

PolsonHiggs
BUSINESS ADVISORS


McCULLOCH
AND PARTNERS
CHARTERED ACCOUNTANTS & BUSINESS ADVISERS

Survey of South Island Business Leaders

June 2011

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1. Introduction

Since 2007, two of the South Island's leading Chartered Accountancy firms – Polson Higgs and McCulloch & Partners have combined to jointly undertake a survey of South Island business leaders.

The survey was launched because we believe there is a need for better information on the issues facing South Island business leaders and the strategies they are using to address those issues.

Our previous surveys have focussed on challenges associated with leadership, organisational culture, employee recruitment and retention, environmental issues and managing in a recession.

Our most recent survey, undertaken in June 2011, has continued our focus on managing in a recession. The survey also includes new questions on the impact of the Christchurch earthquakes on businesses.

The June 2011 survey was undertaken in conjunction with the Canterbury Development Corporation (CDC), and includes responses from a number of businesses that are working with CDC in the Christchurch area

This report presents the results of the June 2011 survey.

2. Survey Methods

In early June 2011, leaders in 314 South Island businesses were invited to participate in an on-line survey.

The survey focussed on five main themes:

1. their expectations for their business, including investment intentions
2. businesses finance options
3. the impact of the 22 February earthquake on their business operations

Respondents were asked to provide their responses by 17 June 2011. At that time, completed questionnaires had been received from 96 respondents.

Half these respondents (49) were located in Christchurch and the remaining 47 were located elsewhere in the South Island, mostly in Otago and Southland.

The responses of Christchurch based and non-Christchurch based businesses are compared throughout this report in order to examine earthquake-specific issues and impacts.

3. Business Environment

Respondents were asked how eight aspects of their business environment had changed over the past 12 months and whether they expected each of these aspects to increase, decrease or stay the same over the next 12 months and five years. Their assessments are shown in Figure 1.¹

Looking Back: The Past 12 Months

Three of the eight aspects of the business environment were considered to have become more difficult over the past 12 months: competition has increased for most businesses; the availability of skilled workers has decreased (especially in Christchurch) and wage expectations of employees have increased.

Reflecting a generally stagnant local economy and earthquake related impacts, businesses reported no significant changes in profitability or in the availability or cost of finance over the past 12 months. Overall, productivity was reported to have improved slightly outside Christchurch, but not within Christchurch (where it has been affected by the earthquakes). Businesses in Christchurch and other areas of the South Island reported overall net improvements in product and service innovation.

Looking Ahead: The Next 12 Months and 5 Years

Looking ahead, businesses expect four aspects of their environment to become more difficult in the short and medium term:

- Competition will increase
- The cost of finance will increase (as the Reserve Bank increases the OCR)
- The availability of skilled workers will decrease (especially in Christchurch)
- The wage expectations of employees will increase

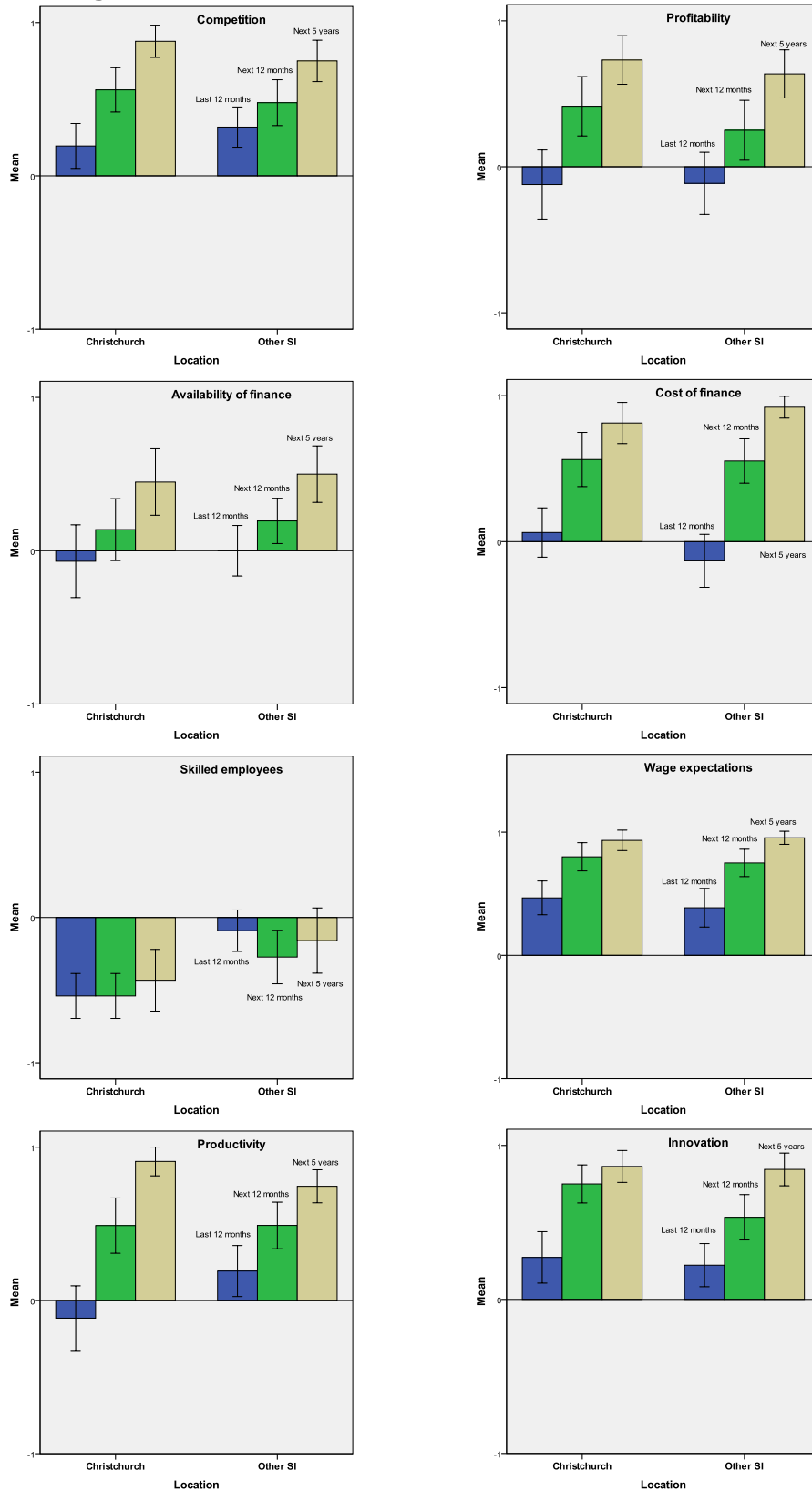
Notwithstanding these difficulties, most businesses expect their profitability to increase, especially over the next 5 years. This improvement in profitability is expected to be driven by improvements in productivity and product/service innovation in an otherwise difficult trading environment.

These results show a typical pattern whereby business growth and profitability are expected to be driven by controllable internal factors (productivity and innovation which will lift demand and margins) in the face of largely uncontrollable negative external factors such as increasing competition, a tightening labour market and rising interest rates.

In summary, while most businesses are optimistic about their individual prospects, they remain cautious about the general business climate in the short and medium term.

¹ Respondents could indicate whether a business aspect had increased, decreased or stayed the same over the past 12 months or was expected to increase, decrease or stay the same in the future. Figure 1 shows mean respondents scores where -1 = decrease, 0 = stay the same, and +1 = increase. The error bars (I) show 90% confidence intervals about the means.

Figure 1



Growth Expectations

Consistent with the findings shown in Figure 1, Figures 2 and 3 below show that most businesses expect to grow over the next two and five years. Christchurch businesses, in particular, are expecting to experience strong short and medium term growth (most expect growth of more than 10% per annum).

Figure 2

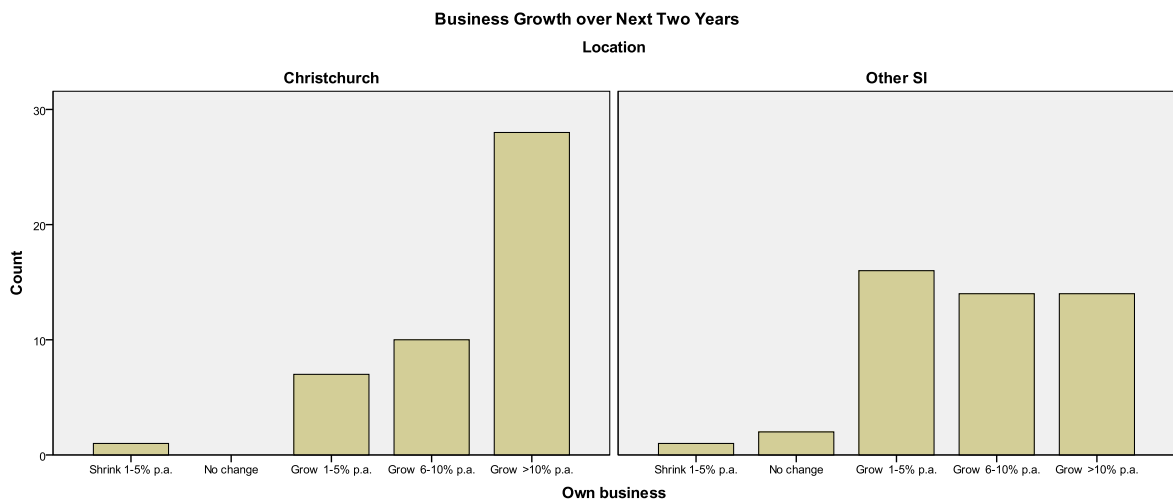
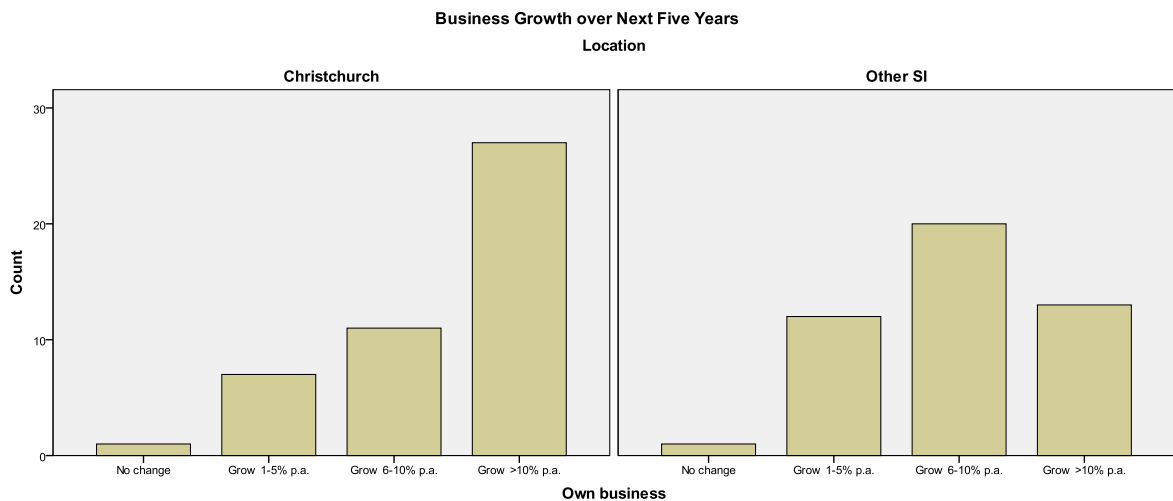


Figure 3

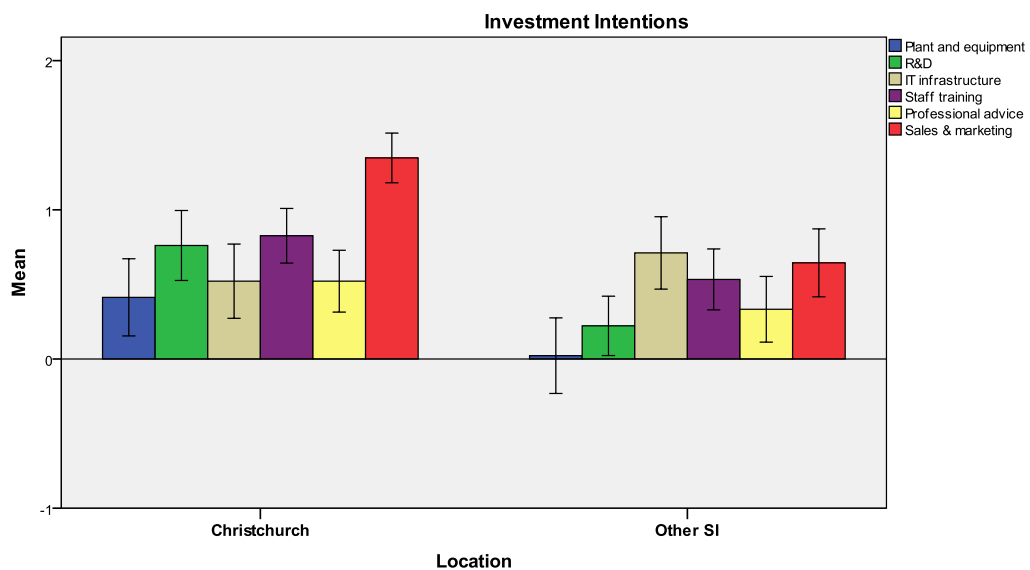


4. Investment Intentions and Finance

Investment Intentions

As Figure 4 shows, overall respondents expect to invest more in their businesses in the next 12 months than they did in the last 12 months². Investment intentions are stronger among Christchurch businesses than non-Christchurch businesses. This surge in investment intentions probably reflects a combination of the lack of investment in Christchurch businesses in the past 12 months and businesses gearing up to meet increased demand driven by the future rebuild of the city.

Figure 4.



² Respondents were asked to indicate whether they expected to invest more or less in the next 12 months than they had in the last 12 months. Figure 4 shows mean scores where -2 = significantly less, -1 = slightly less, 0 = no change, and +1 = slightly more and +2 = significantly more. The error bars (I) show 90% confidence intervals about the means.

5. Employment Conditions and Remuneration

Respondents were asked to indicate how their businesses had responded to changes to the Employment Relations Act and Holidays Act that extended the 90 day statutory trial period option to all employers and enabled employees to cash up one of their 4 weeks of statutory leave entitlement. Tables 1 and 2 below summarise their responses.

Employers are divided in their use of the 90 day trial period, with 37% using it for all new hires, 38% on a case by case basis and 25% not using it at all.

Most employers (66%) are willing to consider requests to cash up a 4th week of leave on a case by case basis.

Table 1

Use of 90 day trial option	Location		
	Christchurch	Other SI	Total
All employees	51.2%	23.3%	36.9%
Case by case	26.8%	48.8%	38.1%
Do not use option	22.0%	27.9%	25.0%
Total	100.0%	100.0%	100.0%

Table 2

Grant requests to cash up 4th week	Location		
	Christchurch	Other SI	Total
Grant all requests	34.1%	9.5%	21.7%
Case by case	56.1%	76.2%	66.3%
Do not grant requests	9.8%	14.3%	12.0%
Total	100.0%	100.0%	100.0%

Chicken or Egg?

The survey uncovered an intriguing correlation between the use of the 90 day trial period and the availability of skilled labour. Businesses that have adopted the 90 day trial period for all employees are much more likely than other businesses (especially those that never use the trial period) to report that the availability of skilled labour has decreased in the past 12 months. See Table 3 below. Two possible explanations for this are that:

- a) the shortage of appropriately skilled employees has encouraged employers to adopt the trial period in order to test the suitability of new employees ; or
- b) employers who have adopted the 90 day trial period are less attractive to prospective skilled employees who have options in the labour market and are not prepared to accept positions with a trial period attached

Further research would be required to establish the causal direction of this relationship.

Table 3

Use of 90 day trial option	Availability of skilled employees			Total
	Decreased	No change	Increased	
All employees	50.0%	26.2%	16.7%	35.0%
Case by case	40.6%	45.2%		40.0%
Do not use option	9.4%	28.6%	83.3%	25.0%
Total	100.0%	100.0%	100.0%	100.0%

$\chi^2 = 17.7, 4df, p = 0.001$

Remuneration

Table 4 shows businesses' expectations of increases to employee base salaries over the next 12 months. Businesses are evenly split between those expecting increases in the 1-2% range and those expecting increases in the 3-5% range. There are no significant differences between businesses located in Christchurch and those located elsewhere. These expectation levels are somewhat higher than those reported in the August 2010 survey.

Table 4

Expected change in base salaries	Location		
	Christchurch	Other SI	Total
Decrease		2.4%	1.2%
No change	14.6%	19.0%	16.9%
1-2%	43.9%	33.3%	38.6%
3-5%	34.1%	45.2%	39.8%
>5%	7.3%		3.6%
Total	100.0%	100.0%	100.0%

6. Impact of the Christchurch Earthquake

The impact of the February 22 earthquake (and subsequent smaller earthquakes) on Christchurch businesses has been well documented in many publications and the results of this survey reinforce many of those findings.

Businesses were asked how the earthquake had impacted upon 12 aspects of their business, with their responses summarised in Figure 5 below³.

While, as would be expected, Christchurch based firms reported being more negatively affected by the earthquake(s) than those based outside Christchurch, it is notable that, overall, non-Christchurch businesses had been significantly negatively affected in five business aspects:

- Collection of debts (perhaps because of cash flow difficulties of Christchurch based debtors)
- Transport and communication
- Access to reinsurance (reflecting concerns about knock-on effects to insurance availability)
- Ability to operate efficiently (especially due to disruption to supply chains and key suppliers)
- Ability to implement business plans

Christchurch businesses themselves reported the largest negative impact related to:

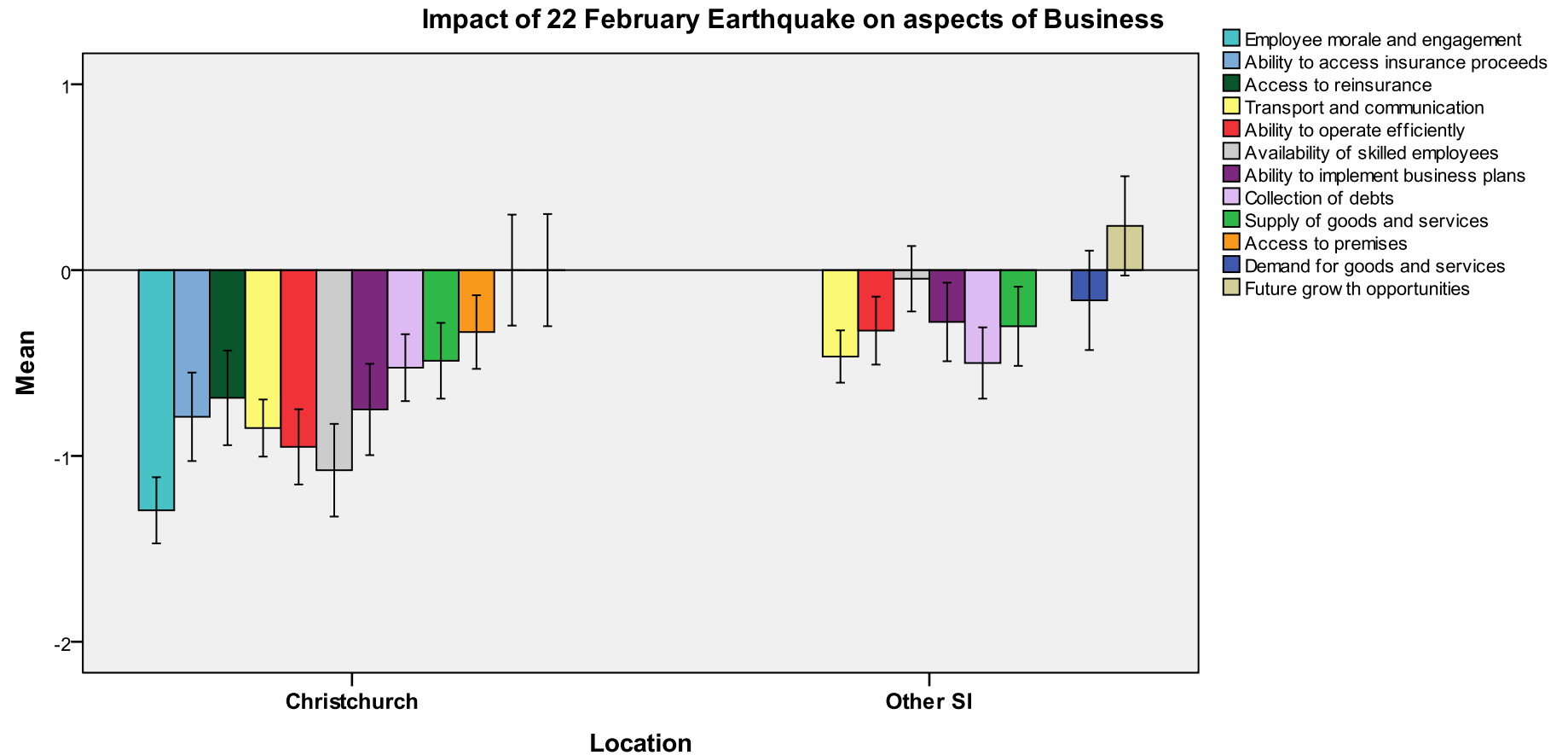
- Employee morale and engagement
- The availability of skilled employees⁴
- The ability to operate efficiently
- Transport and communication
- The ability to access insurance proceeds
- The ability to implement business plans

Overall, Christchurch businesses remain optimistic that they will bounce back from the earthquake, which was considered to have had no net impact on future growth opportunities and demand for goods and services.

³ Respondents could indicate whether the 22 February earthquake had had a positive or negative impact on 12 aspects of their business. Figure 5 shows mean respondents scores where -2 = major negative, -1 = minor negative, 0 = no impact, and +1 = minor positive and +2 = major positive. The error bars (I) show 90% confidence intervals about the means.

⁴ This finding is somewhat counter-intuitive given that there has been a spike in unemployment in Canterbury, but possibly reflecting the particular skills that are required in a post-earthquake economy.

Figure 5



7. Respondent Characteristics

The following tables compare the characteristics of respondents in Christchurch and other South Island areas. Christchurch businesses tend to be concentrated more in the manufacturing and IT sectors, whereas businesses outside Christchurch are distributed more evenly across industry sectors. The size of businesses, as measured by turnover and employees is similar for both groups. Demographically, Christchurch respondents tend to be somewhat younger than respondents outside Christchurch.

Sector	Location		Total
	Christchurch	Other SI	
Agriculture, Forestry and Fishing	2.6%	4.8%	3.7%
Arts, Entertainment and Recreation Services		7.1%	3.7%
Construction and Related Trades	5.1%	7.1%	6.2%
Education and Training	2.6%	2.4%	2.5%
Financial and Insurance Services		14.3%	7.4%
Health Care and Social Assistance		4.8%	2.5%
Information Media and Telecommunications	23.1%	7.1%	14.8%
Manufacturing	35.9%	9.5%	22.2%
Professional, Scientific and Technical Services	17.9%	19.0%	18.5%
Rental, Hiring and Real Estate Services		7.1%	3.7%
Retail Trade	2.6%	7.1%	4.9%
Tourism, Accommodation and Food Services	5.1%	4.8%	4.9%
Transport, Postal and Warehousing		2.4%	1.2%
Wholesale Trade	5.1%	2.4%	3.7%
Total	100.0%	100.0%	100.0%

Size	Location		Total
	Christchurch	Other SI	
1-5 employees	12.5%	16.7%	14.6%
6-19 employees	30.0%	33.3%	31.7%
20-49 employees	17.5%	23.8%	20.7%
50-99 employees	17.5%	4.8%	11.0%
100-499 employees	15.0%	16.7%	15.9%
500+ employees	7.5%	4.8%	6.1%
Total	100.0%	100.0%	100.0%

Turnover	Location		
	Christchurch	Other SI	Total
< \$1m	12.5%	9.3%	10.8%
\$1m to \$5m	35.0%	37.2%	36.1%
\$5m to \$10m	15.0%	20.9%	18.1%
\$10m to \$50m	22.5%	16.3%	19.3%
\$50m to \$100m	10.0%	9.3%	9.6%
\$100m to \$500m		4.7%	2.4%
> \$500m	5.0%	2.3%	3.6%
Total	100.0%	100.0%	100.0%

Age	Location		
	Christchurch	Other SI	Total
25 to 40	17.9%	18.6%	18.3%
41 to 60	79.5%	58.1%	68.3%
Over 60	2.6%	23.3%	13.4%
Total	100.0%	100.0%	100.0%

Gender	Location		
	Christchurch	Other SI	Total
Male	78.9%	90.7%	85.2%
Female	21.1%	9.3%	14.8%
Total	100.0%	100.0%	100.0%