

SMB Job Generation Outlook Q2 2016

The SMB Job Generation Outlook examines executive perspectives on topics affecting America's small to mid-sized business market, including the economy, employment trends, political and sociological environments, and the tangible impact these factors have on SMB business and employment planning.

Top Trends of Q2 2016

The Lucas Group SMB Job Generation Outlook provides a quarterly, trending analysis of the issues most pertinent to today's U.S. small to mid-sized business (SMB) market. The survey takes the temperature of business executives nationwide and delivers insights and statistics to help our readers determine the health of the SMB community, highlight positive and negative macro business climate trends, and assess, in detail, the daily challenges SMBs face.

Where Does Our Data Come From?

With over three years of market data from more than 3,100 SMB executives, the Q2 2016 Outlook report evaluates responses from business leaders who knowledgeably represent the SMB, a foundational sector of the U.S. economy and workforce.

This national survey of SMB presidents, CEOs and business owners reviews quarterly Outlook reports and provides comparative analysis to previous SMB Job Generation Outlook surveys, with both quarterly and year-over-year comparisons. The survey generates responses from over 20 defined business sectors.

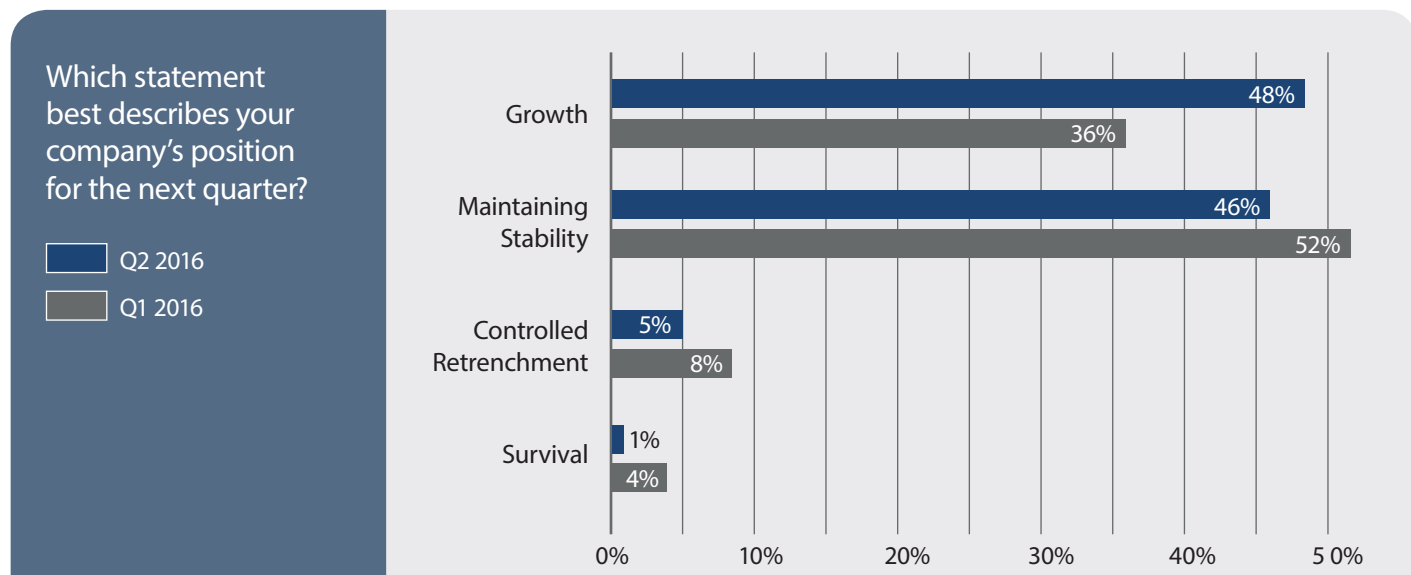
The Q2 2016 report includes a representative cross-selection of industries, regions and company sizes

and structures. Most survey participants have operated for longer than 10 years, report corporate revenue between \$25M and \$600M and employ between 100 and 5,000 people.

SMBs Report Growth and Confidence

Each quarter, the SMB Job Generation Outlook asks executives a baseline question regarding each company's current overall outlook. Are they positioned for growth, stability, controlled retrenchment or survival? This company mode question helps capture a broad-spectrum view of how SMBs currently see themselves in the marketplace.

In Q2 2016, 48% of SMBs reported their companies to be in growth mode – a 12% jump from Q1 2016 as feelings of stability from the previous quarter gave way to feelings of growth. Forty-six percent reported they were in stable, healthy condition (down 6%). Only 6% felt they were in controlled retrenchment or survival mode, down 6% from Q1. In short, all responses were geared towards a solid growth quarter.



Report Confidence and Concerns: 4 Noteworthy Executive Responses

SMBs reported confidence in overall company growth rates and U.S. economic prospects in Q2 of 2016. (See graphics page 3.) Hiring plans remained solid, downsizing plans declined slightly, and the majority of companies reported increasing pay this quarter. With a high demand for skilled workers and the need to fill vacancies (understaffed responses increased 9% this quarter), we expected optimism in job growth to return to higher levels. However, executives actually reported a decline in optimism regarding job growth.

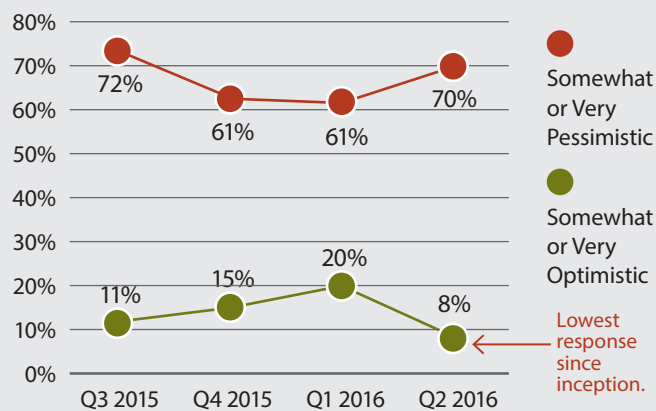
While many factors influence job growth optimism, responses to four survey questions highlighted the possible

underlying reasons for this decline:

1. Optimism in government bipartisanship hits new low (Chart 1)
2. Domestic and international competition spikes (Chart 2)
3. IT, sales and finance talent remain hard to find (Chart 3)
4. Affordable Care Act (ACA) concerns fade, but health care cost concerns mean employees must contribute more to their care (Chart 4)

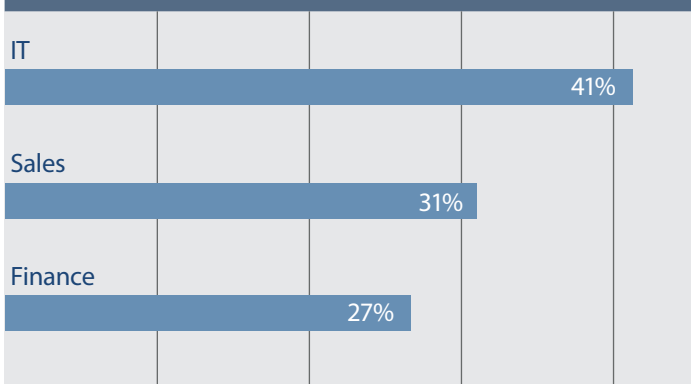
Graphic 1

Please indicate your feelings about Bipartisanship in Federal Governments.



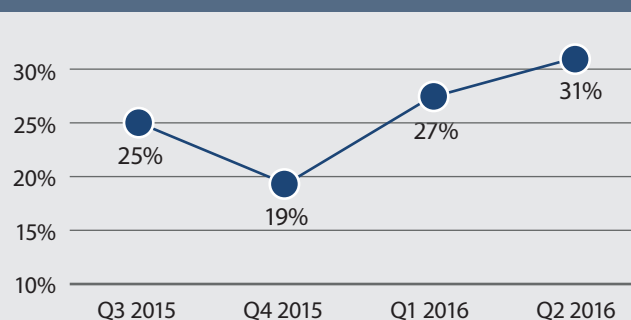
Graphic 3

What areas of open professional and management positions are most difficult for your company to find qualified candidates?



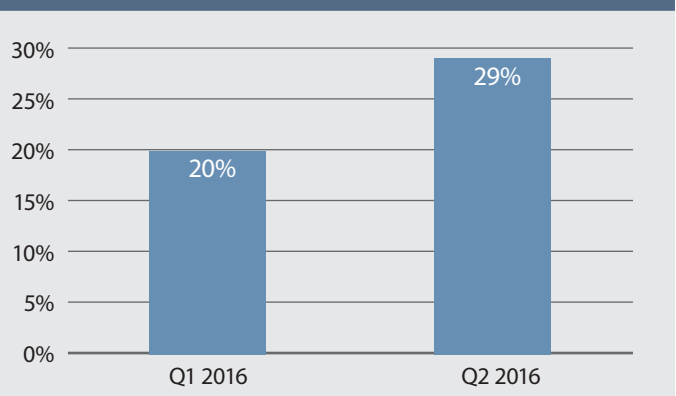
Graphic 2

Please rank the following issues from top to bottom based on the challenge they represent to your company in the next quarter. (Second Place Answer in Q2 2016: Domestic and International Competition)



Graphic 4

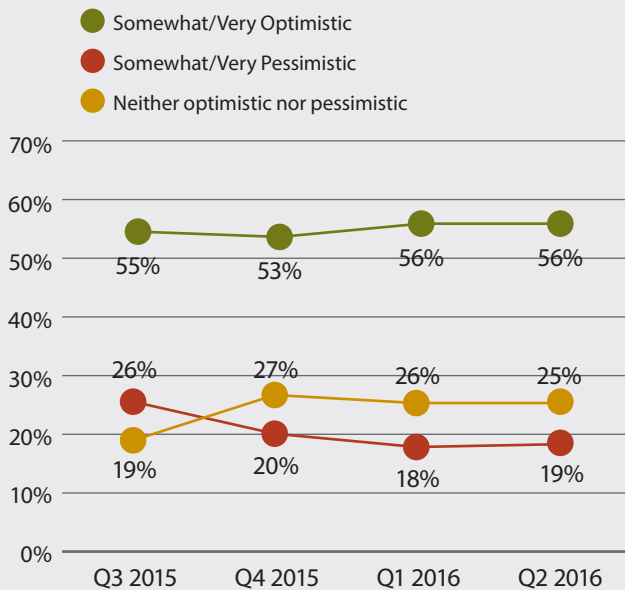
What is your company doing to address health care costs?
Answer: Increase Employee Contribution



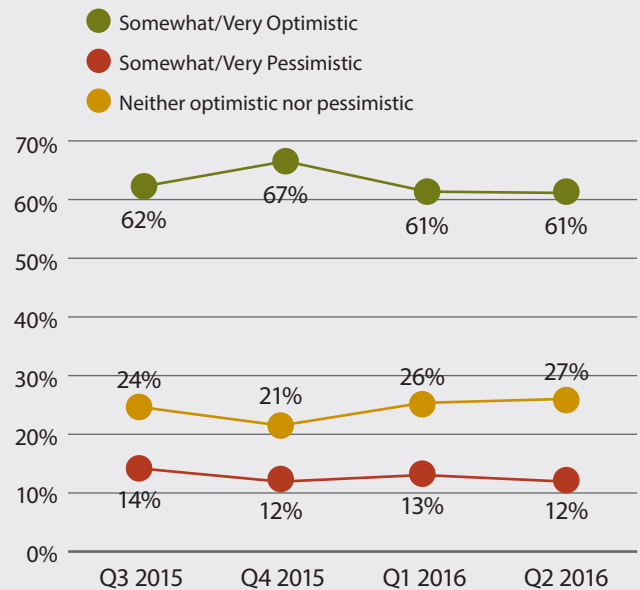
U.S. Economic Prospects, Hiring/Downsizing and Job Generation

A majority of executives feel “somewhat/very optimistic” about the U.S. economy. This positive response has remained consistent over the past year, while “somewhat/very pessimistic” responses have steadily declined. Confidence in economic prospects within the company context also returned solid results in Q2 2016. Over 61% of executives have reported feeling confident about company prospects in each quarter since Q3 2015. Pessimism within the company context remains low, hovering at 12% in Q2 2016. In short, SMBs are consistently both more positive and less negative about their own company’s economic prospects than the U.S. economy’s prospects.

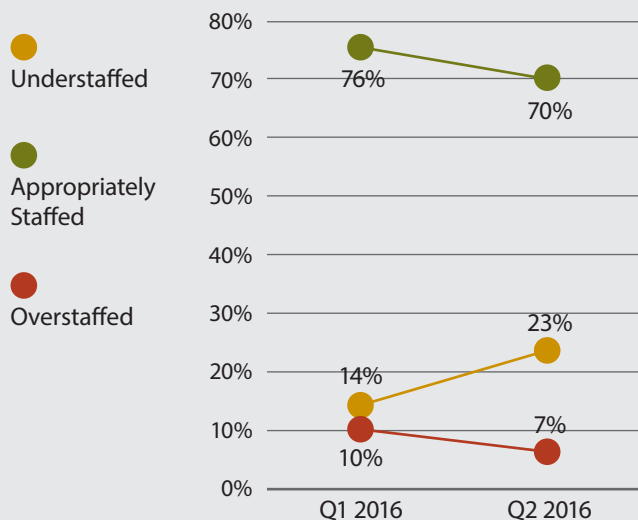
Please indicate your feelings on the economic prospects for the U.S. in the next quarter



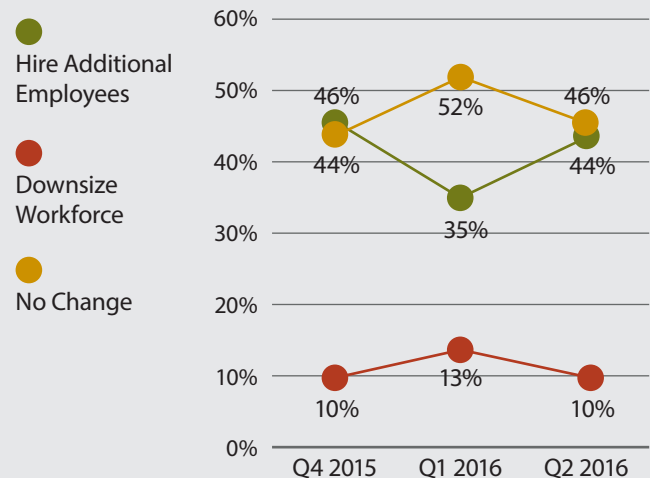
Please indicate your feelings on the economic prospects for your company in the next quarter



Do you consider your company...



What are your hiring or downsizing plans for the next quarter?



Job Growth. SMBs continue to be the driver of job growth in the U.S. Generally, 88% of respondents feel that SMBs are job creators nationally, and 75% also consider their own companies to be job creators locally.

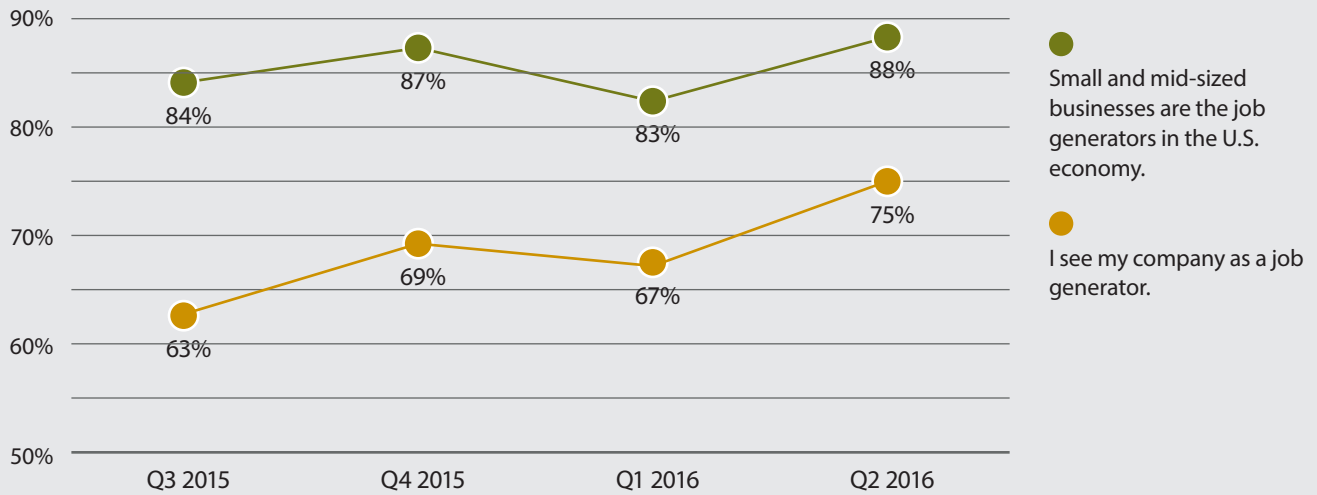
Hiring Plans. After a Q1 drop in reported hiring plans, near-term plans to add SMB employees rebounded in Q2 to more closely mirror Q4 2015 levels. Over the next quarter, 44% of respondents plan to hire more employees, an increase of 9%

over Q1 2016. Only 10% of respondents plan to downside, with the remaining respondents reporting no expected changes. (See page 5 for additional hiring analysis.)

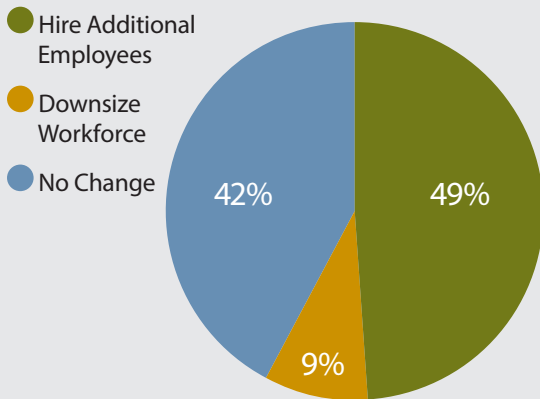
Take-Home Wages. A significant majority (82%) of Q2 2016 executives reported increases in employee take-home pay over the past year. Fifteen percent reported no change, and only 3% reported a decline in employee pay.

Comparison: SMBs are Job Generators for US Economy vs My SMB is a Job Generator

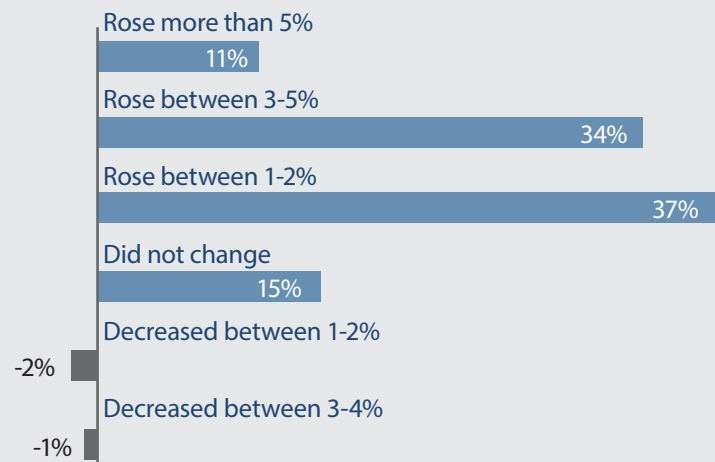
*Note: Data reflects the percentages of respondents who agree or strongly agree with each statement.



What are your hiring or downsizing plans for the next 12 months



Collectively and companywide, how did your employees' take-home wages change in the past 12 months?



SMB Hiring and Downsizing: Quarterly Forecast.

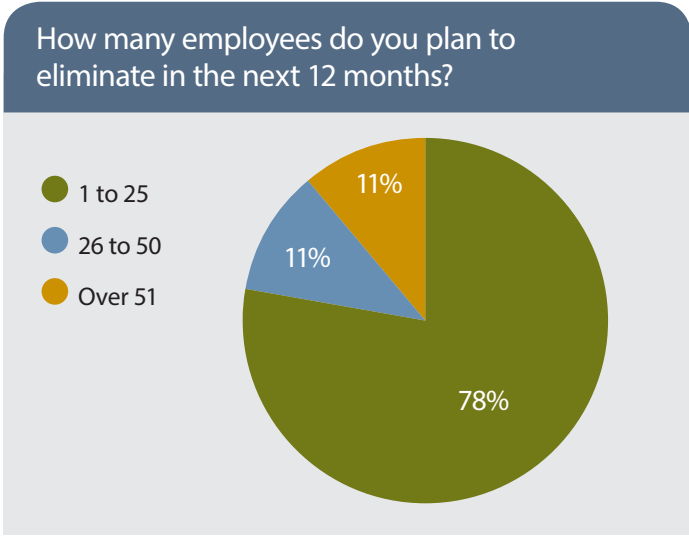
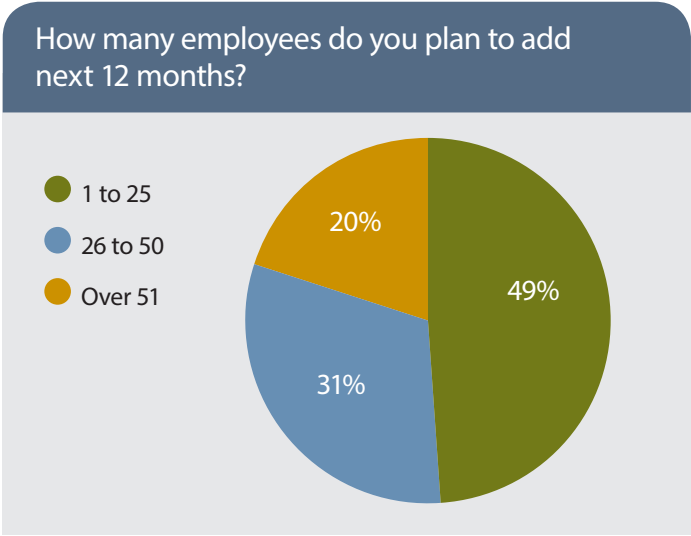
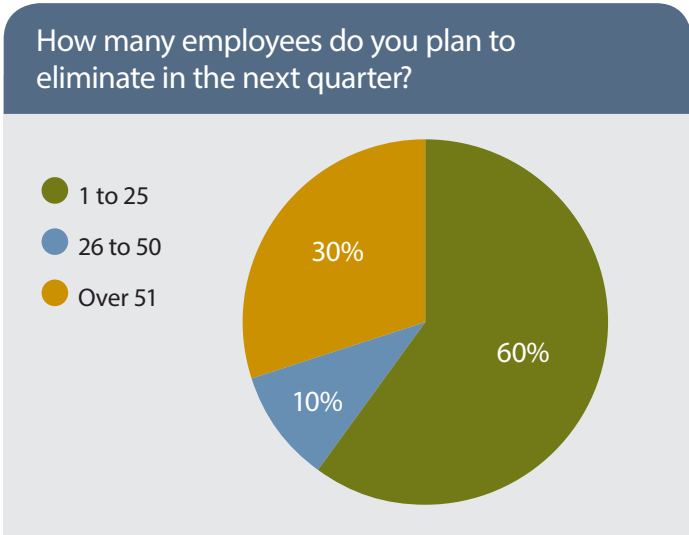
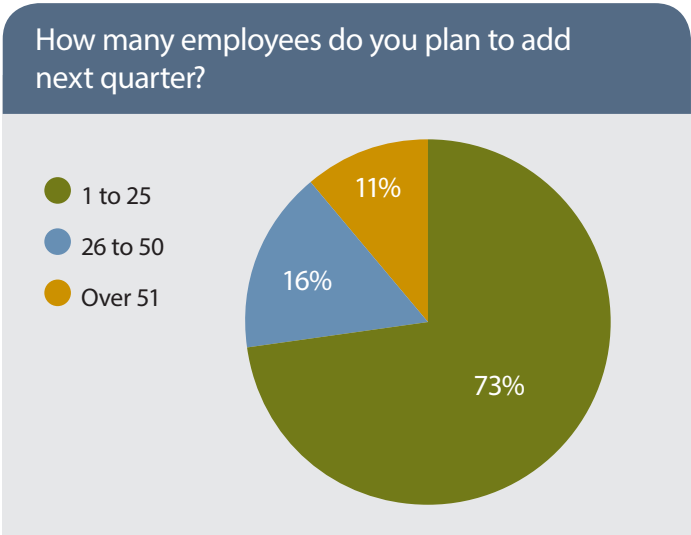
Projected hiring plans for the next quarter are conservative. Less than half of all respondents (44%) plan to hire. Of the SMBs that do report hiring plans, the vast majority (73%) plan to add between one and 25 employees. Only 16% plan to hire 26 to 50 employees and just 11% plan to hire over 51 employees.

Quarterly downsizing plans are also limited. Just 10% of survey respondents indicated plans to downsize. Of these respondents, nearly two-thirds (60%) indicate they will eliminate between one to 25 employees, with 30% of downsizing respondents planning to eliminate 1 to 10 employees and an additional 30% planning to eliminate 11 to 25.

SMB Hiring and Downsizing: Yearly Forecast.

Long-term hiring plans over the next year are slightly stronger than near-term hiring. Nearly half of all respondents (49%) plan to hire additional employees in the next year. Of the respondents who plan to hire, 49% plan to hire between 1 and 25 employees, 31% plan to hire between 26 and 50 employees, and 20% plan to hire over 50 employees.

At the same time, only 9% of survey respondents plan to downsize. Of these respondents, downsizing plans are limited. The vast majority of respondents planning to downsize (78%) anticipate only eliminating between 1 and 25 employees.



Job Growth Prospects: Comparing U.S. Optimism With Company Optimism

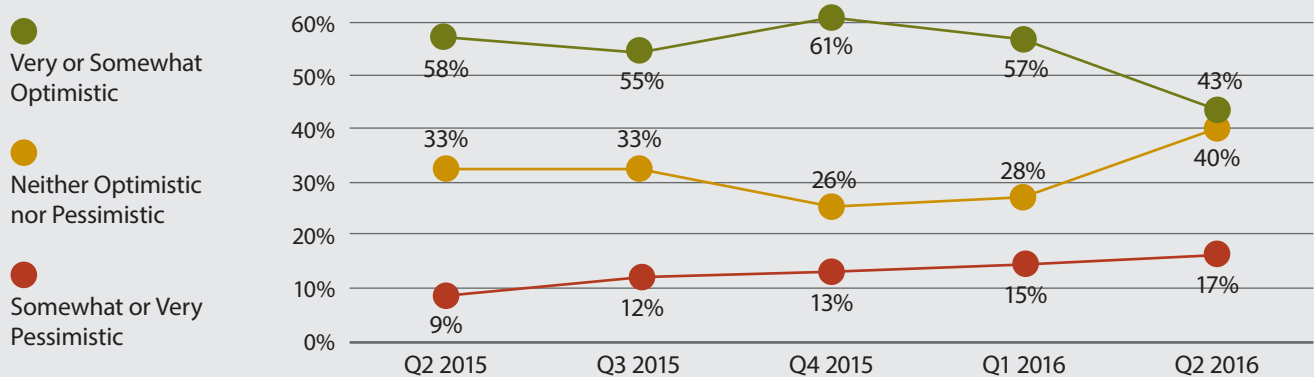
A sizeable number of survey respondents are on the fence about job growth. The category response “Neither Optimistic nor Pessimistic” grew 12% since Q1 2016 to hit 40% in Q2 2016, the highest reported number to date on the survey. In addition, the “Somewhat or Very Pessimistic” response has steadily increased from 9% to 17% over the last year.

In the chart below (“Please indicate your feelings about job growth prospects for your company in the next quarter”), note the shrinking difference gap between the green and red lines. The difference between “Very or Somewhat Optimistic” versus

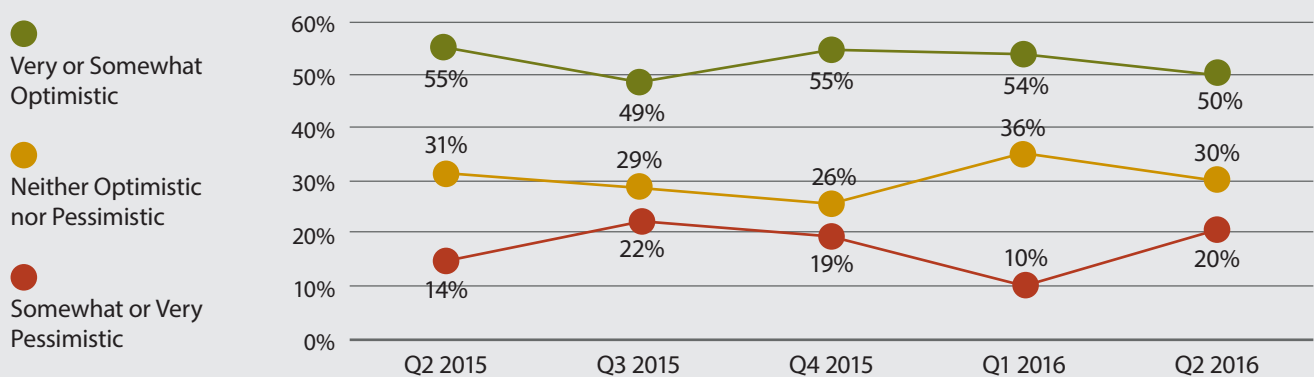
“Somewhat or Very Pessimistic” responses has decreased from a 49 point difference in Q2 2015 (60% versus 9%) to a 26 point difference in Q2 2016 (43% versus 17%).

National Job Growth Prospects. Optimism regarding SMB job growth nationally has cooled slightly, dropping 4% since Q1 2016. The crossover on the final graph comparing optimism (company versus nationally) indicates that for the first time in over a year, SMBs are more optimistic about U.S. growth policies than they are about their own company’s prospects.

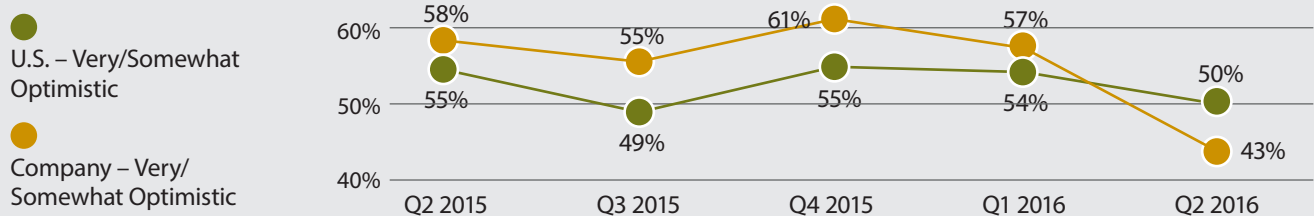
Please indicate your feelings about job growth prospects for your company in the next quarter



Please indicate your feelings about job growth prospects for the U.S. in the next quarter



Indicate your feelings about job growth prospects for the U.S. versus your company in the next quarter



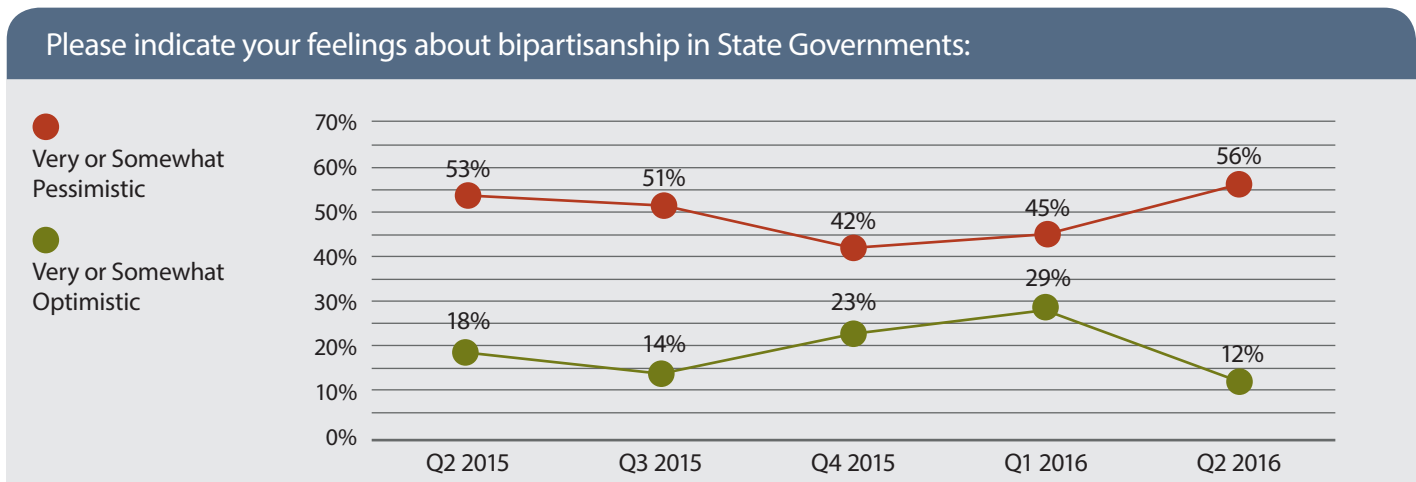
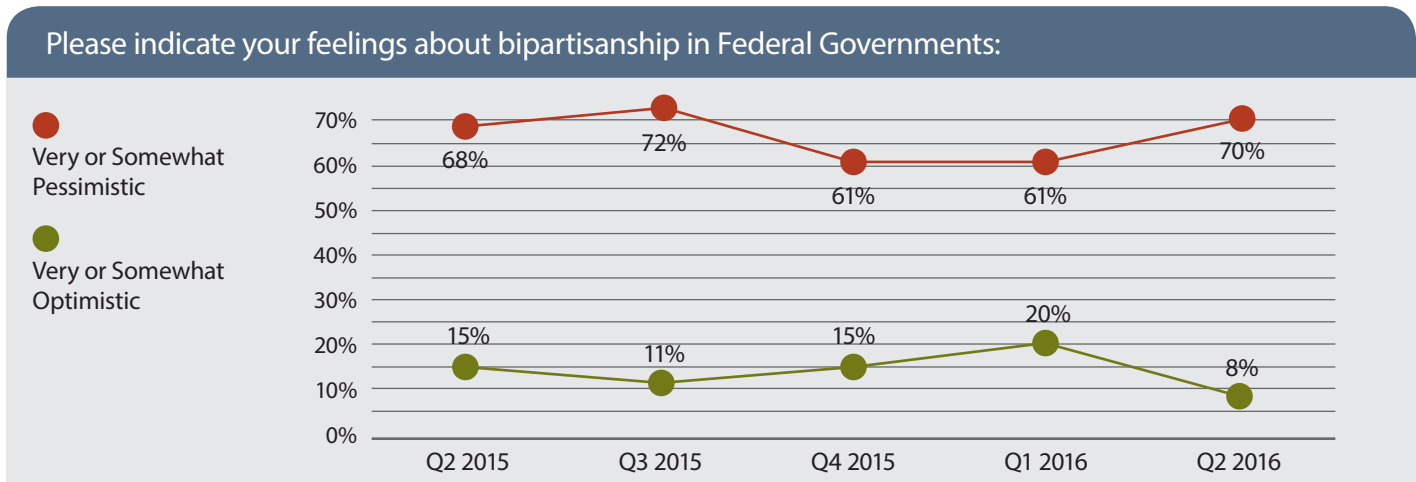
SMB Negativity: Perception of Government Bipartisanship Gridlock Worst On Record

The overwhelming majority of SMBs in the Q2 21016 survey feel government is gridlocked and getting in the way of business. Reported perception of bipartisanship in Congress has declined to the point where SMBs now feel Congress primarily has a negative impact on business.

In Q2 2016, executive respondents reported their lowest optimism level to date, coming in at 8%. In fact, Q3 2014 was the last time optimism in bipartisanship approached such a low number (at 9%). This result may reflect attitude shifts caused by the increase in negative political advertising occurring during election cycles (second and third quarters of even numbered years). Most quarters since Q3 2014 reported results in the

mid-teens. It should be noted that Q2 2016 results did not show the highest pessimism numbers since survey institution, only the lowest optimism numbers.

Optimism for bipartisanship at the state level has also declined since Q4 2015 and Q1 2016. The Q2 2016 drop to 12% optimism is notable, and ties for lowest with two quarters on record (Q2 2014 and Q3 2014). In addition, pessimism rates are the highest reported since Q3 2014. The silver lining to these results? The closer you get to local politics, the more optimistic SMB executives are about the potential for bipartisan solutions.



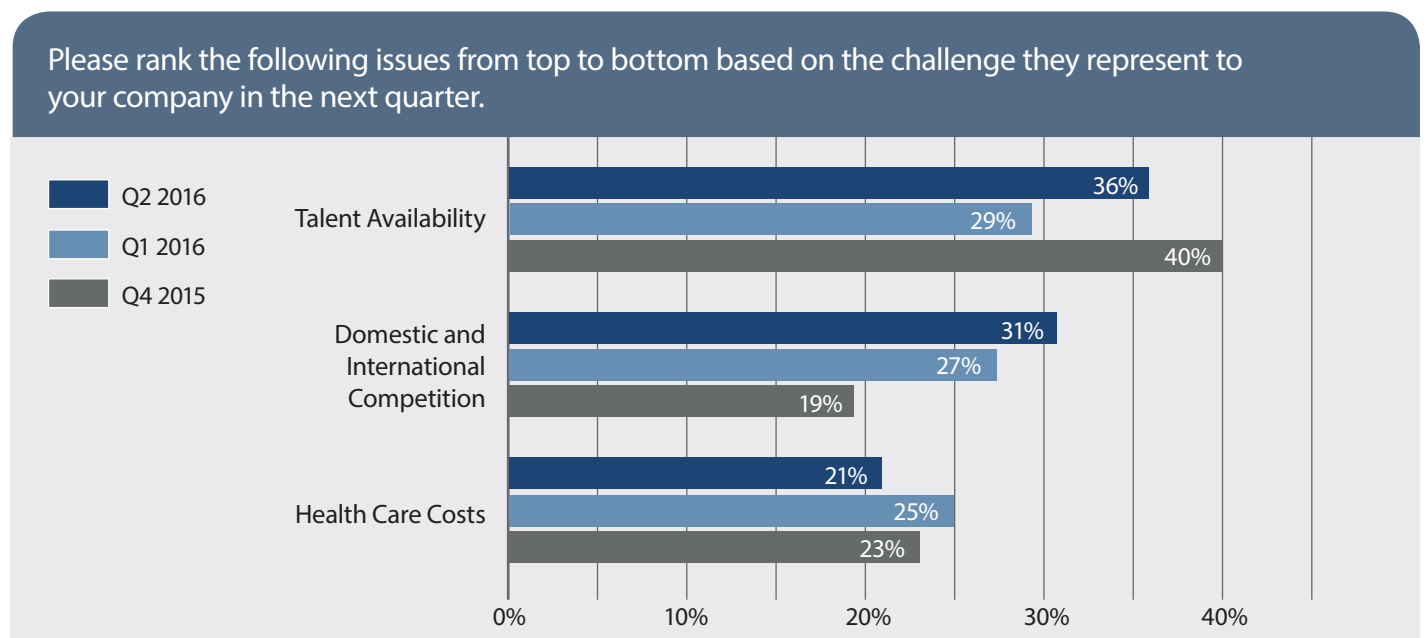
Domestic and International Competition Spikes

The graphic below demonstrates a rapid growth of concern regarding domestic and international competition from Q4 2015 to Q2 2016. Concerns about talent availability have fluctuated over the last six months as competition for top talent has steadily increased. Survey respondents were asked to rank their primary business challenges in the next quarter. “Talent Availability”, “Health Care Costs” and “Domestic and International Competition”

Interestingly, “Talent Availability” still ranks at the top of the list, back up after Q1 2016 (albeit off 4% since Q4 2015). “Health care costs” remain a consistent concern in third place overall, while the “Domestic and international competition” category catapulted from third place to second place over the last three quarters, increasing 12% since Q4 2015.

Domestic and international competition had been hovering in third or fourth place on the list of concerns since 2013 (20% range). The second quarter of 2016 produced the highest concern about competition level that we have seen to date, coming in at 31%.

*While the Q2 survey did not ask participants directly about concerns regarding specific trade deals, laws and regulations, it should be noted that public discourse surrounding the Trans-Pacific Partnership¹ (TPP), NAFTA and other trade agreements has greatly increased during the last quarter. It is possible that news reports and political discussions citing increased international competition and job losses related to trade deals are stoking executive concern about competition.



¹The USTR-EOP reports the full Trans-Pacific Partnership text: [HERE](#).

IT, Sales and Finance Talent Still Hard to Find

Survey respondents reported increased difficulty finding qualified professional talent in Q2 2016. Only 2% of executives say that hiring professional talent is easy and no one said it was very easy. The second quarter of 2016 ties Q1 2015 for the highest reported hiring difficulty in the survey's three-year history.

Finding IT talent continues to be top hiring concern, followed by sales and finance. The need for qualified IT professionals has stayed consistently high (except Q4 2015). Finance has steadily gained since Q3 2015, rising from 9% to 27% over the year. Recruiting and hiring qualified sales employees is still the second largest need, but the urgency of this talent need has decreased over the past two years.

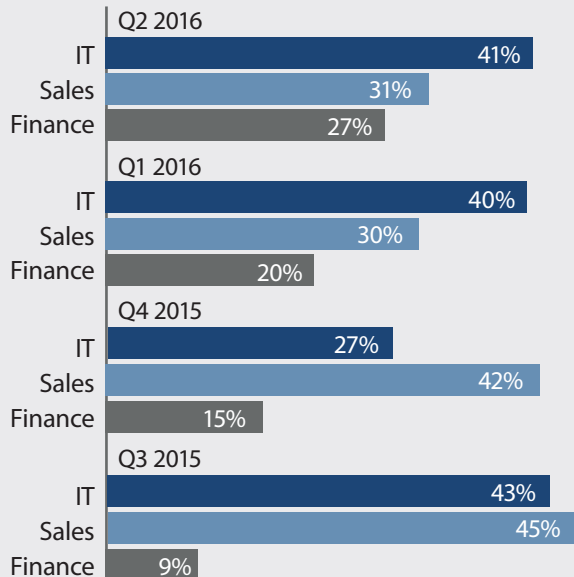
Why is Finding/Hiring IT Talent a Challenge for SMBs? Based on survey findings and the current business climate, these are three possible reasons:

1. For the first time since 2007, the Federal Unemployment Rate has dropped below 5.0 (in 2016); dipping as low as 4.7 in mid-Q2 2016. ([US Bureau of Labor Statistics](#)). Essentially, the best talent may be hired already, forcing businesses to lure top talent away from the competition.
2. The IT sector itself is expanding rapidly. Transitions to cloud

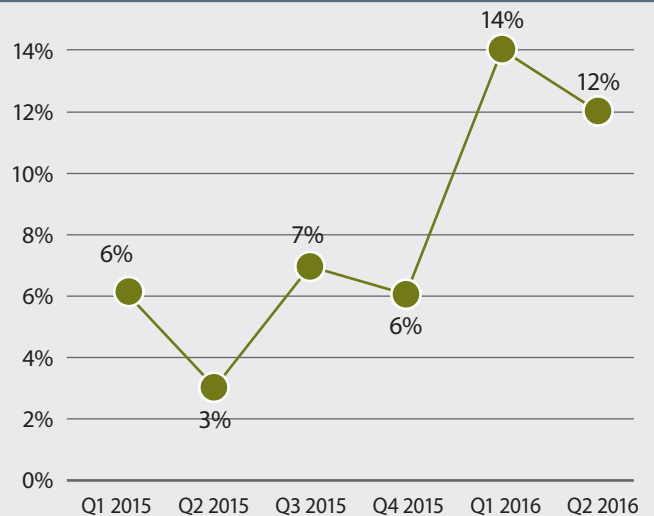
based infrastructure, mobile web and complex cyber security issues require exceptional talent. [According to the USBLS](#), "employment of computer and information technology occupations is projected to grow 12 percent from 2014 to 2024, faster than the average for all occupations. These occupations are expected to add about 488,500 new jobs, from about 3.9 million jobs to about 4.4 million jobs from 2014 to 2024, in part due to a greater emphasis on cloud computing, the collection and storage of big data, more everyday items becoming connected to the Internet in what is commonly referred to as the 'Internet of things,' and the continued demand for mobile computing."

3. H-1B [visa](#) access has generally been limited and challenging for mid-market companies and now it may become [more difficult](#). Seemingly, Congressional concerns differ drastically from concerns reported by executives in our survey. Hiring policy changes, proposed in the U.S. Congress this summer, may prohibit or delay companies from hiring H-1B employees if they employ more than 50 people and more than 50% of their employees are H-1B and L-1 visa holders.

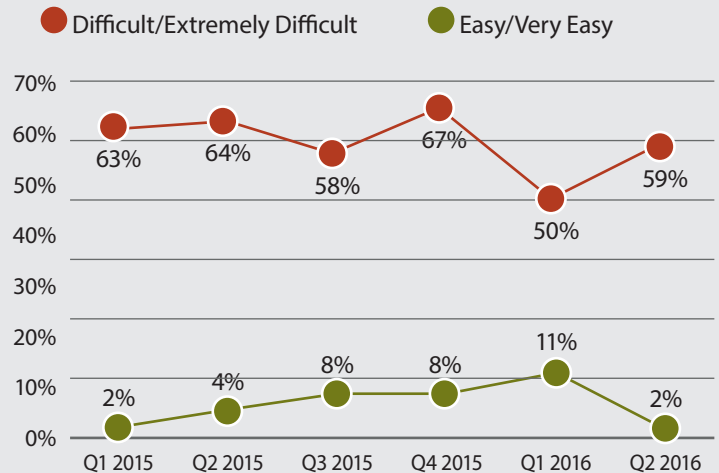
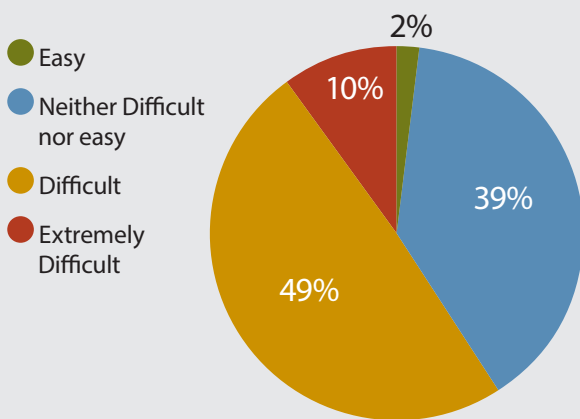
What areas of open professional and management positions are most difficult for your company to find qualified candidates?



What areas of open professional and management positions are most difficult for your company to find qualified candidates?
Answer: Legal



How difficult is it for your company to find qualified candidates for open professional and management positions?



Two interesting notes from the Q2 2016 survey:

1. In the past two quarters, executives reported an increase in difficulty finding and hiring legal talent. Concerns over hiring legal talent are much lower than the top five categories, however the jump could be an interesting trend to track over time. Over the survey's three year history, the last two quarters are much higher than usual with Q1 2016 and Q2 2016 rendering the highest results. Having averaged 7.6% over the past three years, this is the highest response rate to date.

2. When it comes to attracting new talent, many SMB companies seem stymied. Twenty-four percent reported that "we are doing nothing/don't know" how to attract and recruit talent. For those actively pursuing talent, many SMBs continue to rely on salary/bonus offers (27%). Traditional advertising has gradually declined from 18% in Q2 2015 to only 2% today. Surprisingly, survey respondents reported another decrease in online posting (e.g. LinkedIn, CareerBuilder) from a survey high 23% in 2Q 2015, to 12% in Q1 2016, to 8% in Q2 2016.

What is your company doing to attract/recruit qualified professional talent?

Top 3 Responses

Increase/offer competitive salaries/bonuses/compensation packages/benefits

27%

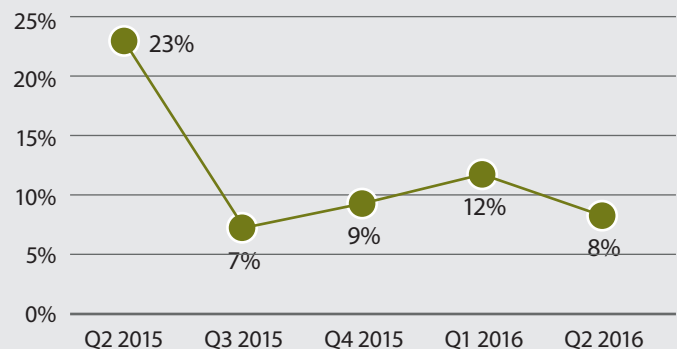
College recruiting/work with universities

12%

Recruiters

10%

Online postings/social media

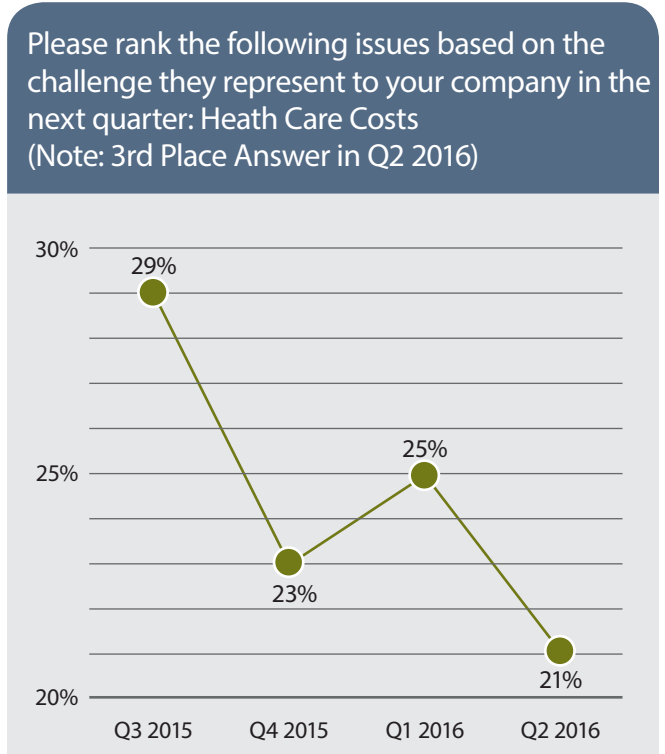
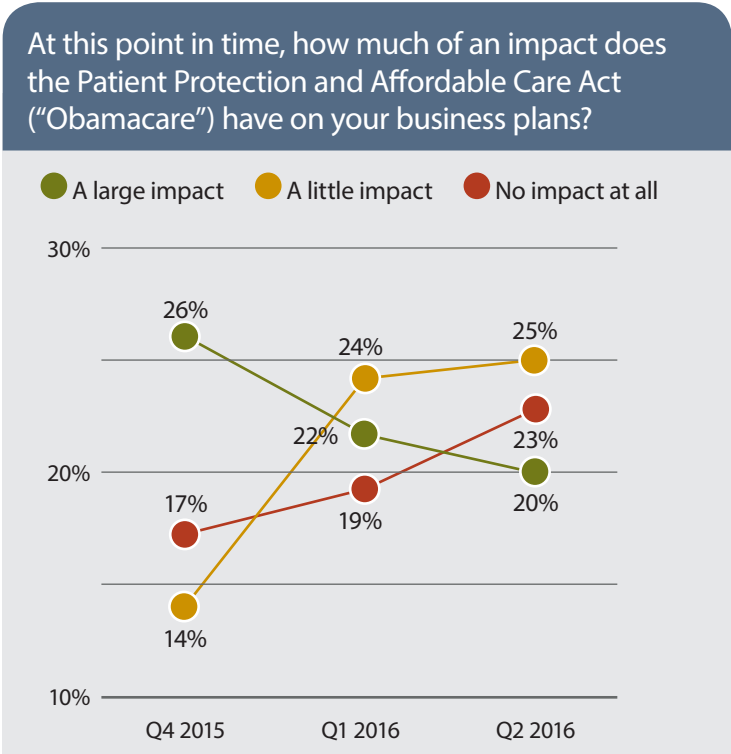


Affordable Care Act Concerns Fade, Health Care Cost Worries Remain

Once a top issue for SMBs, concern over the Affordable Care Act (“Obamacare”) continues to decline. General concerns over health care costs persist, however, prompting SMBs to consider new cost management strategies.

Affordable Care Act. Nearly half of all SMBs (47%) report that ACA has “no impact” (23%) or only “a little impact” (25%) on their business plans. SMBs that felt ACA had a large impact on business plans fell to 20% in Q2 2016, dropping 6% from Q4 2015. This decline in ACA-related concerns may be due to the law’s implementation timeline. As of Q2 2016, most of ACA’s direct employer impacts have already occurred. Businesses now understand how ACA impacts their health care costs and are positioned to respond to these changes.

Health Care Cost Concerns. While health care costs remain a worry for SMBs, talent acquisition/hiring and international competition are now bigger worries. (See chart page 8 for detail.) Concern over health care costs peaked in Q4 2013 when 40% of SMBs listed this as their top issue. Health care cost concerns dominated 2014 and Q1 2015. In Q2 2015, SMB concern over talent acquisition pulled even. Starting with Q4 2015, talent acquisition/hiring emerged as the leading SMB concern. Last quarter (Q2 2016), international competition also surpassed health care. In fact, this quarter (Q2 2016) marks the lowest percentage of SMBs reporting health care cost concerns.



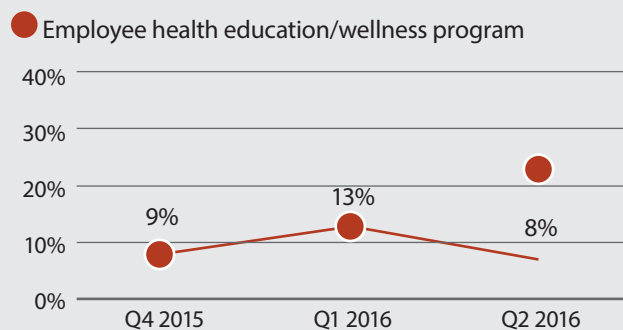
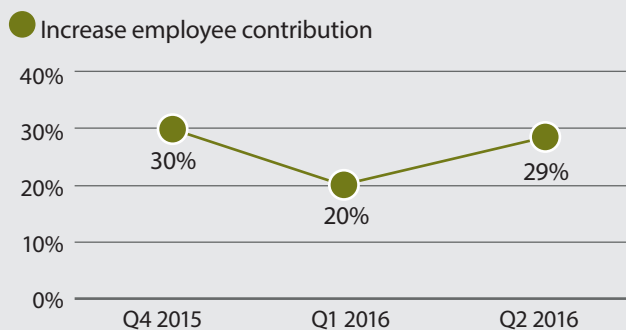
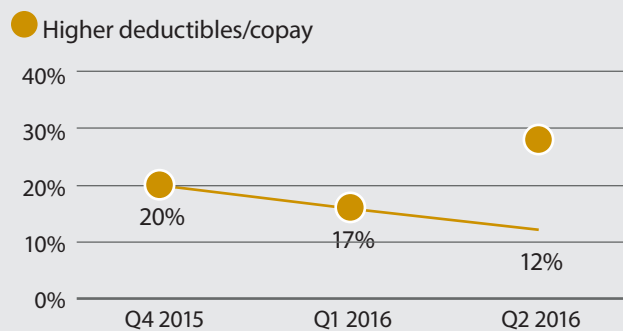
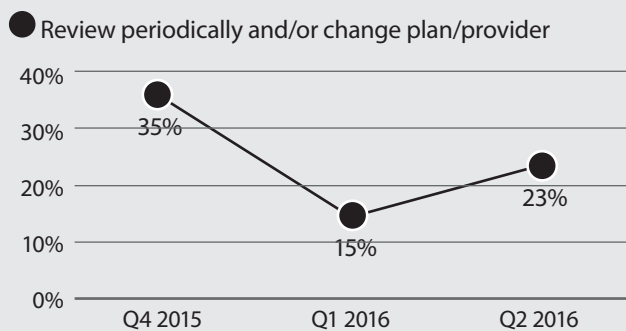
Health Care Affordability. While actual health care costs vary significantly depending on business structure and employee makeup, SMBs are taking similar steps to reduce these expenses.

In Q2 2016, cost shifting seemed to be the most popular method for addressing health care expenses. Nearly one-third of SMBs (29%) are opting to pass along health care costs directly to their employees in the form of increased employee contributions, a 9% increase from Q1 2016.

SMBs are once again reviewing their health care plans and changing providers for better, more affordable options. Previously the most popular option for cost control in Q4 2015, the number of respondents who reported plan shopping/provider changes had dropped by 20% in Q1 2016. Plan shoppers increased by 7% from Q1 2016 to Q2, with 23% reporting periodic reviews or provider changes.

Not all cost control options are popular with SMBs. The use of higher deductibles and copays to manage costs dropped by 5%, part of a continued decline from the end of 2015. The use of employee wellness programs as a means to lower health care costs also declined by 5% from Q1 to Q2 2016.

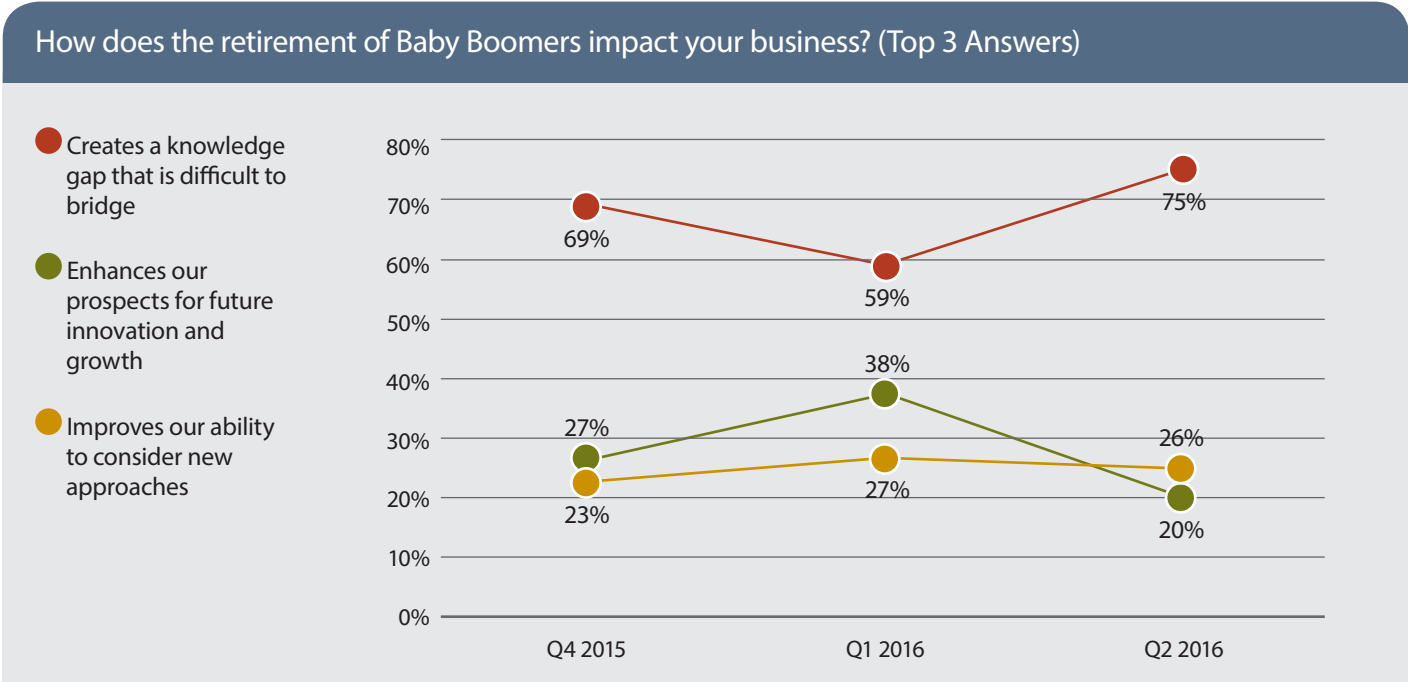
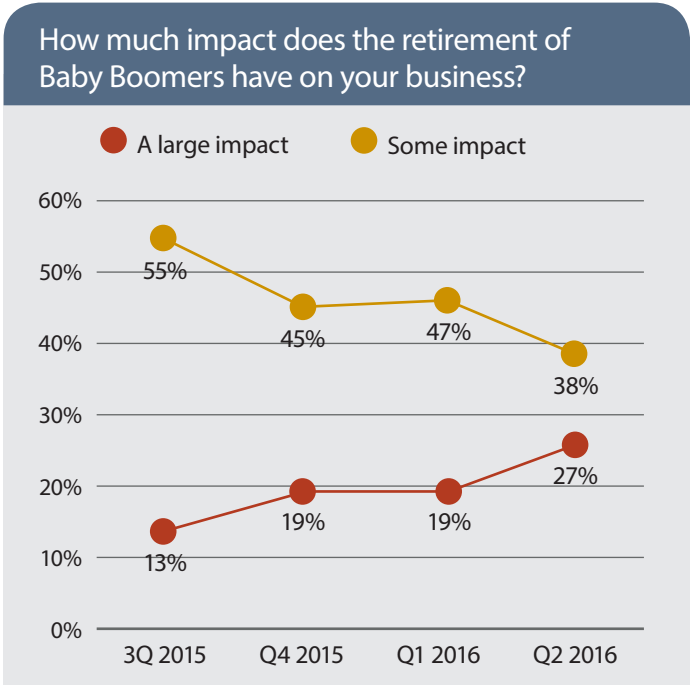
What is your company doing to address health care costs?



Boomer Retirement Impacts SMBs

The impact of Baby Boomer retirement is being felt throughout the economic and employment markets. Seventy-five percent of SMBs report that Baby Boomer retirement is creating a knowledge gap that is difficult for them to bridge, a 16% increase from Q1 2016. Fifteen percent of SMBs expressed concern that retirement rates will impair their ability to compete in the market. Compounding this brain drain, fewer SMBs in Q2 report hiring retirees back on contract, a 5% drop over Q1.

Positive effects of Boomer retirement declined or stagnated in Q2. The prospects for future innovation and growth fell steeply, with only 20% of SMBs reporting this positive effect in Q2, an 18% drop from Q1. Additionally, only 26% of SMBs felt that Boomer retirement improved their ability to consider new approaches and processes.



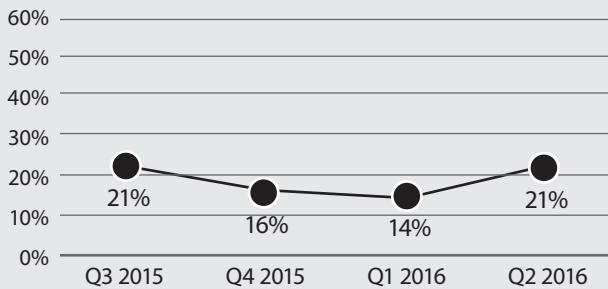
Overtime and Minimum Wage

Statistical results from our survey show that at first glance many SMBs do not seem very concerned about recent or potential changes to overtime and minimum wage regulations. However, a few regulation-based trends are converging and SMBs are keeping close eye on these changes. New overtime rules [go into effect in December 1, 2016](#), just as the holiday season gets underway. While executives currently say that they “do not know what to expect” in regards to the overtime laws, future surveys may reveal differing sentiments as these regulations go live.

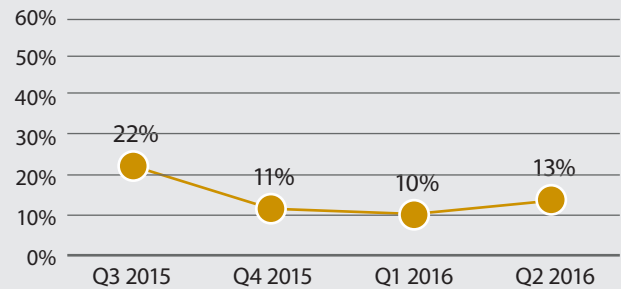
Overall, SMBs did not express concern over proposed or potential minimum wage hikes. If the minimum wage were increased to over \$10 per hour, half of the executives reported that this increase would not impact their business. However, some executives report that minimum wage hikes could negatively affect their customer pricing and hiring plans. In an open response section of the survey, several executives mentioned they may need to further increase the share of health insurance coverage paid by employees. These executives also expressed concern about losing clientele due to price increases and indicated they may need to outsource work to Eastern Europe and Asia.

In terms of impact on your business, if the Federal minimum wage were to increase to over \$10 per hour, what impact would that have on your business?

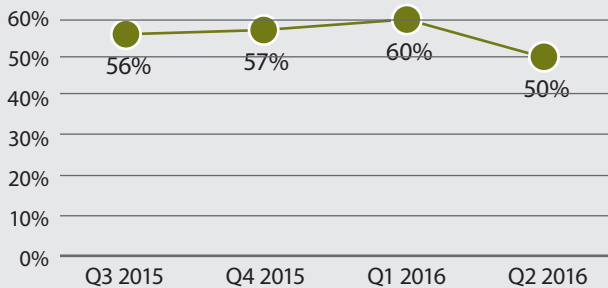
● We will increase prices to our end customers



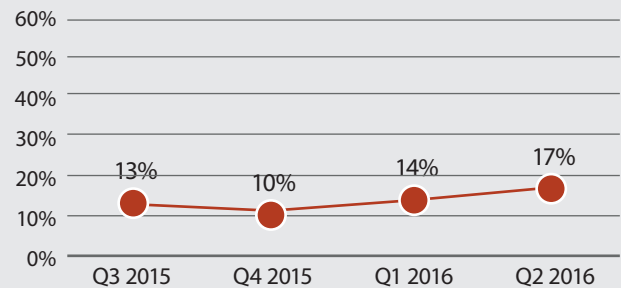
● We will reduce our current workforce



● Will not impact my business

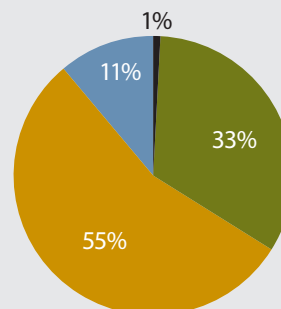


● We will reduce our new hiring plans



The Department of Labor’s May 18, 2016 announcement regarding overtime rules and regulations will:

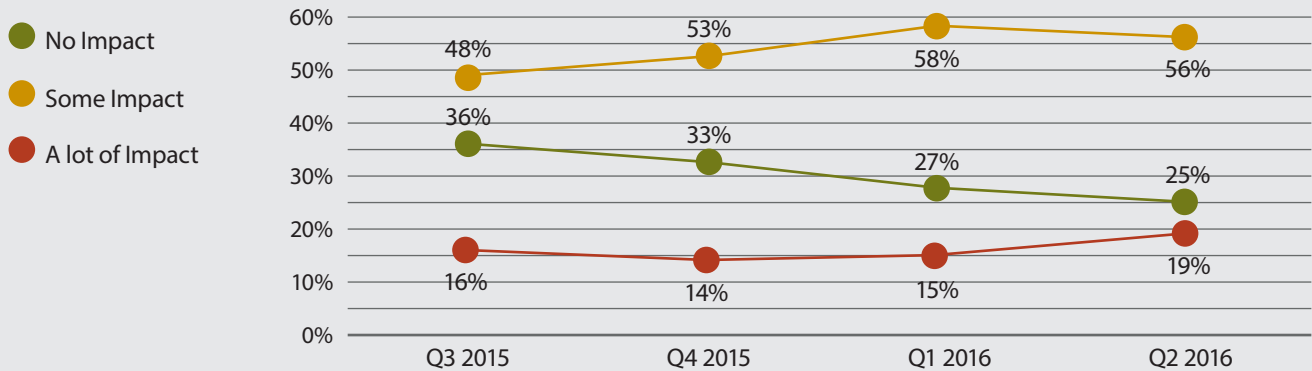
- Help my business
- Harm my business
- Have no impact on my business
- Don’t know



Market and Federal Reserve Impacts

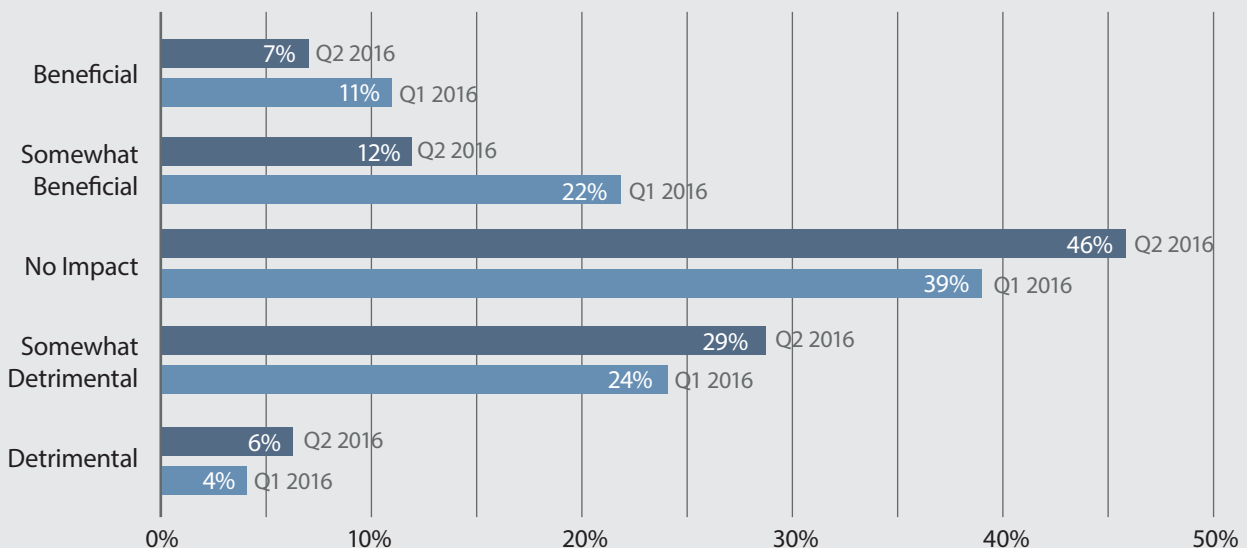
Over the next 12 months, 75% of SMBs now think the activities of the U.S. and global stock markets will have an impact on their business. SMBs feel the markets will have an impact on business decisions. While the “A lot of Impact” category has risen slightly, the “No Impact” category has dropped consistently over the past several quarters.

In terms of impact on your business, how much near-term impact (next 12 months) do the activities of the U.S. and global stock markets have on your company?



In December 2015, the U.S. Federal Reserve decided to increase interest rates for the first time since 2008. Earlier this summer, the Fed decided to keep rates steady for the near-term. This pause in further increases came, perhaps in part, in response to global concerns regarding Brexit. This quarter, SMBs expressed increased concern about further Federal Reserve interest rate hikes. While 7% more respondents think a rate increase will not impact them, the “detrimental or somewhat detrimental to my business” responses were up 7% and the “beneficial or somewhat beneficial to my business” responses were down 14% from Q1 2016.

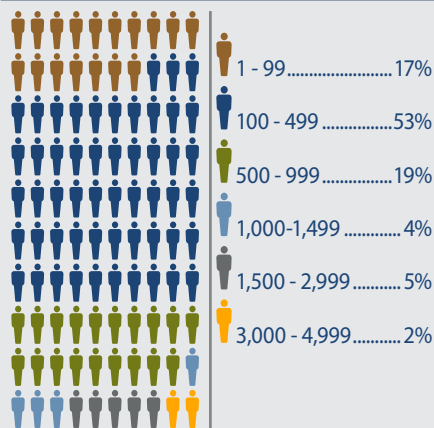
In terms of impact on your business, what effect would an interest rate increase by the Federal Reserve have on your company?



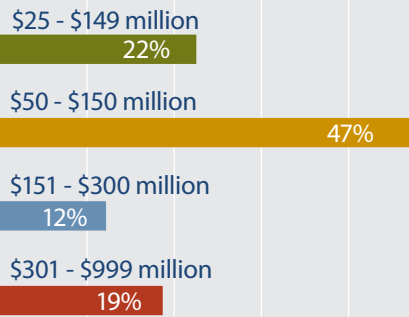
Survey Snapshots

The SMB Job Generation Outlook is an innovative approach to traditional hiring and employment surveys designed to capture the visions and priorities of U.S. SMB executives. Each quarter, the Outlook reports on recent and planned business activities as well as gathers opinions related to workforce and political environments. Since early 2013, Lucas Group has polled almost 3,100 SMB executives from across the country and a cross-section of industry sectors. From family-owned small businesses with several hundred people to mid-market corporations that employ thousands, the Outlook seeks to uncover what the SMB market most wants, needs, worries about and forecasts for the future—the nation’s and their own.

How many employees do you have?



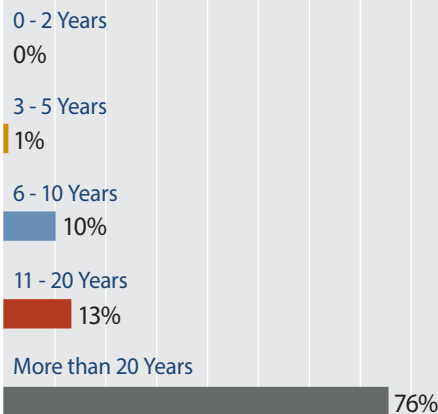
What is your projected 2016 revenue?



In what industry do you compete?

- Manufacturing
- Financial, Insurance and Real Estate
- Business Services
- Information Technology
- Health Care/Medical
- Construction
- Consumer Services
- Energy & Utilities/Oil & Gas
- Transportation Services
- Automotive
- Non-Profit & Membership Organizations
- Wholesale
- Arts, Entertainment & Recreation
- Legal Services
- Pharmaceuticals
- Telecommunications
- Education
- Agriculture & Mining
- Media

How long has your company been in business?



In what region are you located?

