The ANZ Privately-Owned Business Barometer 2009

KEY INSIGHTS





Overview of the Barometer

The ANZ Privately-Owned Business Barometer is an annual survey conducted by Colmar Brunton on behalf of ANZ. It targets privately-owned businesses with an annual turnover of between $10 million and $150 million.

As in previous years, the survey was circulated among just under 2,000 private businesses across New Zealand. We were pleased to receive responses from 31 percent of companies, suggesting that this research is continuing to reach the minds of owners.

Respondents represented all regions and sectors. For the most part the Barometer respondents are key decision-makers within their business and 35 percent are the founders of their companies. Eighty-five percent of businesses have been in operation for more than 10 years.

This year we have divided the Barometer into two documents, the first summarising our insights into the sector, based on the Barometer findings and subsequent conversations, and the key issues and opportunities that we identified via this year's research. The second, the ANZ Privately-Owned Business Barometer Results Summary, provides more details on the findings.

Change brings opportunity & fortune favours the well-prepared

There's no disputing that the current environment is creating challenges for businesses, but it's also creating opportunities for business owners who are able to identify the possibilities and act on them. And the businesses that are best placed to take advantage of these opportunities are those with a clear vision of both where they are now and where they would like to end up.

The global economic situation clearly overshadows the results of the 2009 ANZ Privately-Owned Business Barometer. Despite ongoing media coverage, the majority of business owners remain broadly optimistic. They also recognise the need to respond and are taking steps to minimise the impact on their businesses.

However, in a changing landscape, conventional methods of doing business may no longer be sustainable. This year's results clearly suggest that for many, simply surviving this crisis is a challenge, but thinking beyond the short term is equally important and will be a defining feature of future success.

So what can you do to get your business in the best position to survive the downturn and to thrive during the recovery? From talking to business owners, we've seen some common themes among the companies that are doing well in the current climate. These business owners:

- have a plan that encompasses the broad environment in which the company operates, considers numerous scenarios and charts a course of action for each.
- have a vision of where they would like to be in the future and make decisions to address short-term issues within the context of a long-term objective.
- seek independent thinking to inject different ideas and ask the hard questions to drive performance.

The ANZ Privately-Owned Business Barometer is all about adding value. By gaining a deeper understanding of the issues and opportunities facing New Zealand's private businesses, we are better placed to deliver tangible solutions to business owners. We are also able to raise the level of awareness and debate about the importance of, and key issues affecting, this vital sector.

We would like to thank the business owners who took the time to contribute their views. In testing our interpretation of the results, we held several round-table discussions with business leaders around the country and our thanks to everyone who took part in these.

We trust the ANZ Barometer will once again provide plenty of food for thought and enable you to compare your situation with the views expressed by others in the market.

We look forward to discussing the findings with you in more detail over the next few months. If you have any questions or would like to discuss your situation with any of our team, please refer to the back page for contact details.

GRAHAM TURLEY
Managing Director, Commercial




Defining the issues

There are an estimated 3,500 businesses with annual revenues between $10 million and $150 million in New Zealand, collectively generating around $120 billion in revenues each year – an estimated one-third of our revenue economy. Yet the segment is often overlooked, despite having a value several times the size of our publicly listed markets and forming the engine room of this country's future economic growth.

Given the current international environment, we expected this year's ANZ Privately-Owned Business Barometer to return some interesting results.

We are encouraged to see that business owners have a realistic view of the changed economic landscape and are aware of the need to adapt. When asked how the economic downturn was affecting or changing business owners' behaviour or plans, the top three answers were (in order) reducing costs, managing debtors and engaging with customers.

Clearly businesses are realising that this is a protracted downturn and are doing what they can to minimise risks and maximise their existing relationships.

However, this alone is not sufficient to put your business in a position to thrive when the markets turn. Cash management might be the most important issue to address in an economic crisis but it shouldn't be the only action. During times of uncertainty there is a tendency to look only to the short term, with the end result being that the long term disappears from vision.

New Zealand businesses and their leaders are acknowledged globally for innovation – in their products, their cost-effective and high-quality manufacturing, their positioning against bigger players on the world stage and their adaptability. Yet many business owners are still adopting a conventional approach to managing their businesses, rather than asking if the environment necessitates a new way of thinking.

Different thinking is certainly not absent. A small number of businesses are adopting a very deep methodology in assessing the situation and looking to the future with a plan that will give them options to adapt as they work their way through, and out of, this recession. However, this year's ANZ Barometer suggests that most are still focusing on the obvious immediacies and ignoring the wider environment and the long-term vision.

And there's a very real danger in this trend.

One consistent theme that came from talking to business owners and commentators is that 'rationalisation' of businesses in New Zealand is a very likely outcome of the current situation. The privately-owned business market in New Zealand is highly fragmented, with businesses competing for growth and talent in a finite market. Add the influence of a general demographic of aging owners and the sector becomes ripe for consolidation. When this occurs, the businesses that are likely to thrive are the ones with a long-term vision and an active plan in place to achieve their goals.

Undertaking the ANZ Privately-Owned Business Barometer has taught us one very important point – there is no 'typical' privately-owned business and no 'average' business owner. The businesses and the approaches taken by their owners are as diverse as the products and services they provide. That means there's no 'one size fits all' approach to solve all of the issues or deliver all the opportunities in the sector.

THERE ARE, HOWEVER, SOME KEY ISSUES THAT AFFECT THE SECTOR AS A WHOLE:

A narrow perspective of planning

Seventy-nine percent of businesses undertake long-term strategic planning and 73 percent document these plans. However, evidence suggests that for many, the focus is relatively narrow, is short term in its outlook and is centred largely on costs and financial performance. This raises the question as to whether business owners are thinking broadly enough about their current situations (including a deep assessment of business models) or are thinking truly long-term and defining a visionary objective for their businesses. While we are seeing some clear examples of the benefits this two-fold approach to planning can deliver, too many owners are unable to afford the luxury of taking time out to gain a broad perspective of their businesses and the environment.

An independent perspective – valued but ignored

The majority of business owners we see have an overwhelming passion for their businesses. Most have grown their businesses from scratch and have a strong emotional as well as financial commitment to what they do. But many find it difficult to wear two hats – to separate the perspective of manager and owner. Too few are able to stand back from the day to day and look at the business with a broader perspective. Increasingly, business owners are realising that they can benefit from the broader vision and fresh insights that come from an independent perspective. Despite 81 percent of respondents feeling that outsiders can add value, only 35 percent of respondents are interested in engaging an advisor.

Constraints to growth suggest some broader issues

The Barometer suggests that while owners are generally still looking for growth, the majority are focusing on 'organic' growth rather than considering the opportunities for step-change growth. There is some awareness of the broader opportunities for expansion, particularly via consolidation in this current stage of the economic cycle, but there seems to be some block to this type of activity that cannot be explained by the environment or availability of capital. Owner aversion to significant change and a general reluctance to relinquish control are both factors that seem to be playing a major part in many opting to stick with the status quo.

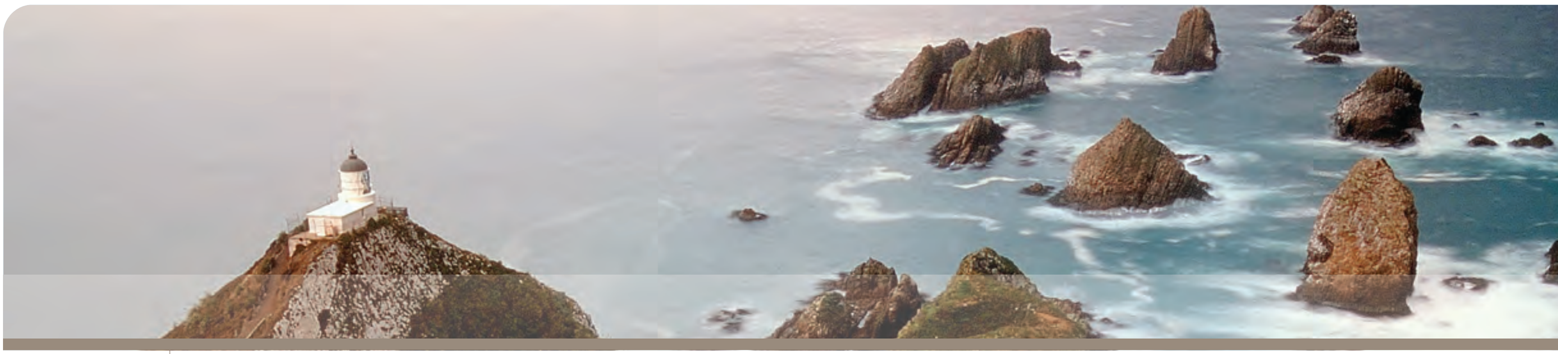
Ownership demographics tell a story

Fifty-nine percent of businesses surveyed have one shareholder who controls more than half of the company and who, in the majority of cases, is also the founder and managing director. Sixty-two percent of these shareholders are over 50 years of age and 23 percent are over 60. Eighty-five percent have operated for more than 10 years. These demographics seem to underpin much of the sentiment and behavior evident in this year's Barometer. Some questions are emerging as to whether this segment of the New Zealand market is dominated by a conservative owner psyche, which may be constraining growth.

Succession is still a big issue

Almost half of all respondents aspire to retire in the next five years, yet most still have no plan in place. With the aspiration and timeframe for retirement remaining constant with the 2007 and 2008 ANZ Barometer findings, fewer owners see this as a pressing issue. For many, day-to-day business matters mean succession is increasingly being put into the bottom drawer to be considered 'at some stage'. Extrapolating the aspiration across this segment of the market suggests that up to 10,000 businesses could change hands in the next five years if owners achieve their objectives.

The potential effects of not dealing with this issue can be significant, impacting on the value of a business, the ability to sell and, in time, owner wealth. If owners don't plan, but decide to ease off on the accelerator, the effects on business performance can be just as destructive. Bottom line: while many owners never want to retire, the demographic suggests this is an issue that must be proactively addressed if owners wish to maximise their options and wealth.

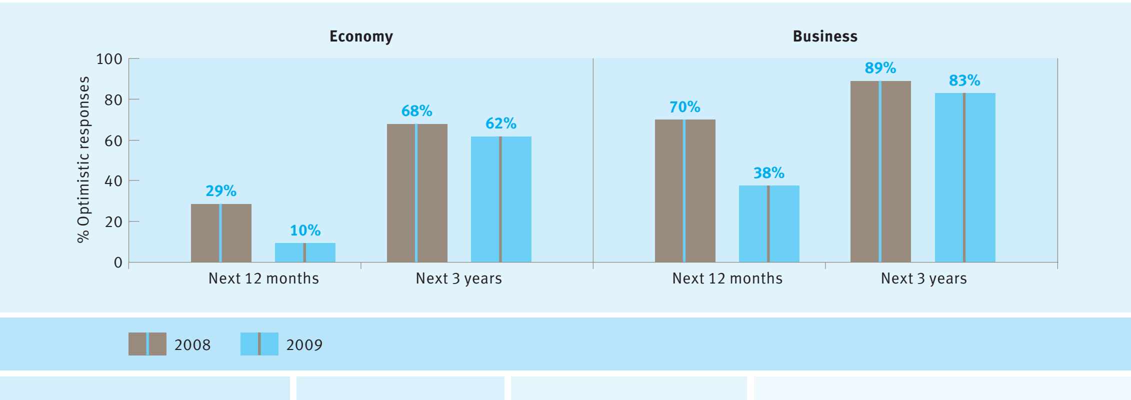


The economic crisis

and its broader implications

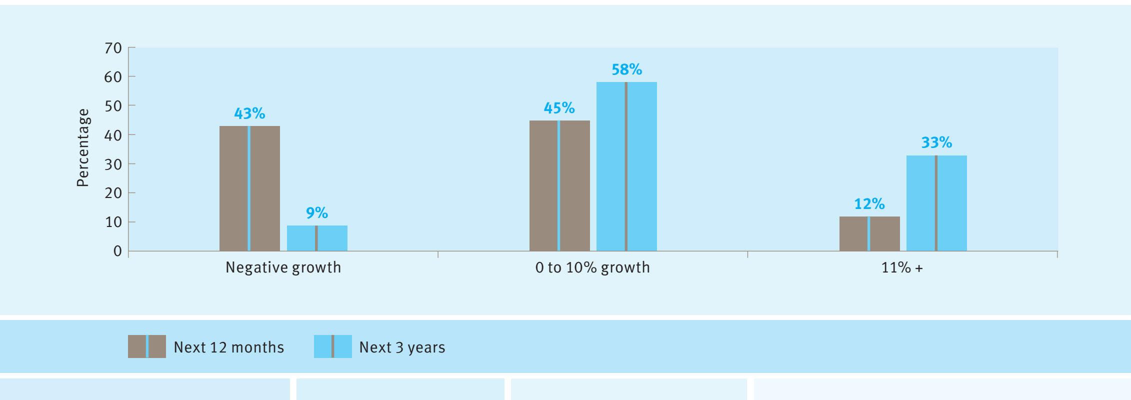
As expected, owners' confidence in prospects for both the economy and their own companies for the 12-month period is lower than it was last year. However, long-term outlooks are similar to last year's Barometer findings (see chart below which shows the percentage of optimistic responses to questions on business and economic outlook).

POSITIVE SENTIMENTS TOWARDS THE ECONOMY AND BUSINESS



When asked to put a figure on growth in the next 12 months and three years, confidence wavered. Almost 90 percent expected less than 10 percent growth in the next 12 months and 43 percent expected negative growth. Only one-third expected growth of more than 10 percent in the next three years.

GROWTH EXPECTATIONS



So with differing levels of optimism, on which view are the owners acting? Are they planning around the assumption the economy will improve in the next three years? Or are they putting plans in place to protect themselves against the likelihood of three-year growth of less than 10 percent?

The evidence suggests that reacting to short-term influences is taking precedence, with little reference to the long-term objectives the business may have.

When asked how the downturn was affecting behaviour, cost reduction topped the list but it wasn't the stand-out that was expected. Further investigation into this point suggests that many businesses have been cutting costs for some time. The New Zealand-centric recession that began in 2007 gave business owners a practice run, with many starting then to trim the sails. More active customer and debtor management ranked two and three, which is an indicator that business owners view the current climate as a protracted downturn and are looking to shore up their relationships early on to buffer themselves against what is to come.

Many, therefore, seem to be taking steps in the right direction. They are identifying the seriousness of the crisis and taking action. Could more be done? If business owners are taking a short-term view only, how can they know if their current actions will help or hinder future success? Are there changes they can make now that will put them in a stronger position when the economy does turn?

For many businesses the downturn will generate growth opportunities via consolidation and changing markets. The vital question is whether they can position themselves to take advantage of those opportunities.

For those in a strong cash position, this isn't an issue, but for many others, the opportunity to expand opens questions about capital, ownership and risk in general. Views of respondents on this are complex.

Not all are choosing to act, for a variety of reasons. Regardless of whether it's risk or opportunity, many owners could do well to heed the advice of Barack Obama's Chief of Staff, Rahm Emanuel, when he said, *"You never want a serious crisis to go to waste… it's an opportunity to do things you could not do before."*

Planning

The importance of vision and a different form of planning

Despite the majority of businesses completing and documenting business and strategic plans, there are question marks around whether they are achieving the right balance of short- and long-term vision.

Consistent with a number eight wire culture – where we just get on with it – business owners have established and developed some extremely successful businesses in this segment, often from humble beginnings. But the current environment is demanding action. The world has changed fundamentally in the past 18 months, and for many, the shift in business is far different from what has been experienced during previous downturns.

Owners are clearly embracing change, with most getting on with it and making necessary changes to cost and customer issues. Are they taking the opportunity to assess the current situation strategically: questioning their business model; reassessing their supplier and customer base; and, in particular, developing a range of scenarios that take into account all possible outcomes and the appropriate responses needed to survive and thrive?

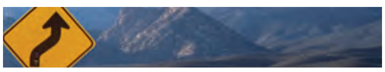
Similarly, are business owners truly standing back from the day-to-day and assessing the long-term possibilities for their businesses? Are they thinking about what could be achieved if capital, people and risk were not constraints?

Both views are important in this environment, and in our experience those adding the two perspectives to their tool box will emerge stronger and go further than those who don't. A worrying constraint revealed by many owners is the lack of time to gain a broad perspective of their business and the environment, despite the fact that there are clear benefits from this approach.

Short-term action is vital. Surviving tomorrow may be all some owners can think about. Others are thinking further about how they can win in three years' time. Without any sense of that long-term perspective, it is hard to make today's important decisions within the clear context of tomorrow.

Put simply, having a view on the future is the difference between travelling with or without a map. With a map you know where you are and where you want to go, and can vary the route along the way but still end up at your desired destination. If you don't have a map and you don't know where you are, chances are you'll end up somewhere but it can be a lot of travel for not much distance.

For some, the current environment provides a welcome opportunity to rationalise cluttered sectors. Others see it as a 'return to normality' or a call for businesses to get back to basics.



While we may not know what the future will look like, the general consensus among the business community is that the environment has changed forever and we are unlikely to go back to the way things were before. Business owners now have a choice – they can continue to plan for the short term and run the risk of being left behind with the economic crisis, or they can accept that the world has changed and embrace new ways of thinking and new ways of planning.

KEY RESULTS

- 79% of respondents undertake long-term strategic planning
- 73% document these plans
- 71% have a formal business plan

"In the current environment you need to be good to operate a business and that's how it should be. (ANZ) put me through hoops recently to get a deal that in the past would have been funded without asking any questions. But what I was required to do was what we should be doing. If you have skin in the game, you are much more likely to do the due diligence."

Kevin Melville, General Manager and a founding shareholder, NME Electrical

Perspective

The value of an impartial perspective

It's lonely at the top and even the most successful business people need trusted advisors to provide a sounding board for ideas and to test the business owner's thinking.

Now in its third year, one result that the Barometer has shown is an increasing awareness of the benefits of a broader vision and fresh insights that come from an independent perspective. Eighty-one percent of owners feel that outsiders can add value and 73 percent are happy to pay.

When the ANZ Barometer questioned who a business owner would ask for advice, accountants were the most cited source, followed by shareholders and lawyers. While in no way suggesting that the company accountant should not provide advice, there is certainly a question about whether a long-term company accountant is truly independent. If they have a deep and long-term involvement with the business, can they bring truly new ideas to the table?

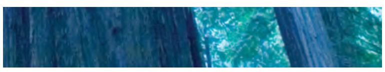
Despite the awareness of the value of independent advisors, business owners show a marked reluctance to engage truly independent outsiders. This vast difference between understanding and action begs the question, 'why?'.

Also concerning is the fact that one third of companies in this segment of the market still have no Board. Of those with a Board, only 38 percent have a director who is truly independent.

As with succession, it's important to note that there is no 'one size fits all' solution. Some need and will benefit from a formal Board, others don't need it or don't want it. For some, an informal catch-up may provide all the advice needed. For others an advisory Board might be the solution. It's up to a business owner to determine a solution that will best address their needs, but in our experience, some form of external perspective can add real value.

A positive trend that has come through the ANZ Barometer is that more owners are differentiating the roles of managers, owners and directors, even if they wear all three hats themselves. Where a Board does exist, the perceived value of Board members is moving from generic 'shareholder wealth' considerations to contributing to strategy, delivering strategic thinking and different ideas.

Clearly, negative connotations towards Boards prevail, with many still associating the word 'Board' with compliance rather than value-add. A bit like the sentiment towards 'consultants', the role of Boards is too often seen to be telling owners what to do rather than simply asking smart questions and helping to achieve objectives.



Regardless of the reasons to not engage outside advice, the benefits can be significant. Outsiders can share their experiences, as well as the lessons they've gathered from other businesses, both to provide new ways of thinking and to assist owners to benchmark their business. They can also ask the right questions – questions that make owners think about what they need to do – and in many cases, persist with such questions to ensure that the business owners take action.

KEY RESULTS

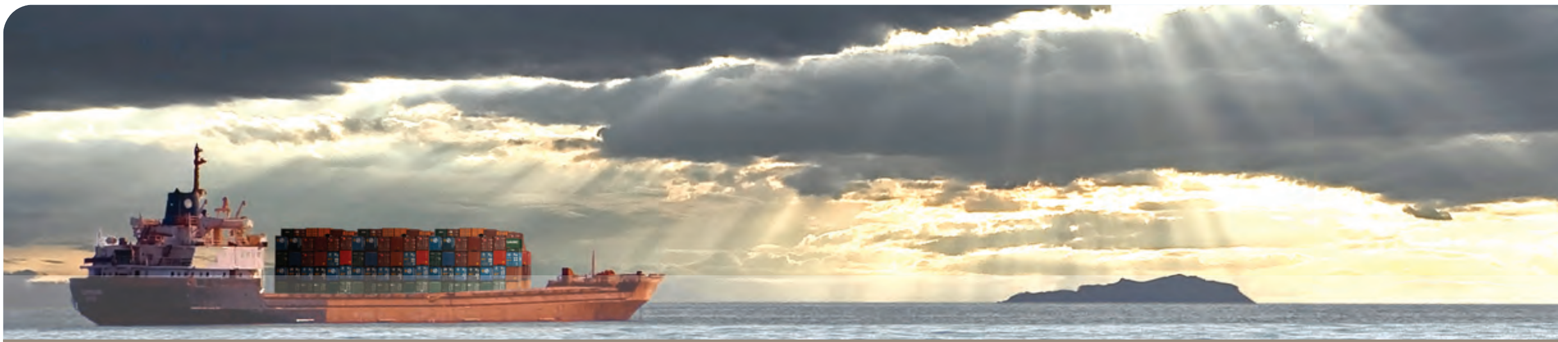
- 84% believe they will benefit from independent thinking
- 81% believe an independent advisor would add value
- 35% are interested in engaging an advisor
- 65% of businesses have a formal Board
- 38% of these have an independent director (who isn't the company accountant or lawyer)

"The role of outsiders isn't to provide the answers but to ask the questions."

Vance Hainsworth, Director and Founder, ENZ Oil

"A good independent advisor will bring value, not only by telling you what you don't know , but also by encouraging discipline in executing appropriate strategy that you already have in mind, that may otherwise 'slip'..."

Bill Gordon, Managing Director, Holmes Group Limited



Capital

Is capital really the constraint it's made out to be?

As the key results table below shows, the questions asked around growth and capital generated some conflicting responses.

While the majority of owners are still planning to grow their business and most require capital to fund this growth, responses show there are mixed messages around the availability of capital. Sixty percent believe capital is not a constraint to growth, consistent with 2008, but the proportion who say capital is readily available has decreased (66 percent versus 78 percent in 2008). Quite naturally, there has been a shift to funding growth via cashflow and existing debt facilities, with 88 percent saying this would be their preferred source of growth funding. Bank debt is still the number one source of external capital, with 65 percent saying they would fund growth by borrowing from the bank (61 percent in 2008). However, owners are more wary of debt this year, with only 66 percent comfortable with debt, compared to 79 percent in 2008.

These conflicting responses suggest that availability of capital may not be the number one issue on owners' minds. In fact, 70 percent feel the biggest constraint to growth is current economic conditions. The responses also suggest that a generally increasing aversion to debt is also playing a role.

When asked what business owners would do if capital wasn't a constraint, the highest ranked options were expanding faster, accelerating plans and acquiring competitors. Yet very few owners seem willing to follow this course, particularly in the current environment.

KEY RESULTS

- 70% of businesses are planning growth
- 75% of businesses say more capital is required to achieve growth, consistent with 2008
- 66% believe capital is readily available, down from 78% in 2008
- 40% feel capital is a constraint to growth (unchanged from 2008)
- Tellingly, owners are much more averse to debt this year, with 36% being averse versus 21% in 2008

So what's stopping them? Perhaps some perceive that funds are not available. Others perhaps are waiting until prices fall before engaging. Is it a by-product of the business lifecycle, with an aging profile of business ownership combining with a commensurate decline in risk appetite? Certainly many owners feel that they do not wish to dilute control, a factor that often comes with the territory of expansion and bringing in new capital.

In previous ANZ Barometers, conducted when the markets were stronger, businesses cited lack of time as the biggest constraint to growth. Now that the markets have cooled, respondents cite the economy most often. Meanwhile commentators cite capital constraints. There is almost certainly truth in all three. The tough question that needs answering is – how many simply lack the confidence to take steps into the unknown?

Succession

Are owners boxing themselves into a corner?

Every year that we run the ANZ Barometer, the average age of owners increases by one year. It may seem logical but it illustrates a very important point – businesses aren't changing hands. Despite the demographics and the fact that their timeframes for retirement remain unchanged, fewer business owners see succession as a pressing issue.

Identifying the reasons for this is challenging. Perhaps it's because in these tough times, owners believe their businesses need them. Or maybe the value of the business has declined in the past 12 months to the point where the owner feels that leaving now isn't an option.

Succession involves more than a transfer of ownership. It is often a release of capital over time and a transition to wealth management for the exiting owner as the business again moves into a rapid growth phase with new owners.

There are two ways this process can play out.

Version one is where the business owner does little planning for the future, then watches the value of their business erode, lets staff leave for better opportunities and sees their retirement plans in tatters while competitors pick over the carcass for customers, assets and key people.

Version two involves business owners accepting that the best way to deal with succession is to tackle it head on; to consider succession in terms of both people and ownership structure, develop scenarios and have a plan. The old adage – "build a well before you need to drink from it" – captures the sentiment. You may never need to drink, but no one ever suffered from having options.

While most businesses identify that they need to think about succession and even claim to be planning, few seem to be actively stepping down the path.

Why? Is it because the options are too hard to identify? Or is it that after so many years at the helm, the thought of sharing control is just too difficult to face? Whatever the situation, the reality is that many businesses are now going through a dramatic revaluation. Whether this is a real decline in value or a market correction off an unsustainable high is a moot point – the fact is that many business owners are now looking at either selling their business for much less than was previously anticipated or delaying retirement to recoup the losses.

Staggered change offers one solution whereby owners gradually release time and capital as they cede control. But the bottom line is clear. If 10,000 businesses start to change hands in the next five or so years, having a plan that can be effectively implemented may maximise the wealth transferred to owners as they move out of the businesses.

KEY RESULTS

- 62% of owners are over 50 years old
- 23% are over 60 years old
- 45% aspire to retire in the next five years
- 11% have a formal plan in place for succession

SO WHAT CAN WE DO TO HELP?

The ANZ Privately-Owned Business Barometer is one way that ANZ is helping to crystallise the key issues affecting the private business sector in New Zealand. Now in its third year, the Barometer has provided us with a deep understanding of attitudes that are driving the business owners in the private sector.

We've been able to use this knowledge to do some things that might help. We are already holding regular industry forums aimed at enabling peers to meet over lunch to contribute to dialogue on their industries and the issues and opportunities they are facing. We've held a series of small director forums targeted at those active in advising private business owners, with a view to gaining a greater understanding of the issues surrounding engagement and a clearer perspective on owners' views on such advisors.

Throughout 2009 we hope to be able to share some of these perspectives with business owners via a series of owner forums, letting them hear from their peers and benefit from the experiences of owners who have embraced different thinking and who have insightful stories to tell.

We've also mobilised a specialist team to support owners in identifying issues and opportunities, in building roadmaps around these areas and in finding and attracting the people and resources necessary to help overcome hurdles and achieve their objectives.

Regardless of your situation, we'd love to talk further. About your business, your industry, about what excites you and what keeps you awake at night.

For further information, please call your relationship manager or email pobb@anz.com

ABOUT ANZ

We are a financial provider that focuses on growth for our customers. We bring innovative financial solutions based on insight and the breadth of our connections and specialties.

Areas where we typically provide solutions and expertise include: trade, foreign exchange, cashflow-backed finance (access to finance without the need for security over property) and efficient financial structuring (discussing efficient and appropriate capital structures for businesses).

We will continue to support businesses with innovative thinking and solutions to help unlock wealth and growth potential.

For further information

For further information on the ANZ Privately-Owned Business Barometer, feel free to contact one of the people listed below:

General enquiries – please email pobb@anz.com

Planning for change enquiries

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