

How firms across HotSW are preparing for Brexit

Report to HotSW LEP, Devon County
Council and Partners

May 2018

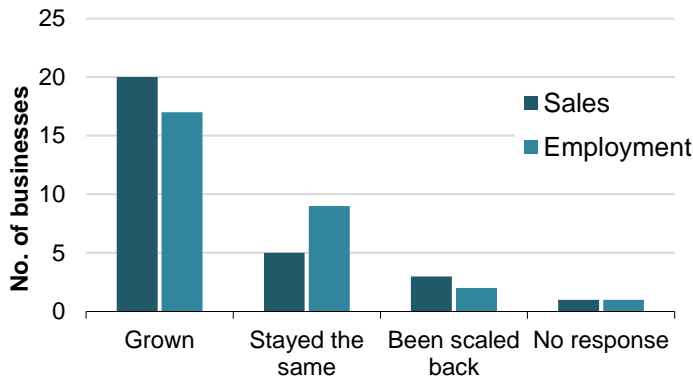
The logo for SQW, consisting of the letters 'SQW' in a bold, dark red, sans-serif font.

KEY FINDINGS FROM THE BUSINESS SURVEY

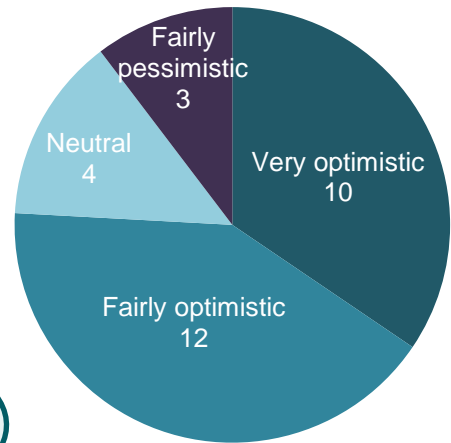
Findings from the 29 businesses consulted across Devon, Somerset, Plymouth and Torbay...

In the last 18 months, the majority of businesses consulted have grown in terms of both sales and employment.

Over the last 18 months...



22 businesses consulted are optimistic about the next two years

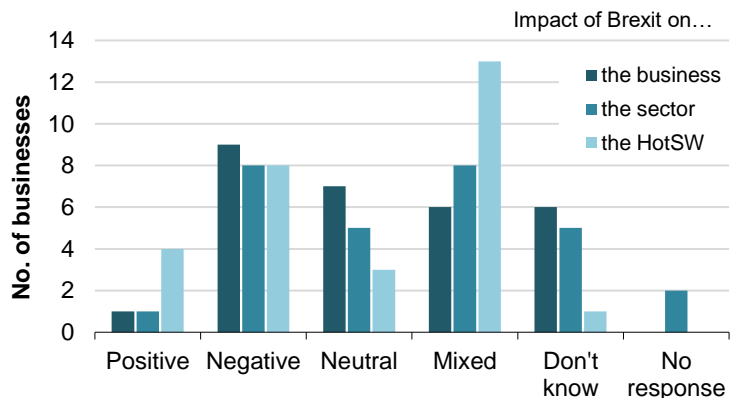


The most common topics being thought about are changes to regulatory alignment and the speed of customs arrangements.



Over two thirds of businesses consulted have done no formal planning for Brexit.

Businesses' assessment of the overall impact of Brexit at this stage is quite varied.



Our overarching finding in relation to businesses' views on Brexit was simply one of uncertainty.

1. Introduction

This research report was commissioned by the Heart of the South West Local Enterprise Partnership (HotSW LEP) and Devon County Council (DCC) to examine how businesses across the HotSW LEP geography are responding to the process of Brexit – Britain’s exit from the European Union (EU).

The research was completed by SQW, an economic development consultancy. It relied on telephone consultations with 29 businesses from across Somerset, Devon, Plymouth and Torbay (see Figure 1-1 below). The businesses surveyed were generally those that have, in the past, had some level of engagement with the upper tier authorities and the LEP. They were not therefore a random sample and should not be seen as representative of the wider HotSW business community. They were however drawn from a wide range of sectors and do therefore provide something of a snapshot from across the economy as a whole.

Figure 1-1: Map of the HotSW LEP area - the focus for the project



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This report was prepared in March and April 2018, drawing on interviews conducted in February and March 2018. The report was thus written almost exactly a year before the United Kingdom is due to leave the European Union (29 March 2019).

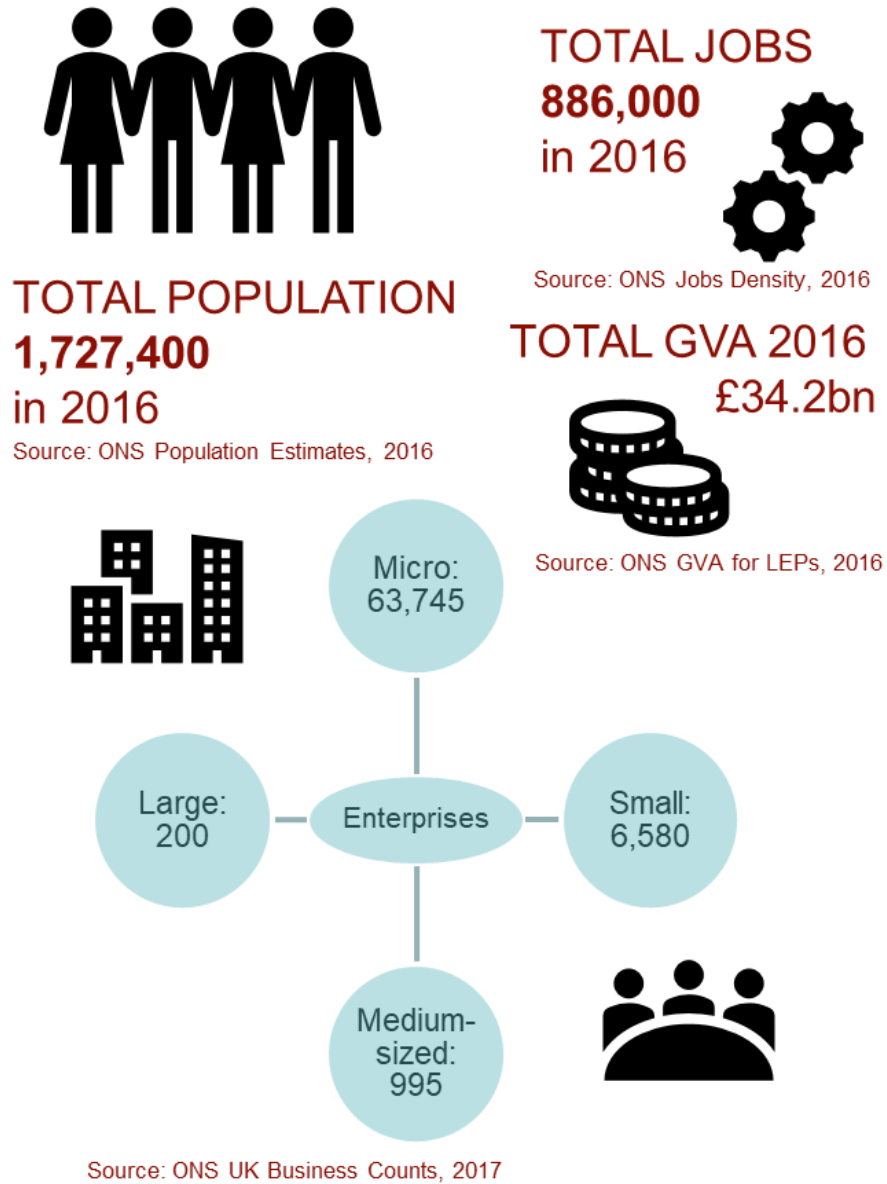
HotSW LEP and DCC intend to repeat this exercise (ideally with the same businesses) in 12 and 24 months’ time. This will help to give a sense of the ways in which firms are adapting as the Brexit process unfolds.

To set the findings in context, Figure 1-2 provides some statistics on the HotSW LEP demography and economy. In 2016, the population of the HotSW LEP was 1.7 million and there were 886,000 jobs. Total GVA for HotSW LEP was £34.2 billion in 2016

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(current prices). The overwhelming majority of enterprises in the HotSW LEP geography (89.1%) are classed as micro-businesses. A further 9.2% are small, 1.4% are medium-sized and 0.2% are large. The sectors with the largest numbers of enterprises are agriculture, forestry & fishing (11,795 enterprises), construction (9,345) and professional, scientific & technical (8,955).¹

Figure 1-2: Heart of the South West LEP demography and economy



¹ Data sourced from ONS

2. Business profile

This section describes the profile of businesses consulted by SQW for this project. With inputs from the local authorities, efforts were made to ensure a good geographical spread across the four (upper tier) local authority areas of Devon, Plymouth, Torbay and Somerset, and to collect the views of firms from a range of sectors.

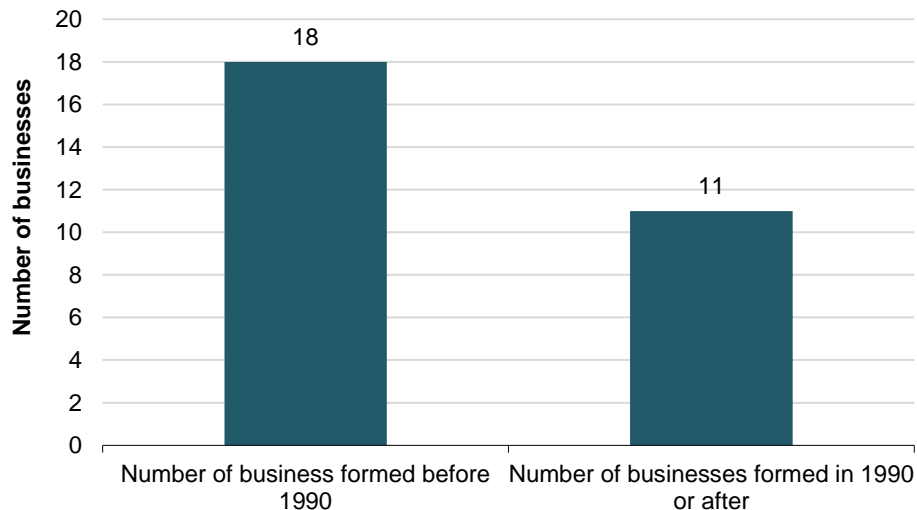
Some 29 businesses from across the HotSW geography were consulted: 12 were in Devon, nine in Plymouth, six in Torbay and two in Somerset. Table 2-1 shows the spread of sectors of activity for the businesses that were consulted.

Table 2-1 Business sectors of activity

Sector	Number of businesses
Manufacturing	5
Professional, scientific and technical activities	5
Food and drink	4
Transport	3
IT technology/software	3
Advanced manufacturing	2
Hospitality	2
Engineering	2
Wholesale	1
Creative	1
No response	1

Figure 2-1 provides information on when the businesses were formed. The majority of businesses consulted were well-established, with 18 formed before 1990 and the remaining 11 formed in 1990 or since then.

Figure 2-1: Year of formation



Most consultees have their main UK site in the HotSW area

Businesses consulted were of varying size but the majority employed some EU nationals

Near the start of the consultations, businesses were asked whether the HotSW LEP area is the location of the main site of their business in the UK. The overwhelming majority of consultees agreed that it was (27) – which is important because it is likely to mean that decisions (relating for example to Brexit) are made locally.

Data were also collected on the number of staff at their site in the HotSW area. Figure 2-2 shows that the businesses consulted varied in size. Using the categories developed by the ONS UK Business Counts dataset, 12 of the businesses consulted fall within the “micro” (0 to 9 employees) and “small” (10 to 49 employees) categories, while a further 12 are “medium-sized” (50 to 249 employees). The remaining five businesses fall within the “large” (250+ employees) category. Figure 2-2 shows that a majority of the businesses consulted (21) employed EU nationals. However, for individual firms, this was generally a small proportion of all employees.

Figure 2-2: Number of employees and whether any are EU nationals

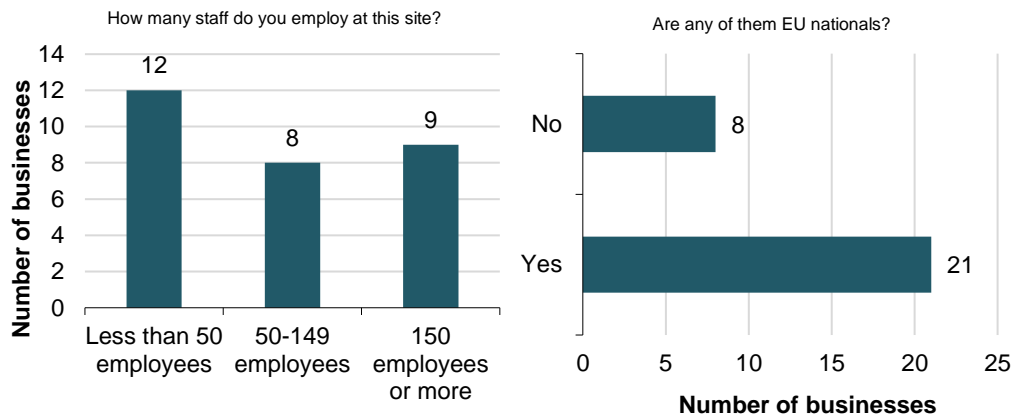
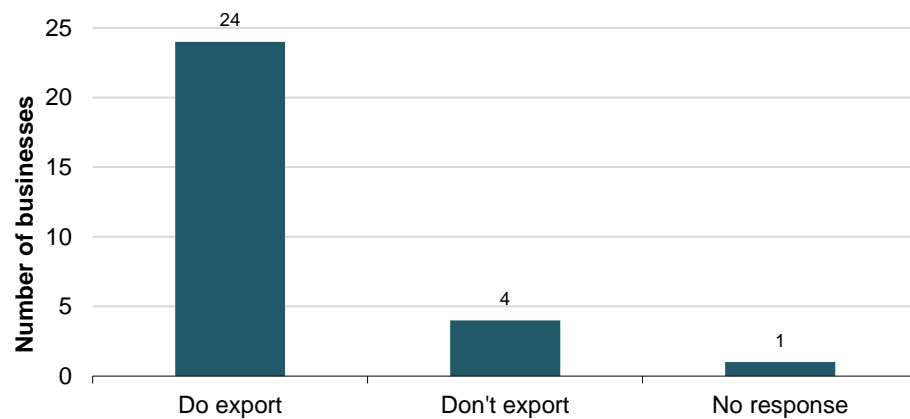


Figure 2-3 shows that 24 of the businesses consulted are currently exporters, either to elsewhere in the EU or outside the EU. For 17 of these businesses, exports account for more than 10% of sales. It should be noted that in the HotSW area as a whole, around 25% of businesses engage in export activity. There are therefore differences between the group of firms interviewed for this study and the population of businesses as a whole.

Figure 2-3: Exporting activity



24 of the businesses consulted are exporters

Summary

Overall, the 29 businesses consulted were generally quite well-established, of varying size, locally controlled, and mostly engaged in some level of exporting. Most employ EU nationals but generally not in large numbers. It is important to acknowledge that this profile differs from the average across HotSW, where the majority of enterprises are micro-businesses.

3. Main findings

This section provides an overview of the main findings from the consultations. The businesses were asked a series of questions to explore their past and future growth and their current thinking in terms of how Brexit will affect their business.

In the 18 months since the referendum on EU membership in June 2016, the majority of businesses consulted have grown in terms of both sales and employment (Figure 3-1). Within this, more businesses have seen sales grow (20) than employment (17). Nine businesses have seen employment stay the same, while five businesses reported broadly unchanged sales.

In the last 18 months, the majority of businesses consulted have grown in terms of both sales and employment

Figure 3-1 Past growth of businesses in terms of sales and employment

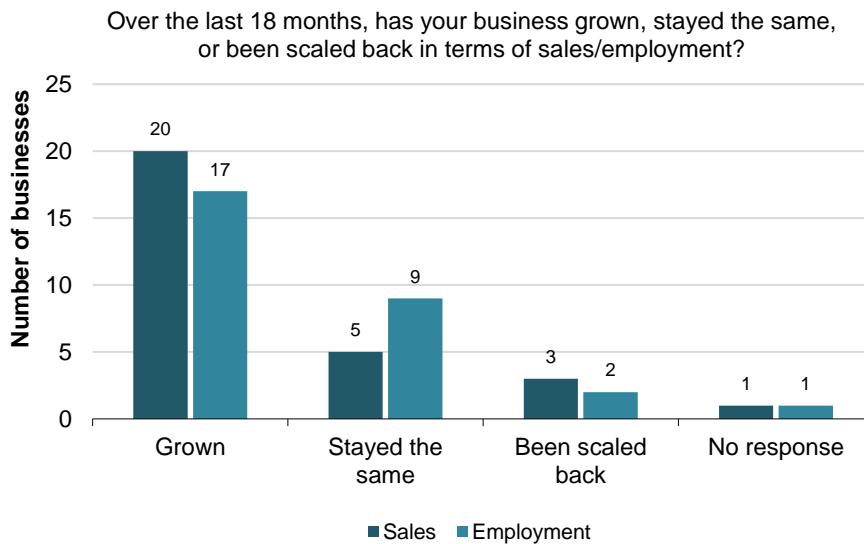


Figure 3-2 shows that three-quarters of the businesses consulted were “very” or “fairly optimistic” about the next two years. The main reasons for this optimism were: businesses' growth trajectories and recent investment; not being dependent on EU markets; their confidence in levels of demand for their product/services; and/or the opportunity that Brexit represents. Seven businesses were “neutral” or “fairly pessimistic” about the next two years. Reasons given for this included the uncertainty surrounding the final Brexit deal and the increased cost of importing goods and materials from Europe.

22 of the businesses consulted are optimistic about the next two years

Figure 3-2: Businesses' optimism about the next two years

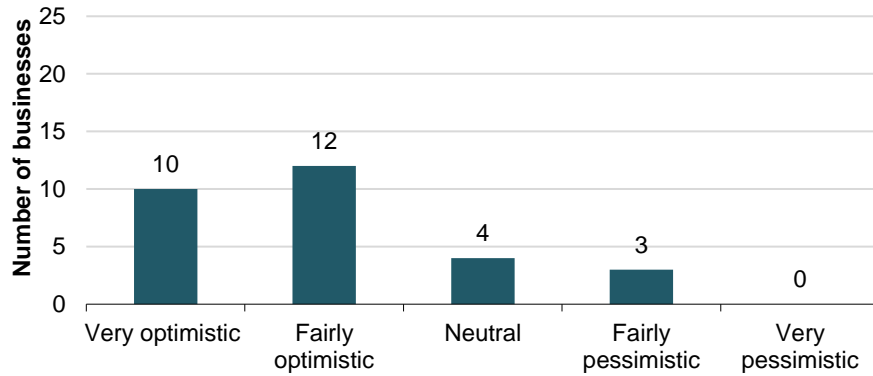


Figure 3-3 shows the future growth expectations of the businesses over the next two years. Almost all were planning on investing in new capital equipment, while 20 out of the 29 businesses were planning on taking on more staff. The balance between the two may have implications for productivity.

Figure 3-3 Expected growth in terms of recruitment and investment in the next two years

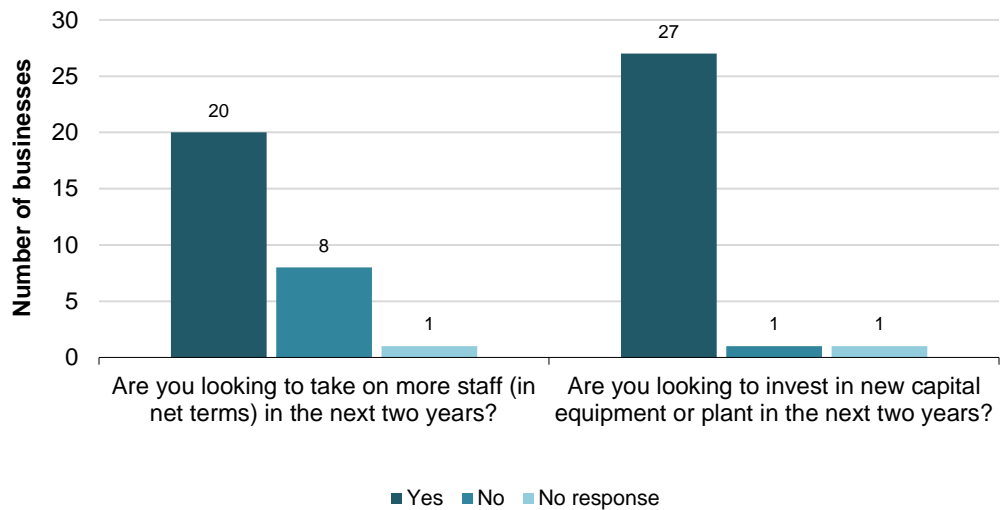
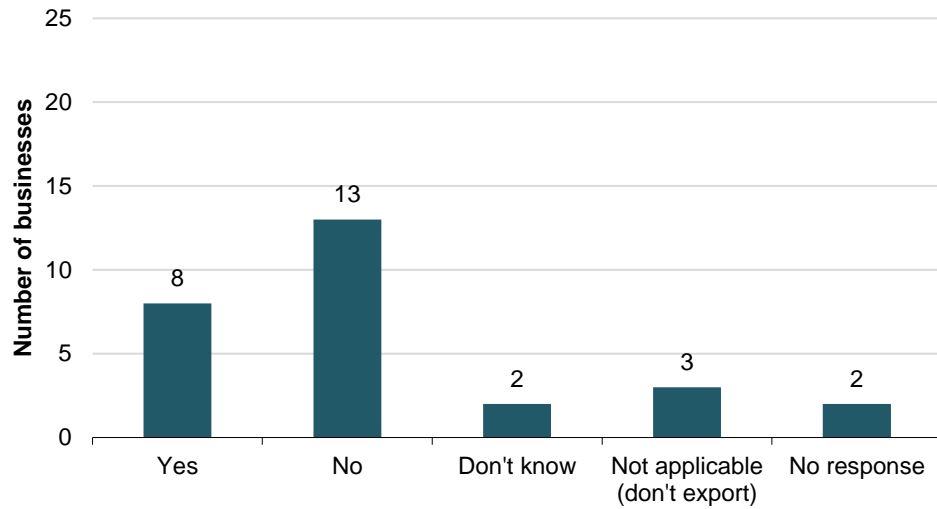


Figure 3-4 shows that among the businesses that export, 13 did not think that the image of British products in their export markets had been affected by the Brexit process so far, while eight thought it had been affected.

In the next two years, 27 businesses are expecting to invest in new equipment and 20 are expecting to take on more staff.

Figure 3-4 Do you think the image of British products in your export markets has been affected at all by Brexit so far?



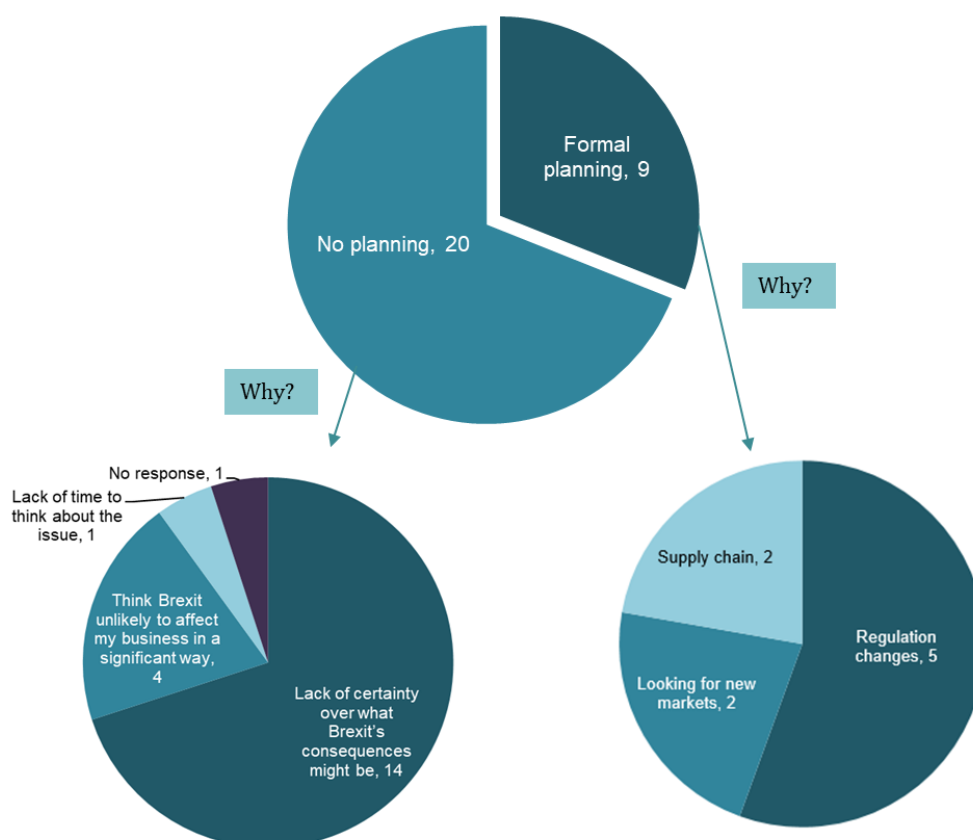
Most of businesses consulted had not yet done any formal planning for Brexit.

Figure 3-5 shows that the majority of businesses consulted had not yet done any formal planning for Brexit. The main reasons given for this were:

- that there is a lack of certainty over what Brexit's consequences might be;
- that Brexit is unlikely to affect the business in a significant way; and
- that the business has lacked time to think about the issue.

The main reasons given by the nine businesses that had started planning were: changes to regulation, supply chain issues and the need to search for new markets.

Figure 3-5: How businesses are preparing for Brexit



Source: SQW analysis of consultations with businesses

Table 3-1 shows that businesses have been consulting a number of different sources in order to find information about the possible effects of Brexit. The most frequently cited sources were trade bodies or associations (8), publicly available or national media (7) and informal discussions with other business people (5).

Table 3-1: Main source of information about the possible effects of Brexit on your business

Source of information	Number of businesses
Trade bodies or associations	8
Publicly available and national media	7
Informal discussions with other business people	5
Have in-house staff working on the subject	4
Professional advisers (lawyers, accountants etc)	3
Government/LEP	2

Source: SQW analysis of consultations with businesses

Businesses have been consulting a variety of sources for information about Brexit.

During the consultations, businesses were asked to consider ten possible changes related to Brexit and were asked to rank them on a scale of 1 to 5 in terms of how hard they were currently thinking about them (where “5” was a topic they were thinking very hard about and “1” was a topic they were giving much less thought to). Table 3-2 below uses the mode² to identify the most common response given for each of the ten.

The two possible changes that businesses were giving the most thought to were “changes to regulatory alignment in their sector” and the “speed of customs arrangements at national borders”. When asked to explain why they were thinking about changes in regulations, several stated that at present, their business needs to comply with EU regulations. If, however, the UK was to diverge from the EU framework after Brexit then businesses would need to comply with another set of regulations and this could add complications. Similarly, a large proportion of businesses thinking about the speed of customs arrangements at national borders were concerned about being able to deliver their products to customers in a timely manner.

The most common topics being thought about are changes to regulatory alignment and the speed of customs arrangements.

Table 3-2: How hard are you thinking about the following topics in relation to Brexit?

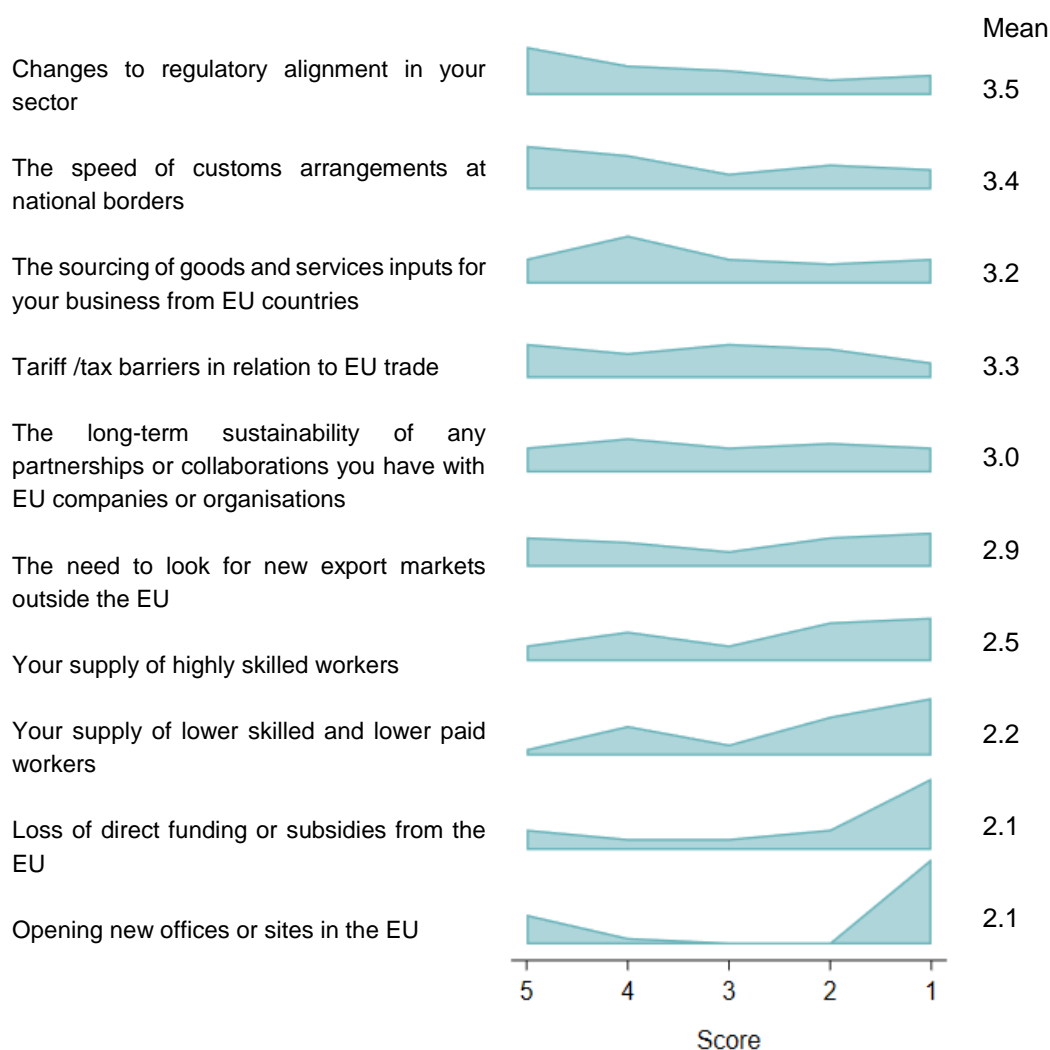
	Mode	
Changes to regulatory alignment in your sector	5	["thinking very hard about it"]
The speed of customs arrangements at national borders	5	
The sourcing of good and services inputs for your business from EU countries	4	
The long-term sustainability of any partnerships or collaborations you have with EU companies or organisations	4	
Tariff /tax barriers in relation to EU trade	3	
The need to look for new export markets outside the EU	1	
Your supply of highly skilled workers	1	
Your supply of lower skilled and lower paid workers	1	
Loss of direct funding or subsidies from the EU	1	
Opening new offices or sites in the EU	1	["giving little thought to it"]

Figure 3-6 presents the same information in a different way. It shows the distribution of responses when consultees were asked to rank the ten possible changes related to Brexit. The height of the charts fluctuates depending on the percentage of respondents giving each score (excluding those that thought the change was not applicable to their business). It suggests that the businesses in aggregate are giving least thought to “opening new offices or sites in the EU” or “the loss of direct funding or subsidies from the EU”.

² The mode is the value that appears most often in a set of data.

The mean³ value of the responses is also provided in Figure 3-6 below. The mean paints a broadly similar picture to the mode.

Figure 3-6: How hard are you thinking about the following topics in relation to Brexit?



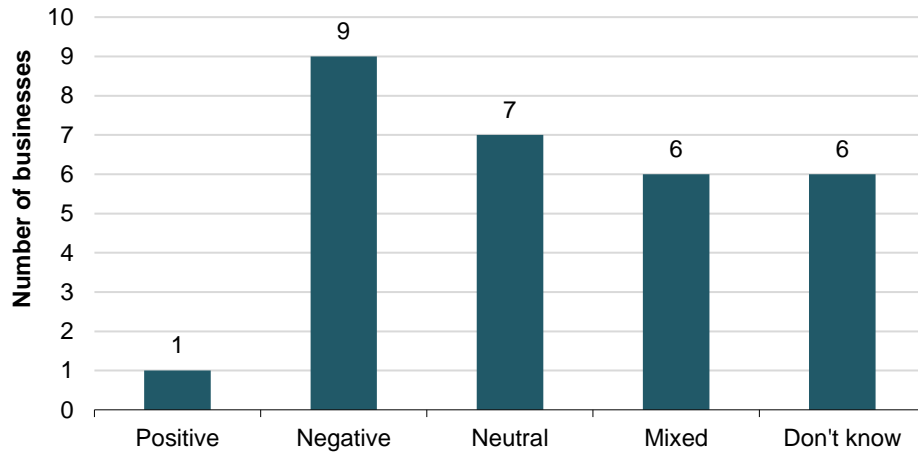
Assessments of the overall impact of Brexit on businesses at this stage are quite diverse.

Figure 3-7 below summarises the responses to what businesses thought the overall impact of Brexit would be **on their business**. Out of the 29 businesses questioned, one considered that Brexit would have a positive impact on their business, nine thought that Brexit would have a negative impact, seven said that Brexit's impact would be neutral, six thought it would have a mixed impact and six were unsure. There were, therefore, a wide range of views.

The businesses that anticipated negative impacts gave a variety of reasons. These included: the problem of sourcing employees from abroad, increased costs associated with the fall in the value of the pound, and/or the possibility of being isolated from EU markets. Those businesses that were neutral generally thought that the impact of Brexit on their business would be minimal.

³ The mean is the sum of the numbers divided by how many numbers there are (also commonly known as the average).

Figure 3-7: What is your overall assessment at this stage of the likely impact of Brexit on your business?

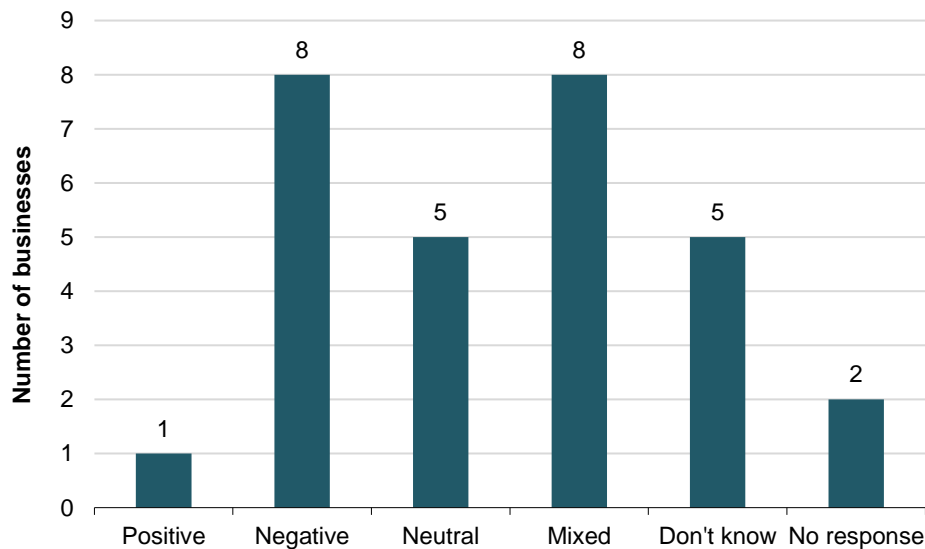


Nine businesses expect Brexit to have a negative impact on their sector.

Figure 3-8 below summarises the responses to a question asking businesses about their overall assessment at this stage of the likely impact of Brexit **on their sector**. Of the 29, one thought that Brexit would have a positive impact on its sector, eight thought that the impact would be negative, five anticipated a neutral impact, eight thought its impact would be mixed, while five were unsure.

The general feeling was that Brexit's impact could range from negligible to significant, with the eventual outcome being heavily dependent on the shape of the Brexit settlement (which was unknown at the time of our fieldwork). For the eight businesses which thought that Brexit would have a negative impact on their sector, the reasons given mirrored those given identified in relation to their own business (i.e. problems around sourcing employees from abroad, increased costs due to the value of the pound having decreased and/or future problems in accessing EU markets).

Figure 3-8: What is your overall assessment at this stage of the likely impact of Brexit on your sector?

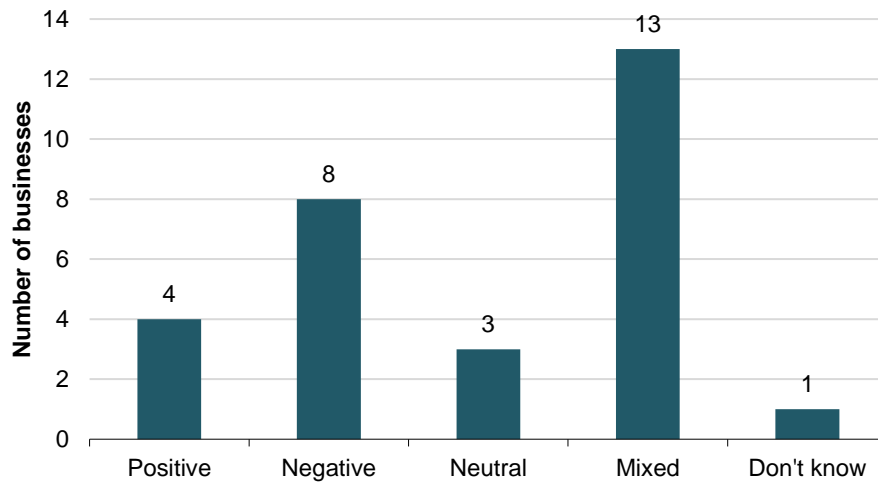


Four businesses consulted expect the impact of Brexit on the HotSW area to be positive – mainly because they think it will benefit tourism.

Figure 3-9 below summarises what businesses thought the overall impact of Brexit would be **on the HotSW area** itself. Four businesses thought that Brexit would have a positive impact on the HotSW area, eight thought its impact would be negative, three expected it to be neutral, 13 anticipated a mixed impact and two were unsure.

The reason given by all the respondents that answered positively was that Brexit presents an opportunity for the area's tourism sector. The reasons given by those that answered negatively were more varied. Some were concerned about the future of EU funding in the area, while others thought that the farming and agriculture sectors could suffer.

Figure 3-9: What is your overall assessment at this stage of the likely impact of Brexit on the HotSW area as a whole?



4. Perspectives of individual businesses

This section describes five case studies (drawn with permission from the 29 consultations) to explore in more depth how individual firms from a variety of sectors are thinking through a range of issues related to Brexit.

Case Study: **SC Group**

Supacat was formed in 1981, originally with a focus on off-road wheeled and tracked vehicles for the defence sector. Subsequently the company grew (mostly organically but also through acquisition) and diversified. In 2015, it created a Group structure (SC Group) with four separate companies: Supacat (designing equipment (including vehicles) for use in harsh environments for defence purposes); SC Innovation (engineering design in other sectors); Proteum (which represents and distributes a portfolio of marine products and services across UK and Ireland) and Blackhill Engineering (an engineering company that provides services including large fabrication and complex machining assembly). As of 2018, the company employed 120 people at its site near Honiton, a market town in East Devon. It also has a small facility in Australia.

Supacat makes up around 80-90% of SC Group and continues to have a strong focus on the defence sector. There is a strong pan-European dimension to defence and it is unclear how this will change following Brexit. It is possible that there will be increased collaboration in defence between remaining EU members, particularly between France and Germany. For UK defence firms, this could be challenging.

Despite uncertainty about what form Brexit will take, SC Group has had many internal discussions around the topic and has been thinking through the possible implications of Brexit. An issue the Group is giving much thought to is how Brexit could affect its supply chain. Currently, some core components are sourced from Europe and existing relationships could be affected by changes in trade arrangements and regulations.

Case Study: **Applied Genomics**

Applied Genomics is one of about 25 small firms based at the Brixham Laboratory in Torbay. Brixham Laboratory was formerly an Astra Zeneca facility and is now owned by Plymouth University.

Applied Genomics provides ecological assessment services including: environmental DNA analysis services for biodiversity monitoring; environmental impact assessment; biosecurity surveillance; and threatened species detection. It is an early-stage micro SME. The business was established in the Torbay area in January 2016 and is supported by a panel of scientific advisors. The firm has undertaken extensive research and development and now has ambitious growth plans.

Currently, all of its sales are in the UK; however, as the environmental genomics market develops, there should be scope for growth internationally. Expansion within the EU single market would be the most obvious starting point. The extent to which this is possible will depend on the nature of the Brexit settlement.

More generally – and despite its small size – Applied Genomics already recruits internationally, reflecting in part its highly specialist activities. In delivering its business plan, international recruitment is likely to continue to be important.

The business has been unable to undertake any formal planning for Brexit, largely due to the continued uncertainty around what the final deal will be. However, it has been thinking hard around some key topics linked to Brexit. Given its focus, the UK's future relationship to EU regulations relating to maintaining strong environmental standards will be of critical importance for Applied Genomics and the wider environmental services industry.

Case Study: **Salcombe Gin**

Salcombe Gin was incorporated in 2014 by two friends, Howard Davies and Angus Lugsdin. They met in the mid-1990s whilst both were teaching sailing at Salcombe Yacht Club. Salcombe Gin started trading in 2016, producing and selling high quality gin as well as opening a shop, a bar and, more recently, a Gin School. Since 2016, the company has grown rapidly, both in terms of sales and employment. It is just starting to export its product. The whole operation, an office and the distillery, is located in and around Salcombe in south Devon. The company currently employs around 20 people.

Overall, the company feels confident in its product and UK sales and is optimistic about opportunities to grow in the next two years. Due to the current uncertainty, the company has postponed formal planning in relation to Brexit. However, tariffs are an issue that the company has been thinking about in this context. Tariffs might affect both products imported from the EU and the company's recent venture into export sales to the EU. They might mean that it looks to other markets outside of the EU to continue to grow its business. More generally, the company observed that many manufacturers in the drinks industry export, and changes to tariffs may affect the pricing of UK beverage products overseas. Although still uncertain, there is some concern that this could affect the industry's export performance as a whole.

Case Study: **Hymid Multi-Shot Ltd**

Hymid Multi-Shot Ltd was established in 1989. It offers innovative design, precision tooling and technical injection moulding services to a blue-chip customer base spread across four different sectors: healthcare, instrumentation, consumer and electronics. The firm's state of the art production facility is in Torquay and 48 people are currently employed there.

The firm's customer base is spread across the UK and Europe, so its operations have a pan-EU dimension. Hymid Multi-Shot sources polymers from the UK and elsewhere in the EU, which are then processed and moulded into plastic components, and then supplied to manufacturing and assembly plants in the UK and Europe. Some European finished goods that contain components made by Hymid are then imported back to the UK for sale. Given the international nature of this process, changing tariffs and customs arrangements may affect the firm's ability to take products to market in a cost-efficient manner.

Hymid Multi-Shot remains cautiously optimistic about the next few years. Despite all the uncertainties, it has started formal planning for Brexit. Firstly, this is focusing on

addressing future supply chain challenges by reducing its dependence on Euro denominated raw materials. Secondly, it is focusing on diversifying its customer base by broadening and deepening working relationships to anticipate and help resolve its customers' own issues with Brexit. These changes are part of the firm's response to Brexit.

Case Study: Condition Monitoring Group Ltd

Condition Monitoring Group Ltd comprises four brands: Beran Instruments, Helitune, SEI and Prosig. The Group specialises in vibration analysis and the science of structural and rotating machinery condition monitoring for the aviation, automotive and power industries.

The head-office is located in Great Torrington, Devon and currently, 90 staff are employed there. Around 55% of the company's sales derive from export markets (and just over half of these are from outside the EU).

Condition Monitoring Group Ltd considers that Brexit will not have a substantial impact on its business. This is partly due to a strategy it initiated before the UK decided to leave the EU. This strategy involved the creation of both German and Italian subsidiaries, reflecting local markets and the location of key collaborators. Having a local presence in these key territories means that the company is well positioned to manage the consequences of Brexit. These businesses also provide insights into how Brexit is being reported by the German and Italian media – which often differs from what is reported in the UK. As a result of Brexit the company is currently considering formation of an additional subsidiary in France as it is an important strategic territory.

The weakness of sterling is beneficial to Condition Monitoring Group as a net exporter. However, one key issue the company is thinking about in relation to Brexit is the impact of changes to regulatory alignment in its sector. Currently, it has to comply with regulations in the EU and USA. If, after leaving the EU, the UK creates its own regulations, the business will have to respond, creating a potential downstream challenge.

5. Conclusion

This project has been based around a relatively small number of discussions with businesses from across the HotSW area – 29 in total. It cannot claim to be representative of all businesses in the area. It does, however, provide a snapshot of the issues businesses are thinking about as of spring 2018.

Our overarching finding in relation to businesses' views on Brexit was simply one of uncertainty. At this stage in the process:

- relatively few firms had done any formal planning for the effects of Brexit, simply because it was unclear what they might be planning for. That said, most appeared to have devoted a good deal of thought to the surrounding issues, drawing on information/insight from a wide range of sources
- in terms of the expected impacts from Brexit, there was a fair degree of ambivalence: whilst rather more firms concluded that the ultimate impacts might be negative than positive, the largest group overall was that which assessed impacts in terms that were “neutral/mixed” or simply “unknown”
- however, the backdrop to all of this was a group of businesses that had grown over the recent past and were – in the main – quite optimistic about their own future growth prospects.

The intention is that the survey will be repeated in 12 and 24 months' time. This will provide an insight into how firms' thinking changes as the Brexit process moves forward. In 12 months' time – if all goes to plan – the UK will no longer be part of the European Union.

In this context, one final point is worth drawing out: from our 29 consultations, the EU's influence on the day-to-day process of doing business was described in very many different ways (from regulatory frameworks, to customs and tariff arrangements, and to recruitment and labour supply) and that influence appeared to be pervasive. For a period of over 40 years, EU membership has fundamentally shaped how business is done in the UK; the Brexit settlement will be agreed by national government in this context. Whatever the formal outcome, 70,000 enterprises across HotSW will each need to develop their own response. By March 2019, there ought to be greater clarity in terms of what this might mean in practice – and the consequences that could follow at the micro level and in aggregate.

Overarching finding of businesses' views on Brexit is one of uncertainty.

Consultations uncovered the pervasive influence the EU has had on the day-to-day process of doing business.