is also embracing business information modelling, a holistic approach designed to improve building time and cost. "We are also reinvesting in our vehicle fleet, so that we have greener, more efficient vehicles and we use drones to do surveys on buildings for the things we can't see," says CEO Stephen Shaylor.

Moore Stephens partner Paul Fenner has noted investment activity among his clients. "I have seen a lot of businesses starting to spend serious cash on good customer relationship management systems," he says. "They are getting more sophisticated analysis on their customer base and are integrating their IT systems so that they talk to each other. They aren't, however, getting hooked into paying silly money for systems. They are investing more wisely, and getting independent consultancy advice."

OMBs may be investing in their businesses, but they are also continuing to keep tight control of costs. Over half (57%) of OMBs surveyed are likely or certain to seek cost reductions in 2016. "Businesses have to keep their costs under control," says Moore Stephens South partner Andrew Henshaw. "There's constant pressure to maintain a competitive sales price and the only way to do that is to be more efficient in what you make or do, and to keep costs under control."

Fig 3. Strategies OMBs are likely/certain to undertake in 2016



Montezuma's: innovative British chocolate with overseas ambitions

CASE STUDY
MOORE STEPHENS

Founded in 2000, West Sussex-based chocolate producer Montezuma's is growing every year, and is expected to do so in 2016. "The state of the economy is important to us, in that people are continuing to spend money on chocolate," says co-founder Helen Pattinson.

The business now employs between 100 and 130 people, depending on the season. Most revenue is generated through third party retailers (achieving double digit growth last year), but the business has six of its own stores and sells through its own website.

Pattinson is relatively confident about hitting the coming year's revenue and profit targets. "It's a competitive market," she says. "We can't compete on price, so have to play off our other strengths – that we are British and have innovative flavour combinations." Growth in 2016 will be boosted by a new contract to supply Sainsbury's. The Montezuma's team has also been teeing up other potential contracts involving overseas retailers, airlines and licensing deals, but will still enjoy growth even if these come to nothing. The business is also looking to open another one or two stores in the next six to 12 months, if the right sites can be found.

Montezuma's already exports to around 20 countries, though most are "small customers", Pattinson says. "A big focus for us is finding more established and larger customers overseas. We are looking further afield, to the US, for example."

Investment is ongoing. "We are installing a new module to our Sage system that will improve our production planning," Pattinson says. "We have also invested in a new website." New machinery will be bought to support the Sainsbury's contract, incurring total costs of around £250,000. "We might use asset-based finance, mainly because I like to have cash in the bank so it's there when I need it," Pattinson says. "Machines are easy to finance and interest rates are low."

Interest in succession planning

Almost half (49%) of OMBs in this year's survey say they are likely or certain to undertake succession planning in 2016. It may be no coincidence that 56% of the business owners surveyed are aged over 50 (including 17% aged 60 plus). Another third (33%) are aged 40 to 50.

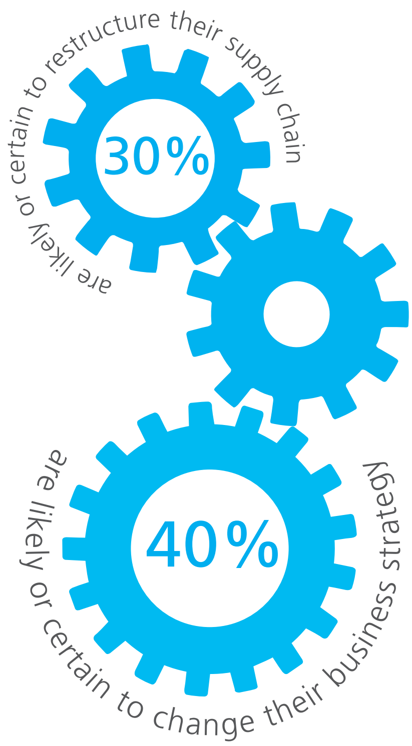
Mervyn Dolan, partner at Moore Stephens Northern Ireland, thinks interest in succession planning is understandable, given the current economic climate. "As the business climate and valuations improve, people who have nursed the business through a difficult time now think it's time to cash in," he says. "They understand the cyclical nature of business, that we are coming out of some very difficult times and that there is likely to be another downturn at some point in the future. If they are going to exit, they want to do it at a time of their choosing, not when it's forced upon them when the price might not be as good."

OMBs need to allow sufficient time for succession plans to be realised, particularly when seeking to sell the business to the management team – often an attractive option. "If you go for a trade sale there will always be downward pressure on price," warns Ashley Conway, a partner at Moore Stephens Stoke. "So why not bring people on through the business who see the long-term value, so you can maximise what you get? I have seen cases where a very generous deal has been done with the former owner, because the new owners can see the business is worth that money. As for the vendor, if you have real confidence in the people taking over the business, you don't fear that you will lose out in an earn-out agreement."

Strategy and supply chain review

A change in business strategy is likely or certain for 40% of OMBs surveyed. This could mean a variety of things, but flexibility and ability to change course fast is a great strength. "Businesses have to constantly re-evaluate what they do and how, and look for ways to stay profitable," says Miles Hewitt-Boorman, Head of Moore Stephens' Thames Valley office. Stoke partner Ashley Conway believes that OMBs in regulated sectors are particularly likely to have to change tack. "Regulations constantly change, so businesses have to retrain or offer different services," he says. "This survey result also reflects the mindset of people who run OMBs, and they tend to be very agile compared to larger businesses."

Just under a third (30%) of OMBs are likely or certain to restructure their supply chain in 2016. This may be in order to negotiate better terms and reduce costs, but there can be good reasons for building stronger relationships with suppliers. "A lot of businesses are trying to protect their supply chain," says Moore Stephens partner Paul Fenner. "Some are creating a group so they all source from each other rather than anywhere else. By strengthening ties they can reduce the risk of a supplier failure and the problems this can cause."



Acorne: investing in technology and people for long-term success

CASE STUDY
MOORE STEPHENS

In business for over 25 years, Buckinghamshire-based Acorne plc is the longest-standing player in the consumer experiences business, with nationally recognised brands including Virgin Experience Days, lastminute.com, Exhilaration and treatme. It has also developed a strong B2B presence in the voucher and gift card sectors, with a range of fully supported products and services including the Virgin Gift Card, Leisure Vouchers and the AS Rosette Voucher. These B2B products are ideal ways for businesses to motivate and reward staff or run sales promotions.

The business has achieved a growth percentage "in the high 20s" for the last couple of years, and expects to achieve double digit growth for 2015-16 financial year. "We are selling into buoyant B2C and B2B markets, we have strong brands and appealing products and major improvements in our technical platforms have enabled us to take advantage of the growth in online sales, particularly tablet and mobile," says Managing Director Paul O'Brien.

The owners have an "enlightened and long-term view" of the business, and have invested in IT, websites and staff training. Investment in IT will continue: "It's a huge priority because we are principally a web-based business," O'Brien explains. "We reinvest to keep our marketing edge and to make sure the customer journey for the web shopper is as seamless as possible." High quality IT systems also help to keep down overheads. "Our transactional volumes are high, so transactional costs are key," O'Brien says. "We aim to use lean practice and to invest in technology to avoid creating unnecessary work. We try to make sure our employment growth is in high-skill, high-tech areas."

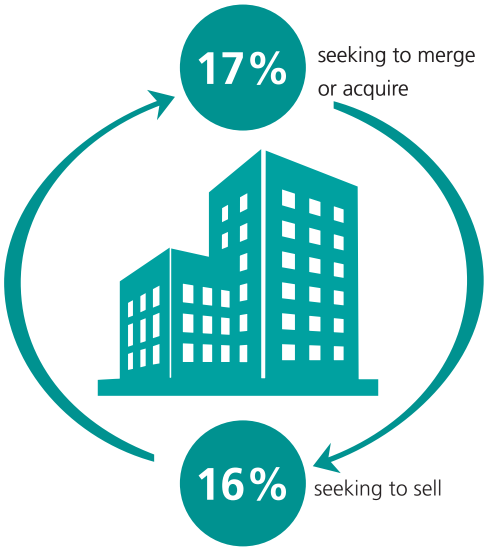
O'Brien is conscious of skills shortages in the Thames Valley region. "We are noticing a squeeze on good people and pressure on pay expectations," he comments. "Finding good people is harder than it was two years ago, so we are trying to increase our collaboration with universities such as Oxford Brookes and Reading."

M&A options?

Around one in six OMBs (17%) are looking to complete a merger or acquisition in 2016. The good news is that 16% of OMBs are looking to sell! Many successful OMBs have grown their business through acquisitions in the past. Experience business Acorne plc is one. "We have grown both organically and through acquisitions," confirms managing Director Paul O'Brien. "We are actively interested in further suitable acquisitions."

"People are aware that a merger or acquisition provides a way to acquire critical mass, new skills or product lines," says Thames Valley partner Miles Hewitt-Boorman. "Given that 16% of OMBs are looking to sell and 49% are looking at succession planning, there could be some M&A opportunities this year."

Just over one in ten OMBs surveyed (11%) are likely or certain to downsize their business in 2016. This isn't necessarily a negative move. "Downsizing does mean you don't have as big a top line, but it doesn't necessarily mean becoming less profitable," Miles Hewitt-Boorman says. "It's the bottom line number that allows you to keep investing in the business."



Eurofilms Extrusion: new equipment expected to fuel UK and overseas sales

CASE STUDY

MOORE STEPHENS

Eurofilms Extrusion Limited is the UK's largest independent manufacturer of pallet wrap stretch film and collation shrink film. Launched in 1995 and based in Telford, Shropshire, the business employs over 80 people and operates 24/7 from a state-of-the art facility containing the latest packaging film extrusion lines.

Over the last three years the business has achieved average annual growth of around 7%, but 14% growth is expected in 2016, largely due to new capacity being installed during 2015. "The total investment cost, including raising the roof to accommodate the new extrusion facility to 25 metres in height, was around £2.3 million," says Managing Director Nick Smith. "The new machine is more technically advanced than our other four machines and produces thinner and stronger film."

Around 85% of sales are UK-based, mainly to supermarkets, food manufacturers, logistics companies and other big businesses that need to stabilise goods being transported by pallet. "Over the last six to seven years we have grown our exports," Smith says. "We intend to increase export sales from 15% to 20% during 2016." Exchange rates are a concern, however. "We don't want a particularly strong pound," Smith says. He also sees strong opportunities in the UK market, where Eurofilms currently has around a 10% share, which is growing by around 1% a year.

Around 60% of Eurofilm's workforce is non-British – many from Poland. Smith says: "Over recent years our employment opportunities have increased significantly and non-UK nationals have integrated very well into the existing workforce and company ethos."

Future risks on the OMB radar

Three risks dominate the worry list for OMBs in 2016: domestic competition, the strength of the UK economy and employee skills shortages.

We gave survey participants a list of possible risks and asked them to pick five that they consider a concern to their business in 2016. The threat from domestic competition came out on top (it was second last year), identified as a concern by 53% of OMBs. Similarly, 27% in this year's survey highlight the risk posed by international competition.

"The way to deal with competition is to make sure you have the best product and the best people, so you get some sort of competitive edge," advises Andrew Henshaw from Moore Stephens South. "Pricing is important, but how you deal with your customer is just as important."

As with last year, economic risks weigh heavily on OMBs' minds. Over half of those surveyed (52%) are concerned about the strength of the UK economy (this was the top risk in last year's survey), and a third (33%) view the strength of the global economy as a risk. Economic worries also continue to reveal themselves in that 25% of survey participants identify exchange rate fluctuations as a risk, and 13% have concerns about interest rate fluctuations.

Employee skills shortages are seen as a major concern, coming third in our risk rankings this year – the same position as in last year's report. Of OMBs surveyed, 45% see employee skills shortages as a risk to their business in 2016. "OMBs across all sectors are saying their most common frustration is resourcing," Gareth Magee explains from Moore Stephens Scotland. "Growth is returning, but they can't get enough people. OMBs are feeling the impact of the recession and the lack of investment in people over the last few years in terms of a famine of available talent. OMBs now need to focus on being innovative in resourcing and recruitment and rethinking benefits, and they need to really sell themselves to candidates in a way they perhaps haven't needed to before."

Thames Valley partner Miles Hewitt-Boorman believes some OMBs are taking action to try to retain good staff. "It's cheaper to keep staff and train them than it is to lose them and rehire," he says. "I'm seeing a lot more interest among clients in staff incentives that tie people into the business as opposed to in-year remuneration. With share options, for example, you are more likely to be tied into the long-term success of the business."

Tax concerns

A quarter (25%) of OMBs surveyed identified the business tax environment as a risk, while 16% have concerns about the personal tax environment. Given that HMRC launched a consultation on company distributions during our survey period, some concern might be justified. But OMBs perhaps need to look at the bigger picture.

Kevin Phillips, a tax partner at Moore Stephens London says: "OMBs have probably benefited most from reductions in corporate tax rates, and more reductions have been signposted in the life of this parliament,". "From a risk perspective, the corporate tax environment for OMBs looks pretty stable, and the Government is preparing another corporate tax roadmap to give some guidance on the future direction of policy, which should help businesses to plan ahead."

OMBs have some concerns about the impact of wider business taxes, not just corporation tax. For example, Kat Heathcote, director of Witherby Publishing Group, believes the taxation of employee benefits makes it hard for employers to support their staff. "If you offer a staff benefit like health cover they won't take it because they are scared of the tax," she says. "Every benefit we give them, from free food – we are on an industrial estate with no shops around, through to child care – they have to pay tax on."

"The way to deal with competition is to make sure you have the best product and the best people."

Future risks on the OMB radar/continued

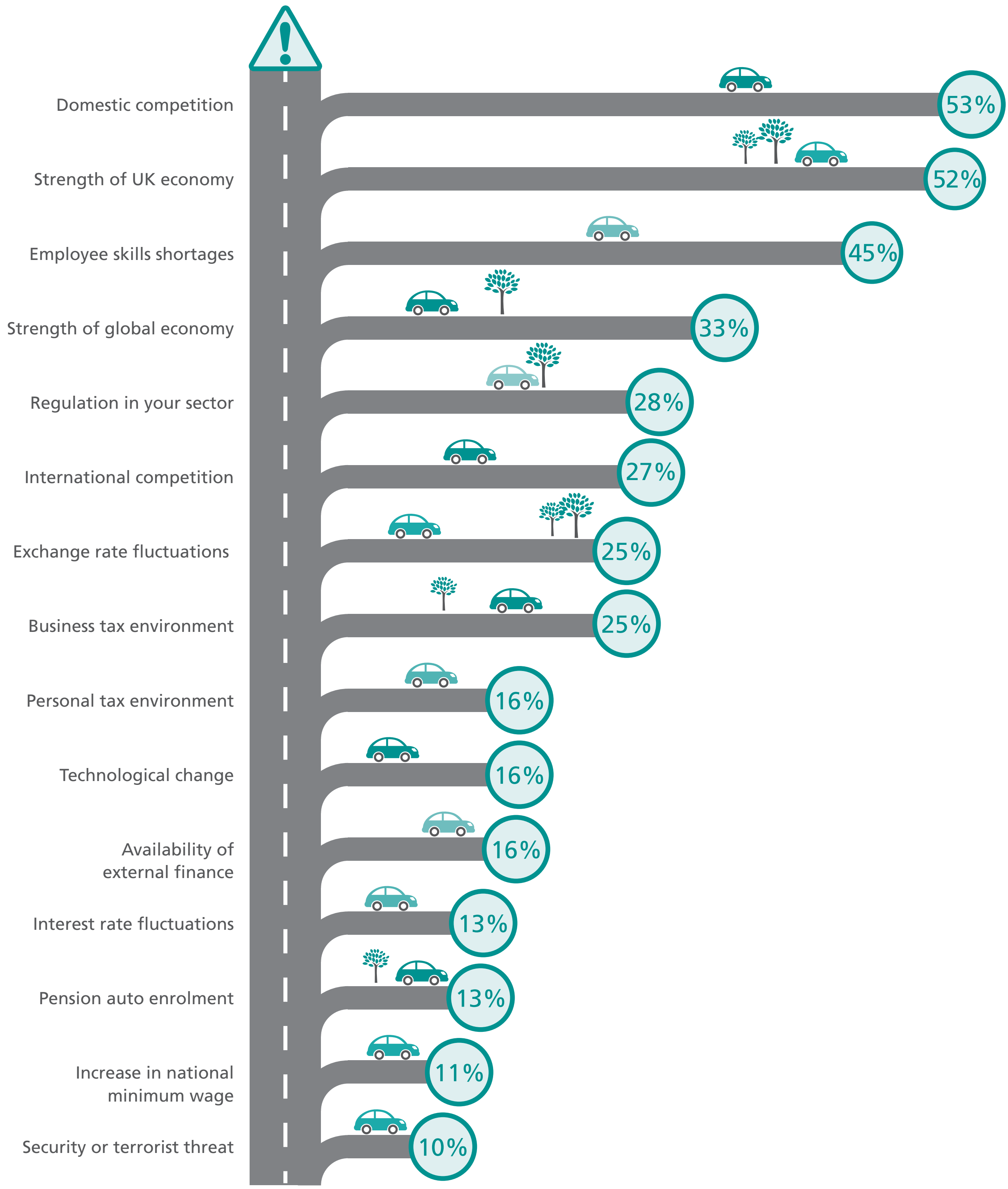


Fig 4. Risks concerning OMBs in 2016

Ongoing finance risks

A minority (16%) of OMBs surveyed see the availability of external finance as a risk to their business. However, the availability of funds for OMBs is generally thought to have improved. “The banks are prepared to lend, but OMBs have to demonstrate that they at least have a business plan,” says Ashley Conway from Moore Stephens Stoke. “If businesses are keen to access funds, it is there. A couple of clients have been looking at new sources, such as crowd funding. The younger generation in particular are not constrained by the usual fundraising routes.”

Mervyn Dolan, a partner in Moore Stephens Northern Ireland, agrees. “In the last six months or so, banks have become more proactive and are competing for business,” he says. “If OMBs are looking to finance new projects, they should shop around. If you were unhappy with your provider a year ago, you might have found it hard to re-bank. Now it’s a cost-free change. Some banks are offering to pay fees incurred. OMBs should also look at non-bank, specialist finance providers, such as asset-based lenders.”

Gareth Magee, a partner at Moore Stephens Scotland, urges OMBs to focus on their own resources. “In Scotland, we have a rich ‘business angel’ culture in terms of supporting early stage businesses. As a result, many OMBs focus on external sources of finance – whether from an angel, bank, Scottish Enterprise, or a grant. They forget about the importance of generating cash for themselves. The easiest business to fund is one that doesn’t need funding. OMBs need to regain that steely focus on generating cash. If OMBs were to focus on only one thing, this should be it.”

QTH: innovation and cost control provide firm foundations

Rob Lewis is an entrepreneur based in Northern Ireland. He founded property development company QTH Limited in early 2009. Rob also operates Signature HS, through which homes are sold and customer-tailoring services provided. In September 2015, Rob formed Opature Limited in Reading to sell home-tailoring software to the major house builders in England and Scotland. “The web-hosted software as a service delivers a robust operating model for builders to engage with their customers and realise home customisation on site,“ Rob says. “This software isn’t just about customer satisfaction, enhanced sales and business optimisation, it’s about generating an additional and fresh revenue stream.” In addition, Rob is a director of SoftIron, a hardware and software company headquartered in Southampton with a research and development facility in San Francisco.

Focusing on QTH and 2016, Rob sees risks to his business coming from interest rate fluctuations, the business tax environment and employee skills shortages. Nevertheless, he anticipates 2016 being a little better than 2015. “We don’t base our confidence solely on the economy but on a commitment to continual improvement and the delivery of a differentiated product, facilitated by a resilient and tenacious team who operate from stable underlying business.”

While always looking to innovate in his businesses, cost reduction is an ongoing goal. “We consistently target the delivery of cost reduction and performance improvement initiatives as we try to refine what we do,” Rob says. He also invests in his staff. “We put emphasis on strength based training,” he says. “We try to conservatively grow the team, but when in place we endeavour to manage away from high staff turnover and therefore invest quite heavily in our current team.”

Rob does not think Britain should leave the EU. “Confidence in the economy may be adversely affected,” he believes, but he would like the Government to negotiate more competitive economic and legislative terms.

CASE STUDY
MOORE STEPHENS

How is the increased dividend tax rate affecting OMB behaviour?

A major change to OMB taxation comes into effect from 6 April 2016, with the increased tax rate on dividends. Surprisingly, only 28% of OMBs surveyed expect to pay a larger than usual dividend before the higher rate comes into force.

After 6 April 2016, 73% expect to pay the same amount in dividends to shareholders – reflecting the fact that, even after the increase in dividend tax rate, dividends remain the most tax-efficient form of remuneration for many business owners. "The increased tax on dividends is unwelcome, but ultimately most people would see paying a dividend as an intrinsic part of their remuneration policy," says Moore Stephens partner Kevin Phillips. "It's understandable that people might bring forward a dividend they might otherwise have paid after April 2016, but after that I suspect many will resort to what they have always done. The tax on dividends is still less than the tax on earnings. The difference has been eroded, but paying dividends is still more tax efficient."

Witherby Publishing Group: carving a profitable niche in the shipping sector

CASE STUDY
MOORE STEPHENS

Based in Livingston in Scotland and established in 2008 through the merger of two companies (one dating back to 1740), Witherby Publishing Group has carved out a profitable niche for itself primarily serving the shipping sector, with around 85% of its customers based overseas.

With the majority of their business in the tanker market, co-owner Kat Heathcote is very confident about the general outlook for 2016 and about hitting revenue and profit targets. "Shipping doesn't follow the same drivers as the rest of the economy, particularly in our area, which is hazardous cargoes," she says. "Freight rates are high, shipping companies are investing and there's regulatory change. So there's a lot going on in our industry." New regulation is welcome as it generates the need for new business information.

Around 18 months ago the business adjusted its operating strategy, reviewing its publications, products and the content it was producing. "We had a look at what was and wasn't profitable, and made some changes," Heathcote says. "So we are now publishing less, but publishing more carefully." This strategy will be continued through 2016. The business will also look at how it uses technology, both internally and in terms of how it delivers its products electronically to clients.

The business employs around 40 people and staff training is also a priority. "As you grow you need to grow your staff and you need to ask them to do different things," Heathcote says. "So we will be recruiting and training up existing staff."

The EU referendum

The issue of whether businesses benefit from the European Union is likely to be a feature of the debate in the run-up to the June 2016 referendum on Britain's continued membership. OMBs have strong feelings on the matter – but they don't all agree.

When asked if Britain should leave the EU, 60% of OMBs surveyed said it should not, with just 17% supporting a 'Brexit'. Almost a quarter (23%) don't know, waiting to be persuaded by the pre-referendum debate, or wanting to see what new terms David Cameron can negotiate.

Some regional variations emerge, with OMBs headquartered in England somewhat more likely to want an exit: 19% of English OMBs think Britain should leave the EU, compared to 10% of Scottish OMBs. (65% of Scottish OMBs think Britain should stay in, compared to 60% of English OMBs.) Within England, a quarter (25%) of OMBs based in the East (not including the South-East) think Britain should leave, and 23% of OMBs based in the North. OMBs in the South, London and the Midlands tend to feel more strongly that Britain should not leave (63%, 62% and 60% respectively).

Why Britain should stay in

Most OMBs wanting to stay in the EU cite the importance of mainland Europe for trade. They comment that leaving would be "an economic disaster" and "insanity", and that "the UK is a hub for foreign business entering the EU". One commented that "trade routes need to remain open and free movement of labour and resources are key to creating a liquid market overseas". Another OMB said that leaving would mean "taking unreasonable risk with the UK domestic economy". One noted: "Departing would diminish Britain's presence on the world stage and affect areas such as defence, farming and not just trade."

Some OMBs acknowledge problems with EU bureaucracy and limitations on UK legislative freedom, but think staying in is the best way to achieve reform. Some are also hoping for improved membership terms. One OMB argued that we "need to stay from a trade perspective but have more freedom on law making and legislation i.e. employment legislation". One pragmatic OMB said: "It's not perfect but we know where we stand."

Why Britain should leave

OMBs in favour of leaving the EU think Britain would regain "control of our own destiny", benefit from less regulation and bureaucracy and increase its ability to limit immigration. Some argue that UK-EU trade will remain strong because "the EU exports more to the UK than the UK exports to the EU, therefore the EU needs the UK more than the UK needs the EU". Some membership opponents believe that other states fail to comply with EU regulations as thoroughly as the UK does, therefore putting UK businesses at a disadvantage, and some think that Britain could do better by developing a more global perspective. Other OMBs are concerned about what they perceive to be socialist tendencies in Brussels. One commented that "centralised state control is less effective than free markets".

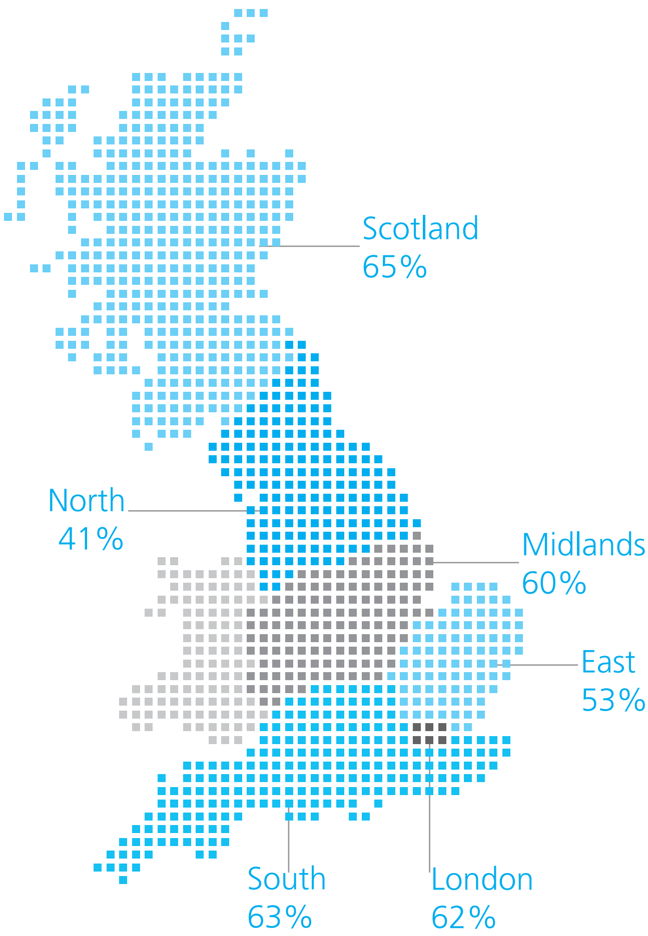


Fig 5. OMBs wanting to stay within the EU

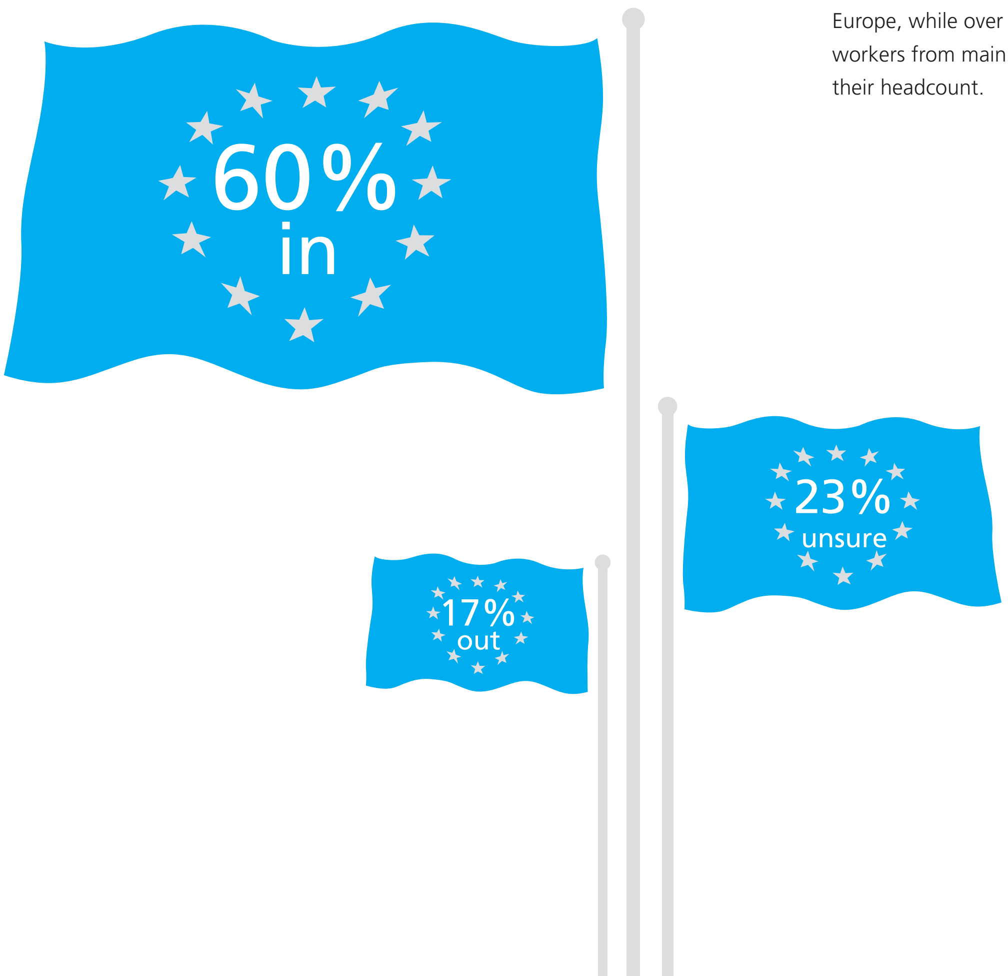
How a Brexit would impact OMBs' businesses

Less than half of OMBs surveyed (46%) think that leaving would actually have a negative impact. The biggest proportion (49%) of survey participants think that leaving the EU would have no impact on their business. Just 5% see any potential positive impact.

On the positive impact side, OMBs refer to the potential for less regulation and red tape to reduce their costs. Those expecting no impact explain that they do not trade with the EU, or believe that EU businesses would still need to trade with the UK. One commented: "It's the products that dictate relationships, not the politicians." Another said: "Freedom from EU restriction would in turn lead to the UK being a more attractive country in which to invest, particularly in manufacturing."

However, many OMBs that do trade with the EU fear that their businesses would be negatively affected by an EU exit. Reasons given include the risk of increased costs of imported supplies, the loss of inward investment into the UK, and an exit of foreign companies from the UK. One said: "I have customers who are foreign owned and have said they will move to the continent if we leave the EU." Another commented: "US clients (and pipeline prospects) may react unfavourably." The downside of reduced access to EU labour was also highlighted. One OMB noted that "the skilled labour pool will be severely reduced" and another predicted that restrictions on the free movement of labour would "undoubtedly increase costs".

It may be that some OMBs are underestimating the benefit of their ready access to EU labour. Half of the OMBs surveyed employ at least some workers originating from mainland EU countries. Almost a quarter (24%) say that over 20% of their workforce is from mainland Europe, while over one in ten (13%) report that workers from mainland Europe make up over 75% of their headcount.



Conclusion: tough lessons, stronger businesses

OMBs are resilient, generally optimistic and committed to investing in their businesses. This year's survey shows that many have concerns about the risks they face – risks often beyond their control, being determined by Government policy and economic conditions. But OMBs are implementing strategies designed to mitigate these threats and support future growth.

Though the recession is another year further in the past, OMBs remember the tough times and the lessons they learnt. Some feel stronger as a result, capable of building more profitable businesses in future. Stephen Shaylor, CEO of construction company Shaylor Group, captures this mood. Although 2011 and 2012 were the toughest years in recent history for his company, he says: "The business is better placed and I'm a better person as a result. It's about not taking anything for granted; about making sure you are sufficiently reserved and provisioned, and have the ability to withstand shocks. It's also about contracts, the terms on which you engage."

15 ways to build a successful business in 2016

- Address skills shortages by taking an innovative approach to recruitment, developing relationships with local schools, colleges and universities.
- Nurture your talent and invest in training and development – people may develop capabilities that enable them to take on more senior roles.
- Consider whether tax-efficient long-term incentive plans could help you retain key employees in the business, particularly those vulnerable to poaching by competitors.
- Focus on cash generation – by generating cash you can seize opportunities and invest in your business, without necessarily having to rely on external funders.
- If you do seek external finance, shop around and consider all the funding routes open to you, from asset-based lenders to peer-to-peer and crowdfunding platforms.
- Target quality customers and build strong relationships with them – such customers will support the resilience and growth of your business.
- Review your supply chain and consider whether any opportunities exist for closer working relationships.
- Make your capital expenditure count – don't be led by tax reliefs or incentives but focus on what will increase efficiency, sales, service quality, etc.
- Invest wisely in technology – cloud-based systems make new technology more affordable and more widely-accessible than ever.
- Examine your marketing spend: should you be applying it in different ways, perhaps experimenting with digital marketing?
- Even if you are growing, keep a tight control on costs to maintain your margins.
- If organic growth is slow or stalled, consider acquiring another business – a competitor, supplier or customer.
- Be opportunistic and look for ways to diversify your business, e.g. by increasing overseas sales – but plan carefully before trying to enter foreign markets and take professional advice.
- Be flexible and prepared to change your business strategy if it no longer works – a great strength of OMBs is their ability to make rapid decisions and respond fast to changing market conditions.
- Don't forget about succession planning – it can take several years to groom an upcoming management team or address internal issues that would put off an external buyer.

Our solutions

66% are certain to launch new products or services or IT systems in 2016

The IT function represents one of the largest investments that businesses make, and therefore it is important to understand your IT-related risks, and be confident that the systems you have in place are secure, resilient and fit for purpose. Our IT Consulting team provides expertise in all aspects of IT governance, risk management and assurance.

57% are likely or certain to seek cost reductions

Currently, most businesses, regardless of size, are handling low value administrative and processing functions in ways that are not cost effective. By outsourcing these activities, companies can benefit from reduced costs as well as improved reliability, accuracy and resilience. Through Stream – our cloud-based outsourcing solution – we offer a highly dynamic and efficient online finance and accounting solution, including payroll and bookkeeping services.

56% of owners are aged over 50

Our Corporate Finance team helps clients analyse the options available to them when selling or handing on the reins of their business. We know how much importance OMBs place on the future of their business, and we look to find a strategy that best suits each owner. This may include selling to a competitor, your management team, private equity or passing the business to a family member.

55% expect to introduce new production techniques or undertake some other form of innovation

If businesses are investing in new technologies and innovation then they could qualify for R&D tax relief. SMEs can enhance their qualifying expenditure by 130% as well as having the option to convert tax losses created by the relief into cash. Large companies can also benefit by virtue of a cash credit equivalent to 11% of their qualifying costs, thereby triggering reductions in tax liabilities or repayments in the event of a loss. We have extensive experience in assisting companies identify qualifying projects and submitting claims to HMRC.

40% are likely or certain to change their business strategy

Having a robust strategy in place is crucial for any business. We can provide assistance with business plans and implementing safeguards to protect your assets. Most businesses have growth high on the agenda and we can support this through providing financial forecast model preparation, access to funding, acquisitions, company restructuring and strategic reviews.

34% are likely or certain to expand overseas

International operations are often a challenge to manage. Dealing with many foreign service providers and keeping up with foreign accounting, tax, legal and HR requirements can be onerous and time consuming. We can help you with these challenges and help maximise the efficiency of your international operations. Moore Stephens International Limited is one of the largest international accounting and consulting groups worldwide. Today the network comprises 657 offices in 106 countries throughout the world.

25% of OMBs surveyed identify the business tax environment as a risk

In this challenging economic environment, businesses face pressure to explain their tax affairs transparently, manage risk and maximise opportunities. We can help you ensure you have made the appropriate disclosures, advise you on structures to manage commercial and tax risk, and assist you in optimising tax reliefs.

About Moore Stephens

Moore Stephens is a top ten accounting and advisory network, with offices throughout the UK and member firms across the globe.

Our clients range from individuals and entrepreneurs, to large organisations and complex international businesses. We partner with them, support their aspirations and contribute to their success. In-depth understanding of our clients allows us to deliver focused accounting and advisory solutions, both locally and globally.

Clients have access to bespoke services and solutions, including audit and assurance, business support and outsourcing, payroll and employers' support, business and personal tax, governance and risk, corporate finance, forensic accounting, wealth management, IT consultancy, and restructuring and insolvency.

Our success stems from our industry focus, which enables us to provide an innovative and personal service to our clients in a range of sectors.

Moore Stephens globally

Moore Stephens International is a top ten global accountancy and consulting network, headquartered in London. With fees of over US$2.66 billion and offices in 106 countries, clients have access to the resources and capabilities to meet their global needs.

By combining local expertise and experience with the breadth of our UK and worldwide networks, clients can be confident that, whatever their requirement, Moore Stephens provides the right solution to their local, national and international needs.

We would like to thank the following for their help with this report:

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