Semper International Second Quarter 2014 Industry Insight Survey

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Semper International: Second Quarter 2014 Industry Insight Survey

The 2Q Economy: Telltale Signs of Change

From a macro perspective, our industry has witnessed remarkable change riding the economic recession and (potential) recovery over the past seven or eight years. If you haven't been simply hiding under a rock, the smart money says that you have been cutting your pennies into thirds, and those thirds into ninths.

Companies have explored every possible avenue to reduce costs or the potential to cheaply increase distribution. These strategies range from the high tech, exemplified by Amazon's futuristic helicopter delivery system and the pre-positioning of products based on real-time browsing shopping cart actions, to customized 3D printing and the slightly less technical shift to on-demand printing and shipping tools now deployed by book publishing firms.

However, at some point, cost cutting measures are simply not enough to change business results. Today, the number one game in town is top line sales growth. Further, when demand is not easily created through organic strategies, firms are looking to merger and acquisition strategies.

Evidence of this new trend is rampant in a variety of industries worldwide, where consolidation is becoming the norm, from Pfizer announcing its intent to purchase Astra Zeneca, to GE absorbing Alstom in France, to the Quad purchase of Brown Printing and Microsoft/Nokia unions.

Tepid Signs of Life from Reporting Companies in the First Quarter

In the most recent quarter, these higher trends are colliding to cause fingers of change moving through the industry. Hopefully, we are closer to the end of this economic roller coaster than the middle, though, I remain vigilant for extended signs that, after seven years, the economy can start to stand on its own.

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Unfortunately, the troubling slowdown that impacted the fourth quarter of 2013 continued into the first quarter of 2014 as the GDP growth rate of .1% was much lower than Q4 2013. Also, many of our responding companies reported a serious freeze in new orders causing many to question if the recovery was real or not.

Further, new unemployment filings were higher than they probably should have been. It may be the Fed was overly aggressive with down shifting quantitative easing (QE), and this reduction in liquidity may potentially jeopardize the recovery. In testament in our survey, when asked about new capital investments, companies reported 25% fewer purchases than they made in the previous quarter.

That was the bad news. The good news is that despite these hiccups, most of the companies covered by our survey reported being profitable – and – they reported a sharp increase in sales over the two last weeks! Expectations are reportedly still high, with clients anticipating these positive sales to continue through the current quarter.

Still, despite this sales optimism, companies returned to their economic vigilance, indicating they are more concerned about the current state of the general economy than they were last quarter.

Why Would A Staffing Company Do an Industry Survey?

Over ten years ago, Semper recognized that our experience in staffing allowed us to see economic trends affecting the allied industries we staff. Staffing tends to be a leading economic indicator and in our 20+ years of watching this economic cycle, we have come to understand the labor market a bit.

Here's what this cycle looks like:

- When the economy starts to pick up, companies tend to hire more flex staffing before they ramp up their full time staff, as they are unsure of the long-term economic direction, or whether they should invest in full time staff.
- As the economy starts gaining momentum, firms increase their flex-to-hire staffing as they have confidence in their prospects over time. This demand continues through the top of the economic cycle, where most companies are looking for full time people all the time.
- Later, as the economy starts to cool, deployed flex workers are released before they eliminate core full-time workers positions.
- Finally, in the bottom of the labor cycle, firms rarely look for full time workers unless they are replacing core staff, but use flexible staffing to meet unexpected – but positive – near term demand.

While our client's privacy is always a paramount concern, we believe using the aggregate survey data to help analyze common themes to be beneficial. The fact that we provide staffing for a variety of companies across disciplines, specialties and competitive lines in the industry – print and beyond, allows us a unique vantage point to see who is busy, when they are busy, what cyclical segments impact various industry segments and what macro issues impact everyone.

When we first launched the survey, our goal was to continue in that vein, aggregating this information to the industry as a public service for free. Over the years, as the survey has become more popular, and we have watched the industry itself change, we have refined and improved our questions and processes whist still providing the service gratis.

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This year, based on your suggestions and feedback, and the increased interest, we have decided to take it a step further, by aggregating the data into an executive summary with key insights we pulled from this data, and advanced our design and presentation to welcome our increasingly graphic digital audience.

Executive Summary: 3 Key Themes with 12 Specific Insights from the Second Quarter Survey

We scoured the data looking to shed light on whether we are looking at a turning of the economic tide. Reading all the responses from over 300 business owners, it looks like the industry at large expects to see several steady quarters of growth interrupted with mini slowdowns in demand, as buyers continue to feel a bit of economic PTSD. Hopefully, these fits and stalls will smooth out, and we will eventually find ourselves in a period of sustained demand.

We've broken down the data into 3 Key Themes:

- Dollars and Cents
- Competitive Threats and Company Responses
- Staffing Trends

Each theme is broken down further into 12 critical insights that we saw in the survey data:

- Insight 1: Current Revenues Remain Relatively Low
- Insight 2: However, Firms Are Beginning to Report Positive Revenue Growth
- Insight 3: Nearly 75% of Businesses Reported Profits in the First Quarter
- Insight 4: Sales Slowed a Bit This Quarter – Though, It May Have Been the Snow
- Insight 5: Despite a Hiccup, Firms Remain Bullish on Sales Growth
- Insight 6: While Still Troubling, the Over all Economy Is Marginalizing As a Threat
- Insight 7: Companies Are Divided Regarding Diversification
- Insight 8: They Are Also Divided On What Markets to Diversify Into
- Insight 9: Firms Report Low Rates of Capital Investment
- Insight 10: Staffing Rates Are Changing - In Both Directions
- Insight 11: Insurance and Taxes Are Driving Labor Costs
- Insight 12: Skilled Staffing Fulfillment is (Slowly) Moving Online

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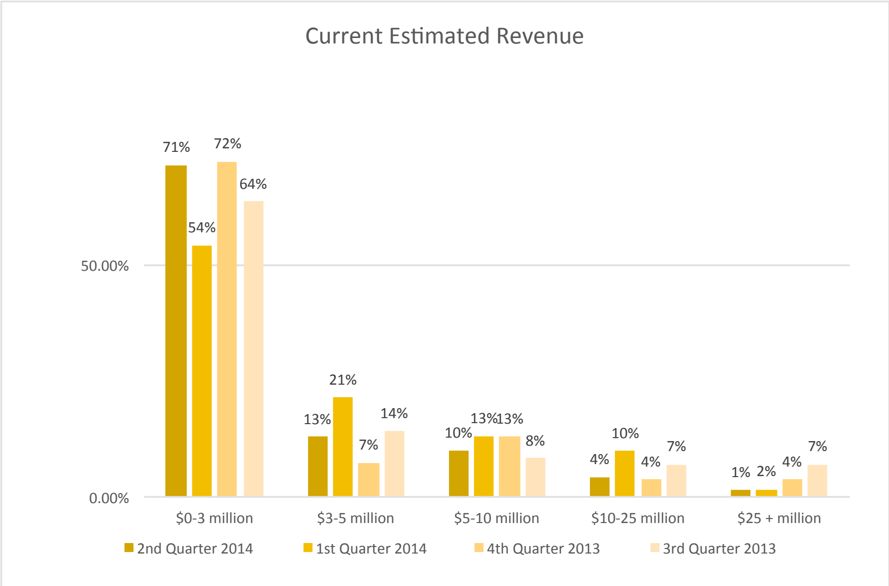
I. Dollars and Cents

Insight 1: Current Revenues Remain Relatively Low

We added a category to this question this quarter, expanding the $0 - $5 million range to provide a $0 - 3 million range. Clearly, this category more closely aligns with the industry's current revenue statistics.

There are two potential factors contributing to this data. First, despite a spate of consolidation in the industry, the impact of the past years' depression remains heavy, with lower revenues and increased price pressures holding most enterprises under the three million mark in sales.

The other alternative trend likely reflected is the dominance of the small business community in our responding audience, with over 30% of responding companies coming in with less than 10 employees. Small businesses account for nearly 54% of all U.S. sales, according to the Small Business Association (SBA). While these firms are integral to the lifeblood of our economy, they will inevitably also report relatively smaller sales numbers.

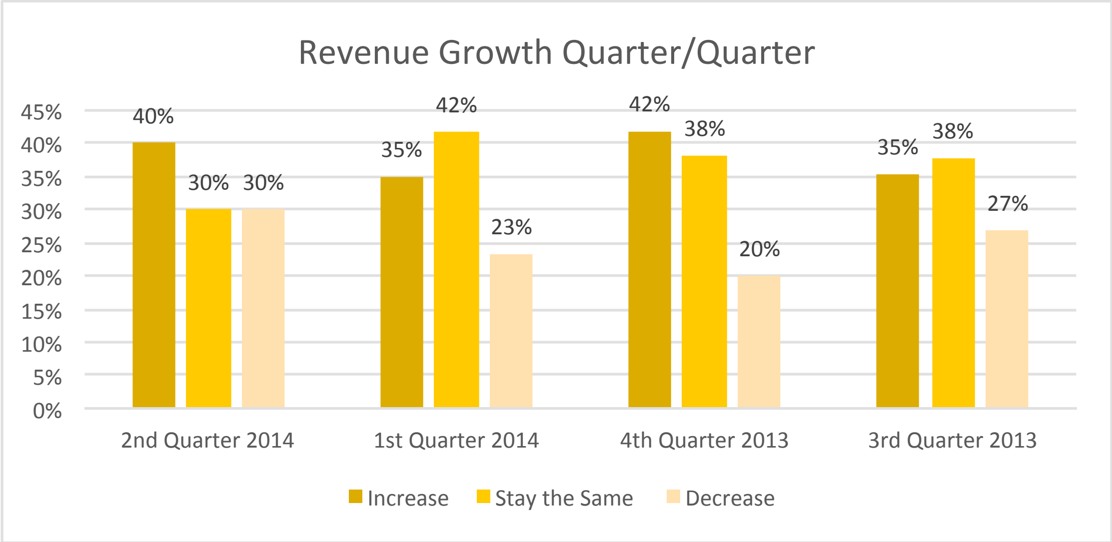


Question: What was your company's estimated revenue last quarter?

Insight 2: However, Firms Are Beginning to Report Positive Revenue Growth

One of the bright stars in our data this quarter is the quarterly revenue growth, with 40% of companies reporting increased revenue for the second quarter – a 5% increase in just three months.

We will continue to watch these numbers over the next several quarters, but this increased positivity, coupled with the positive sales and profitability numbers we witnessed from clients foretell at least some forces of good in the economy as well.



Question: How does [your revenue] compare to last quarter?

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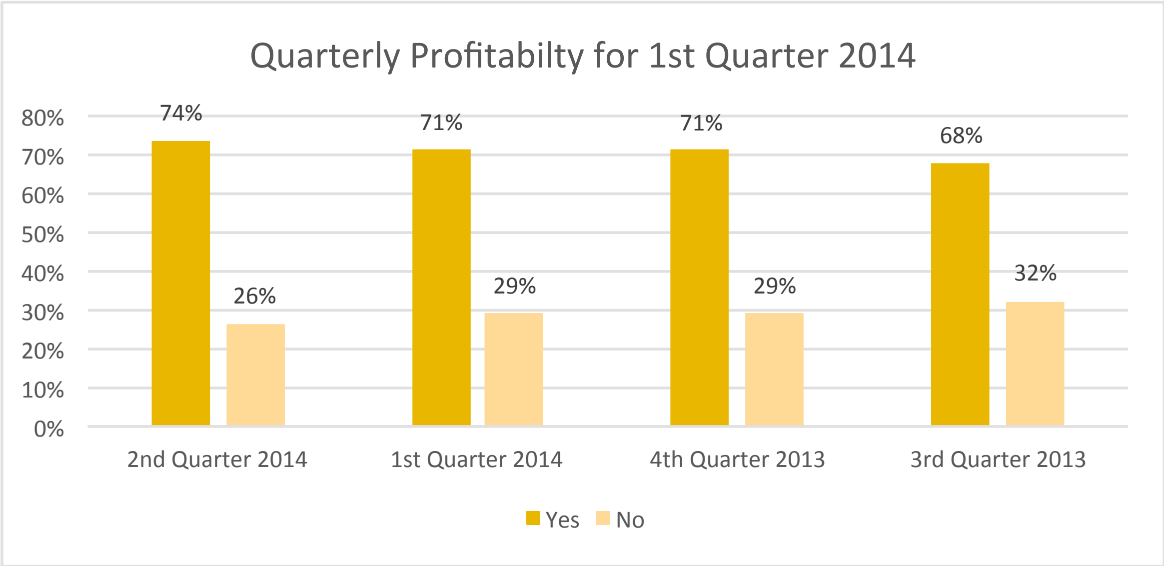
Insight 3: Nearly 75% of Businesses Reported Profits in the Second Quarter

Another positive in our data were the nearly ¾ of companies who reported positive quarterly profits in the second quarter – the third quarter in a row that more than 70% of firms saw profits rise.

These numbers are a pleasure to see that after all these years, companies' survival instincts remain intact. As firms learned to control costs, their profits responded quickly and rose. Ideally, with less government reporting and regulation, this trend would continue.



Question: Did your company have a profitable first quarter 2014?

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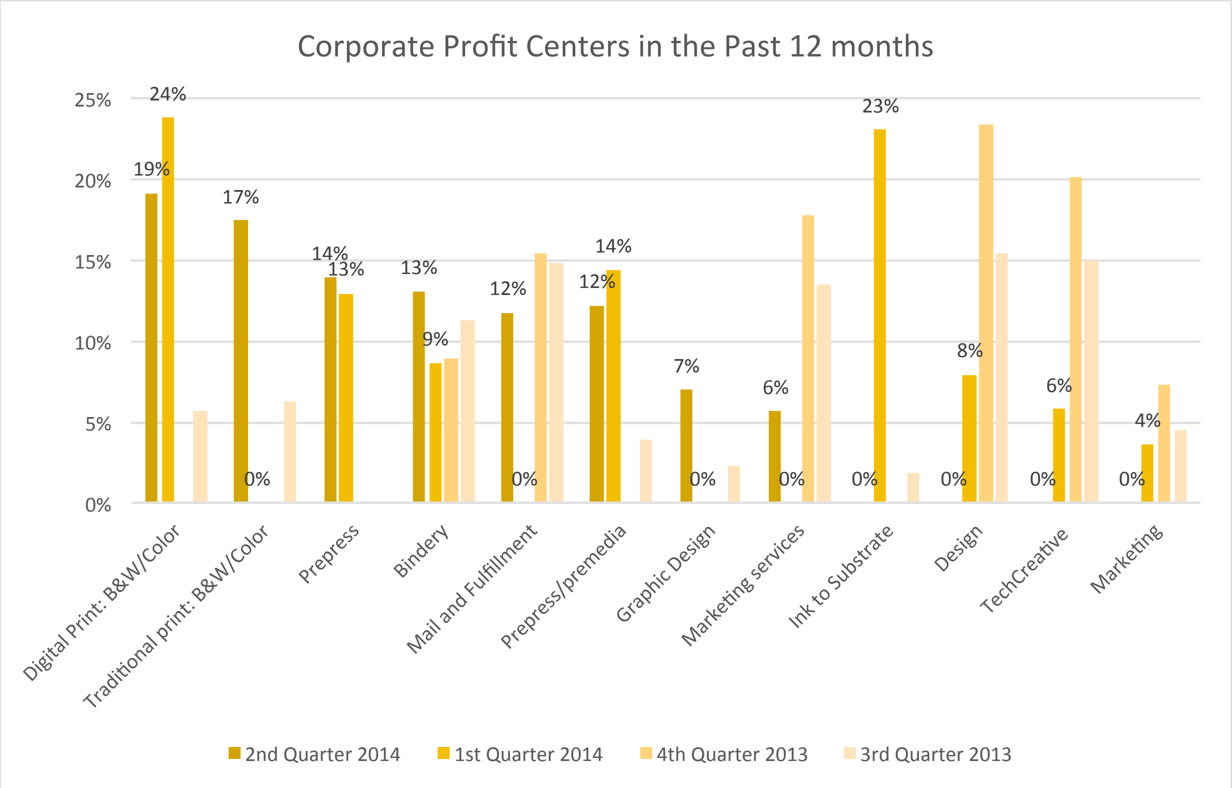
We also wanted to delve a bit deeper into corporate profits by teasing out which business units most contributed to profitability. Here, we see a bit of a mixed bag, with a variety of different units contributing.

Looking at the various profit centers over time, it's clear that (while dispersed), firms are finding the most margin in digital – via either content prep, reproduction or distribution. We are starting to see a new trend emerge into what we call TechCreative, a high margin area that intersects both creative and technology markets which we have seen rise over the past several quarters.



Question: What are the primary profit centers in your organization?

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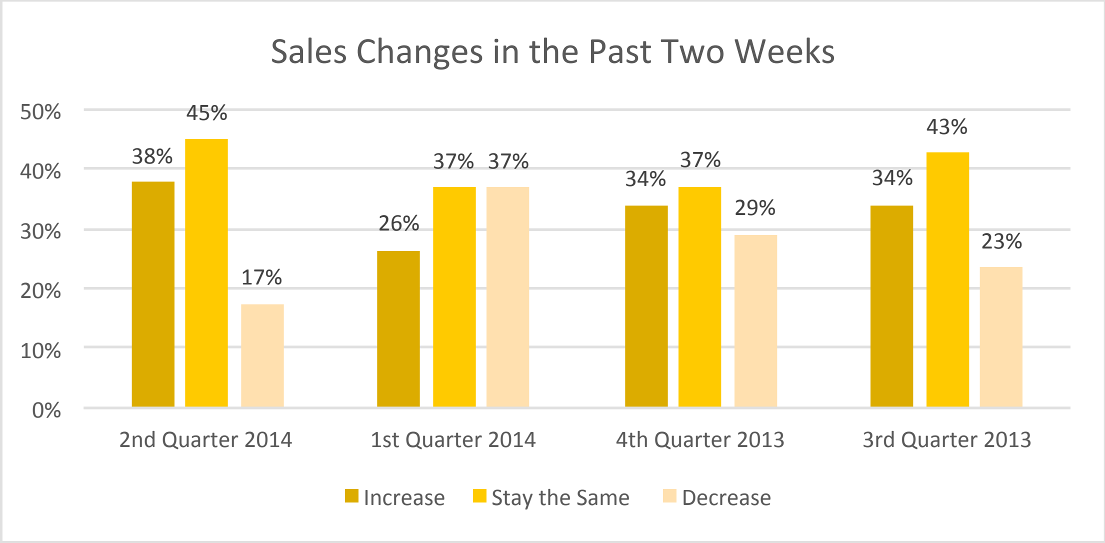
Insight 4: Sales Slowed a Bit This Quarter – Though, It May Have Been the Snow

While there was a good deal of the media discussion in the past quarter regarding the sales "slow down", the difference in first quarter and second quarter numbers indicate it might have been primarily due to weather, there are clearly other drivers working against the industry.

We began tracking our first quarter numbers in December before the heavy weather hit, yet you can see that only 26% of companies reported positive sales increases, indicating there are drivers other than the weather in play, such as perhaps the Fed easing.

What is clearly encouraging is that second quarter sales changes have not only rebounded to fourth quarter levels, but risen to 38% reporting positive profits – which potentially means that as the late winter snow lifts, so too will our economic indicators. This is definitely encouraging, and we hope this trend continues.



Question: How have sales changed in the last 2 weeks?

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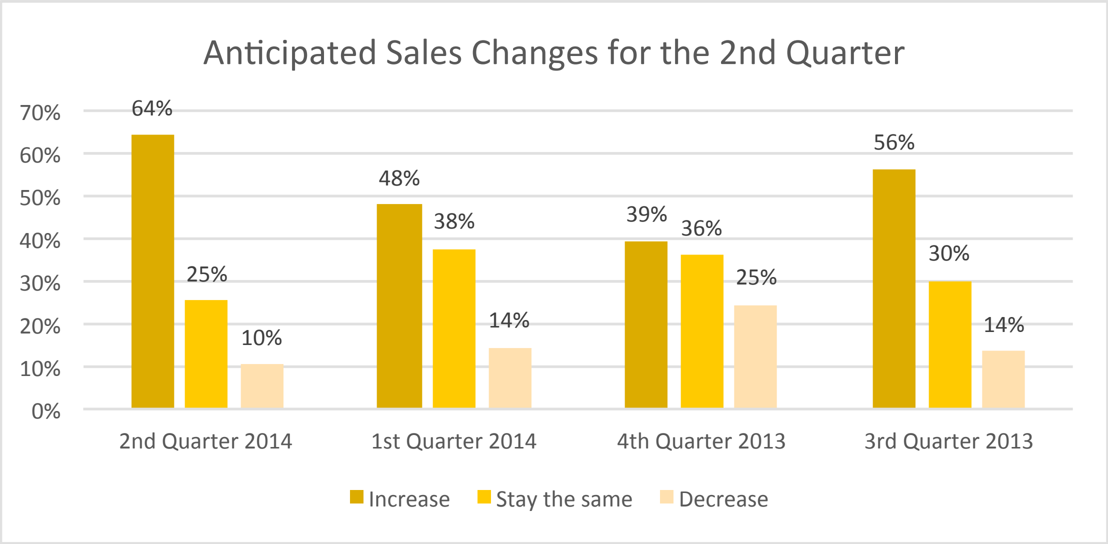
Insight 5: Despite a Hiccup, Firms Remain Bullish on Sales Growth

Similarly positive are the number of responding companies who anticipate positive sales moving through the second quarter. While nearly 40% of firms reported positive sales growth in the past two weeks (see the chart above), more than 64% expect sales to increase – an indication that companies are anticipating sustained sales volumes through the month of May, and beyond.

Though some of this optimism may just be dint of will (it's hard to stay pessimistic forever), the clear increases with sales, coupled with the positive business forecasting we see in the anticipated sales changes are all good signs of long-term recovery.



Question: How do you expect sales to change during the second quarter of 2014?

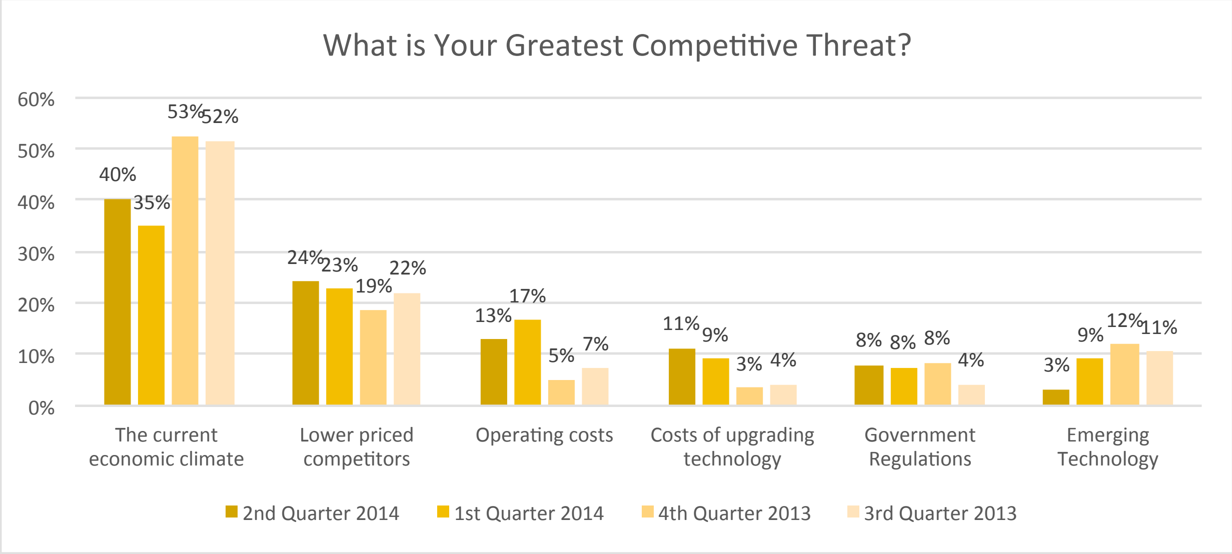
II. Competitive Threats and Company Responses

Insight 6: While Still Troubling, the Economy Is Marginalizing As a Threat

This quarter, like many before it over the past several years, the overall economy continues to be the primary concern for many companies, with 42% of firms reporting they are still a bit bearish regarding our general economic health.

However, emerging from the trend lines is also an indication that the economy is becoming less of a threat that it was in the deep end of the depression. In fact, for the second quarter in a row, more than half of our reporting firms cited something other than the economy as their top concern, as lower priced competitors (24%), rising operating costs (13%) and technical upgrade expenses (11%) are also coming to the fore.

This makes sense as many in the industry have fought to stay above water by reducing prices in the last year – keeping business but reducing margins forcing razor share attention on costs. We agree with the nearly one quarter of companies who are concerned about competing on price alone – it often ends up a fool's game for all involved.



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Insight 7: Companies Are Divided Regarding Diversification

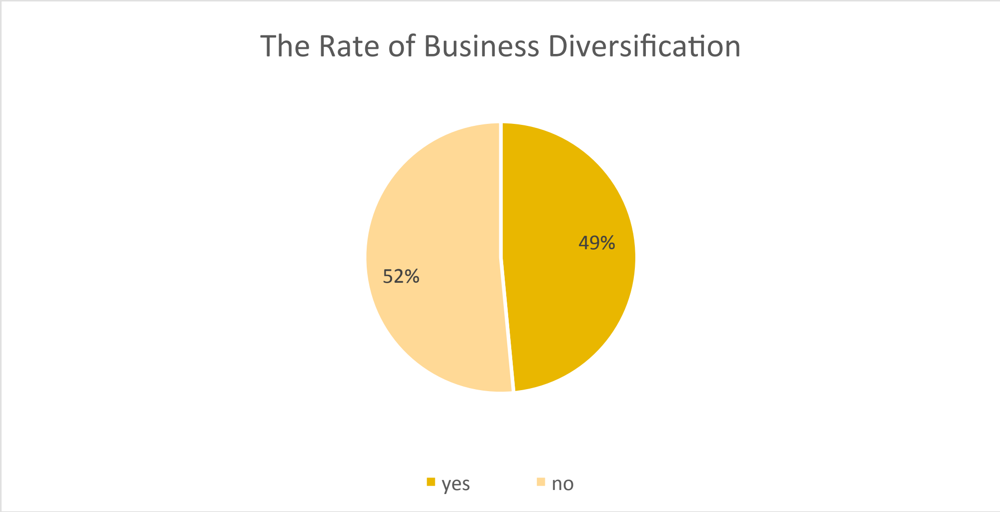
Other interesting data to come out of this survey is the near 50/50 split that companies reported with regards to business diversification. We have seen a great deal of change in the Allied creative industries, and we feel those companies who ignore the pressures to adapt do so at their own peril.

While emerging technology did not yet receive top billing as a critical threat among our constituents, we still think there are trends to pay attention to here.

We are witnessing a technological wildfire spreading through the business world, which will likely be increasingly reflected in our data over the next several quarters. The advent of the internet, increasingly aggressive automation, resource constriction, and unprecedented pricing pressures, are all colliding to force an incredibly rapid rate of change.

For example, the new 3D printing technology may prove to be an industry game changer for more than just the printing industry. Here, with some core customization features, a company can provide an individual product on demand. Imagine the ramifications for food, shipping and manufacturing processes if every household suddenly has an on demand printer – the possibilities are truly endless.

While nearly half our reporting businesses clearly see the writing on the wall and are taking steps to move into new arenas, there is a danger for the 49% who have yet to take these threats seriously.



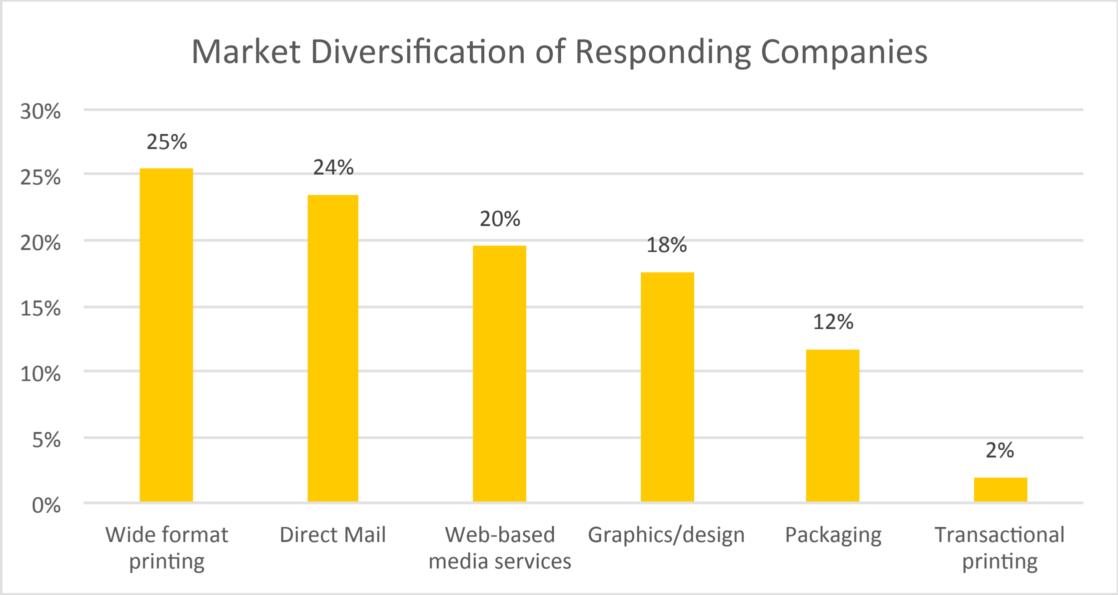
Question: Are you currently diversifying your business?

Insight 8: They Are Also Divided On What Markets to Diversify Into

For those companies that are diversifying, the markets that they have chosen to diversify into is also fascinating. You can see a variety of trends when looking at the top three areas companies have chosen to diversify into:

- Wide Format printing accounts for 25% of firm's diversification strategies, which makes sense, as this strategy would be close to home for many printing firms.
- Similarly, at 24% of the industry, moving into Direct mail strategies would be familiar territory for a variety of companies, though we wonder with the rise of inbound marketing strategies if this is a long term recipe for success?
- Rounding out the top three, is the 20% of companies who are delving into web-based media. While this may be a bit more of an up-front stretch, it will be interesting to watch these firms, and see if this digital bent also has more traction as a long-term play.

We all understand that diversification is important, but also that developing core competencies is expensive and takes time. If you decide to diversify, you need to make sure the ROI is there. We're excited to see how these strategies play out over time.



Question: What area are you diversifying into?

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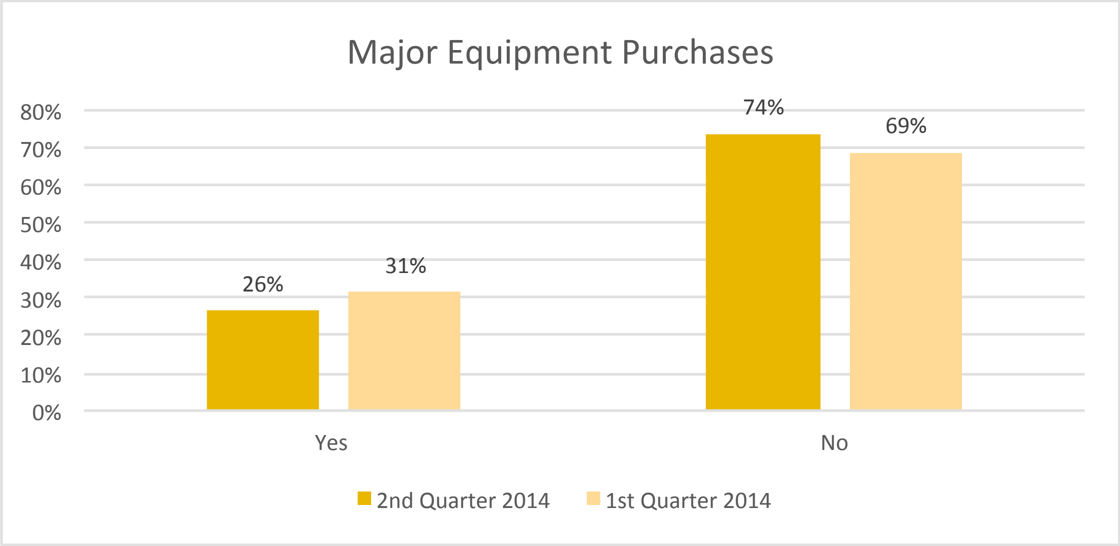
Insight 9: Firms Report Low Rates of Capital Investment

This is a newer question for our survey, so we are largely dealing with new data. However, over the past two quarters, the trend so far is that companies are less likely to make a capital purchase this quarter than in Survey 1Q14.

This data may be reflective of real time changes in the economy. Looking at U.S. GDP numbers, investment in inventory was also down across the board, so we see this data as an indication that companies in close touch with their demand pulse and react quickly to tighten the purse strings when slowdowns occur like we witnessed in the first quarter of 2014. Hopefully, the positive sales data we saw in this quarter's forward-looking survey questions will bear out, and we will witness increasing Capitol Expenditure outlays in the coming months.

For those companies who did make a purchase last quarter, investments tend to reflect growth in areas of profit. Firms reported outlays in digital prep and reproduction equipment, along with a smattering of bindery equipment replacement. Digital presses and servers lead the way in purchases.



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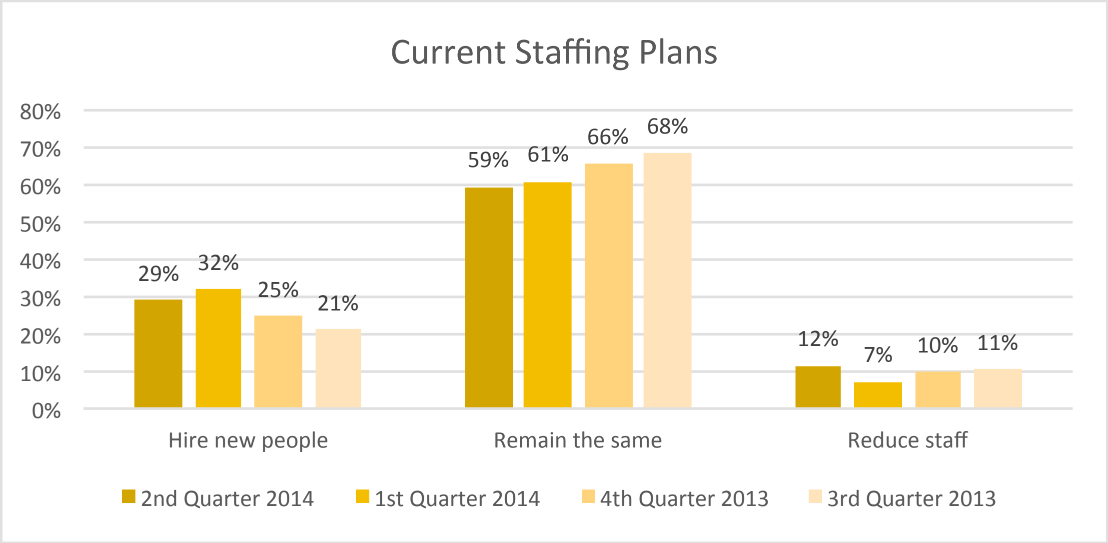
III. Staffing Trends

Insight 10: Staffing Rates Are Changing - In Both Directions

The questions focused on hiring trends are, predictably, extremely interesting to us. Here, we see that hiring new people is trending positively, with 29% of companies expecting to increase their staff this quarter.

Simultaneously, the data also showed an increase in staff reductions, with 12% of companies anticipating layoffs this quarter. This is likely a reflection of slowed demand in the first quarter – and may also be the reason we saw an increase in reported profits this quarter.

Today, companies are so lean and they move so fast, often it appears the only place they can still cut quickly is head count flexible or otherwise. And, with employment costs rising this play can seem to make sense at the time. However, we caution prudence before you begin to make cuts, as this strategy may ultimately bite from behind. In the end your company is only the sum of its people. As we move cautiously into the new economic upswing, your staff will remember how they were treated in the lean years and react accordingly, with either loyalty or a wandering eye.



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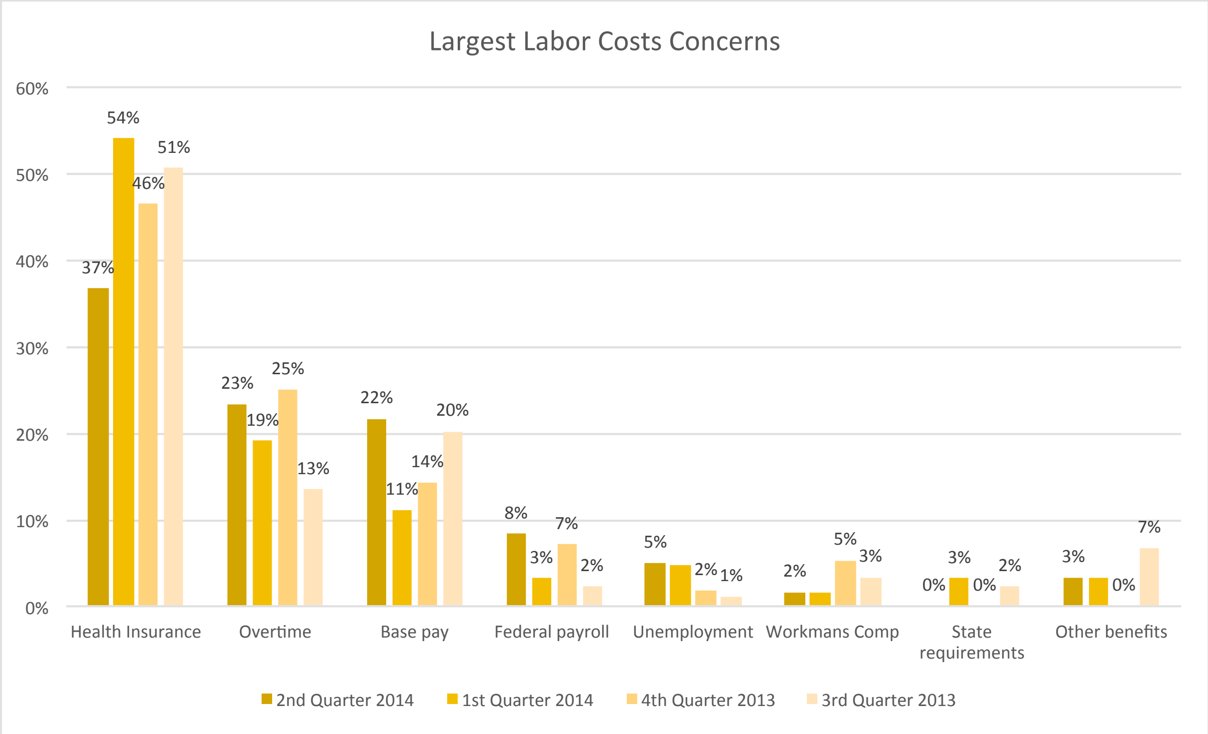
Insight 11: Insurance and Taxes Are Driving Labor Costs

This question addresses the changing costs of labor, which are a huge behind-the-scenes driver for staffing decisions.

What is surprising (and potentially unclear to employees) is that the take-home portion of labor costs – what an employee takes home as a salary – is at one of the lowest levels ever - roughly 1/3 of the total pay rate. Today, companies and employees pay roughly two-thirds of the salary towards Federal and state taxes, insurance, benefits, administration and other taxes and fees such as local or county taxes.

As you can see here, costs such as health insurance are rising so quickly, that it comes as little surprise that employers are hesitant to hire (as reflected in the chart above).

One positive indicator of a rising economic cycle is the attention firms are paying to base rates, with 22% saying this is their largest cost in the second quarter. In fact, this is the first survey since 2007 that has witnessed a spike in respondents concerned over base pay rates. As the economy recovers and firms need quality employees to meet the rising demand, we expect this attention to base pay levels to rise even more. We hope equal attention is focused on the other hidden 2/3 of labor costs.



Question: Regarding labor costs, what component of the costs has been increasing the fastest last quarter?

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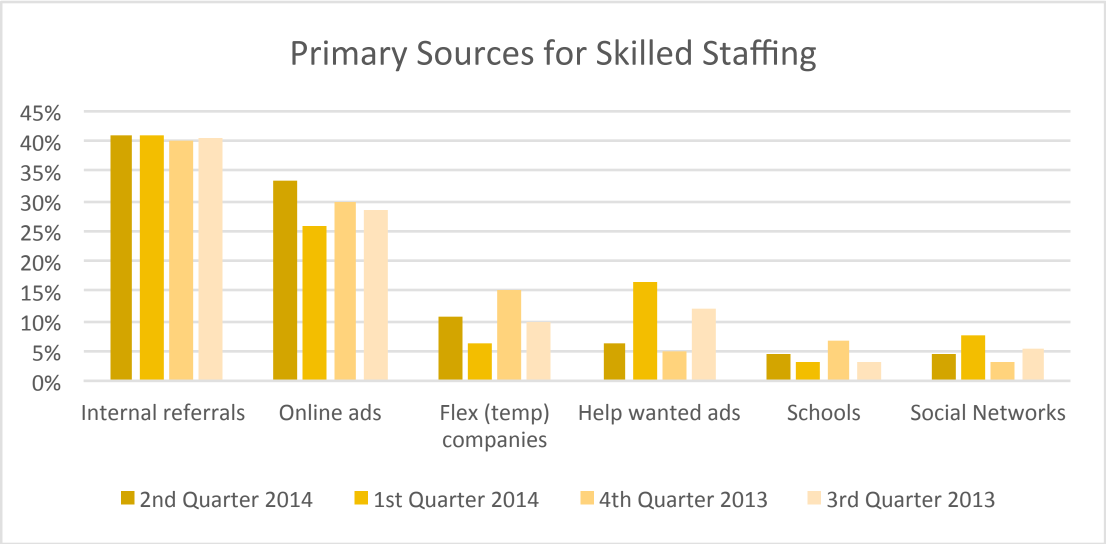
Insight 12: Skilled Staffing Fulfillment is (Slowly) Moving Online

The final question in our survey speaks to where firms are finding their skilled staff. Perhaps there is no surprise that referrals continue to drive the majority of new staffing fulfillment, but we are also witnessing an interesting rise in online referrals and flex hiring opportunities.

Of slight concern here is the very low levels (less than 5%) of skilled staff coming from schools or universities. The challenge here is that many schools have significantly reduced or eliminated training programs for our industry – as they instead offer classes in areas they see as growth areas. This lack of formal education bodes poorly for the industry, and means that in order to stay competitive, we will need to set up more innovative forms of apprentice training, or band together to establish association training resources. Once demand returns, expect companies to move quickly to meet these new training concerns.



Question: What are your primary sources for skilled staffing?

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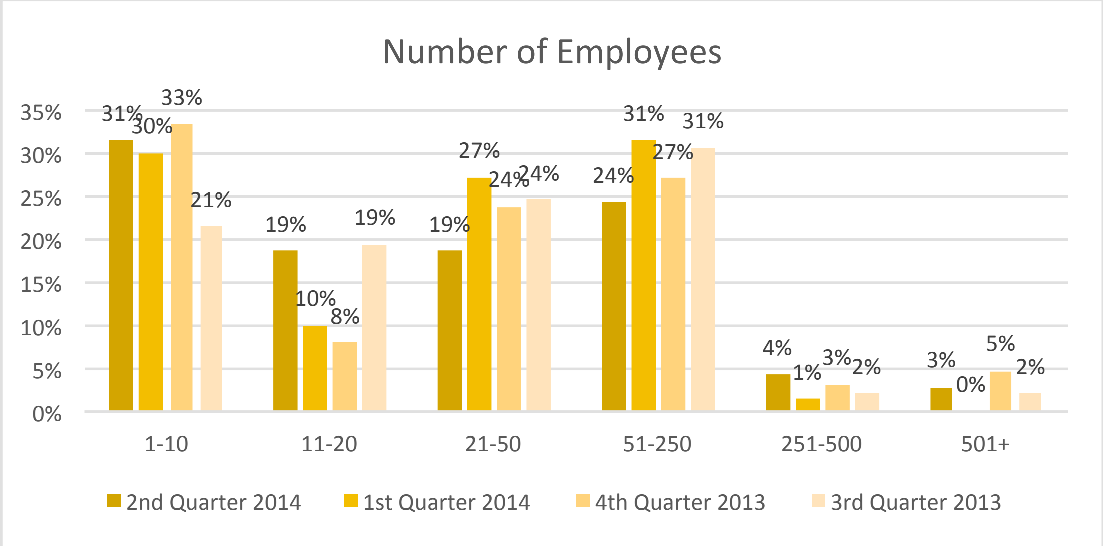
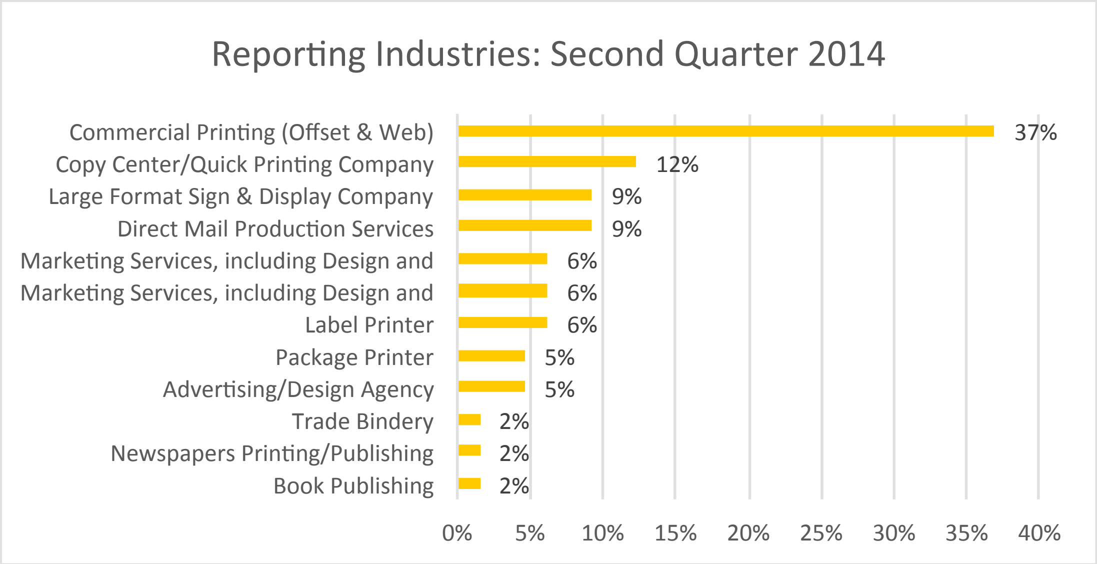
IV. Demographics



Question: How many employees do you have within your organization?



Question: Please select the industry(s) that best describe your business.

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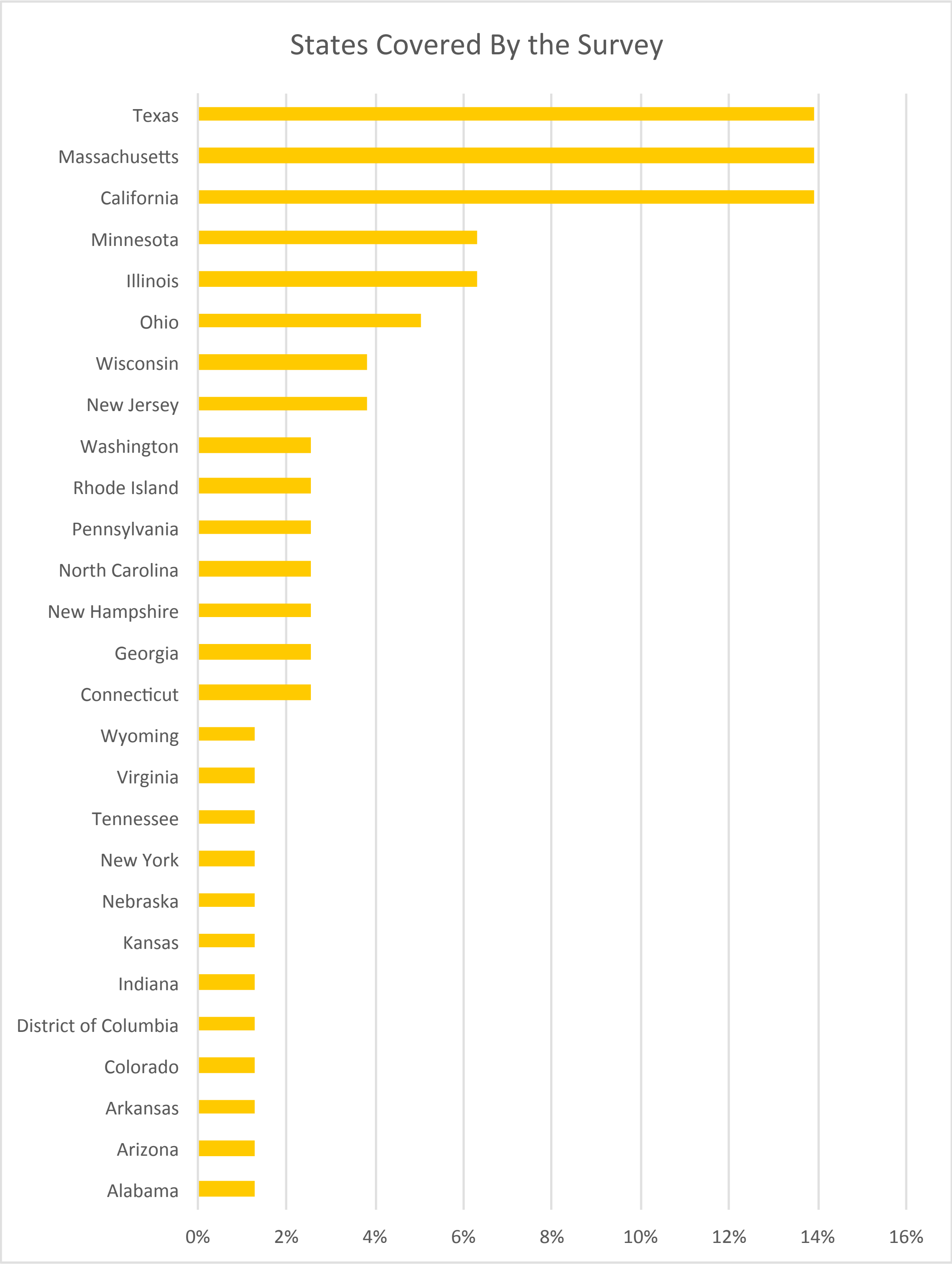

Question: What state are you located in?

V. Survey Methodology

Semper International provides this survey based on quarterly estimate of trends in the printing and graphics industries. To prevent bias, the survey questions were designed by Semper corporate partner Cvent. Questions were designed to be both qualitative and quantitative. To preserve confidentiality, individual company information is not part of the tabulation. Survey participants are more than 301 small, medium and large printing companies, both clients and prospects of Semper International. Participants provide data on revenue and hiring a well as estimated outlooks on future trends. Data was requested from a random sample. They were not screened.