MHA Manufacturing Newsletter

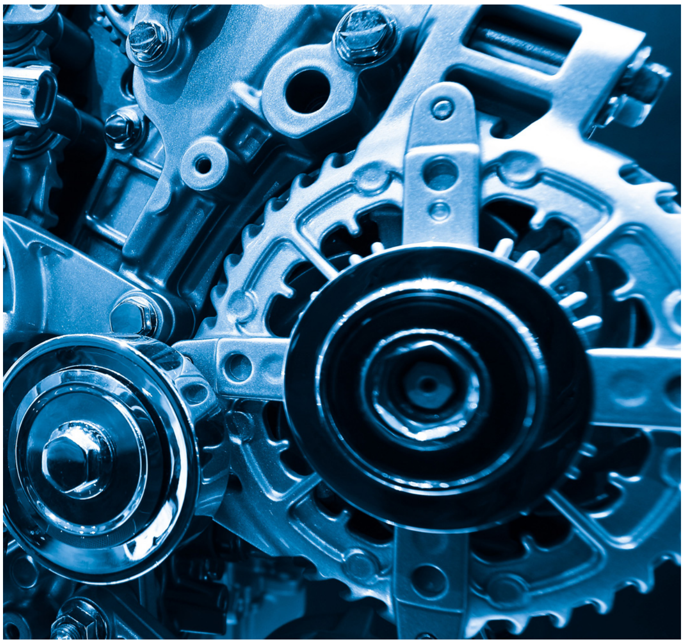
August 2012

About MHA

MHA is an invitation only UK wide association of progressive and respected accountancy and business advisory firms. Each MHA member firm offers a broad range of services including accountancy, tax and corporate finance, as well as sector specialisms, and work collaboratively under the MHA banner when clients have multiple locations or specific national needs.

MHA firms are characterised by their strong regional reputation for providing outstanding accountancy and business advice to entrepreneurial businesses. With 37 nationwide offices MHA is able to balance national access and capability with the local insight and perspective that individual member firms offer their clients.

As well as our national presence MHA is a member of Morison International, giving access to a global network of trusted advisers which is especially important to the manufacturing sector with the push to re-balance the UK economy.



MHA Manufacturing Survey 2012
Six Month Review

Although the government has stressed the importance of the manufacturing sector to the process of economic recovery, many are still sceptical as to whether this has translated into positive action. Indeed, data from the July Markit/CIPS purchasing managers' index (PMI) showed that manufacturing production shrank at its fastest rate since 2009. Its findings also suggested that the sector still has further to contract before we see any recovery.

However, the quarterly National Barometer report from the Manufacturing Advisory Service gives a conflicting view. Its findings paint a more positive picture of the sector, saying that over half of its respondents had experienced an increase in orders over the last 6 months with the same number predicting a similar rise before the year is out.

The MHA Manufacturing and Engineering Survey Report in January 2012 highlighted a number of key industry concerns. Most worrying of these was the perceived lack of government strategy, as well as little understanding of the support available for the sector. Six months on, we take a look at some of the key findings of the 2012 report and the changes we have seen since then.

Government strategy

The MHA survey highlighted a perceived lack of government strategy with more than 90% of those surveyed believing there was no national strategy in place for the sector. As a result of this troubling statistic, MHA entered into a number of conversations with Government ministers. These were met by the reassurance that manufacturing had been placed at the centre of the economic strategy with campaigns such as Make it in Great Britain, “aiming to transform the image of modern British manufacturing and to raise awareness of its importance for the economy”. Responses to the 2013 survey will hopefully show the effectiveness of such campaigns over the coming 6 months.

Growth in export markets

One of the survey’s encouraging findings was the amount of export activity being undertaken, particularly for SMEs. 72% of those surveyed were already actively exporting, with Asia coming second to the eurozone as an export destination. Tensions around the eurozone have been ever present in 2012 and companies are increasingly looking to traditionally higher risk markets to maintain their competitive advantage. One respondent suggested it was necessary to "significantly increase awareness of export opportunities in high growth markets."

However, the Eurozone crisis has had repercussions around the world with slow growth reported in the manufacturing sectors of the US, India and China. Initiatives launched this year by UKTI, such as the Gateway to Global Growth have been implemented in order to support SMEs in their overseas expansion plans. In addition, MHA offers an Export for Growth guide for both experienced exporters and those taking their first steps. The guide highlights the gains to be had, as well as the potential pitfalls to be aware of.

With a wider pool of support for those who do export or are considering it, we should see an increase in confidence among manufacturers with regards to their trading relationships.

Support for the manufacturing industry
Whilst the survey highlighted respondent's lack of awareness of the assistance available to them in the form of grants, it also stressed the increasing strain in banking relationships. 42% of respondents felt that their bank was not providing adequate support, with a lack of access to funds being the main area of tension. Despite the difficulties, the report indicated that only 20% of respondents intended to change or had recently changed their bank. It remains to be seen whether initiatives such as the launch of the Funding for Lending scheme and the announcement of a further £50bn of quantitative easing will do anything to reverse this trend in the 2013 survey.

Where next?
With Government pledges to recognise the importance of the manufacturing sector in revitalising the current economic climate, it is hoped that the 2013 MHA Manufacturing & Engineering Survey will provide a more positive outlook for the sector.

MHA will be conducting its 2013 Manufacturing and Engineering Survey in January. If you are interested in taking part in our survey or receiving a copy of next year's report please email hannah.fish@mhllp.co.uk

Lean Manufacturing

By Steve Cartwright from MHA member Henderson Loggie

One of the most significant issues to come out of the 2012 MHA Manufacturing and Engineering Survey was that only 40% of respondents have, or intend to introduce lean manufacturing processes.

Over the last 20 years the manufacturing and engineering sector here in the UK has been hit hard by competition based in regions of the world where labour rates and general operating costs are significantly lower than here in the UK; Eastern Europe, the Indian sub-continent and China. To remain competitive with these low cost competitors many UK based manufacturers have reacted by either outsourcing their manufacturing to sub-contractors operating in these regions or by creating their own manufacturing facilities in these regions, offshoring. Both options result in job losses in the UK, not just for the companies themselves but also within their supply chains.

The UK is not the only economy to have suffered this, most of Western Europe and the US has seen similar trends. In a recent article Jeffrey Immelt the CEO of GE one of the world's largest companies stated that GE

- was outsourcing less and producing more in the US;
- had created more than 7,000 manufacturing jobs in the US in 2010 and 2011;
- had announced its first new product line in the US in 50 years followed by a similar announcement six months later; and
- had announced they would create 4 US Centres of Excellence for the design and manufacture of refrigerators creating thousands of new jobs.

One of the keys to this success story was GE's adoption of lean manufacturing to **improve competitiveness**. In 2009 GE used lean methodologies to redesign a 25 year old dishwasher line which resulted in

Labour efficiency **improved by 30%**
Inventory **reduced by 60%**
Time to produce **reduced by 68%;** and
Space required **reduced by more than 80%**

If GE can achieve these results by reducing waste and making manufacturing a competitive advantage in the US, then why aren't the majority of UK businesses applying this approach?

Whilst the above results are spectacular, research shows that for a typical business, up to **20% of total costs** can be classified as waste. Waste is defined as being any activity that consumes resources/incurs expenditure that does not add value for the end customer. In very simple terms, lean is a methodology for identifying waste and reducing/eliminating it.

The purpose of this article is not to get into the detail about lean practices, however one aspect of lean that should not be underestimated is this; Lean is management philosophy that will require every element of an organisation to change and to be applied successfully will require commitment and strong leadership.

The business environment is extremely competitive and this is not going to change, therefore if UK manufacturing and engineering sector is to grow and prosper, it must be competitive. GE has proved it can do this in the US, the UK has some of the most productive car plants in the world and the common denominator, lean.

Why then would your business not have plans introduce lean manufacturing?

Developing an appetite for developing Markets (as published in Fresh Business Thinking)

Recognition by the Prime Minister David Cameron that overseas trading relationships should be strengthened echoes many voices in the manufacturing industry. His recent official tour of Asia and 2010's trade mission to India reinforces the Government's commitment to strengthening trade links and encouraging UK businesses to export to ensure growth during stringent economic times and when emerging from recession. Optimism among SME manufacturers is already high with almost 80% predicting growth over the next 12 months, indicates research from MHA*, the UK wide group of independent accountants and business advisers. More encouragingly, many of those surveyed are recognising the importance of international trade with 72% currently exporting. While much of this activity is centred on the Eurozone, more and more companies are embracing the challenges surrounding developing markets to drive growth in sluggish domestic markets. The key findings of the MHA Manufacturing and Engineering survey indicated an interesting trend in export location with marginally more respondents exporting to Asia than North America. Africa was also cited as an export destination for 30% of the respondents. "Despite this activity more must still be done to ensure that manufacturers are aware of the opportunities of new markets" comments Mike Brown, Chairman of MHA. "41% of respondents felt that better understanding was needed particularly around exporting and local partners and regulatory issues also proved a concern." When it comes to international trade and export activity there are several key considerations to be aware of as Mike Brown points out:

1) Explore new horizons

Manufacturing firms in the UK remain overwhelmingly reliant on the Eurozone; it is cited as an export location for almost 90% of the businesses surveyed who are currently exporting. Understanding the opportunities in new and emerging markets can ensure your business does not lose out to competition from lower cost producers. Traditionally higher risk markets such as Asia and Africa were encouragingly utilised by many of our survey respondents and we would urge others to consider the opportunities these markets may provide.

2) Utilise local experience

Local knowledge is often the best way to overcome the tricky cultural nuances which may not be immediately obvious. While sourcing and understanding local partners is often raised as a key concern, seeking professional advice and assistance to investigate the options can make all the difference. 30% of those surveyed by MHA also indicated that they wanted more understanding about regulatory issues while supply chain security and international tax were other concerns raised by respondents. Making sure that you have the support and information you need when exploring new markets can ensure your on-going success.

3) Plan for tomorrow

With a brighter economic future ahead now is the time for businesses to plan for growth. It is important to understand the marketplace and more importantly your competitors. Understanding the funding which is available can give you an important advantage. Almost half of the manufacturing firms we surveyed believed they were not eligible for any grants and of those who believe they do have access to grants, only 20% are currently planning on taking advantage of them. Understanding your options and making the most of the assistance available to you can ensure your future success.

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Capital Allowances For Fixtures

By Alastair Wilson of MHA member Tait Walker

Major changes to the rules on claiming capital allowances on fixtures in buildings were included in Finance Bill 2012 and buyers of commercial properties risk missing out on significant amounts of tax relief if the rules are not fully understood.

Background

Prior to April 2012 where a building contained fixtures (e.g. sanitary appliances and fittings, hot water and heating installations, ventilation and air conditioning installations and lifts) the buyer and seller could fix the part of the price apportioned to the fixtures by agreeing what is known as a section 198 election. Alternatively, if no apportionment was agreed, the buyer could make their own apportionment on a just and reasonable basis, regardless of whether the seller had previously claimed capital allowances. There was no time limit for the buyer to include any qualifying expenditure in its capital allowances pools and therefore claims could be made several years after the building was acquired.
Changes to this are being implement in two stages. Firstly, changes were applied from April 2012 and then further changes will come into force from April 2014.

Changes from April 2012

For expenditure incurred on or after 1 April 2012 (or 6 April 2012 for an unincorporated business) allowances will only be available on fixtures if, within 2 years, either:

- The buyer and seller have jointly entered into a section 198 election, or
- Either party refers the matter to a tax tribunal to determine the amount to be allocated to fixtures.

If, within two years of the transaction, no election is made or the amount is not referred to the tax tribunal, then no capital allowances will be due to the buyer or to any subsequent owner of the property.

Changes from April 2014

From April 2014, if the seller has not previously claimed allowances, the buyer of the property will only be able to claim capital allowances on fixtures if the seller has "pooled" the qualifying expenditure. This means that the seller must include the expenditure in its capital allowances computation in either the accounting period in which the property is sold, or in an earlier period.

Action to be taken

Property buyers and sellers should seek specialist advice when entering into property transactions. If the requirements are not satisfied then the purchaser and any subsequent owner of the property will **never** be able to claim capital allowances on the fixtures. This could result in a significant loss of tax relief to the purchaser and may reduce the future sale price of the property.

The next MHA newsletter will be available in January 2013.

MEMBER OFFICES

BLOOMER HEAVEN
Head Office: Birmingham
Contact Number: 0121 2360 465
www.bloomerheaven.co.uk

BROOMFIELD & ALEXANDER
Head Office: Cardiff
Contact Number: 02920 549 939
www.broomfield.co.uk

CARPENTER BOX
Head Office: Worthing
Contact Number: 01903 234094
www.carpenterbox.com

HENDERSON LOGGIE
Head Office: Dundee
Contact Number: 01382 201 234
www.hendersonloggie.co.uk

LARKING GOWEN
Head Office: Norwich
Contact Number: 01603 624 181
www.larking-gowen.co.uk

MHA MACINTYRE HUDSON
Head Office: London
Contact Number: 0207 429 4100
www.macintyrehudson.co.uk

MOORE AND SMALLEY
Head Office: Preston
Contact Number: 01772 821 021
www.mooreandsmalley.co.uk

TAIT WALKER
Head Office: Newcastle
Contact Number: 0191 2850321
www.taitwalker.co.uk

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