



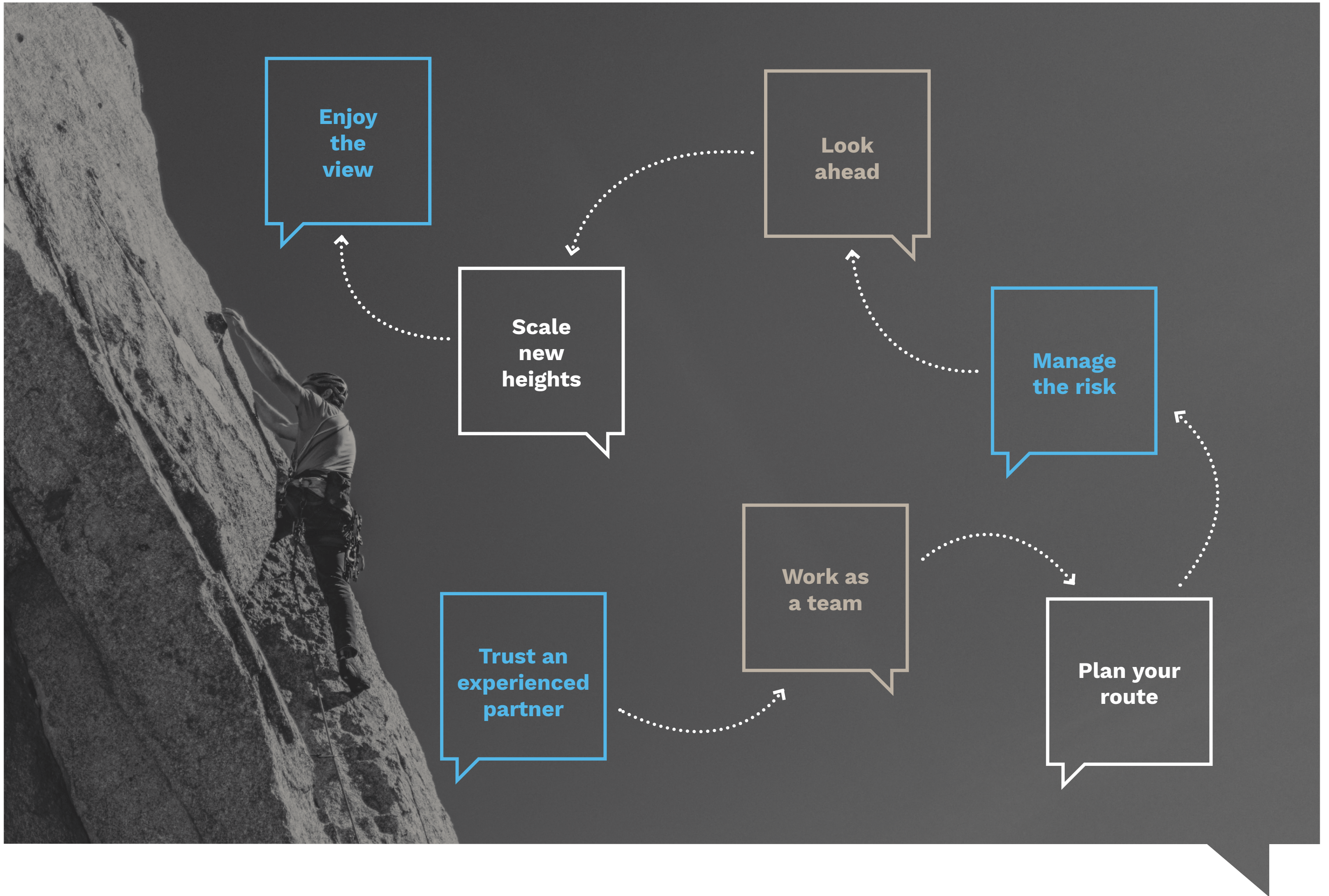
# 2020/21 SME Research Report

SMEs need a sounding board they can turn to and trust to reduce Non-financial Risks, improve business performance and owners' quality of life.

**insight**

Profit. Cash Flow. Value.







# Foreword

## A Word about Risks



While small to medium (SME) business owners may believe they have some level of control or influence over factors that affect their business and that they are adequately managing their risks, this is frequently not the case. External factors can develop quickly and in unpredictable ways to disrupt the status quo and significantly impact any business's operating conditions.

Who would have envisaged that in the space of a few weeks we would witness the locking down of entire countries, the banning of international travel and such volatile stockmarkets. These events highlight how interconnected we are and how fragile and vulnerable economies have become.

There is also significant pressure on businesses to maintain their reputation and image. We have all seen the direct and immediate impact of a public scandal on a business's bottom line.

To be successful in today's complicated world, business owners have to understand and manage these broader responsibilities. Owners have to expect that change will happen, and happen quickly.

While more businesses are preparing business continuity and disaster recovery plans, only the largest companies have the resources for regular crisis planning and scenario testing. Many owners have no significant experience in how to deal with unexpected disruptions to their market,

customer base or inputs (e.g. utilities, supplies and materials or transport).

While each crisis does eventually pass, SMEs that survive are those that have plans in place. Those SMEs that see, adapt and take advantage of opportunities that arise out of crises can emerge stronger.

Adversity also leads to opportunity. Business owners can aim to do more than react. They can act strategically, looking for opportunities and adapting to the new reality to grow and thrive.

We want to support our clients tackling today's challenges and help them build a profitable and sustainable business. SMEs are a highly valued client segment within our practice client base.

With the support of our research partner, Bstar, we are able to share insights into what's happening in the SME sector. Our 2020/21 SME Research Report discusses top business risks, analyses key non-financial risk and value drivers and introduces important industry profitability and valuation benchmarking data.

We have provided more information on the unique sounding board services we offer and how these services can de-risk your business, grow and improve profitability and cash flow, and ultimately grow its value.

We hope you enjoy reading the Report, and we welcome and value your feedback.



# Executive Summary

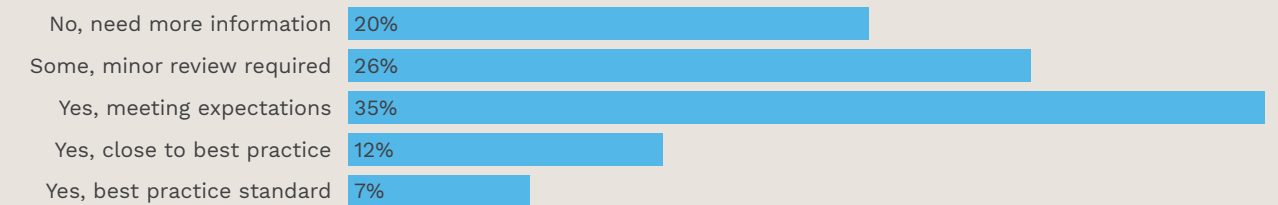
## Key Insight

SMEs need a sounding board they can turn to and trust to reduce Non-financial Risks, improve business performance and owners' quality of life.

We are all increasingly interconnected, and impacted by both local and global events. Business owners are having to deal with and manage an increasing range of risks that affect their day-to-day business operations. As the range of risks extends and becomes more complicated, they require new and varied methods of management.

“Governance is an area where we’re really lacking.”

### Governance Policies, Procedures and Training Programs in place (e.g. for directors, executives and key staff)



Source: RAVDA Data

These risks come in myriad forms, can be internal or external, specific to an industry or business, and local or global in impact - refer to the box for some current examples. We call these **Non-financial Risks** as they are not purely financial, and generally do not emerge from the financial accounts of an SME.

## Wide range of Non-financial Risks

Risks that impact business operations take many different forms.

### EXTERNAL RISKS

**Economic conditions**  
(e.g. downturns, recession)

**Government policies and legislation**

**Natural disasters**  
(e.g. droughts, fire, flood, storms, earthquakes)

**Epidemics and Pandemics**

### INTERNAL RISKS

**Operational**

**Conduct**

(e.g. bullying, sexual harassment)

**Compliance**

(e.g. breaching laws or regulations)

**Privacy breaches**

**Staff** (e.g. underpayment, payroll tax)

**Reputation** (e.g. social media posts)

**Key person** (e.g. ill health)

**Succession**

(e.g. no identified successors)

**Premises**

**Competitor**

(e.g. price wars or under quoting)

**Political changes, elections**

**Cyber attack**

**Exchange rates**

**Inflationary pressures**

**Corporate failures**

**Inquiries and Royal Commissions**



However, when Non-financial Risks are not well managed, they can quickly affect the profitability and impact the survival of an SME.

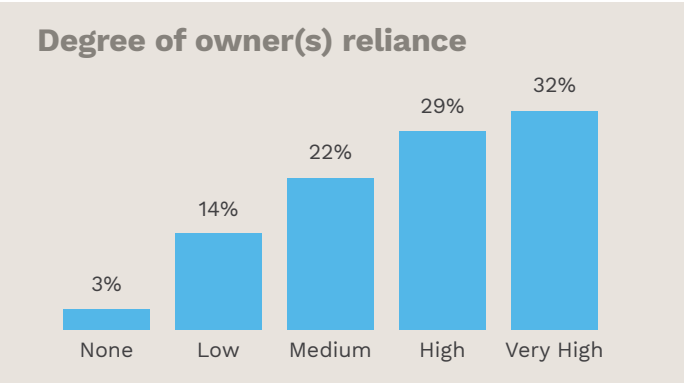
The impact of Non-financial Risks has been recognised by the Australian Securities and Investments Commission (ASIC). In a recent report<sup>1</sup> ASIC reminded directors of companies of their responsibilities to focus on managing these wider risks. The report showed why ASIC considers good management of Non-financial Risks to be essential to the long term success of a business enterprise.

“The costs and consequences of poorly handled non-financial risks can be immense and, at an extreme, catastrophic.”  
(James Shipton, ASIC Chair)

How are SMEs currently handling these risks?

To find out how SMEs are currently dealing with risks, we asked business owners a number of questions about all types of risk. We used both a short Business Risks Survey (10 questions) and a more detailed Risk and Value Driver Assessment (80 questions).

While each business is unique, our research shows that business owners have common experiences and share common concerns. While there is no ‘one-size-fits-all’ solution, the starting point is for business owners to identify and prioritise the risks that affect their business.



“All our eggs are in this basket at the moment and the business has got to start earning us some money soon! I’m pretty uncomfortable with the level of risk.”

Many SMEs are being overwhelmed with the challenges and increasing pressures facing their business and **61%** of SMEs report a high (**29%**) or very high (**32%**) degree of owner reliance.

**Succession risk was the highest risk identified by the Business Risks Survey.** Further detailed analysis<sup>2</sup> showed only **18%** of business owners have documented management and ownership succession plans in place, with more than half of those plans (**11%**) needing to be reviewed and updated.

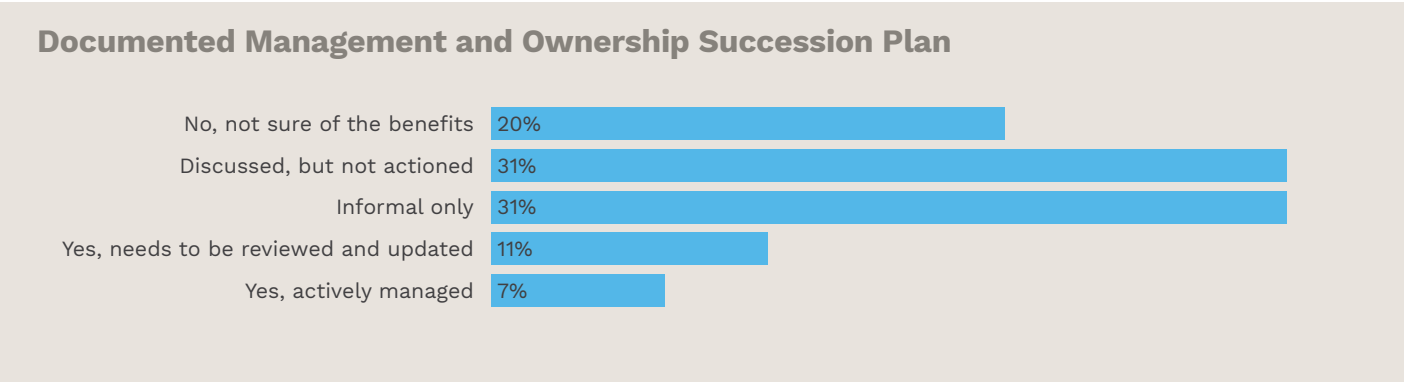
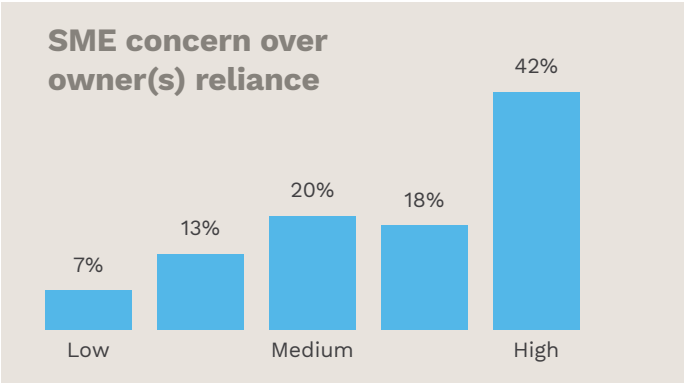
Succession: Australia and New Zealand Comparison

Only one in three (**36%**) of NZ SMEs and one in four (**25%**) Australian SMEs had succession arrangements in place. Additional data makes it clear that less have documented management and ownership succession plans in place.

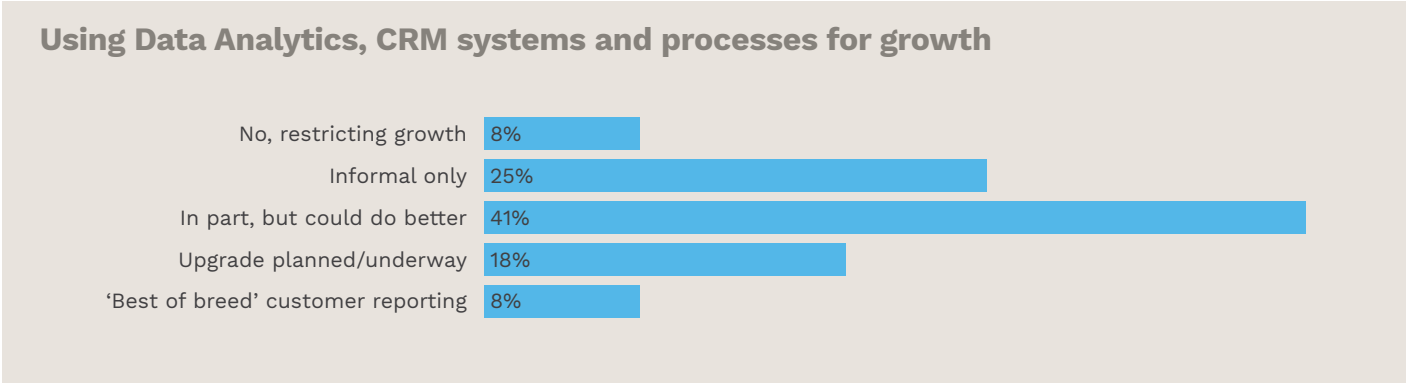
Financial Risks

Financial risks are also challenging, as **57%** of SMEs had gross profit margin growth of less than **5%**, including **25%** with shrinking margins.

1. The Director and Officer Oversight of Non-financial Risk Report released by ASIC’s Corporate Governance Taskforce on 2 October 2019 (see [www.asic.gov.au](http://www.asic.gov.au))  
2. Refer to the Finance Valuation Succession and Estate Planning section for more information.



Source: RAVDA data



Source: RAVDA data

“There is a lot of financial information that is available from our systems, but it is not being used or analysed.”

Growth is difficult, but only **8%** are currently using best of breed data analytics, CRM systems and processes to manage customer relationships, grow sales and attract new customers. **65%** listed it as a medium to high or high concern.

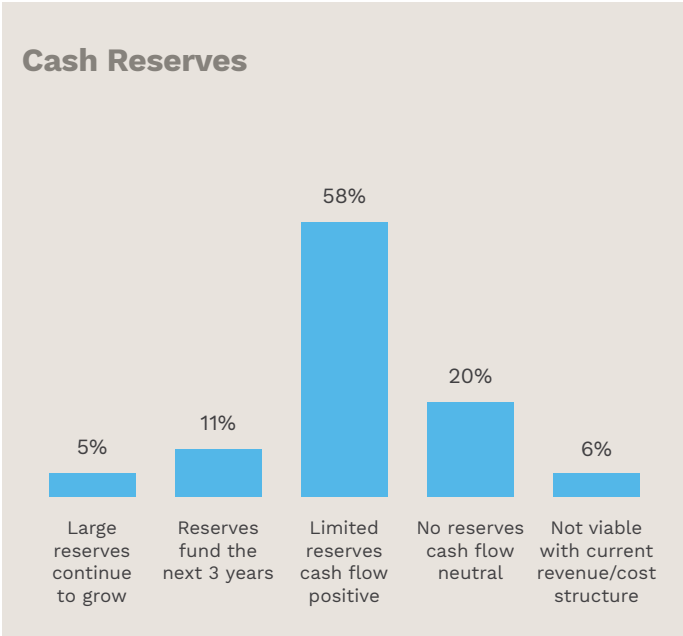
Cash Reserves

Surprisingly, a majority (**78%**) of SMEs are vulnerable to even a short term shock or disruption, indicating they held either no cash reserves (**20%**) or ‘limited’ cash reserves (**58%**).

“Our main exposure remains our relatively low cash reserves and the seasonal downturn over Christmas.”

Lack of Planning

Only a quarter (**26%**) of SMEs engaged in regular planning, with only **6%** having comprehensive current plans that were actively managed.



Source: RAVDA data

“We make a lot of informal plans and sometimes roll things out, in hope more than anything. Some things work, and some things don’t.”

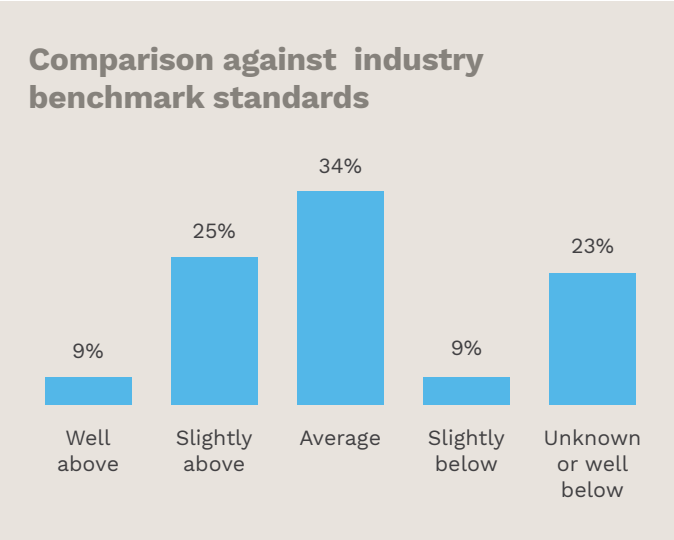
The standout personal risks all relate to planning for the future. Across three measures, **two in three individuals** have not taken action to make themselves financially independent.

“I didn’t enter into small business to build an asset, I created a job I’d love with a pathway to high income. It’s really happened organically and without planning. I need help to shape it into something saleable, with future value, but I still have time to do so.”

Risk and Value Drivers

The full Report features in-depth analysis, statistics and comments in relation to a business’s key risk and value drivers across ten categories. We captured this information, including business owners’ comments and level of concern through our detailed **Risk and Value Driver Assessment or ‘RAVDA’**.





Source: RAVDA data

“In our sector, technology is disrupting the role that humans play. Much of what was done by a human five years ago is now entirely being done by tech, changing the roles we play. We are trying to position ourselves as helping clients to use the right tech, with the right strategy.”

### RAVDA Benchmarks

The full Report includes a list of RAVDA benchmarks listed by ANZSIC divisions<sup>3</sup>.

“Who wants to be average? We want to be the benchmark and need a plan to get there.”

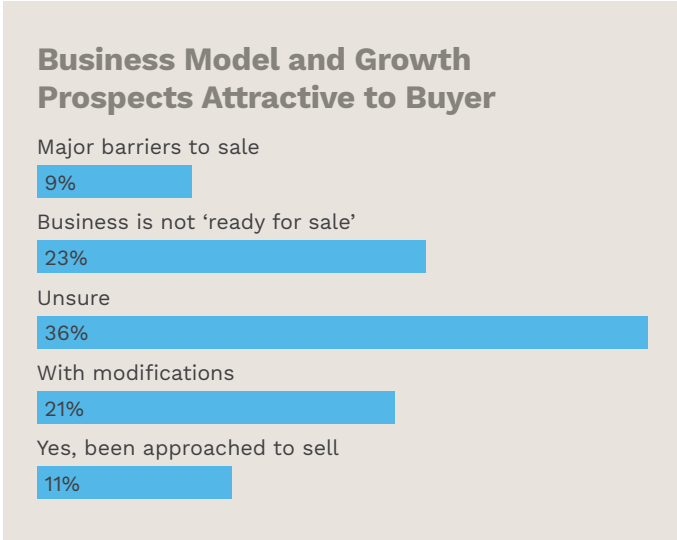
### Most Profitable and Valuable SME Businesses

The Report highlights the most profitable and valuable industry segments, SME profitability and valuation statistics and lists the most accurate industry average risk, profitability and valuation benchmarks.

### Shared Experiences and Improvement Ideas

We have included real life comments and observations from SMEs who have shared their experiences, frustrations and aspirations on their business and what they are doing to achieve success. **The Report features ideas to reduce all types of risks.**

3. Australian and New Zealand Standard Industrial Classification (ANZSIC) refer to [www.abs.gov.au](http://www.abs.gov.au) for more information



**Key idea: Customers & Market Demand**  
 Analyse your sales per customer group to determine your customer 'sensitivity' risk.

**Key idea: Staff**  
 Survey your staff to improve communication and engagement.

**Key idea: Owner(s)**  
 Develop a business operations manual to reduce owner(s) reliance.

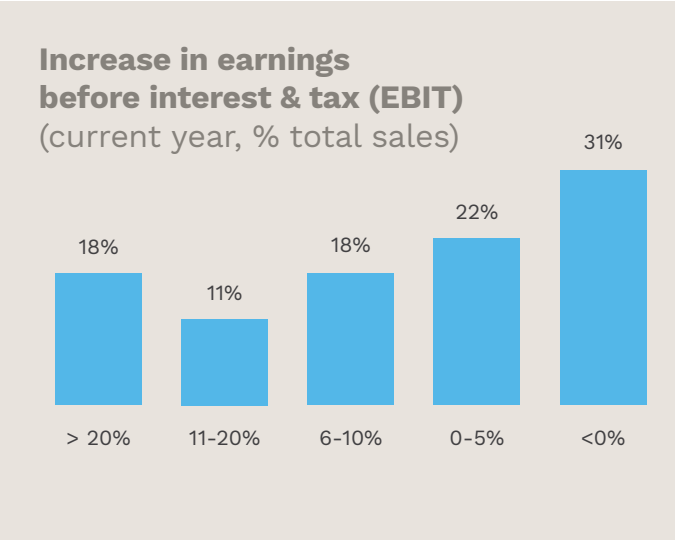
### Key Observation - Sounding Board Support

Business owners are increasingly aware that the pressures of running an SME are as individual as their business. In addition to financial matters, there is a wide range of risks that need to be managed on a daily basis. They are looking for ways to manage those risks, and proactively adapt to changes.

But reliance on business owners is already very high, and the level of planning is low. Many are already stretched, and it is easy to see risk management as an additional responsibility, increasing the burden on owners.

“Business planning has only started this year and is a work in process. We have new plans and strategies currently in play but it’s too soon to judge the effects.”

SMEs are looking for solutions, ways to lighten their load, but they can’t do it alone. This research highlights **business owners need the support of a sounding board**. The primary support needed is with planning, but the advice and support provided by a trusted adviser goes well beyond looking at the numbers.



Source: RAVDA data

“I created our last Business Plan which to be honest was largely ignored by my co-owners. Rather than start another cycle, I challenged them about growth and the need to bring different thinking into the business. We are now getting external help.”

### How will a Sounding Board help an SME business?

A professional **sounding board** will provide advice and support where owners need it most, allowing them to:

- Build confidence with independent and objective professional advice;
- Identify, manage and reduce key qualitative and financial business risks;
- Step away from their business to focus on planning;
- Be held accountable for implementing the

FINANCIAL BENEFITS	NON-FINANCIAL BENEFITS
Improved financial reporting, profitability, cash flow and risks score	Aligned owners, less owner reliance
Benchmark performance	Engaged, productive staff
Reduced operating costs	Better business resilience for change
Higher business value, lower value gap risk - business revaluation	Better lifestyle with less stress
	Stronger family group
	Business legacy

### What is a sounding board?

A **sounding board** is a person you run things by, or **someone** you turn to for advice\*.

The ability to discuss issues with someone you trust helps to develop ideas and solutions, while sharing the load, and reducing stress. Your sounding board can agree or provide a different point of view, and bring new skills to solve issues.

\* www.yourdictionary.com

- changes necessary to improve performance;
- Achieve a more balanced personal, business and family lifestyle.

“Our approach is, don’t be afraid to try new things but know when to cut your losses.”

### Outcomes Matter

Business owners are focused on outcomes. However, sometimes the personal, family or lifestyle benefits outweigh the financial metrics.

“We engaged [our accountant] to chair our board of advice. Our primary goal was to replace me so I could spend more time with our children. They are young and I didn’t want to miss this important part of our lives together as a family”.

Sounding Board Relationships and Services

There are a range of sounding board services available to SMEs. Each service is tailored to the key need of the business owner(s) and will change as the business grows (refer to the Appendix in the full Report).

BUSINESS PROFILE	KEY ISSUE	SOLUTION BOARD SERVICE & OBJECTIVE
Small	44% of SMEs don't have a business plan.	<b>Business Planning Mentoring</b> Prepare and document a business plan.
Medium	31% of SMEs had less than 0% growth in Profitability.	<b>CFO Service</b> Establish accurate financial reporting, improve profitability and cash flow.
Large	Only 12% of SME owner(s) were not intending to rely on the sale of their interest in the business to fund their retirement or next business venture.	<b>Board of Advice Program</b> Determine the 'true' business value, grow and transition the value to reduce the owner(s) value gap risk.

Source: RAVDA Data

The Report includes a Matrix (refer to the Appendix in the full Report) outlining the different advisory solutions available to our SME clients to minimise key risks and grow their business. Support can be delivered face-to-face or remotely, through online tools, virtual meetings and webinars.

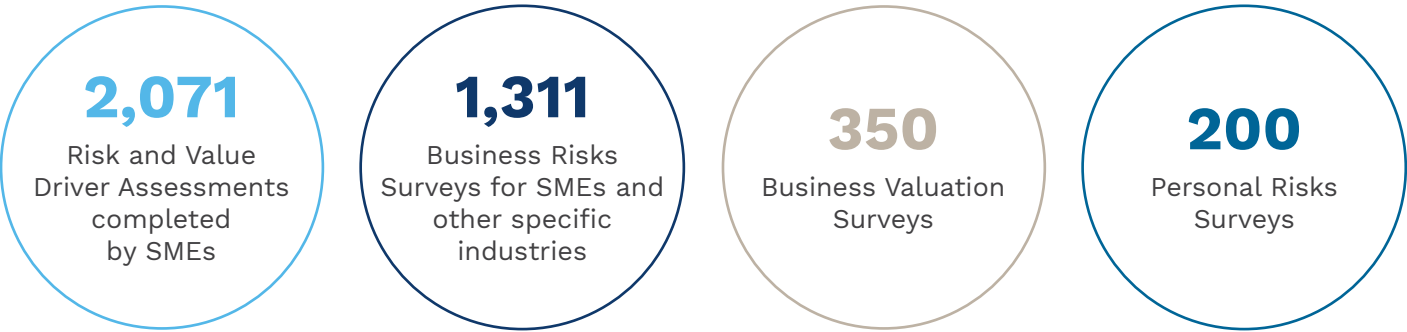
3 Steps to Success

We encourage our clients and readers of this Report to take action to get support and recommend one or all of the following steps:

- 1 Understand the risk and value drivers in your business.
- 2 Collaborate to improve business performance.
- 3 Select a partner to support success.

Sources of Information

The primary source of data for this Report were responses from SME clients of accounting practices relating to the two-year period from January 2017 to December 2019. This included more than 4,500 observations and comments from SME owners. We have drawn on an extensive database of more than 6,000 valuation and performance benchmarks and more than 5,000 benchmarked Risk and Value Driver Assessments. A range of different SME client engagement/business advisory tools were available for the statistical information:



What's in the full report?

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- Executive Summary
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  - How are SMEs currently handling these risks?
  - Key Observation - Sounding Board Support
- Top Business Risks
- Risk and Value Drivers
- Most Profitable SME Businesses
- Most Valuable SME Businesses
- 3 Steps to Success
- APPENDIX: SOLUTIONS
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  - Sounding Board Relationships



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