

Guide to Finance

The best manufacturing finance articles from our award-winning team



Foreword

This e-book brings together the seven most popular articles on Manufacturing Finance from The Manufacturer's award-winning team, featuring articles covering access to finance, working capital, non-commodity costs, energy charges, hedging, research and development tax credits and a variety of use-cases.

This is the perfect guide for manufacturers at any stage of developing their finance strategy, whether it's investment, growth or risk. Manufacturing finance professionals have never been faced with so much

uncertainty – and opportunity. On the one hand manufacturers face uncertain market access, currency volatility, and supplier risk. Yet there are also new export opportunities, the reshoring of the manufacturing supply chain, and the benefits of factory digitalisation.

The guide looks at some of the challenges of the Finance role, such as the importance of getting pricing right and value creation versus value extraction, taking control of raw materials costs, avoiding excessive energy costs and investment in new

technologies & systems. It contains some useful introductory conversations with teams with a successful track-record of delivering finance strategies in their sector.

The opportunity to meet with other manufacturers who are at different stages of their finance strategy and get the answers to your questions through meaningful conversations can begin at the UK's only dedicated finance conference for manufacturers: Manufacturing Finance Summit.

Consumers prepared to pay up to 22% more for brand Britain



As Britain prepares to negotiate fresh trade deals abroad, new global research from Barclays Corporate Banking reveals 39% of international consumers would be more inclined to buy a product if it displayed the Union Jack.

This was especially true for consumers in Asia and the Middle East (India, 67%; UAE, 62%; China, 61%), who have stronger associations of quality with Brand Britain, according to the research.

Younger people were also more swayed by the Union Jack – nearly half (48%) said this would encourage them to make a purchase, compared to a quarter (24%) of over 55s. In fact, this jumped to almost three-quarters (73%) when looking at 25–34 year olds in China.

An international survey of 8,060 people from eight markets (France, Germany, Republic of Ireland, India, China, UAE, the US, and South Africa) uncovered the most coveted British goods abroad, and the premiums foreign consumers are prepared to pay for 'Brand Britain' products.

Food topped the list, with international consumers willing to pay 22% more for food labelled as British-made.

The fashion and automotive industries are also set to reap the rewards, with cars (10%), clothes (9%) and alcohol (9%) the items that international consumers most consider worth paying a price premium for, if they are labelled as being British made.

Produced as part of the Barclays Brand Britain: Export Opportunities for UK Businesses report, economic modelling shows the tangible benefits

of a positive perception abroad. An additional £3.45bn could be generated in revenue by deploying targeted marketing focused on the provenance of British products.

While the modelling focused on eight key countries, the rewards could be multiplied still further if other markets were to be factored into the analysis.

Global appeal of Brand Britain

The extent to which country of origin affects buying behaviour should not be underestimated – with the exception of homeware, alcohol and soft drinks, consumers said that provenance was an important influence on the decision to purchase in all product categories.

This was especially pronounced with foodstuffs, where 66% said the country of origin would affect their choice.

It is therefore reassuring that international consumers view British goods so favourably. While all product categories saw positive results, British cars and clothes were hailed as the pinnacle of quality merchandise.

This perception of quality drives international consumers' willingness to pay more for British goods (42%), closely followed by reliability (31%) and the knowledge that they are internationally respected (32%).

Asian consumers also highlighted the status that comes with buying British, with 31% of those in India citing this as one of the reasons they would pay a premium.

Indeed, British goods are so popular that more than half (51%) of international shoppers would hold out

for a British product, rather than buy a non-British item, while one-in-nine (12%) believe that British goods are the best in the world.

Emerging markets back Britain

As export trade to non-EU countries increased 1.5% in the three months to December, the research found that the biggest opportunities for British businesses to grow exports in emerging, high-growth markets.

While the EU and the US remain the biggest trading partners for the UK, there are significant opportunities for British businesses to grow exports to less traditional market, such as China and India.

The research found that perceptions have a direct impact on the amount consumers are prepared to pay, which makes emerging markets a prime target for exporters: 64% of Indian consumers, 57% of Chinese, and 48% in both South Africa and UAE said they would pay more for goods made in the UK because they believe the quality to be higher.

This is in comparison to our European neighbours, who are more restrained in their praise of British goods. Just 29% of respondents in France would pay more for goods made in the UK because they perceive the quality as higher.

Economic modelling suggests this could translate into an additional £426m in revenue from China, £93m from India, and £92m from the UAE generated by British-labelled products.

Jonny Williamson, The Manufacturer

The price is right: the secrets of unlocking manufacturing profits

In his keynote at the last Manufacturing Finance Summit, Dr Peter Colman – a partner at the global pricing strategy consultancy, Simon-Kucher & Partners – explained the importance of getting pricing right.

Following a day of roundtable conversations, Dr Peter Colman took to the stage to deliver his Manufacturing Finance Summit 2018 keynote.

Pricing power is the single most important business lever, according to Dr Colman, who kicked his presentation off with a quote from business magnate, Warren Buffett:

"If you've got the power to raise prices without losing business to a competitor, you've got a very good business. But if you have to have to prayer session before raising the price by 10%, then you've got a terrible business."

Many companies want to raise prices, but most struggle, noted Dr Colman. Currently, businesses typically achieve little more than a third (37%) of the price increases they seek on average, i.e. trying to raise the price of a product by 5%, but achieving just 1.9%.

He commented: "That is the lowest realisation rate we have ever measured in our Global Pricing Studies. In 2012,

companies achieved 50% of their planned price increases, on average.

Value creation vs value extraction

According to Dr Colman, most companies are better at value creation than value extraction: "Pricing often comes down to guesswork. Too few people know how to quantify value, articulate it and determine a price accordingly."

That's disastrous, he warned, as price is the stronger profit driver a business has in its arsenal. Data from Simon-Kucher & Partners shows that a:

- 5% improvement in variable cost results in a 13% improvement in operating income
- 5% improvement in fixed cost results in a 15% improvement in operating income
- 5% improvement in volume results in a 20% improvement in operating income
- 5% improvement in price results in a 33% improvement in operating income

The problem, Dr Colman noted, was that pricing is unlike any other process. Achieving accurate pricing is also complex because it typically involved too many people, too many options, too many interactions and too little time.

Adding a further layer of difficulty is the fact that three-quarters (75%) of businesses have experienced higher price

pressure in the past two years, according to Simon-Kucher & Partners data.

The top five reasons for this are low-price competition (47%), increased customer negotiation power (33%), increased price transparency (32%), increased professional procurement processes (23%), and a need to meet targets (16%).

It's worth noting that apart from the final reason (need to meet targets), each of the other reasons were external, rather than internal pressures.

Dr Colman added: "Another reason cited was 'Our customers tell us we are too expensive'. Of course they do! Internally, we place far more emphasis on this than our customers do – you need to assess the value you are bringing and the willingness of customers to pay for that value."

His closing words were that there are three kinds of companies:

- Those who make things happen
- Those who watch things happen
- Those who wonder what happened

Which one accurately describes your business?

Jonny Williamson, The Manufacturer



Foreign-owned manufacturers are twice as productive as British-owned

Employees at foreign-owned manufacturing firms in Britain are twice as productive as those at domestic-owned manufacturers, according to new research.

The report from EEF found that domestic-owned firms suffer from multiple problems including poor management practices, underinvestment in capital and labour, and weaker access to finance.

All of which have contributed to UK productivity growth flatlining since the financial crisis a decade ago.

Titled *Piecing Together the Puzzle*, it analyses numerous factors affecting domestic manufacturers' productivity and recommends policies the government could introduce to overcome the so-called "productivity puzzle."

The recommendations include reinstating the Regional Growth Fund, and funding training programmes for small businesses. It says the government should prioritise 'tipping the balance in favour of investment now' and developing "focused support for adopting better management practices."

It also advocates using the Apprenticeship Levy framework to incentivise management training with an extra £30m in the levy pot to fund this. Firms would then be able to use their levy funds to train up to five managers.

The government should also set up a Continuing Professional Development

account scheme to encourage individuals to undergo management training.

"The research by EEF is a significant contribution to the public debate on productivity," says Geraint Johnes, Professor of Economics at Lancaster University Management School.

It states that foreign-owned manufacturers operating in the UK are more likely to use internal finance, invest more in their own employees, and have higher management scores than domestic owned firms.

"Management and leadership are known to be important factors in determining productivity, and the quality of leadership is known to vary a lot across firms," says Professor Johnes.

The report also found that in 2015, UK-owned manufacturing firms were 48% as productive as foreign-owned firms based in the UK. The productivity gap in the UK also widened between 2008 and 2015.

In contrast, the gap in Germany between domestic and foreign-owned firms shrank considerably.

Johnes says the emphasis on foreign ownership should be treated with caution though: "We know that bigger firms, by and large, tend to be among the most productive. So, an out-and-out comparison of the performance of foreign-owned firms and domestically-owned firms could be misleading because it's not a like-for-like comparison."

He says the manufacturing industry is

composed of "high-performing firms and stragglers." "There are likely to be some quick wins in improving the performance of the stragglers, but firms that are performing well also need to be pushing back the frontiers."

The report says the productivity problem has been exacerbated by the Brexit vote because manufacturers have been reluctant to make new investments. A 'no-deal' Brexit it states will create "potential for further deterioration" in business investment which could only be filled by greater government support.

The Chancellor of the Exchequer Philip Hammond will deliver his budget on Monday 29 October. EEF has repeatedly called on him to focus on improving productivity and reforming the Apprenticeship Levy, arguing that the levy is a major factor behind the significant drop in apprenticeships.

David Spencer of Leeds Business School believes a commitment from the Chancellor to ending austerity would be a "step forward" and would "help to create favourable conditions for firms to invest."

Professor Spencer agrees with the report's words that manufacturers require certainty over the Brexit deal because the current ambiguity is hindering investment. "Until UK firms can see certainty over the future of the UK's relationship with the EU then investment will be less than it might be," he remarked.

The EEF report builds on the findings of its *Unpacking the Puzzle* report from May earlier this year which investigated UK manufacturers' contribution to the productivity decline.

Jonny Williamson, The Manufacturer



UK manufacturers sitting on £250bn in potential working capital

New analysis from Wyelands Bank reveals UK mid-sized, or "Brittelstand", manufacturers have £252bn in assets that they could use to access working capital to help them grow.

The research analyses 23,000 mid-sized businesses turning over £10m to £300m across the manufacturing supply chain.

Wyelands Bank, set up to help small and medium businesses to trade, grow and create jobs, used government data to understand the total stock and debtor assets available to these businesses. The research assesses the working capital potential.

It shows that within the manufacturing supply chain, original equipment manufacturers have the highest proportion of working capital assets compared to turnover at 28% on average.

Manufacturers have the second highest proportion compared to turnover at 26% on average. Distributors are third with 25% on average. Raw materials suppliers have the lowest proportion of working capital assets compared to turnover at 24% on average.

Businesses within the manufacturing supply chain include tier three businesses, or raw material suppliers, tier two businesses, or manufacturers, tier one businesses, or distributors, and original equipment manufacturers.

When assessing by revenue band, businesses turning over £10m to £50m

have more than a quarter of their average annual turnover tied up in stock and debtors assets.

Manufacturers – or tier two businesses – within the £10m to £50m turnover band have the highest proportion of assets tied up across the supply chain at 28% of annual revenue on average.

Meanwhile, businesses turning over £151m to £300m have the lowest proportion of assets tied up in stock and debtors of all businesses analysed.

These companies have a fifth of their annual revenue tied up on average.

Raw materials suppliers have the lowest proportion tied up in stock across the supply chain. They carry only 8%, or £16m on average, of annual turnover in stock.

Iain Hunter, CEO of Wyelands Bank, said: "our analysis shows the proportion of assets that UK Brittelstand manufacturers have that could be used to free up working capital.

"Larger businesses often need less financing because they have more leverage with their customers. Smaller businesses, however, can often struggle for this reason.

"Freeing up these potential working capital assets can help provide the finance that businesses need to fulfil new orders and grow. There are often simple ways to fund growth without having to give up equity.

"At Wyelands Bank we get to know our customers and have the flexibility to tailor the right solutions for their business."

Could your business be sitting on untapped assets?

Wyelands Bank has been set up to help firms trade, grow and create jobs. Its analysis of mid-market manufacturing firms shows that the average business may have more than £10m tied up in working capital or other assets which could potentially be used to raise finance.

This free report: <http://bit.ly/2Jr7Brs>

- shows how the UK's "Brittelstand" manufacturers, turning over between £10 and £300m, have more than £250bn of working capital assets between them which could be used to raise finance.
- Compares firms in different stages of the industrial supply chain to see how their profiles differ. Many have 25% of their turnover tied up in unpaid invoices and stock alone
- Utilising these working capital assets can help provide the finance that businesses need to fulfil new orders and grow. There are often simple ways to fund growth without having to give up equity.

Jonny Williamson, The Manufacturer



Risk/Reward Revisited
15 May 2019, Oxford

What is Manufacturing Finance Summit?

Manufacturing Finance Summit is the UK's largest gathering of manufacturing finance professionals – 80 growth-minded finance executives from across automotive, aerospace, defence, electronics, food and drink and FMCG coming together to examine how the finance function is changing within UK manufacturers.

manufacturing-finance.uk

- 80 ATTENDEES
- 20 SPEAKERS
- 12 DISCUSSION GROUPS
- 3 STREAMS



Why do non-commodity costs add so much to your energy bill?

Non-commodity cost charges – or third-party costs – are expected to account for around 60% of a UK manufacturer's energy bills by 2020, more than twice as much as a decade ago.

So, what lies behind the increase to non-commodity costs and – more importantly – what can businesses do to ease the financial burden?

To learn more, The Manufacturer recently sat down with David Oliver, an energy expert from business utility specialist, Inenco.

What factors lie behind the sustained increases to non-commodity cost charges?

David Oliver: Unquestionably, climate change – and governments' policies regarding climate change over the past decade.

Winter Outlook: Manufacturers' energy cost forecast for 2018 and beyond

As we approach the new year, many manufacturers are concerned about the upcoming political and economic changes and how their bottom line will be affected.

Faced with record-high costs and ongoing uncertainty, it pays for manufacturers to reassess their energy risk management strategies to consider how the cost of energy will impact their organisation.

A FREE new report provides a forecast of energy costs over the coming months and compares three manufacturers with and without Energy Intensive Industries exemption and Climate Change Agreements.

To read the comparison, along with a demonstration of the steep curve that continues to rise, please download it here: <http://bit.ly/2FpL5Lq>

Society's shift towards renewables didn't just happen through market forces, the right subsidies were put in place to make it happen. Those subsidies largely lie behind the high price increases businesses are experiencing.

Let's breakdown a typical energy bill. For a manufacturer with an average electricity cost of 10p/kWh (£100/MWh), about 22% of the bill is down to renewable obligations such as wind or solar farms and waste or biomass energy plants; about 6% is feed-in tariffs arising from domestic, roof-mounted solar panels for example; and around 4% is the new Contracts for Difference (part of the government's Electricity Market Reform (EMR) programme).

Together, those subsidies total around one third of your bill.

The other contributing factor is network or "system" charges. Triads or Transmission Network Use of System (TNUoS) charges have risen by about 10% year-on-year, and there's a couple of reasons why.

First, the national grid was put in place more than half a century ago and it desperately needs upgrading, repairing and modernising. Second, when the national grid was originally designed, it was distributing electricity from power stations in the Midlands to cities.

Those power stations have since closed, so the transmission network is having to undergo substantial upgrades, at great cost, to source power from new plants and offshore wind farms spread across a much larger area. You can clearly see that cost reflected in triad prices per kilowatt hitting more than twice as much as they were a decade ago.

Furthermore, distribution costs have risen well ahead of inflation and we've seen the introduction of the Climate Change Levy (CCL), which was originally set out as a renewable tax; but is now essentially a stealth tax as

it's based on kilowatt hours not carbon emissions.

Against that backdrop, what actions can manufacturers take to avoid excessive charges?

First, look at when you are using energy – manufacturers will pay higher system charges for using electricity during peak periods, so shifting load away from these time scales will alleviate some of the strain.

If you have some flexibility to shift demand, you might also benefit from participating in demand response schemes – being paid to turn down consumption during peak demand to alleviate strain on the national grid, in return for payments.

Second, check whether your organisation is eligible for exemptions. If you're an intensive energy user, chances are you'll probably have an energy purchasing team or manager in-house. Typically, you'll also be part of a trade federation or association, who will highlight any changes that are coming and where support is available.

If you're not classed as an intensive energy user, then that's where Inenco comes in to highlight, for example, possible exemption opportunities. In some instances, we're talking about millions of pounds' worth of savings, so awareness of what's happening and where support can be found is vital.

Many businesses are lucky in that they operate in one of the industries covered by the Energy Intensive Industries (EII) legislation, which exempts them from a significant amount of some non-commodity costs – to find out more, visit Inenco's EII hub: <http://bit.ly/2HNDIPL>

It's worth noting that rising energy costs will mean more manufacturers may become eligible to receive some exemptions – because energy is



becoming a bigger share of their total outgoings.

Currently there's a consultation around extending the EII scheme by reducing the entrance threshold. The result of that is likely to be made later this year, with any changes introduced sometime next year.

On paper, extending the threshold to allow more businesses to benefit sounds positive; but the way these work is that everybody else must pay the subsidy for you. So, the energy intensive industries are being cross-subsidised by the rest of the energy consumers. Good news for them, bad news for everyone else.

And finally, the best way to alleviate rising costs is by energy reduction measures (which you can learn more about here: <http://bit.ly/2TkUK9Y>)

Recognising that our energy demands are only going to increase in the future, Ofgem are compiling a root-and-branch review of the way that network charges are implemented and create a system not

charges are implemented and create a system not that is only fairer, but also encourages the right behaviours.

Network access is a key part of the Ofgem review as sharing capacity fairly is becoming an ever-increasing concern. Capacity in this context means the maximum amount of electricity that you are contracted to receive from your network operator. You pay a fixed charge each month based on the amount of capacity that you have agreed and will receive an excess penalty if you exceed this in any given month.

As an example of Ofgem's concern, business A may have very good electrical capacity on their site, but only utilise half. Their neighbour, business B, utilises all their electrical capacity and is therefore looking to increase it.

Surely, the business with the excess capacity should be making that available to others. However, currently, Distribution Network Officers (DNOs) can't do that because as far as they're concerned,

there's not enough capacity in the area.

Ofgem would also appear to be clamping down on businesses who avoid triad charges by switching on generators or switching off production.

As far as Inenco is concerned, that's a good thing for industrial customers to do because it reduces demand on the national grid and therefore makes it easier for it to survive.

Ofgem's view, however, is that all businesses should be paying their fair share of triads. So, we think there's going to be a wholesale change in the methodology of charging for triads or Transmission Network Use of System (TNUoS).

The challenge for Ofgem, is that they are trying to strike a balance that's fair for everyone – domestic and industrial users, and typical manufacturing businesses and more energy intensive users. They are aware of industries and our concerns and they do seem to be listening, but any changes to triads could prove contentious.

Jonny Williamson, The Manufacturer

The price of plastic: taking control of raw material costs

The price of plastics is volatile – not only because it depends heavily on the price of oil, but also because it's affected by other market conditions.

For manufacturers using plastics, this can be a bottom-line headache; but, as Callum Macpherson, Head of Commodities at Investec explains, ways to hedge against price fluctuation are emerging.

Plastic is widely used in all sorts of products – whether that's low-density formulations used for packaging or high-density plastic used for products like piping and plastic lumber.

In Europe, plastics are mainly produced from petroleum products and therefore the price of crude is one of the key factors that affect plastic costs, making it very volatile.

However, there are additional factors that can allow plastic prices to take on a life of their own, such as capacity constraints and stockpiling by users.

Over the past five years, the price of plastic has swung from £850/MT (metric tonne) to highs of more than £1300/MT. These variations have the potential to materially affect the bottom line; however, many manufacturers aren't aware that plastic can be hedged.

It can be – and we're seeing a lot of interest from manufacturers who use plastics and want to manage their exposure to price moves.

Mark Amphlett, general manager for Amtek Plastics, in Newton Abbott (Devon) commented, "We're a processor of plastic raw material, wholly reliant on the distribution channel in the UK and Europe, and price fluctuations have become an unpleasant everyday experience for us.

"Passing on material price increases to our clients can be problematic, especially when the increases are far

in excess of the standard rate of inflation. This can be difficult to explain because the price rises are not always based on an increase in the foundation of the finished raw material that we purchase.

"Our distribution channels justify high increases as, 'due to tight supply of raw materials and order books full to capacity', which is also hard to explain to end users. This is especially true for specialist materials – ones that are specified from a handful of European manufacturers, or even just one.

Recycled plastic polymers = Polyethylene and polypropylene are the two most common forms of plastic. Polyethylene and polypropylene are the two most common forms of plastic.

"Taking all of these factors into account, I would welcome any options to help stabilise raw material prices. It is such a large proportion of our cost base that any assistance in removing this 'unknown' would be of huge benefit – not just for us, but for our industry in general."

What's the supply chain for plastic?

Plastic 101: crude oil is a mixture of hydrocarbons with different boiling points.

A refinery uses those different boiling points to separate out the components of crude oil into useful products, including gasoline, diesel, jet fuel, fuel oil and naphtha.

Naphtha can be processed further via a process known as 'cracking' to produce key plastics feedstocks such as ethylene and propylene. These can then be polymerised to produce polyethylene and polypropylene – between them the two most common forms of plastic.

Other plastics, such as PET, are also formed through processing petroleum products. In addition to producing 'virgin' plastic from petroleum products, recycled material can also be used or blended with virgin plastic.

What drives the price of plastic – is it just oil?

Oil is a big driver, as it's the origin of petrochemicals, at least in the way they're produced in Europe.

However, oil is by no means the whole story. First, there are different price sensitivities in different parts of the chain. Naphtha is a liquid at room temperature and therefore relatively easy to store and transport. However, ethylene is a gas, which is more challenging.

Plastics themselves are resilient and of course solid, meaning that they can be easily stored for long periods of time in a standard warehouse.

Several factors can lead to plastics price variations deviating from crude:

- There is a finite amount of processing capacity available. This acts as a brake on production, and can keep plastic prices high when demand is strong
- The production of plastics and their feedstocks is energy intensive, which can exacerbate the impact of changes in oil prices
- Logistic challenges with transporting gaseous feedstocks like ethylene can make it hard to eliminate regional price differences (European prices are much higher than US ones)
- Since plastic is durable and easy to store, producers sometimes stock up on it when they feel that prices are low, and dip into this inventory when prices are high. This can have a dampening effect on price moves, but can also lead to plastics prices pre-empting moves in oil prices.

In practice, the two graphs shown above detail how plastic prices have moved over the past few years, with oil also included for reference.

What's likely to happen to plastic prices in the future?

For a product based on oil, volatility is a given. However, it's possible to take a considered view on the factors

that will be relevant in the longer term.

The US shale boom has led to considerable growth in the availability of light products in the US – natural gas and petroleum gas are products that lend themselves to producing petrochemicals.

At the same time, petrochemical infrastructure is expanding and adapting to accommodate the growth in light products and natural gas. However, the US is also developing capacity to liquefy and export natural gas and gaseous feedstocks for plastics to supply international petrochemical markets.

Looking to the demand side of the equation, while fossil fuels as sources of energy may eventually be displaced to a material extent by other forms of energy, for now, demand for oil generally looks set to continue growing.

Meanwhile, plastic demand tends to be associated with global growth and so could also be expected to continue growing.

What is hedging?

Hedging is a way of limiting your exposure to price fluctuations. If you know you'll need 1,000 metric tonnes of plastic over the next year, you can choose to pay the 'spot' rate – the variable price on the day you need it – or use hedging products to fix a price for the year, so that the hedging company takes the risk instead of you.

Can I hedge plastic?

Unlike currencies and commodities like oil, financial markets for plastics are relatively new. It has historically proven difficult to hedge, largely because it's not traded as actively as other products such as oil.

That's a problem for manufacturers who need to control input prices. Using oil products like naphtha, or even crude itself, as a proxy hedge has often been disappointing in the past, because as explained above, the prices of oil and plastic can diverge.

Recently though, the markets for end products like plastic have become more liquid, and are no longer solely

the domain of large petrochemical companies. In practice, that means that there's more of a market for plastics and banks and financial institutions can offer hedging products – taking on the risks associated with price rises – more easily than before.

Thanks to the emergence of these new alternative products, manufacturers can now hedge plastics in the same way that they'd hedge a currency or another commodity, to manage risk. Lots of these companies work in industries where they can't pass on price rises – for example, where a contract sets a fixed price, or there are high levels of competition in the market – and are pleasantly surprised that these new products exist.

Polyethylene and polypropylene are the two most common forms of plastic.

Jonny Williamson, The Manufacturer



What's the best kept secret in UK manufacturing?

Research & Development Tax Credits are an often overlooked benefit for companies of all sizes. Many businesses are missing out on claims worth thousands of pounds.

Simon Bulteel of Cooden Tax Consulting has filed numerous successful claims and shares his insight into how your company could be rewarded for innovation.

I'll give you a few clues, it's not the productivity gap, it's got nothing to do with Brexit but it is related to innovation!

Innovative businesses should be applying for R&D Tax Relief – image courtesy of Deposit photos.

I've read a number of articles about innovation in The Manufacturer recently, and not one has mentioned Research & Development Tax Relief or R&D Tax Credits! Perhaps I just didn't choose my sample well enough!

In a way I found it slightly disappointing that R&D Tax Relief didn't take a very important place in these articles, but I am not surprised.

Despite having been available to SME companies since 2000 and to larger businesses a couple of years later, it remains probably the best kept secret in most industries across the UK, so why should manufacturing be any different?

In a nutshell R&D Tax Relief is there to reward any company that is "innovating" in the fields of science or technology. That generally means that any New Product Development or any product improvements are likely to be eligible to claim. It can also be extended to new manufacturing processes, process improvement and pilot and bespoke production.

So why is it a secret?

That's a very interesting question that

there is no easy answer for, but in our experience, it is a combination of the following:

- a lack of communication from HMRC promoting R&D Tax Relief;
- a lack of knowledge in accountancy firms how to apply the R&D Tax Relief rules to a business;
- a concern amongst accountants about promoting it to established businesses they have dealt with for numerous years;
- risk averse owners and managers who think that a claim might be a "red flag" to HMRC;
- companies that are claiming are getting both a competitive and cashflow advantage over their peer group and therefore aren't really promoting it to one another; and
- Agencies like Innovate aren't allowed to actively introduce the companies who receive grant funding from them to professional service

providers they are only allowed to nudge companies that they might be able to claim.

Despite the lack of promotion by HMRC, government are actively willing businesses to claim, because they know a little helping hand now will more likely than not lead to higher tax revenues in the future.

A quick look at the Innovation Landscape.

The Office for National Statistics publishes an annual review of the R&D Tax Relief scheme, they published it in September and the findings particularly for manufacturing businesses are interesting.

Over 9,600 claims were made by small and medium-sized manufacturing companies under the SME Scheme, those that employ less than 500 employees, and have a turnover of less than £100m or a balance sheet value less than £86m, those claims were worth around £410m to those businesses, that's an average claim value of over £42k. Spring Statement 2018 allocates the

first wave of funding, providing over £95m for 13 areas across the UK.

Over 9,600 claims were made by small and medium-sized manufacturing companies under the SME Scheme.

A further 915 claims were made by small and medium-sized companies who had been subcontracted by a large or overseas company to perform some Research and Development, those claims under the less rewarding RDEC scheme were worth a further £35m. Those claims make up a total of 26.54% of all claims submitted by SMEs.

When you look at claims made by large companies under the RDEC Scheme a total of 890 companies claimed over £600m, that's an average claim of nearly £675k.

The Schemes in a nutshell

The SME Scheme generates an additional deduction of 130% of the eligible R&D expenses, which for a profit-making company could generate a tax saving at 19% of 24.7% of the eligible costs. For a loss-making company, the loss can be surrendered for an R&D Tax Credit of up to 33.35% of the eligible costs.

Under RDEC, you are able to generate an Expenditure Credit of 12% of the eligible costs, which will be taxable, the expenditure credit would then be deducted from the final tax liability, creating a tax saving equivalent to 9.72% of the spend.

Eligible costs include:

Staff costs – wages, salaries, bonuses, Ers NI, Ers Pension Contributions out of pocket expenses incurred for R&D

Third Party costs – Subcontractors (not eligible under RDEC) and agency workers (externally provided workers)

Consumed materials – either in the process or the manufacturing of a prototype and includes light, heat and water.

Software costs

TAKE THE NEXT STEP

**MANUFACTURING
FINANCE SUMMIT**

Risk/Reward Revisited
15 May 2019, Oxford



What does the finance function look like in high-growth manufacturers? Where can risk and opportunity be better balanced across your supply chain? How can manufacturers monetise digital transformation?



Find answers to these questions at the 2nd annual Manufacturing Finance Summit:

- The UK's largest gathering of manufacturing finance professionals from across multiple industries.
- Spend time talking to like-minded manufacturers about the same

business issues you face.

- A uniquely interactive format that ensures you leave the conference with practical insights taken from across the UK industrial landscape



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