eci

GROWTH SURVEY 2016

B R E X I T

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About ECI – Building Successful Businesses

ECI is the UK's leading growth-focused private equity firm.

We invest in management buyouts and buyins for majority or minority equity investments in medium sized UK growth companies within the Business & Financial Services, Consumer, TMT, Industrials, and Healthcare sectors.

For more than 40 years we've invested across these sectors, gaining a wealth of experience in supporting high growth businesses with a deal size of £20m to £150m.

253
investments over 40 years.

£10bn
total enterprise value of exits.

Total UK employees across ECI's portfolio

over 6,200

and average headcount growth is circa 10% p.a.

Investing the latest fund, ECI 10, with a total value of

£512m

Foreword

As the UK seeks to forge a new relationship with the world, raising the productivity of our economy has never been more important. It is productivity growth that will help spread prosperity outside London and the South East and drive the UK economy through the uncertain times ahead.

The success of the UK's fastest growing firms will be vital in achieving this goal. Scale up companies added almost £60bn to the UK economy from 2010-13. And, in 2013, just 4% of fast-growing companies were responsible for nearly 20% of productivity growth in the UK economy – a truly remarkable statistic. Highly productive firms are twice as common within the scale up community. Put simply, what matters to growth companies matters for the UK economy as a whole.

Access to the single market and the European workforce were highlighted as the most important aspects of future negotiations with the EU.

The latest ECI growth survey provides a timely reminder of what growth companies need to succeed. Now in its seventh year, the findings highlight the need to maintain the principle of openness in the UK economy, and support the CBI's own research. Respondents cited access to the single market and the European workforce as the most important aspects of future negotiations between the new UK Government and the European Union.

Meanwhile, there is much that can be done within the domestic agenda – particularly around skills. The Apprenticeship Levy remains both an opportunity and a concern – the Department for Education, with its new and expanded remit, will need to give serious consideration to the Levy's current design and timetable.

Businesses have a vital role to play in building the skills of the UK workforce. The increasing demand for higher skilled people must be met by a willingness of firms to narrow the chasm between education and the workplace. And on this there is welcome progress across the country. More businesses are supporting schools, offering careers advice and investing in workplace training, but firms they need to continue to up their game.

Elsewhere, the ECI growth survey highlights firms' fears regarding declining inward investment. The CBI has been vocal in urging the Government to get on with the key infrastructure decisions, such as HS2 and aviation capacity. The recent green light for expansion at City Airport sends a positive signal, though making a decision on a new runway in the South East remains an urgent priority.

Innovation will also be critical, and in the uncertain times ahead we need to encourage investment in new technologies. It will come as no secret to readers of this survey that the UK lags behind its international peers on research and development spending, which is vital for innovation. Raising our combined government and business R&D spend to 3% of GDP by 2020, coupled with exploring greater export opportunities, will help to fill the order books of growth companies. And maintaining access to finance will help them invest to take advantage of such opportunities.

Making progress in these areas will give our growth firms the best possible environment in which to thrive, by driving productivity and helping to create an economy that works for everyone.

We face challenging times ahead – but there are opportunities as well. The UK remains a vibrant and open nation, and one of the best countries in the world to do business. Now is the time to take advantage of opportunities for productivity growth to make it even better.

Carolyn Fairbairn
Director-General of the CBI

Growth businesses not immune to Brexit vote

46%

of growth businesses have downgraded their revenue forecasts. Just 11% have increased forecasts.

Despite this difficulty, they remain positive on growth

67%

More than 2 in 3 respondents expect positive revenue growth in spite of Brexit.

The renegotiation with the EU is the number one barrier to growing exports

Political instability a cause for concern for growth businesses

32%

Nearly one-third of participants cited political instability as the biggest concern for their business.

77%

77% of growth businesses are still experiencing skills shortages, although this is down from 91% in 2015.

Maintaining access for EU workforce a priority for growth businesses

58%

When asked to state their biggest priorities for EU negotiations, 58% highlighted access to EU workers.

42%

Skills shortages in technical, engineering and R&D roles were reported by 42% of respondents.

Apprenticeships continue to remain important

42%

Expanding apprenticeship schemes will help to reduce skills shortage, according to 42% of respondents.

Contents

Executive summary

This is seventh year that ECI has polled Britain's growth companies on their sentiment and outlook. We focus on this segment of UK plc because it produces the most promising entrepreneurs that we like to partner with. But we also believe it is vital to understand the issues that affect these companies, precisely because they are amongst the UK's most important job and wealth creators, the future of our economy.

Last year's survey gave us one overwhelmingly clear conclusion – that the vast majority of growth companies wanted the UK to remain in the European Union. Twelve months on, the country has voted to leave, so where does that leave our leading growth companies?

As you will see from this report, they are worried that the economy will take a turn for the worse. But what is striking is their resilience and determination to just 'get on with it', building their top lines and investing to power future growth.

They are also very clear about what they want the Government to secure in its future Brexit negotiations - continued access to the single market is their number one priority. A significant majority also want to preserve access to Europe's workforce, and almost one in three companies also want the Government to reduce Brussels red tape.

It's no surprise that fast growing companies are determined to be able to keep hiring from Europe, especially in the midst of a chronic skills shortage. Some 77% of companies surveyed cited some type of skills shortage; down on last year but still worryingly high, especially for firms in the South-West & Wales, as well as healthcare, industrials and consumer businesses.

"The message is clear: growth companies will do their bit to help our economy to continue thriving."

In terms of the wider economy, a steady drip of negative data has pointed to a deteriorating economic landscape – and this is by far the biggest concern for growth companies, with 69% citing it as their biggest concern. However, some more positive data has recently emerged, which suggests that the gloomier projections for the medium-term economic outlook appear overblown.

Crucially, companies are also worried about whether they can get the finance they need to grow. It is a significant concern that access to finance has deteriorated for the first time in five years with 61% of companies saying they expect it to be difficult to secure finance, more than doubling from last year. Clearly, the Government and the Bank of England will need to do more to ensure that Britain's job creators get the funding they need in order to keep their businesses and the wider economy on track.

Nevertheless, it is heartening to see how entrepreneurs remain determined to succeed in the face of such serious challenges. More than two thirds expect to grow revenues over the next twelve months and 43% are looking forward to double digit growth. How will they get there? Through investment - with more firms planning to boost investment and hiring than those looking to cut - and through exports, with North America and Europe topping the list of target markets.

The message is clear: growth companies will do their bit to help our economy to continue thriving. Now it's up to the Government to create and sustain the conditions necessary for this to happen.

Chris Watt
Investment Committee Member & Partner

Key findings

From the 2016 Growth Survey

Biggest priority
Access to single market.

82%

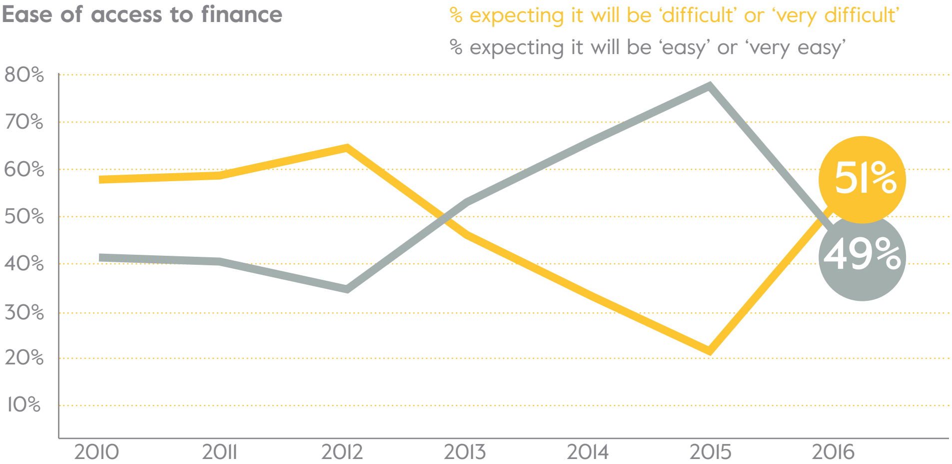
Biggest fear
Economic slowdown.

69%

"Our members are most concerned about declining inward investment and the strength of sterling. They want the confidence to make decisions on recruitment, investment and R&D – areas where the Government can make an impact now."

Emma-Jane Packe
MD, The Supper Club

Ease of access to finance



Companies suffering skills shortage

91%

2015

77%

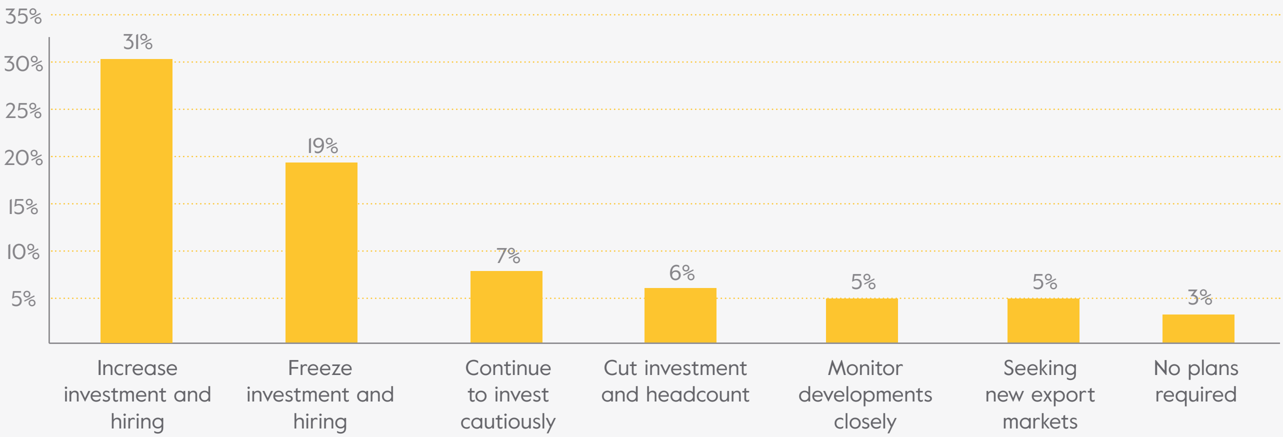
2016

Despite a fall of 14%, more than three in four growth businesses still report a skills shortage.

Improving the links between business and education bodies was cited by 68% of respondents as the number one solution to this problem.

68%

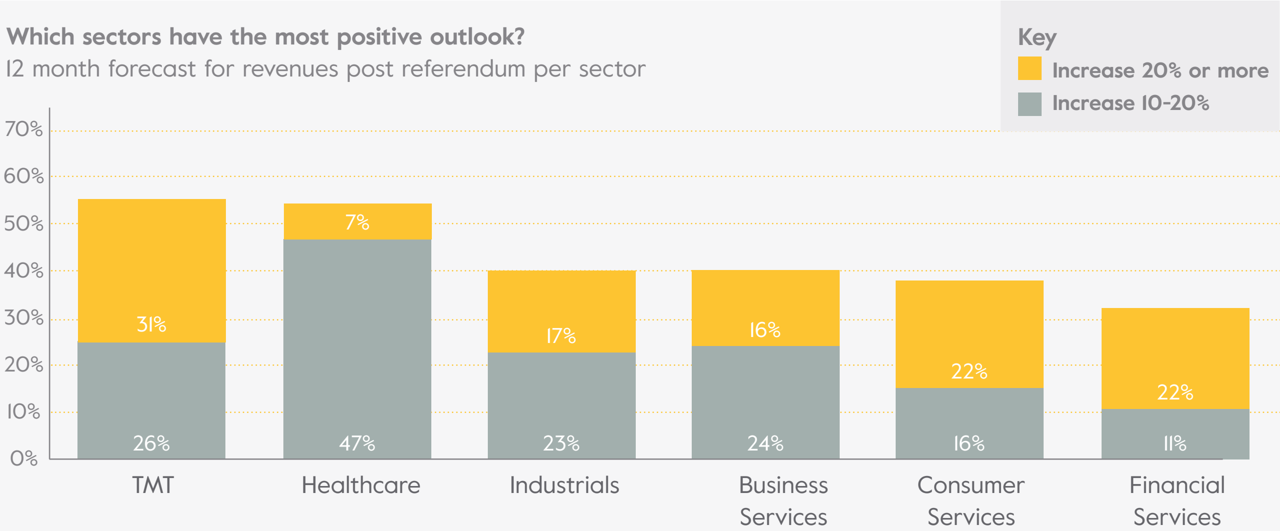
How growth companies plan to mitigate challenges ahead



Priorities of growth companies in upcoming Brexit negotiations

Which sectors have the most positive outlook?

12 month forecast for revenues post referendum per sector



What growth companies want

82%

Maintain access to Single Market.

58%

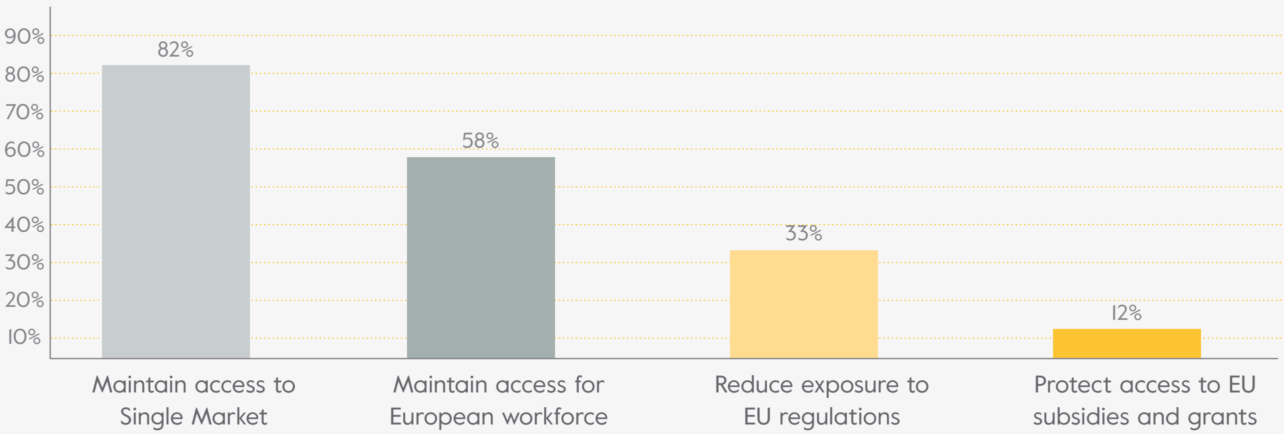
Maintain access for European workforce.

Millions of people across the world watched in shock as we chose to end our 43-year relationship with the European Union on June 23. Despite tight polls, the final result was widely unexpected and saw voters from Birmingham to Dover make their feelings perfectly clear. Britain's new Prime Minister Theresa May now faces a tough task with years of tricky Brexit negotiations ahead. As she prepares to engage with her European counterparts, what is on the wish list of Britain's growth companies, the lifeblood of our economy?

The overwhelming priority for these businesses is to maintain access to the Single Market, comprising 'four freedoms' in goods, services, capital and people (more on this final one in just a moment). In total, 82% of growth companies said this was a major concern for them.

This should come as no surprise given how Europe remains a vital export market for the UK, with 45% of respondents looking to grow within the region. These concerns also reflect the fears of many Remain campaigners who warned that the British economy would contract if we lost access to the Single Market. A pre-referendum report by HM Treasury estimated that if Britain negotiated a bilateral trade agreement with the EU on similar terms to Canada's EU deal, its economy would be 6% smaller in 15 years. The same report estimated the economy would be 9.5% smaller over the

Priorities that growth companies want the Government to pursue in negotiations with the EU



same period if Britain was to fall back on its membership of the World Trade Organisation.

Growth companies don't just want continued access to the Single Market; they also want access to its work force. 58% of growth companies cite this as a priority, a figure that is especially high among consumer (64%), healthcare (73%) and TMT companies (63%), as well as companies in the Midlands (65%), a region that largely backed Brexit.

Theresa May has said she will take into account voters' views on immigration, but it is difficult to see how Britain can maintain access to the Single Market without accepting the free movement of labour.

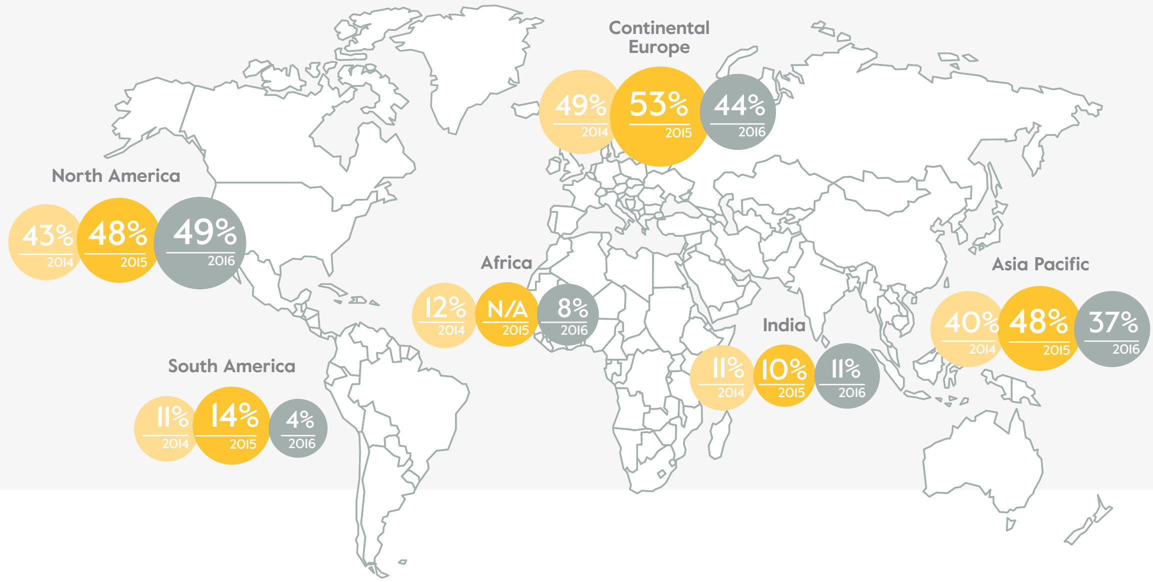
> **"The overwhelming priority for these businesses is to maintain access to the Single Market, comprising 'four freedoms' in goods, services, capital and people."**

The resolution of this thorny dilemma will be closely watched by growth companies, which need access to European workers. As we will see in the next chapter, it is also clear that businesses are suffering from a skills shortage, a problem they fear will be exacerbated by shrinking the pool of available workers.

Further down the scale, 33% of respondents say they want the Government to help reduce their exposure to EU regulations, though this rises to 50% for industrial companies. Brussels red tape was cited by the Leave campaign as one of the benefits of Brexit and clearly quite a few growth companies agree with that. Just 12% of companies want the UK's negotiations with the EU to prioritise the protection of access to subsidies and grants. Chancellor Phillip Hammond has already said that the Government will honour EU funding worth £4 billion a year.

So what does this all tell us? It tells us that although Britain is yet to trigger Article 50 and formally start the process of leaving the EU, growth companies are very clear about what they want their Government to deliver for them: continued access to both the Single Market and Europe's workforce are major priorities. A significant minority are also calling for less red tape. Can the Government deliver? Brexiteers fought and won the referendum on a promise to control immigration. Europe's leaders warn they cannot back down over the four freedoms. It therefore remains unclear whether the wishes of growth companies will be met.

Most attractive regions for export growth



What growth companies fear

69%
Economic downturn.

39%
Restricted access to EU single market.

The build-up to the Brexit referendum lasted for what seemed a lifetime and will probably be best remembered for the Leave campaign's dubious spending pledges and Remain's so-called "Project Fear".

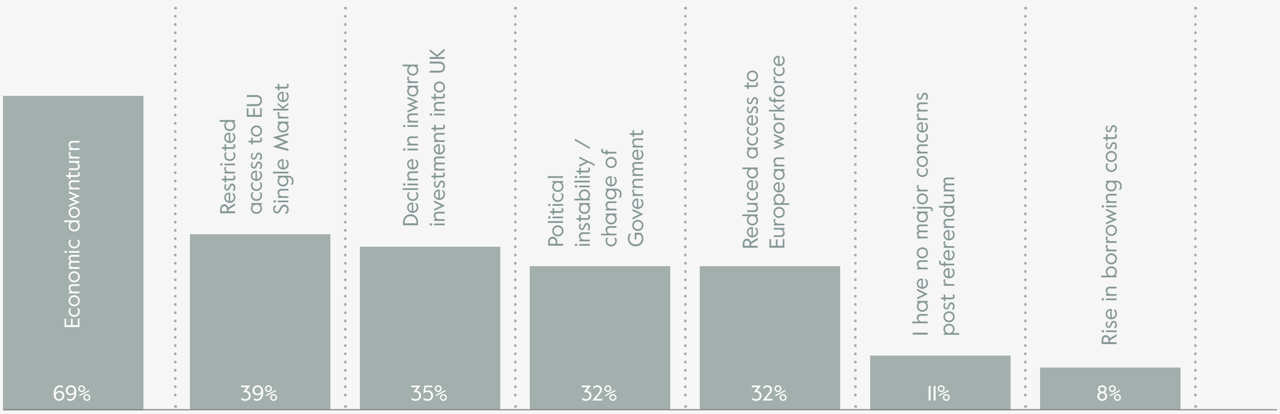
The latter was spearheaded by the former Prime Minister David Cameron and his Chancellor George Osborne, who claimed that leaving the EU would cause an "immediate and profound" economic shock, followed by a year-long recession and the loss of up to 820,000 jobs.

Growth companies clearly now fear recession with mixed economic data suggesting that dark clouds loom over the UK economy. In total, 69% of respondents say that the threat of a downturn is a major concern for them.

Political instability is also a significant fear for 32% of companies and was heightened the morning after the referendum when David Cameron resigned. While his successor Theresa May has seamlessly transitioned into her role, the Government is likely to come under great scrutiny over the coming months and years as the Brexit negotiations begin to take shape. The outlook for the opposition Labour Party is arguably even worse.

One of the most positive messages to come out of the ECI Growth Survey in recent years has been a considerable improvement in access to finance since

Biggest concerns for growth companies



the depths of the financial crisis. It is therefore a major concern that the figures have worsened this year with 51% of companies saying they believe it will be difficult to access finance over the next 12 months, more than double the 22% recorded in 2015. This concern is particularly prevalent in Scotland, with 83% of businesses expecting to find it difficult to access growth finance.

Digging deeper into the numbers, growth companies' appetite for private equity funding, bank debt and the public markets has fallen and the percentage saying they will use internal cash flow to fund growth - a more cautious approach- has edged up from 94% to 96%. Does this mean that growth expectations are lower in the wake of the Brexit vote? We'll explore that in the next chapter.

The Bank of England will certainly hope that the measures it has taken to stimulate the economy - cutting interest rates to a record low and launching more quantitative easing - bear fruit.

As we saw in the previous chapter, more than half of the companies surveyed this year want the Government to support the free movement of labour in its Brexit negotiations with the EU. If this does not happen, many experts believe that the skills gap facing Britain's growth businesses will widen.

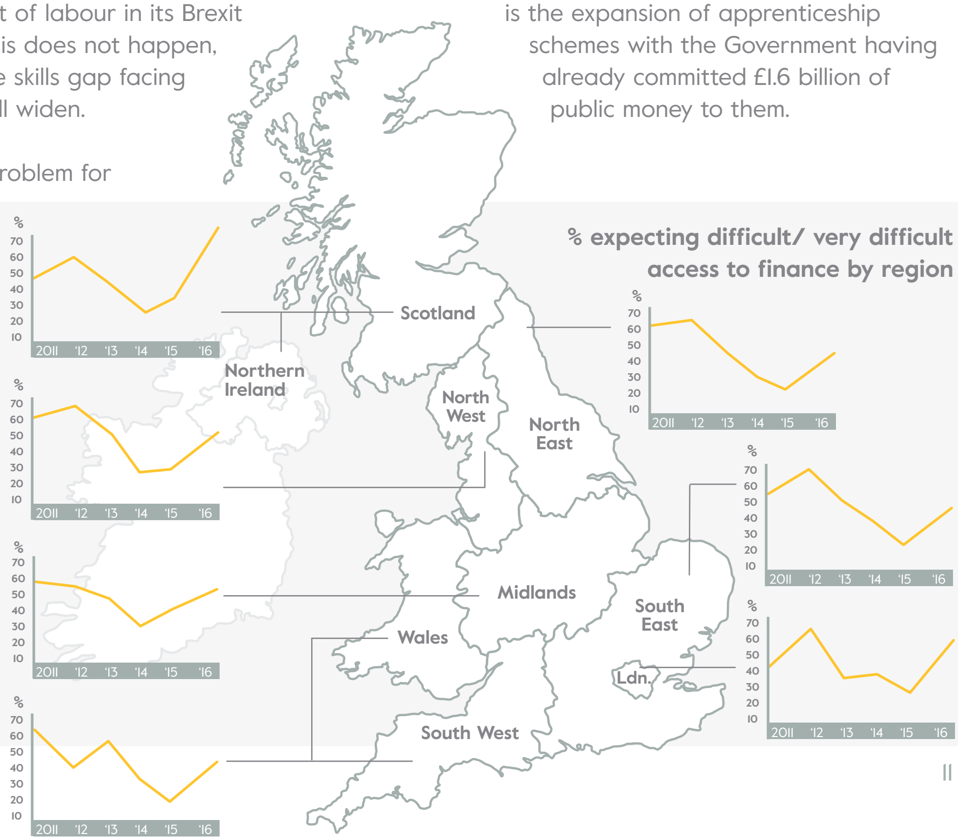
That gap certainly seems a problem for growth companies with 77% revealing that they are experiencing a skills shortage, compared to 91% in 2015. Although this figure has fallen, it remains an important issue and is most acutely felt by healthcare (86%), consumer (85%) and industrials (80%) businesses. Importantly, more than two in three businesses said they support the CBI's policy of encouraging stronger links between business and education bodies in order to tackle skills shortages. Business in the Community, a community outreach charity, has established more than 470 partnerships with businesses and schools in some of the UK's most disadvantaged areas and is working with the CBI to help broaden the base of skilled workers across the country.

> **"The Bank of England will certainly hope that the measures it has taken to stimulate the economy bear fruit."**

Other measures favoured by growth companies include removing the net migration target – the difference between the number of people coming into the UK for at least a year and those leaving - which they say restricts the ability to import talent. Another is the expansion of apprenticeship schemes with the Government having already committed £1.6 billion of public money to them.

51%

of growth companies expect it to be difficult or very difficult to gain access to finance compared to 22% in 2015.



Resilience

80%

of industrials companies expect revenue growth.

16%

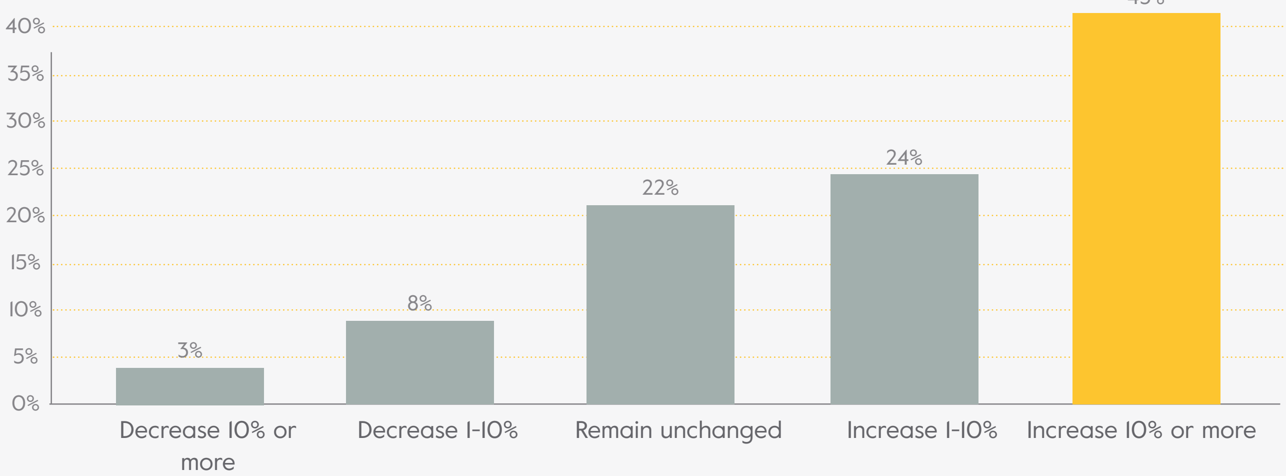
of consumer companies expect revenue to decline.

With so much uncertainty facing Britain's growth companies, it would be no surprise to see many of them putting their pre-referendum expansion plans on hold. Last year's survey made it clear that growth companies were in favour of staying in the EU, with 91% in favour of maintaining the status quo. Over the past two chapters, we've seen that Brexit - with all its implications- is a major concern. However, instead of retreating, businesses are rolling up their sleeves and 'getting on with it': just 11% expect revenues to shrink over the next 12 months whilst more than two-thirds expect revenues to increase, with 43% expecting double-digit growth.

Analysing the numbers in more detail, it is companies in the consumer sector that are the least positive with as many as 16% expecting a decrease in revenues, in contrast to the 80% of healthcare companies, 80% in industrials and 73%% in TMT expecting an increase.

Another positive message coming out of this year's survey is that more companies plan to increase investment and hiring than those that plan to freeze or cut spending. This will be welcomed by those economists and business leaders who fear that Brexit will lead to wide scale job cuts across the country and falling GDP, one of the key predictions made by the Remain camp in the lead up to the vote.

12 month outlook for revenues post referendum



When asked how the outcome of the referendum has affected their outlook, a similar number of respondents predicted no impact (43%) compared to those anticipating a negative effect (46%) demonstrating the resilience of our businesses. The consumer sector appears to be the most impacted with 58% of businesses saying their outlook is more negative, perhaps reflecting a fear that they will be badly impacted by a fall in consumer confidence.

Regionally, companies in Scotland and Northern Ireland are the most pessimistic, with no respondents reporting a positive impact. This is in stark contrast to the North West, where one in four companies responding that Brexit has actively improved the forecasts for their businesses.

Looking ahead, exports are likely to be a crucial growth driver for many companies over the next few months, as a cheaper pound boosts the sale of goods and services overseas. Sterling tumbled to a 30-year low hours after Britain voted to leave the EU and falling interest rates and more quantitative easing here should keep it low.

So, what are growth companies planning to do? Well, nealy half are planning on growing exports in North America (49%), a marginal uptick on 2015. Interestingly however, the amount of companies looking to export to continental Europe has fallen from 53% to 44%.

This could fall even further if Britain loses access to the single market after Brexit negotiations complete.

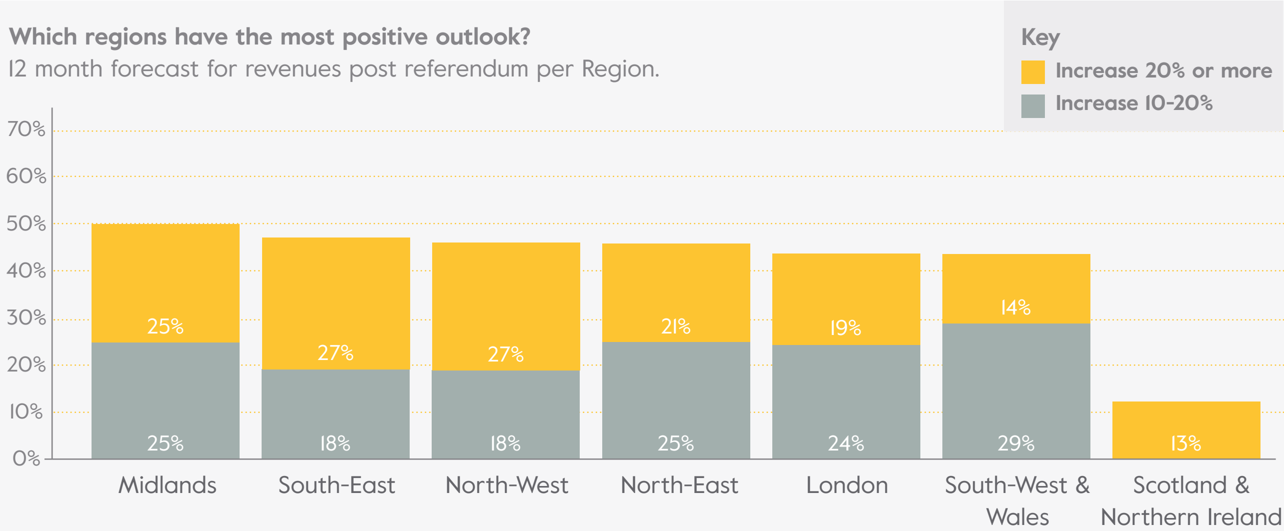
In terms of barriers to exports, it is not surprising that the strength of sterling is no longer cited as a major concern, with just 12% citing it this year compared to 34% last year. Previously cited 'barriers' including "a lack of international expertise" are now less common, falling 24% to 9% year-on-year, as are "overseas regulation", 26% to 12%, and "language barriers", 10% to 2%. This all suggests that our growth companies are becoming more international in their focus rather than concentrating solely on the UK.

> **"Exports are likely to be a crucial growth driver for many companies, as a cheaper pound boosts the sale of goods and services overseas."**

Overall, the message is clear: Britain remains open for business, despite entering into one of the most uncertain periods in its recent history. Our growth companies may have plenty to worry about, but they are also resilient demonstrating that they will continue to invest, grow their headcount and export in order to realise their full potential over the coming years.

Which regions have the most positive outlook?

12 month forecast for revenues post referendum per Region.



Case study
Make It Cheaper

Like most of the entrepreneurs who took part in last year's Growth Survey, Jonathan Elliott, CEO of business utilities savings experts Make It Cheaper, believed Britain was better off remaining in the European Union rather than opting for Brexit.

"I wanted to remain," he says. "But the decision has now been made and we have to be careful not to talk ourselves into a recession."

Founded in 2008, London-based Make It Cheaper has become a firm favourite of British businesses, helping them save an average 20% on their energy, telecoms and insurance bills. Mr Elliott says it is well positioned to deal with any economic slowdown and is on course to have helped its customers save £1 billion by 2018.

"We have a counter-cyclical business model because businesses always need insurance and utilities," he adds. "Our services are important when there's a squeeze on their finances."

As an employer of more than 200 staff in London and a further ten in Merseyside, Mr Elliott admits to having concerns over the future rights of Europeans to work in the UK, especially with a workforce containing staff from across the continent.

However, he does see a silver lining in the clouds. "I think there's a lot of (EU) regulation out that may have originally been well intended, but has been badly executed. It would be good to see the removal of some unnecessary red tape."

"The decision has now been made and we have to be careful not to talk ourselves into a recession."

Jonathan Elliott, founder and CEO

Case study
Ramsden International

Ramsden International has been helping British expats buy home comforts like PG Tips since the 1970s. Part of a family group of businesses, the Grimsby-based company now exports 24,000 products to 130 countries.

Headquartered in an area that overwhelmingly backed Brexit, Ramsden International has an annual turnover of £50 million and overseas offices in six places, including Bangkok, Sydney and Johannesburg. The company's 85 members of staff speak 14 different languages.

Sean Ramsden, the third generation of his family to work in the group, believes it could benefit from Britain's decision to leave the European Union.

"We actually think Brexit will be a positive thing for us," he says. "For a start, we are an exporter, so we have benefitted from the fall in the value of sterling."

"Looking further ahead, our hope is that post-Brexit, Britain will be able to negotiate better trade deals with countries like Canada and Australia as we don't think that the EU has done a good job in this area. This is important to us as we're seeing demand grow at a faster rate in markets outside Europe."

Mr Ramsden agrees with most of the companies taking part in this year's Growth Survey that access to the single market is a must have in Britain's Brexit negotiations with the EU.

"Free trade is a good thing that drives economic growth."

> "Our hope is that post-Brexit, Britain will be able to negotiate better trade deals with countries like Canada and Australia."
>
> **Sean Ramsden, CEO**

Case study
IT Lab

IT Lab, the managed services provider to companies including McLaren, is a poster child for Britain's fast-growing technology sector. Founded by Sebastian Gray in 1998, it has since developed a strong and varied customer base.

IT Lab provides support and expertise to 24,000 people across 860 corporate customers.

The award-winning company provides a range of services including 24/7 support, cloud services, ERP software implementation, technology transformation and change projects, strategic consulting and analytics.

The IT outsourcing market in which it operates is forecast to grow by 8% per annum over the next couple of years, leaving the company well positioned to continue its impressive growth story, which has seen revenues more than double over a three year period.

"As a company, we wanted Britain to remain in the European Union without a doubt," CEO Peter Sweetbaum, says. "Nobody wanted instability or uncertainty."

With workers from all over the world across offices in the UK and South Africa, he adds that the free movement of Labour is an important factor in the company being able to find skilled workers. However, like many other growth companies, he welcomes the prospect of less red tape from Brussels.

But will Brexit ever happen? "I have my doubts that the UK or even Europe will view this as the best outcome," says Mr Sweetbaum. "The growing terrorist threat could mean Europe becomes more reflective about the free movement of people and I'm not sure that Theresa May wants to risk Scotland leaving the UK."

"As a company, we wanted Britain to remain in the EU without a doubt. Nobody wanted instability or uncertainty."

Peter Sweetbaum, CEO

Case study
PCA Predict

Having lost a large chunk of his savings in a business venture at the height of the dotcom boom, Guy Mucklow could have easily thrown in the towel and returned to his successful career in the City.

However, undeterred by the failure of his Pubowner.com business, he persevered and launched PCA Predict in 2000, a company that specialises in selling software that automatically completes online address forms when users enter their postcodes.

With 30% annual growth over the past decade and turnover of £15 million a year, PCA's customer base includes the likes of ASOS and Tesco.

Mr Mucklow says his company will press ahead with plans to invest in the US and Canada, despite Britain's decision to leave the EU, but admits it has been costly. "The fall in the value of sterling since the referendum has added to the costs of funding our US business," he says.

"Another consequence of Brexit is the likelihood of lower interest rates over the long-term and even the possibility of having to pay banks to deposit money with them. It wasn't so long ago that interest received was a decent line item in our accounts earning us £100,000 plus per annum. It could soon become a significant cost centre."

Despite Brexit, Mr Mucklow remains optimistic about his company's future and says he expects the company to maintain its impressive rate of growth.

> "The fall in the value of sterling since the referendum has added to the costs of funding our US business."
>
> **Guy Mucklow, co-founder and president**

Case study

Carfinance247

Louis Rix was destined for a career in the motor trade when he left school at 16. Louis' father runs a car dealership and his grandfather was a car trader in the north of England, so it only seemed natural that he would eventually join them in the industry.

Unlike the rest of his family though, Mr Rix and his brother Reg, swapped the forecourt for the internet launching Netcars2000 at the turn of the century, a competitor to Auto Trader which was acquired by the RAC in 2013.

During their time at Netcars2000, the brothers discovered that consumers were having difficulty finding suitable financing options and, spotting a gap in the online market, they launched Carfinance247 in 2006.

Jointly running a car financing company, Mr Rix is well placed to judge how Britain's decision to leave the EU has affected consumer confidence. Whilst demand for used car finance has held steady since June, he concedes that potential rising debts and unemployment could hit sentiment in the sector.

However, the Bank of England's decision to cut interest rates to 0.25% could boost the industry. "Lower interest rates benefit us as they have a big impact on disposable incomes, which promotes increased consumer purchasing. Unlike new cars, used car sales have always experienced more resilience too."

Having posted revenues of £25m for year-end 2016, Mr Rix is set to press ahead with plans to invest in new headquarters for its growing team, currently at 320, despite economic uncertainty.

"We have no plans to cut investment but will certainly remain cautiously optimistic over the next few months," he adds.

> "Lower interest rates benefit us as they have a big impact on disposable incomes, which promotes increased consumer purchasing."
>
> **Louis Rix, co-founder and director**

Case study
rhubarb

If you've recently enjoyed a luxurious day out at Ascot or Goodwood or maybe an evening at the Royal Albert Hall, then there's every chance you will have enjoyed some of *rhubarb's* culinary delights.

The company, which was founded in 1996, specialises in providing premium food and beverages at iconic locations.

"In today's world every business needs a strong edge to thrive and grow," CEO PB Jacobse says. "Ours is being palpably premium where our clients want something special and are prepared to pay for it."

Although the falling value of sterling post-Brexit has hit some companies, it has also attracted overseas tourists to destinations like London and led to Britons taking staycations. This has proved a boom at attractions like the Sky Garden at 20 Fenchurch Street – otherwise known as the "Walkie Talkie" - another *rhubarb* venue.

"We plan carefully for business challenges, such as Brexit, and are confident that our business model is robust given our focus on the premium market, underpinned by long term contracts," Mr Jacobse says.

rhubarb is now 11 times larger than it was when Mr Jacobse joined the company and has completed its transition from a small owner-managed business into a high-growth corporate company.

"Our customers, both business and consumer, continue to be delighted with what we provide for them," he adds.

"We plan carefully for business challenges, such as Brexit, and are confident that our business model is robust given our focus on the premium market."

PB Jacobse, CEO

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