

PRIVATE BUSINESS RESEARCH AUGUST 2011

Australian businesses are positioning for growth

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“Businesses are positioning for growth, with many considering M&A and Joint ventures”

This report provides the consolidated views of almost 600 Private Businesses on their challenges, priorities and outlook. Also included is commentary from *BRW*, ANZ, Melbourne Business School, *IBISWorld* and Bond University.

The overriding theme to emerge from this year's Private Business study is the clear positioning of many businesses to set the path for growth.

Australian Private Businesses have shown resilience and adaptability to change over recent years, with strong balance sheets as a result of careful financial management throughout and post the GFC. Around three quarters of businesses said they now have a tighter focus on cost control than they did a few years ago, and they also have more robust risk management practices and business continuity planning processes than previously.

ANZ Economics' view is Australia is in a relatively solid position should another sharp disruption to global financial markets eventuate. Indeed, should the global economy

slowly recover as expected, then Australia remains well-placed to continue to capitalise on the further development of Asia. In the short-term, the size of Australia's mining investment pipeline is still likely to result in above trend growth for the years ahead.

While businesses are reporting cautious optimism about the economic outlook in the next 12 months, together with a range of challenges to be addressed that could potentially constrain performance, they continue to look for new ways to grow their businesses.

Growth is reported to be coming from improved sales of existing products, new products and merger, acquisition and joint-venture activity. There is a material increase in mergers and acquisitions, nearly doubling since last year. There is a corresponding increase in the engagement of M&A specialists in 2011.

It is essential that businesses have robust growth strategies in place, together with contingency plans for a range of eventualities.

KEY HIGHLIGHTS

BUSINESS IMPACTS

- > Many business procedures have tightened up in recent years. More than 75 percent of respondents report more robust business continuity, risk management and cost control compared to pre-GFC practices.

BUSINESS SENTIMENT

- > Business owners are cautious about the performance of the Australian economy and consumer sentiment in the coming year.
- > Businesses in Western Australia feel more positive about economic prospects than elsewhere.
- > Businesses in South Australia and Victoria believe the outlook for their employment markets is weaker.

STRESS FACTORS

- > Staffing issues are still the main cause of concern to private business owners.
- > Margins, costs and cash flow are key concerns for many businesses.
- > The potential introduction of a carbon tax is a concern for 30 percent.
- > Around 20 percent of organisations are more likely to be focused on budgeting and forecasting.
- > South Australian business owners are less concerned by the issues of succession planning or business continuity planning than those in other states.
- > Queensland and Western Australian businesses are most concerned about labour costs.

GROWTH AND BUSINESS INVESTMENT

- > Businesses around the country are investing more to position themselves for growth this year, with 75 percent of businesses anticipating business growth in the medium term.
- > There is an increased appetite for joint ventures, partnerships and merger and acquisitions.

- > 29 percent of businesses looking at increasing investment in Asia in the next three years.
- > Banks and financial institutions are the key source of funding for four out of five businesses.
- > Growth initiatives are more apparent in Western Australia than anywhere else.

BUSINESS ADVICE

- > There has been an increase in the number of M&A specialists used this year.
- > Lawyers and solicitors are the most popularly used advisers to larger businesses.
- > Increase in use of bankers in past 12 months.
- > Accountants are the most commonly used advisers to small to medium sized firms.

MANAGEMENT AND STRATEGIC PLANNING

- > Around 50 percent of companies have independent directors.
- > 50 percent businesses are operating without formalised succession plans.
- > Up to one fifth of businesses do not have documented short and medium term strategic plans.

SUCCESSION AND EXIT PLANNING

- > One in ten business owners indicated that they will exit their business during the next year.
- > More than half of the survey respondents acknowledge their exit plans are vague.
- > One quarter of respondents anticipate there may be issues to be resolved before they can execute a business exit.
- > Finding a suitable successor, either internally or through a professional search is the most common stumbling block to successful exit.
- > The most likely path to exit the businesses is to undertake a trade sale.

'GROWTH READY' STRATEGIES

With businesses forecasting growth, but facing constraints that could impact performance, decision makers should adopt “growth ready” strategies to maximise future opportunities, while managing the present.

Recommended 'growth ready' strategies include:

- > Doing the same but better in a mature market is often the best way to grow and progress. However diversifying comes with potentially greater benefits but often increased risks, from entering new markets, with new clients and new products or geographies. Even after extended evaluation of the ROI and negotiations, businesses must be prepared to say 'no' if required criteria for a new venture cannot be fulfilled.
- > Set and share a clear strategic vision, inclusive of contingency plans. A clear vision of how a business will deal with various situations can serve to make a business more responsive, and reduce shareholder conflict, when potentially difficult decisions are discussed and agreed in advance.
- > Careful financial management is essential. Businesses indicate they are doing this better than 2-3 years ago and this should continue. This should include closely monitoring any incremental changes in key success metrics, from margins to business processes to anticipate and address issues early.
- > Review competitive position and points of difference in light of weak consumer sentiment and longer sales cycles. Competitive pressures, especially for firms in the non-services sector are being exacerbated by the high value of the \$A. Strategies for expanding channels to market could be considered, especially with the growth in online communication.
- > Review risk management strategies to hedge against market uncertainty.
- > Consider external expertise and non executive directors for an independent view on plans for growth and succession, including M&A, transition and HR planning, and risk management.
- > For the 10 percent of owners that anticipate leaving the business in the next year (and 50 percent within five years) robust exit planning is needed. This will help to maximise the outcome and business value.

COMMENTARY FROM THE EDITOR, *BRW*



This is the fourth year that *BRW* has worked alongside ANZ to identify and celebrate the success of some of the best private businesses in Australia. As a magazine which seeks to provide insights to businesses, it is a privilege for us to talk with some of the best run businesses in Australia and share with our readers their journey and the secrets of their success.

The general economic environment has been a tough one to navigate in the past couple of years. The volatility introduced by the global financial crisis in 2008 has never really died away, and in fact roared back with a vengeance in August this year. The private sector has not been immune for this – like all companies they have struggled with tight credit markets, a strong labour market and weak consumer demand.

However, in many ways the private sector has coped better than the public sector – undoubtedly not being subject to the vagaries of the stock market allows them to

concentrate more on core business, rather than responding to shareholder fears.

So when we look at the performance of the Top 500 Private Companies in *BRW*'s flagship issue, we can see that from these leading private companies that the economic torpor has not slowed them down.

Both in terms of revenue and employment their figures have gone up this year and in fact the research on the Top 500 by *IBISWorld* shows that over the past decade these companies have outperformed the ASX 200 by 2.4 percent.

For these reasons the private sector is reasonably optimistic about the future. It's worth remembering that volatile times bring as much opportunity as they do danger – for the private sector the focus is on the former, rather than the latter.

Kate Mills
Editor, *BRW*
August, 2011

COMMENTARY FROM ANZ

We are once again pleased to join with *BRW* to bring you the highlights of the Private Business research study for 2011. The findings from this study help us to understand the collective view of private businesses and develop strategies to better support our clients.

The study certainly reflects the conversations we are having with our clients. Corporate Australia has shown its remarkable resilience and adaptability to change, with strong balance sheets as a result of careful financial management throughout and post the GFC. And while businesses are reporting cautious optimism about the economic outlook in the next 12 months, they continue to look for new ways to grow their businesses.

The majority of businesses in the study anticipate growth, and many are considering M&A and joint ventures, therefore businesses should be planning and prepared to take advantage of growth opportunities.

This year's study reported 'planning' is still an area for improvement, with around 20 percent of businesses without a strategic plan, 50 percent without a succession plan, while around half of businesses are without an independent

executive director (who could be used as a sounding board for plans). These figures continue to place businesses at risk of not being prepared to take advantage of future opportunities.

A clear vision of how a business will deal with various situations can serve to make a business more responsive, and reduce shareholder conflict, when potentially difficult decisions are discussed and agreed in advance.

Obtaining independent expert advice could be the difference between success and failure, when developing and executing plans. From assessing the opportunities (such as an M&A), and assessing the risks; through to strategies to address the 'war for talent'.

Bankers have been again identified as a key service provider. Staying close to your banker is vital to ensure you have the right strategies and financial solutions to support your business priorities.

We hope the findings from this study provide good insight into the challenges and views as presented by private business owners.

Michael Rose

Acting Head of Corporate Banking Australia

BUSINESS IMPACTS

- > Business indicators improved on 2010 findings.
- > Timely debtor payments was the most notable area of improvement since 2010.
- > More than 75 percent of respondents report more robust business continuity, risk management and cost control compared to pre-GFC practices.

In this year's research the key business indicators show marginal improvements on relatively positive sentiment in 2010:

- > 57 percent of businesses reported that sales had increased in the past year.
- > 46 percent said the number of business enquiries had increased.
- > 48 percent reported increased net profit after tax.

DEBTOR CYCLES

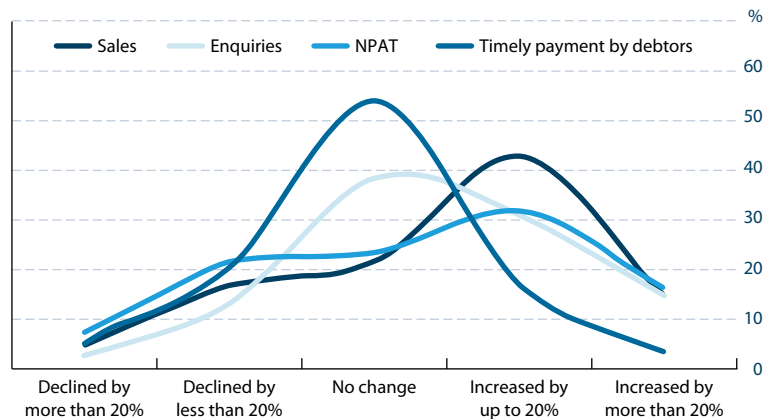
A good indicator that business conditions improved broadly is to look at one of the traditional problems faced by many businesses; the failure of customers to settle up their accounts. 20.2 percent of business owners said the timeliness of payments had improved this year, compared to just 12.9 percent in 2010, suggesting that cash started to flow more freely.

ACCESS TO FUNDING

One of the outcomes of the GFC was less ready access to funding in some quarters, and while this year's study shows that funding remains an issue for some businesses, it is less pronounced than in previous years, suggesting various markets are poised for growth activity.

When asked about the impact of current market conditions on the cost of funding, 56.3 percent of business owners said it was tighter or higher, and 42.2 percent said the

INCREASE/DECREASE IN KEY BUSINESS ACTIVITIES 2011 n = 577



20 percent of business owners said the timeliness of payments had improved this year, compared to 12.9 percent in 2010.

requirements for working capital funding had become tougher.

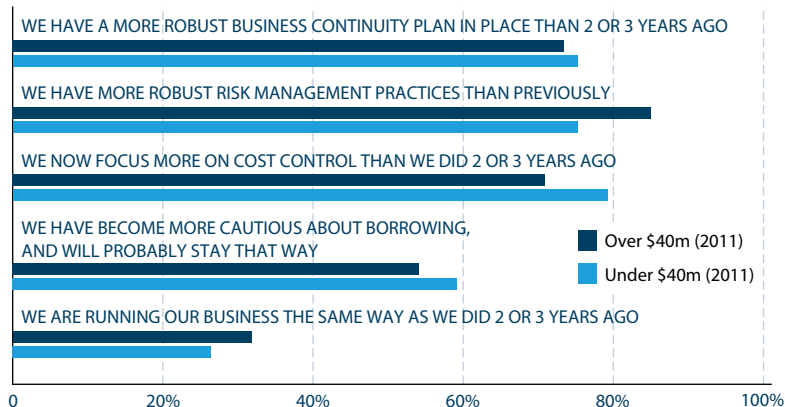
However the majority believed that nothing much had changed in many areas related to funding requirements. Over half of respondents felt there had been no change in requirements for collateral, debt margins, their ability to manage debt and importantly their ability to access funding.

MANAGEMENT PRACTICES

This year's study for the first time asked business owners about how the prevailing economic conditions were affecting the way they ran their businesses. It is clear that for some the lessons learned during the GFC have been put into practice in the subsequent years.

Over three quarters of businesses said they now have a tighter focus on cost control than they did a few years back, and they also had more robust risk management practices and business continuity planning processes than previously.

MANAGEMENT PRACTICES OVER TIME 2011 (BY TURNOVER P.A.) n = 577



BUSINESS SENTIMENT

- > Business owners are cautious about the performance of the Australian economy and consumer sentiment in the coming year.
- > The impact of the high Australian dollar is weighing on businesses.
- > Businesses in Western Australia feel more positive about economic prospects than elsewhere.
- > Businesses in South Australia and Victoria believe the outlook for their employment markets is weaker.

There is no hiding away from the fact that while businesses are feeling the positive aspects of an economy that has moved on from the GFC, there are fears about fresh clouds on the horizon.

Economic turmoil in the Euro Zone and fears of a new US recession have caused stock market jitters, and are doubtlessly factors in a general sense of trepidation, which emerged in 2011's study.

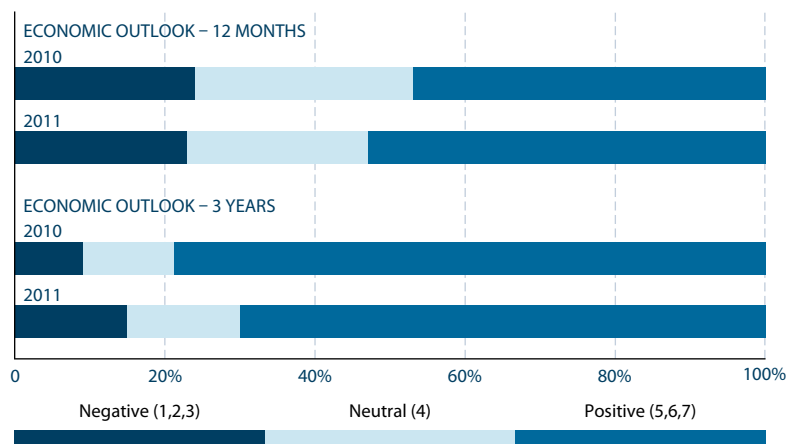
OUTLOOK FOR ECONOMY AND PROFITABILITY

At the time of this study, perceptions of the performance of the Australian economy in the next 12 months remain relatively positive, with little change in comparison to 2010 sentiment, but it is in the three-year outlook where more caution is apparent. While 78 percent of respondents in 2010 felt positive about the economic outlook three years ahead, this has dropped to 70 percent in 2011.

Similarly profitability expectations have declined in the medium term. Last year 71 percent of firms, regardless of size, were anticipating profitability in the next three years. While a majority of business owners still feel positive about this in 2011, the number has dropped to 64 percent.

Sentiment around other macro-economic indicators such as employment levels,

ECONOMIC SENTIMENT – THE PERFORMANCE OF THE AUSTRALIAN ECONOMY FOR THE NEXT 12 MONTHS AND 3 YEARS 2010-2011 n = 730



Expectations rated on a scale of 1=very negative, 4=neutral, 7=very positive

Sentiment around other macro-economic indicators such as employment levels, Australian terms of trade and business investment levels remains positive this year.

Australian terms of trade and business investment levels remains in positive territory this year.

There were concerns about the impact of the strengthening Australian dollar raised in the 2010 study, but these have raised noticeably alongside the currency's value. With the Aussie dollar regularly reaching \$US1.10 during the year, the last thing businesses need is declining local spending to compound reduced margins on overseas sales.

STATE VIEW

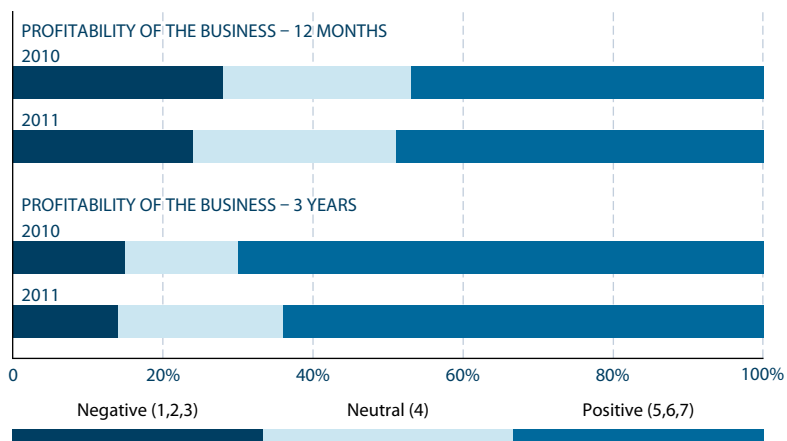
An increased scope of the study this year means data can be analysed more clearly on a state-by-state basis, providing insight into the outlook around the country.

Business owners in the West are markedly more optimistic about every measure covered in the questioning and Western Australia is the only state not to venture into negative territory with regard to consumer sentiment.

Amongst other states there is a more homogenous feel to the findings. Businesses in South Australia and Victoria believe the outlook for the employment market is a little weaker in their state and SA respondents were noticeably the most concerned about the impact of the high \$A on their prospects.

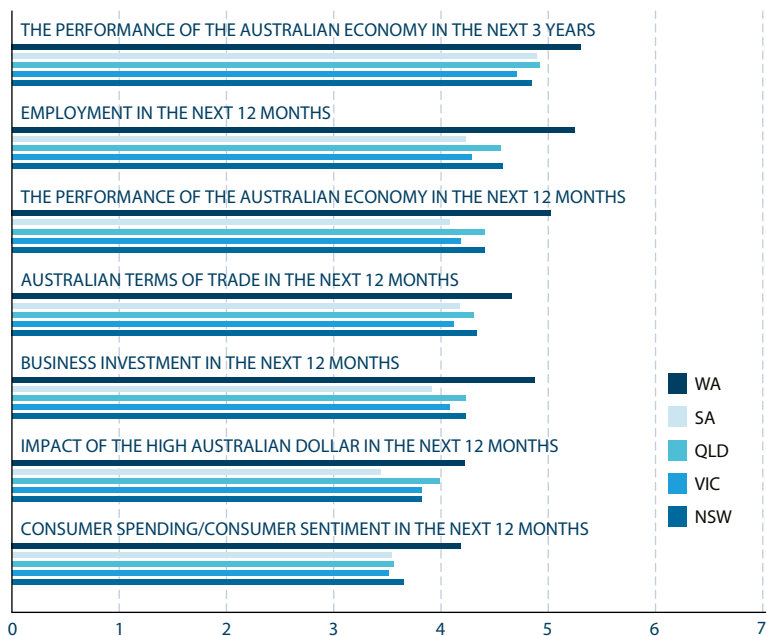
Refer to latest economic commentary

ANTICIPATED PROFITABILITY FOR OWN BUSINESS FOR THE NEXT 12 MONTHS AND 3 YEARS 2010-2011 n = 730



Expectations rated on a scale of 1=very negative, 4=neutral, 7=very positive

OUTLOOK FOR THE AUSTRALIAN ECONOMY 2011 (BY STATE) n = 577



Expectations rated on a scale of 1=very negative, 4=neutral, 7=very positive

STRESS FACTORS – ISSUES SENDING BUSINESS OWNERS GREY

- > Staffing issues are still the main cause of concern to private business owners.
- > Margins, costs and cash flow are key concerns for many businesses.
- > The potential introduction of a carbon tax is a concern for 30 percent.
- > Larger organisations are more likely to be focused on budgeting and forecasting.
- > South Australian business owners are less concerned by the issues of succession planning or business continuity planning than those in other states.
- > Queensland and Western Australian businesses are most concerned about labour costs.

ATTRACTING AND RETAINING STAFF

While there is a notable reduction in the number of business owners that nominated staff attraction and retention as a headache this year, it still tops the list as the most pressing concern. This is the case for both the attraction of management staff and workers in general.

MARGINS AND CASHFLOW

Unsurprisingly perennial issues also rank highly in the list of troubles with margins and cashflow rating frequent mentions from survey respondents. Interestingly though concerns about margin pressure seem to have fallen significantly in 2011 compared to 2010's study. In businesses of all sizes last year over 50 percent of respondents concerned about their margins, and this has dropped to just over 30 percent this year.

LABOUR COSTS

When asked about labour costs this year, 30.4 percent of businesses with turnover over \$40 million said it was a point of consternation.

CARBON TAX

The survey was conducted prior to the government unveiling the details of its proposed Carbon Tax, but business owners

were asked whether its potential introduction was a significant concern.

Unsurprisingly it was of more concern to smaller organisations, but the Carbon Tax was far from being a source of widespread panic, despite some commentary to the contrary.

BUSINESS CONTINUITY PLANNING, BUDGETING AND FORECASTING

Internal strategy related issues such as business continuity planning, budgeting and forecasting come lower down the overall list of worries, but are still rated as a major concern by around 20 percent of respondents.

While 15 percent of businesses turning over more than \$40 million a year view budgeting and forecasting as a significant concern, 20 percent of their peers at the smaller end of town feel the same.

Conflict with other shareholders does not come up across the board, but continues to be a cause of concern for around 10 percent of respondents. The number of larger organisations troubled by rifts between owners and shareholders has fallen by more than 50 percent. In 2010 it was flagged by 22 percent, and this has now dropped to 10.6 percent.

STATE VIEW

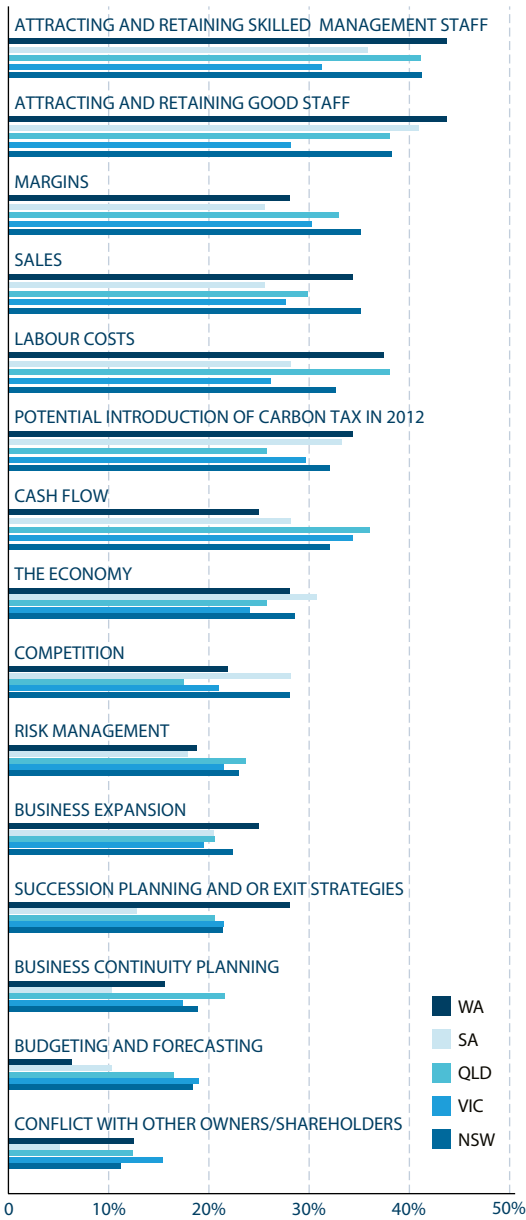
At a state level, in keeping with a less optimistic outlook for employment, Victorian business decision makers are less concerned about attracting and retaining staff than their peers elsewhere in Australia— although it does remain high on their list of concerns.

The positive sentiment about growth opportunities, and a well publicised skills shortage in some areas in the Western Australian economy means the issue of staffing is the biggest worry.

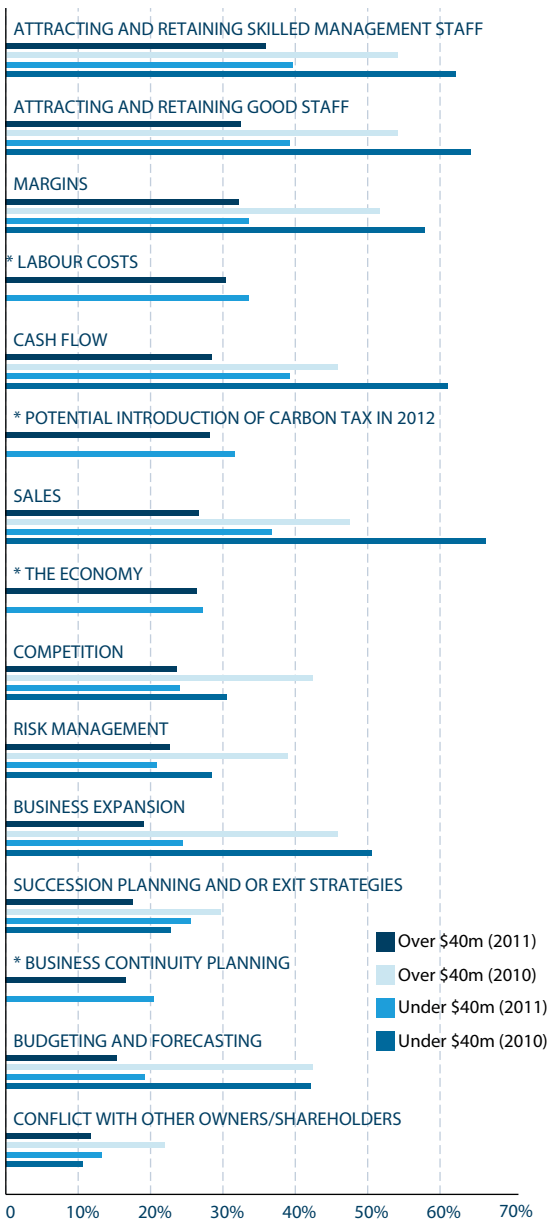
Interestingly cashflow concerns are more prevalent in Queensland and Victoria, and South Australian business owners are significantly less concerned by the issues of succession planning or business continuity planning.

Concerns about the level of competition stands out more in New South Wales and South Australia, while the problem of attracting and retaining the best staff of noticeably less concern to Victorian-based firms.

ISSUES OF SIGNIFICANT CONCERN 2010-2011
(BY STATE) N = 559



ISSUES OF SIGNIFICANT CONCERN 2010-2011
(BY TURNOVER P.A.) N = 730



*Introduced to the survey in 2011

GROWTH & BUSINESS INVESTMENT

- > Businesses around the country are investing more to position themselves for growth this year.
- > There is an increased appetite for joint ventures, partnerships and merger and acquisition.
- > 29 percent of businesses looking at increasing investment in Asia in the next three years.
- > Banks and financial institutions are the key source of funding for four out of five businesses.
- > Growth initiatives are more apparent in WA than anywhere else.

POSITIONING FOR GROWTH

Perhaps the strongest theme to emerge from this year's study was the clear positioning of many businesses to set the path for a growth trajectory.

Across business sizes and across the country, the majority of businesses in the survey reported that they are anticipating growth in both the short and medium term.

In both the year ahead and across the next three years the principal source of anticipated growth is organic, with three quarters identifying increased sales of currently traded goods and services as the growth engine of their business.

However in a sign that innovation and re-invention are refreshingly prevalent, around half of the businesses responding in 2011's study nominated new products or services as a further source of anticipated growth. In the three year timeframe an increased number of businesses of all sizes expected to grow through the introduction of new products.

Businesses with turnover below \$40 million appear more likely to innovate with new products to achieve growth over the next three years, with 61.6 percent saying it was their expectation by 2014. This was in comparison to 57.8 percent in 2010, and there was also a marginal increase in the

expectations for new products across three years among the larger firms surveyed this year as well.

PARTNERSHIPS, JOINT VENTURES, MERGERS AND ACQUISITIONS

Notably in 2011, there is an increased appetite for growth via partnerships and joint venture opportunities – and there is also increasing interest in mergers and acquisition. This is particularly clear in businesses with turnover exceeding \$40 million, which have nearly doubled their reported interest in this form of growth, from 16 percent in 2010 to 28 percent in 2011.

Business owners showed that their appetite for M&A is more pronounced over a three year time frame, rather than in the immediate future. While 25.2 percent of firms with turnover below \$40 million say they are anticipating growth through M&A in the next 12 months, this raises to 33.6 percent over in three years.

Similarly 28.1 percent of larger firms are eyeing M&A growth in the year ahead, while 37.3 percent expect it to happen over the next three years.

When it comes to the minority of businesses that are fearing a contraction of their business in the next 12 months, the situation has worsened most notably in the larger

companies with turnover above \$40 million. In this group the number of businesses expecting to shrink in the year ahead has increased from just 5.6 percent last year to 10.1 percent in 2011.

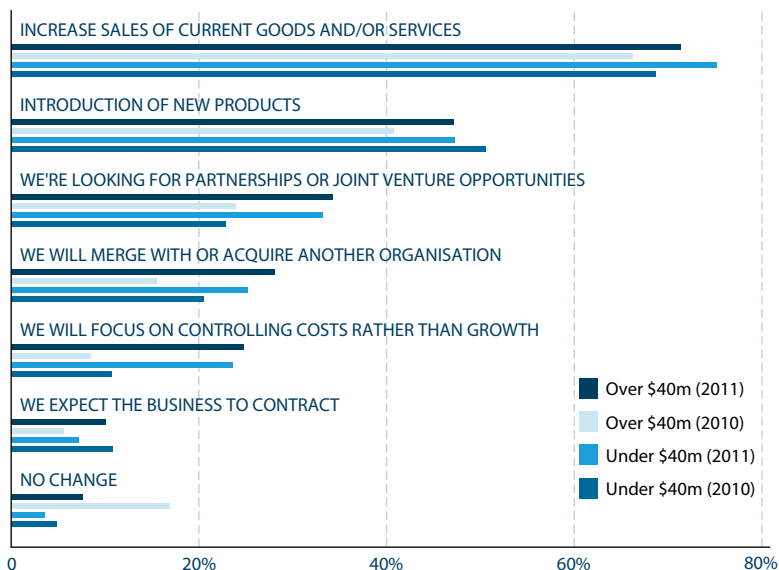
Conversely the number of smaller organisations expecting to shrink in the next year has reduced from 10.8 percent in 2010 to 7.2 percent in 2011.

SOURCE OF FUNDING

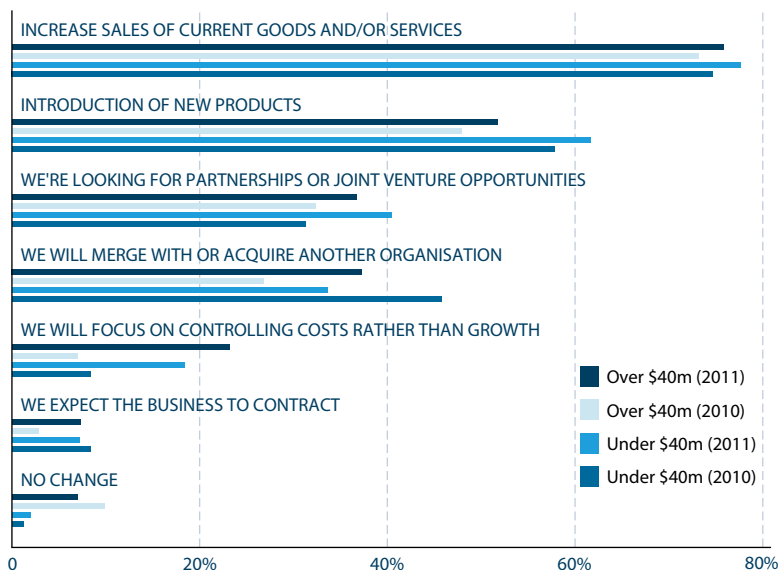
With an appetite for growth prevalent, the issue of funding in order to support it, is as important as ever. By far and away the most likely source of funding for the majority of private business owners surveyed is borrowing from banks and other financial institutions.

Banks and other financial institutions remain the key source of funding for four out of five businesses. Current shareholders could provide financial support for growth in around 30 percent of cases while private equity, capital markets and venture capital are selected as potential funding providers by fewer respondents.

BUSINESS GROWTH IN THE NEXT 12 MONTHS 2010-2011 (BY TURNOVER P.A.) n = 730



BUSINESS GROWTH IN THE NEXT THREE YEARS 2010-2011 (BY TURNOVER P.A.) n = 730



INVESTMENT PLANS

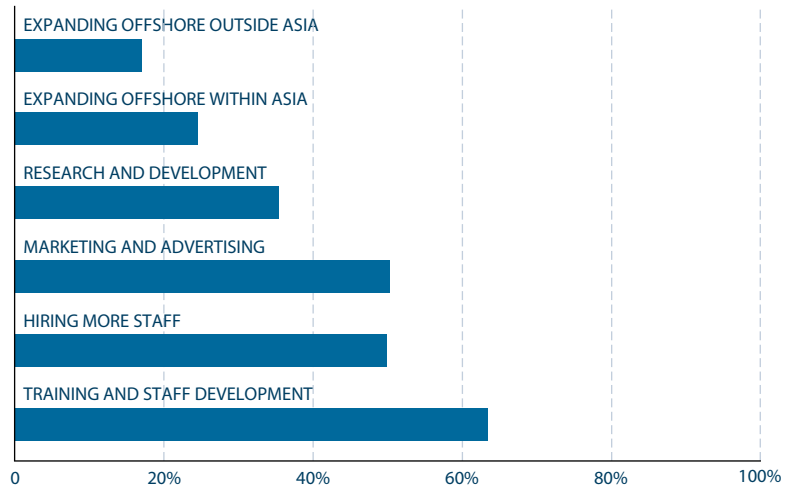
Business decision makers also reported an uptick in investment plans for their business in the short and medium term, to support growth strategies. A greater investment in current staff (63 percent) is closely followed by 50 percent of respondents indicating an increased investment in hiring new staff.

Spending on marketing and advertising is forecast to increase and one third of businesses plan to up their investment in research and development.

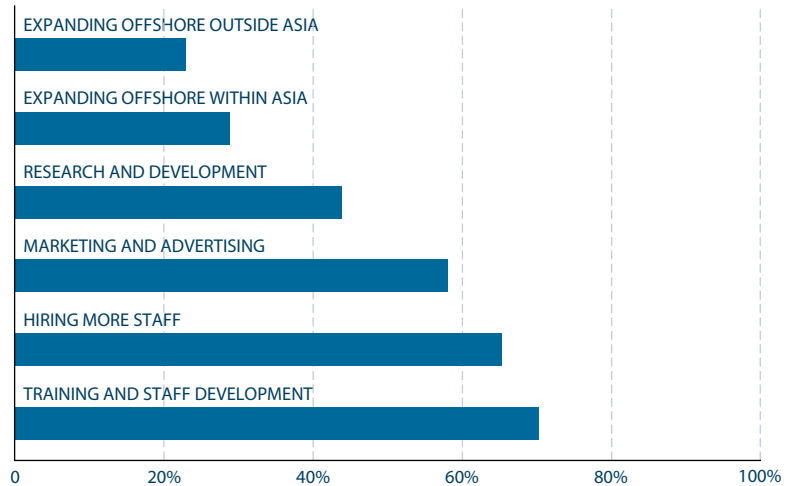
Expansion plans are not just confined to the local operations of privately-owned businesses, with around one quarter of all participants in this 2011 study indicating their business would be increasing their investment in growth into Asia. Nearly one-fifth (17 percent) are looking at expanding further afield, beyond Asia.

The level of overseas expansion plans increase in the medium term with nearly 29 percent of businesses looking at increased activity offshore in Asia in the next three years.

PLANS FOR INCREASED INVESTMENT IN THE NEXT 12 MONTHS (2011) n = 577



PLANS FOR INCREASED INVESTMENT IN THE NEXT 3 YEARS (2011) n = 577



STATE VIEW

At a state level, businesses in South Australia report somewhat lower expectations of growth, regardless of whether that is through organic sources, new products or joint ventures and M&A activities.

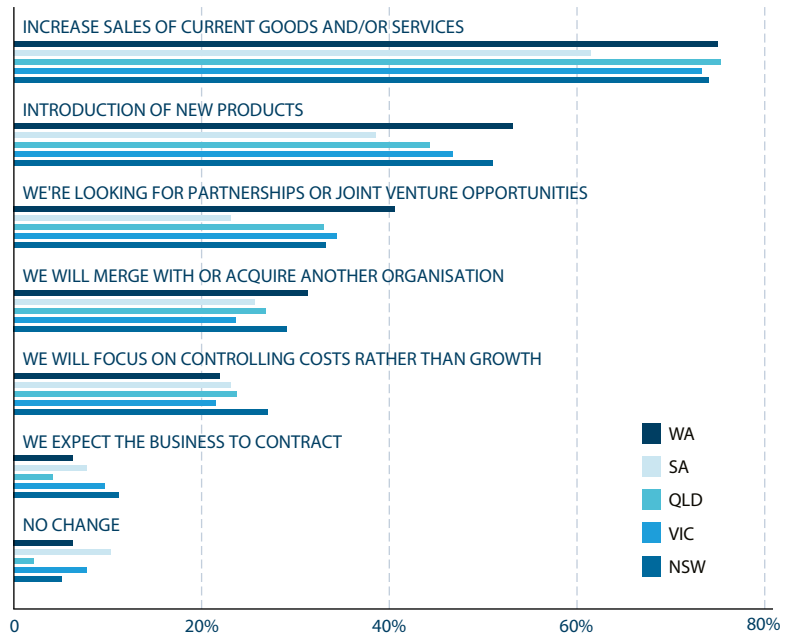
New South Wales, Victoria and Queensland are planning for organic growth at the same rate as in Western Australia, but Western Australian businesses show a greater level of expectation for growth through the development of new products, and other non-organic forms of growth.

Businesses in South Australia appear to be more steady-as-she-goes than organisations in other parts of the country. They are less likely to be optimistic about their growth prospects, but conversely are less likely to expect contraction in their business than their peers in Victoria and New South Wales.

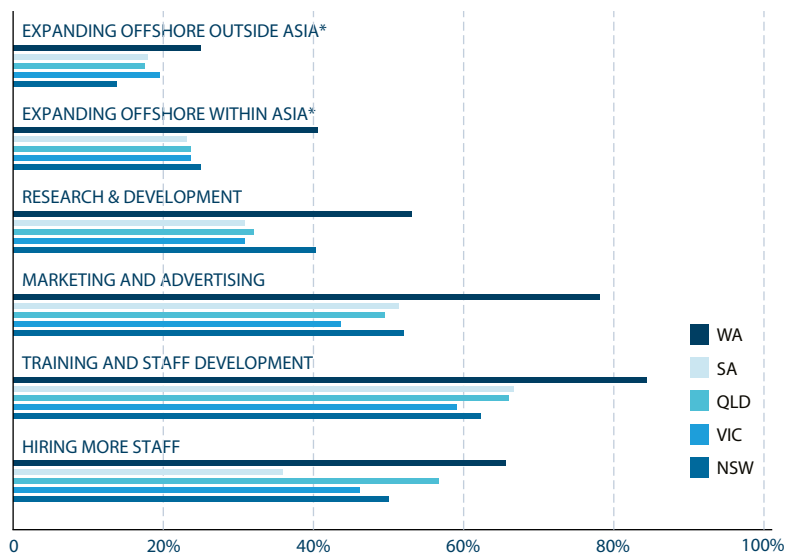
Western Australian-based firms are investing the most in hiring new staff and marketing and advertising their wares. Along with WA, NSW businesses are investing more in R&D.

NSW-based businesses appear the least likely to expand outside of Asia, whereas they are more likely than any of the states, other than WA, to expand within the Asian region.

BUSINESS GROWTH IN THE NEXT 12 MONTHS 2010-2011 (BY STATE) n = 559



PLANS FOR INCREASED INVESTMENT IN THE NEXT 12 MONTHS (BY STATE) n = 577



PREPARING FOR GROWTH

When the business gurus and academics think about growth, and how to prepare for it, they ask one key question. Are you planning to grow by scaling in your existing business, or are you going to change business to grow?

Scaling – growing in your current business is about competition. This type of growth is low risk, since you already understand the industry, its customers and idiosyncracies. Growth of this sort normally requires a keen eye for small incremental improvements, in well understood markets doing the same but better is often the best way to progress. You also need a war chest, since out-competing the competition normally means out-investing them too. Scaling works well where the industry has plenty of potential, and where the company already has a strong advantage in the eyes of its consumers.

Moving into a new business to grow is risky. You may be changing market, and serving a customer you have not dealt with previously. You may be changing what you offer, and taking to market a product or service you have not dealt with before. Business writers love this kind of growth. Firms that bet the farm on big dramatic changes that will revolutionise their industry can guarantee the attention of the business press. Businesses that refuse to take such chances as their industry changes around them are loved by business writers too – unfortunately normally

the obituary writers. Kodak for instance, has been singled out by the experts for failing to jump to digital technologies as the traditional film business failed.

The good thing about jumping to new markets is that the risks are obvious. Managers and boards can see the risks and therefore invest in understanding them, preparing carefully and set reasonable expectations. There is plenty of advice available about how to manage the risks, such as operating the new business separately to avoid importing existing cultures and assumptions, bringing in staff from outside the existing business and working hard to make sure that information is flowing into the business from outside.

Where firms are most likely to fail is when they mistake one sort of growth for the other. In particular, if they think they are scaling when in fact their entering a new market. Changes that look small carry the biggest risks. Moving from supplying an industrial customer to a domestic customer, for instance, looks like a small change, but can require huge changes in design of the offer, distribution, promotion, packaging, pricing and so on. The first step in being prepared for growth is knowing what sort of growth you are planning for or experiencing.

Professor Richard Speed
Melbourne Business School

Recently we have experienced a sudden correction in financial markets. These sharp moves have been driven by heightened concerns over global growth and sovereign debt, across Europe but also the US. While there is a risk of another financial crisis, we do not forecast a repeat of the 2008 global financial crisis or global recession. Importantly for Australia, we believe there are significant differences between now and the global financial crisis. These differences, together with a continued strong growth outlook for China, mean that prospects for Australia remain favourable, albeit mixed across sectors and geographies.

The recent sharp falls in equity markets across Europe, the US and to a lesser extent Australia have been sudden. *These sorts of corrections are not uncommon and in fact we had a similar correction in the Australian equity market last year. In April and March 2010 the S&P200 index had a correction of over 14.5 percent.*

So what brought about this recent market correction? European and US economic growth concerns coupled with high levels of debt in these economies.

Advanced economy sovereign debt issues came to the fore in mid-2011. US government debt is currently 70 percent of GDP. For the entire Eurozone, the average government debt to GDP ratio is 85 percent, but many countries sit well above this average (ie. Greece is 144 percent, Ireland is 94 percent, Portugal is 83 percent and Italy is 118 percent). In comparison, Australian government debt is under 10 percent of GDP. US political tensions around reducing government debt and the subsequent downgrade of US debt by Standard and Poors (S&P) highlighted this constraint on governments. The key risk for global policy-makers is that these sovereign debt concerns will spillover into the private sector (eg. an unsustainable hit to private bank's balance sheets from a default or 'haircut' on sovereign debt). Avoiding such contagion has so far prevented current market turmoil from developing into a full-blown financial crisis as we saw with the collapse of Lehman's in

September 2008. This must remain a priority for policy-makers.

Despite recent sharp moves in financial markets, and a weak medium-term growth outlook for the G3, we do not expect the global economy to fall back into recession. A rebound in global manufacturing activity (following disruptions from the Japanese earthquake), lower petrol prices and high corporate profitability (with corporate profits at a record share of GDP in the US) should all provide important support to growth in the second half of this year. Also helpful are recent policy measures, including a commitment from the US Federal Reserve to keep official US rates near zero until mid-2013.

But, it will take many years, and in some cases decades, of fiscal consolidation (ie. government spending cuts and tax increases) to reduce European and US government debt levels. This fiscal repair will be a significant drag on overall economic growth in these regions. Moreover, the household sector in these economies remains highly indebted. Further household balance sheet repair will continue to constrain household spending in these economies. With consumption accounting for over two thirds of GDP in these economies, this will also be a significant drag on overall economic growth. We therefore expect slow growth in the US and Europe for years to come.

Lower consumption growth has also been present in Australia and a source of mixed domestic economic conditions. Businesses reliant on consumer discretionary spending (eg. retailing) have generally experienced slow growth.

But there are some key differences between these other advanced economies and Australia. The most significant of which are the prices for Australia's exports. The prices of resource exports are at highly elevated levels, largely due to strong Chinese demand. Despite recent G3 wobbles, we expect that a supportive government and ongoing urbanisation will keep Chinese demand for these resources robust for years to come. ANZ is forecasting

Chinese economic growth of 9.5 percent in 2012.

How do higher commodity prices help the broader Australian economy? If our 'worst-case' scenario was to come to bear and we saw another global financial shock, what is different in Australia from 2008?

Like in 2008, higher commodity prices have led to a strong mining investment pipeline (see chart below). In 2011, this pipeline is more advanced than when the global economy weakened in 2008, with many of these projects having already commenced. This is likely to see a considerable amount of job creation not only in the mining and engineering industries. The income from these industries is typically spent through the broader economy or returned through profits to shareholders (via superannuation and investments).

The Australian consumer is in a far better position than other advanced economies. In the last few years Australian households have become notably more 'cautious', increasing savings. This has seen the household savings ratio rise to a multi-decade high of 11.5 percent. Whilst this cautious consumer behaviour has hurt some businesses in retailing, it does mean that the Australian household, and thus broader economy, has a strong 'buffer' to withstand any significant disruption in asset prices (ie. such as the recent correction in equity prices) as well as any unexpected rise in the unemployment rate.

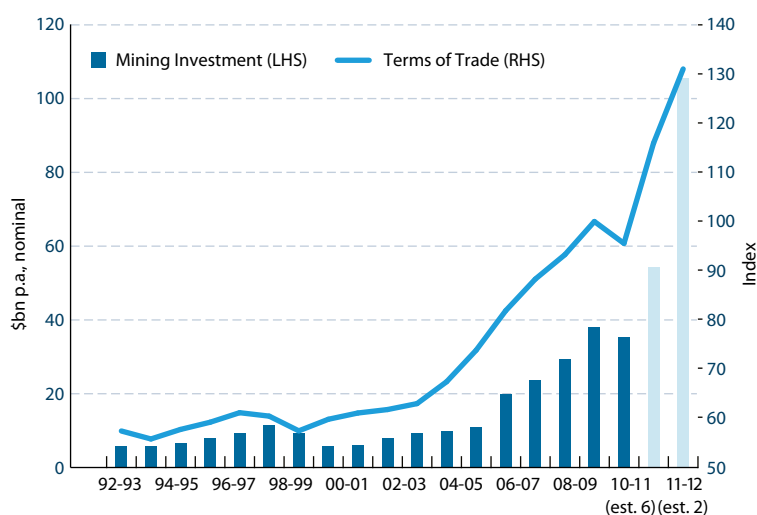
Another important difference between now and 2008 is that Australia has a reduced reliance on external funding. In 2008, with strong credit growth and negative savings in the prior years, Australian banks were highly reliant on the funding markets of Europe and the US to support this high local borrowing. However, since the global financial crisis in 2008, private savings have risen and credit growth has slowed. Reduced borrowing has left Australia's banking system far less reliant or vulnerable to movements in wholesale funding markets, and thus an overseas financial crisis. Likewise, Australian businesses have also paid down debts and many are holding large amounts of cash. This is especially true for the large mining companies which have the strong investment pipelines.

Overall, we view Australia as being in a relatively solid position should another sharp disruption to global financial markets eventuate. Indeed, should the global economy slowly recover as we expect, then Australia remains well-placed to

ASX 200



AUSTRALIAN MINING INVESTMENT V'S THE TERMS OF TRADE



NB. Terms of trade ratio of export prices to import prices.

continue to capitalise on the further development of Asia. In the short-term, the size of Australia's mining investment pipeline is still likely to result in above trend growth for the years ahead. However, with consumer savings likely to remain high, and the A\$ elevated, industries exposed to these variables will continue to face challenges. Monetary policy will continue to navigate this two-speed economy against a background of already high local inflation. We expect the RBA to keep interest rates around current levels for an extended period of time.

Katie Dean

Head of Australian Macroeconomics

18 August 2011

BUSINESS ADVICE

- > The number of M&A specialists used this year has increased by over 50 percent.
- > Lawyers and solicitors are the most popularly used advisers to larger businesses.
- > Increase in use of bankers in past 12 months.
- > Accountants are the most commonly used advisers to small to medium sized firms.

No business owner can go it alone without expert advice in certain areas, and the sources of business advice most likely to have been used in the past year, according to the study are lawyers and solicitors, accountants and bankers.

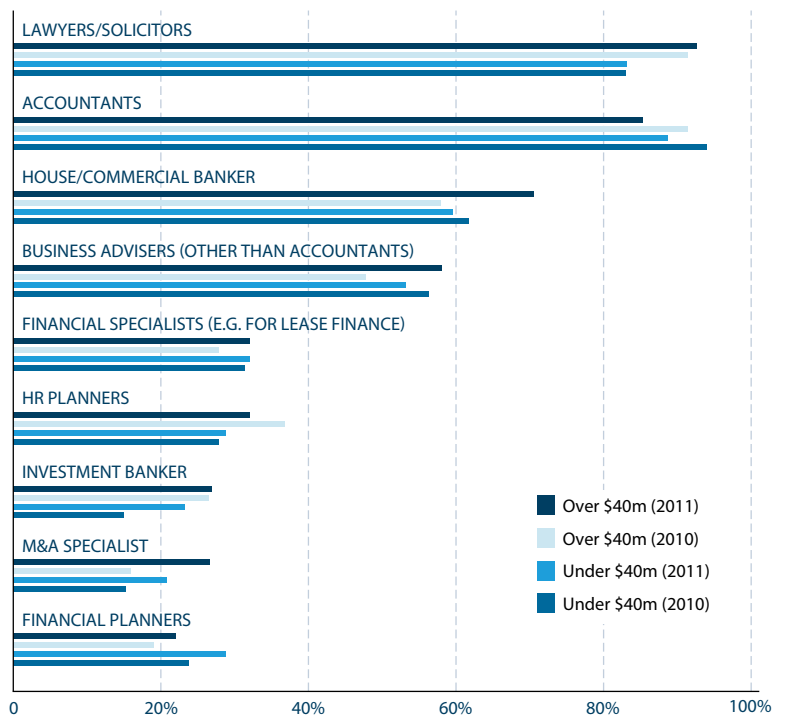
Growth aspirations are again clear in this section of the study, and are reflected by an increased desire to undertake joint ventures and M&A. The likelihood of businesses having consulted a specialist in this area has increased markedly during 2011.

In larger firms, 26 percent have consulted with M&A specialists, up from 15.9 percent in the previous year. Meanwhile in smaller firms M&A experts were brought in by 20.8 percent, in comparison to 15.2 percent in 2010.

Because smaller organisations are less likely to have the staff to do everything in-house the most commonly-used specialist in businesses with turnover under \$40 million is accountants. This year 94 percent of the smaller to medium-sized companies paid for accountancy services, this was up slightly from 91.5 percent in 2010.

Meanwhile at the bigger end of town, lawyers and solicitors are the most commonly sought after advisers, with 92.7 percent of larger companies seeking their counsel, in comparison to 83.2 percent of smaller companies.

**KEY SOURCES OF BUSINESS ADVICE 2010-2011
(BY TURNOVER P.A.) n=730**



Highlighting a continuing concern in smaller businesses about the difficulty to find and keep staff, HR planners continue to grow in importance in 2011. Financial planners are also being sought by smaller businesses this year, with 28.8 percent, up from 23.8 percent last year.

MANAGEMENT AND STRATEGIC PLANNING

- > 50 percent of companies do not have independent directors.
- > 50 percent businesses are operating without formalised succession plans.
- > Up to one fifth of businesses do not have documented short and medium term strategic plan.

In last year's study there were some concerns raised about the lack of formalised strategic planning and oversight in some privately-held businesses – particularly those under \$40 million in annual turnover.

Some of these issues remain in 2011.

BOARD OF DIRECTORS

While the majority of businesses in this study have a board of directors, the rigour of their scrutiny of the business is called into question inside the 15-20 percent of companies in which the board meets less than four times a year.

Less than half of the small to medium sized companies surveyed (42.8 percent) have any independent directors and only just over half (54 percent) of businesses with a turnover exceeding \$40 million have independent oversight.

While this remains a smaller percentage than might be expected, it should be noted that this is a notable increase on 2010. Across business sizes 49.4 percent of firms now have independent boards, in comparison to 34.9 percent in 2010's findings.

RISK MANAGEMENT

The majority of respondents in the study indicate that they have more robust risk management plans than previously, and that their business continuity planning has improved in the past two or three years.

STRATEGIC PLANNING

The use of short and medium term strategic planning has not changed in the past year at least, with up to 20 percent of businesses admitting to having no such plans formally documented.

Despite many businesses believing they have a strong handle on business continuity planning, it may not be as robust as many believe, because too many companies are operating without formal succession plans in place for key roles in the company.

While succession and strategic planning may not be the most dynamic or exciting parts of the business they undeniably provide structure and plans of action that can be implemented quickly and in a less haphazard fashion. Also in times of stress and disagreement amongst shareholders, formalised documents of a business' intentions can help executives steer a path through choppy waters. Such plans should also be reviewed regularly.

SUCCESSION AND EXIT PLANNING

- > One in ten business owners indicated that they will exit their business during the next year.
- > More than half of the survey respondents acknowledge their exit plans are vague.
- > One quarter of respondents anticipate there may be issues to be resolved before they can execute a business exit.
- > Finding a suitable successor, either internally or through a professional search is the most common stumbling block to successful exit.
- > The most likely path to exit the businesses is to undertake a trade sale.

Consistent with previous years' findings, up to one in ten business owners indicated that they will exit their business during the next year. Looking further ahead, a far more significant number – a little over half – of respondents reported that they plan to exit their business in the next five years.

This includes about half, who said they will retire, rather than move onto other business ventures.

More than half of the survey respondents (56.1 percent) admitted that their exit plans are currently vague, with none of the crucial details properly considered.

Unfortunately for many business owners, they find out that a lack of planning can leave them insufficiently prepared for the large transfer of assets and ownerships in a sometimes compressed timeframe.

Finding a suitable successor, either internally or through a professional search is the most common stumbling block perceived for exit strategies in both smaller and larger firms.

Another potential hold up considered by business owners keen to sell out is the challenge of agreeing a value for the business. A significant 38.7 percent of larger business owners fear being unable to agree on a price, a doubt shared by 31.4 percent of their peers in firms with turnover below \$40 million per annum.

With many businesses reporting a lack of formal succession plans for key roles and not necessarily having strategic plans in place some more preparation might be needed before business owners can cash out and walk away.

With business owners less inclined to take their companies public, the most likely path to exit the businesses is to undertake a trade sale. Just over a quarter of respondents in the 2011 survey said a sale to external investors was their most likely exit strategy.

This was closely followed by a management buy out, which is favoured by 22.9 percent of business owners surveyed. Also mooted as potential exit schemes by numerous respondents were family successions, and then IPOs.

PLANNING FOR EXIT

With numerous respondents indicating different potential barriers to exiting their businesses, and particular concerns mentioned regarding conflict with shareholders and expected difficulty in anointing a successor, it appears prudent for many business owners to begin planning their exits with at least a five year timescale. For those hoping to exit sooner than that, who do not have any plans in place, now is the time to make sure the necessary thought is applied and documented. Being prepared is half the battle in securing a satisfactory end to the business journey.

FAMILIES IN BUSINESS THROUGH THE AGES

Research conducted at the Australian Centre for Family Business (ACFB) at Bond University since 1994 has uncovered that the main contributor to family business sustainability can be traced to the introduction of appropriate architecture and governance mechanisms that identify and address the fundamental need to plan well in advance. As within publicly-held companies, family business boards of directors see leadership succession as one of their primary functions. But these family business directors also understand the pivotal role of the incumbent leader and appreciate that to transition a leader in a family business is a drawn out process typically taking up to seven years.

Another research finding helping families in business address systems synergy challenges relates to understanding the responsibility of ownership. Educating next generation family members of this notion is key to family harmony and successful ownership transition. Understanding their role as stewards helps the younger generation appreciate the family's values and the complex responsibilities of ownership. As such, more so than in non-family businesses, there is a need to simultaneously manage complex family and business paradoxes. For example, they need to concurrently understand the importance of values and to continue the business differently while being as, if not more, entrepreneurial than their predecessors.

ACFB scholars have been able to efficiently collate their research findings into the ways that differences manifest in the family business context using their AGES framework (an acronym for Architecture, Governance, Entrepreneurship, and Stewardship):

- > **Architecture:** Proper architecture ensures that appropriate systems and structures are in place to implement the formulated strategy, as well as, when the time comes, to ensure the leadership succession process is transparent.
- > **Governance:** Introducing family and business governance ensures that the growing

ownership group's expectations and input are captured, and, most importantly, that family governance initiatives such as a family constitution and family council are introduced to ensure family members, including those not working in the business, have a voice.

- > **Entrepreneurship:** As the future of the business is dependent upon entrepreneurial leadership and strategic thinking, there needs to be a continuation of the founder's or subsequent leadership's entrepreneurial zeal and any future leader must have demonstrated entrepreneurial expertise, as well as have had profit centre responsibility, on their route to their CEO position.
- > **Stewardship:** A stewardship orientation is what fundamentally defines a family business that has a stated intention to stay family owned and from an individual perspective the leader must embrace this, but just as vital, is that they must have the leadership competence to engender this in both the family and among the various stakeholders of the business.

As the majority of businesses in the world are family owned, family businesses are the economic and social life blood of all communities. They are renowned for their resilience, their ability to absorb hardship and survive economic downturns, and their unorthodox strategies and approaches to, among other things, growth and debt. Though myths have abounded about their apparent limitations, irrefutable evidence now points to the superiority of family businesses across an array of key performance metrics. Education programs built around the four AGES platforms for incumbent and future leaders as well as the many professional adviser groups and financiers who work alongside them are assisting families in business negotiate through the paradoxes they face...and ultimately contribute to their long term sustainability.

Professor Ken Moores AM and Dr Justin Craig
Co-Directors: Australian Centre for Family Business at Bond University
www.bond.edu.au/acfb

The global economy of 230 nations has recovered strongly in 2010 and 2011 (so far), due mainly to massive quantitative easing: read “pump-priming” or “running the printing presses” in old jargon. Yet, of the 4 percent growth in both years, over half (2.6 percent) of this global growth is coming from Asia; and the lion’s share of this, in turn, from China and India.

Being part of the Asian mega-region, having four-fifths of our exports within that region, with a low public debt (under a quarter of our GDP), and with a minerals pricing boom Australia’s private businesses are doing better than the ongoing GFC suggested we might. Then again, cyclones, floods, an over-valued A\$, a mishmash federal government, anti-business IR laws and planned new tax regimes (mining super-profits and carbon) have negated most of the positives. As a result, our real economic growth in F2011 was a little above 2 percent compared with our long term average of closer to 3.5 percent. Most expect a return to this level in F2012.

However, the annual *BRW* Top 500 Privates and the *BRW* ANZ private business research of an even larger number have revealed healthier achievements and prospects for our private businesses. Our largest 500 Privates have seen growth of 11.5 percent in revenue and 3.2 percent in employment this year compared with 8.6 percent for all businesses and 2.4 percent for the nation’s workforce. The year ahead looks prospective according to the *BRW* ANZ private business research with 75 percent seeing growth in existing products and a 47 percent with new products.

Economic growth in Western Australia is likely to be the most positive, as it was in F2011. Across the entire economy with total revenue of \$3.8 trillion, real growth was 6.7 percent for WA compared with: ACT (4.5 percent); Queensland (3.3 percent); Victoria and SA (3.0 percent); the NT (2.9 percent); and NSW and Tasmania (2.7 percent). Ironically the make-up of the nation’s 500 largest private enterprises in the latest *BRW* ANZ private business research – given the big number of exits and new entrants – favoured SA

(23 percent), Tasmania (19 percent) and Victoria (16 percent in revenue growth terms, with WA and the ACT near the bottom of the ladder.

Growth is vital to any business and the list below reminds us how to achieve it.

The *BRW* ANZ private business research, interestingly points to nearly a quarter of surveyed companies planning offshore expansion over the next three years: 29 percent inside Asia, and 23 percent outside Asia in the world’s other six regions. In the 2012 calendar year, the Economist’s forecast for the world’s real growth is 3.9 percent (with some downside possibility) and for Asia a whopping 6.8 percent. The fastest growing big nations include: China (8.7 percent); India (8.6 percent); Indonesia (6.2 percent); Taiwan (4.5 percent) and South Korea (4.0 percent) in this mega-region.

Growth from any initiative is welcome, and it seems that the nation’s privates use all the available channels; and in so doing, outpace the economy in most years.

Phil Ruthven
Chairman, *IBISWorld*

GROWTH STRATEGIES

- 1. Active Assets.** Use scarce finance – equity & debt – in active assets (IP, skilled staff, growth cash) not passive assets (land, buildings, equipment and stock) which can be leased or factored.
- 2. Uniqueness.** In slow markets, get organic growth through market share with lower costs or a unique selling proposition (USP). Constantly innovate and develop new products, or new systems that make you more competitive in growth or slow markets.
- 3. Rationalisation.** Acquisition of competitors (M&A).
- 4. Positioning.** Seek out and dominate market segments that make you master of your own destiny as an ultra niche specialists (1 percent share), niche operator (5 percent) or an industry major (25 percent-75 percent share).
- 5. Geographic Expansion.** Have a mindset of borderless geography that invites you to grow nationally or internationally (Asia-Pacific is 25 times bigger and the world is 80 times bigger than Australia).

IBISWorld

WHERE KNOWLEDGE IS POWER

METHODOLOGY

This report is the fourth annual *BRW* ANZ study into the issues facing businesses in the private sector in Australia.

The survey collates the results of the responses to a phone and online survey from a national random sample of private businesses across all sectors with a turnover ranging from \$10 million per annum to more than \$400 million per annum.

Over 570 owners and / or key decision makers participated in this year's study. They provided information on their outlook for their own organisations, the outlook for the Australian economy, key issues for their organisation, the issues that are causing them the most concern, the use (and relative importance) of a range of business advisers and specialists. They also provided information on the board structure for their organisation (if there was one in place) as well as the use of strategic planning, succession planning and the exit plans for business owners.

Where the research draws comparisons with 2010, 730 responses are included.

Data collection was carried out in May and June 2011.

The research was conducted on behalf of *BRW* and ANZ by Financial Review Business Intelligence.

Financial Review Business Intelligence, part of the Financial Review Group at Fairfax Media, specialises in research in the business sector and especially among business owners and senior decision makers.

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