

# NBR special report

## SMEs

SMEs are a crucial component of New Zealand's economic landscape and an important source of employment. But the path to recovery from recent economic challenges has squeezed business margins, resulting in reduced profitability and hiring intentions. Retained earnings have also dried up, and credit availability is still difficult, forcing many SMEs to finance their firms with personal credit cards. Experts believe the Rugby World Cup may provide a boost to the trading environment and SMEs could optimise profits by engaging in training to enhance business skills. This special report looks at the challenges and opportunities facing SMEs.

# Getting best advice for the recovery

Many SME owner-managers struggle to effectively manage across all facets of their business.

However, with the help of advisers, SMEs can ensure they have the best understanding of the marketplace and optimum business model, in turn assisting profitability and bank interactions.

### Key competencies

New Zealand Chartered Accountants chairman Merv Gyde said where SMEs had a good understanding of the typical business model, they made good margins on their products and services.

"However, the big limiting factor is these people's lack of marketing skill, and as a consequence, there is often a lack of sales volume."

He said this meant bottom line



**Merv Gyde**

profit was limited by a lack of volume, rather than external factors like taxes and funding costs.

As long as fixed costs were controlled and sales volume was sufficient to cover direct costs, such external factors are not necessarily an issue.

This type of financial model – which Mr Gyde said NZCA

accounting firms were experienced in advising businesses on – is what was needed for the business to then be able to provide an adequate return to the owner.

### Relationship with banks

SME owner-managers who ensured they have a high level of personal business competency were likely to have more successful interactions with banks.

Mr Gyde said banks were supportive of SMEs and remained keen lenders despite the financial crisis.

"With SMEs, banks lend to people, not the business, so it's the people who need to demonstrate their ability, rather than simply show a good business."

Banks like to look at several years' past results to assess the

owner/manager competence in the core areas of business before then discussing in person their future cashflow projections.

This is in contrast to bigger businesses. Mr Gyde said the inherent strength and robustness of a large business commanded a bank's respect. "So it's the business itself, rather than the people who run it, who will get the loan."

### Sector trends

Due in large part to the global financial crisis, most SMEs have experienced a huge fall in turnover in the last two years. Mr Gyde said this had compressed profits often to below a sustainable level.

He said some SMEs had closed doors as the result of a voluntary decision by the owner, after cash-flow fell too low.

"You would expect then that the SMEs that have survived would benefit from the declining competition but that hasn't necessarily been the case."

A recently published nationwide research report on SMEs commissioned by NZCA found 59% of SMEs surveyed were forecasting growth in the year ahead. Much of that growth is expected to come from new customers.

"The SMEs that have survived are clearly well-funded and therefore sustainable, which means if they position themselves properly for the recovery, they should thrive over the next few years."

Mr Gyde said NZCA accounting firms were well placed to help their clients position themselves for the recovery that would surely come.

