

SMEs Business Optimism Survey

Q2, 2016

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The Introduction

AT A GLANCE

- The Composite BCI has edged up by 1.4 points over the previous quarter's reading, moving from 109.6 points in Q1, 2016 to 111.0 points in Q2, 2016, with business confidence levels in the second quarter similar to those in the first quarter.
- Large companies continue to maintain a more optimistic stance compared to SMEs with composite BCI scores of 121.8 and 111.0 points respectively. Large companies have indicated a stronger outlook for revenues, volumes, hiring, profitability and purchase orders. SMEs are however modestly more optimistic about their selling prices.
- The proportion of respondents that expect the business situation to improve stands at 43%, which is higher than the 37% in the last quarter; another 44% anticipate stability, while the remaining 13% of the firms have forecast deterioration.
- The key hurdles for SMEs are competition, cost of rental/leasing, delays in payments/receivables and poor demand/market conditions.
- The proportion of businesses that intend to invest in capacity expansion and technology upgrades has increased in Q2, 2016 compared to the previous quarter; 68% of the SMEs plan to invest in expansion of capacity in Q2, 2016 versus 60% in Q1, 2016 and 65% intend to upgrade technology in Q2, 2016 versus 57% in Q1, 2016.
- 89% of the SMEs have not implemented any type of innovation in their businesses. Of the remaining, 38% indicated that the main purpose for implementing innovation was *quality improvement*

The Department of Economic Development (DED) is a Dubai government Department that has the mandate to help achieve the key strategic objectives of fostering 'Sustainable Economic Development' and strengthening the 'Competitiveness of Dubai'. In order to gauge the perceptions of the business community, DED has been conducting Dubai's Quarterly Business Surveys which provides a snapshot of Dubai's current economic activity and the outlook for the quarter ahead.

This document presents a summary of the survey conducted in the 2nd Quarter of 2016. The survey was administered to 410 SMEs in Dubai.

In addition to the current situation and future expectations, the survey addresses key challenges impacting business growth and development and assesses the investment outlook for the coming twelve months.

METHODOLOGY

The Quarterly Business Survey for Q2, 2016 was conducted for 410 businesses in Dubai. The sample included a mix of micro, small and medium enterprises and ensured an adequate representation from the manufacturing, trading and services sectors.

A detailed break up of respondents by sector is as follows:

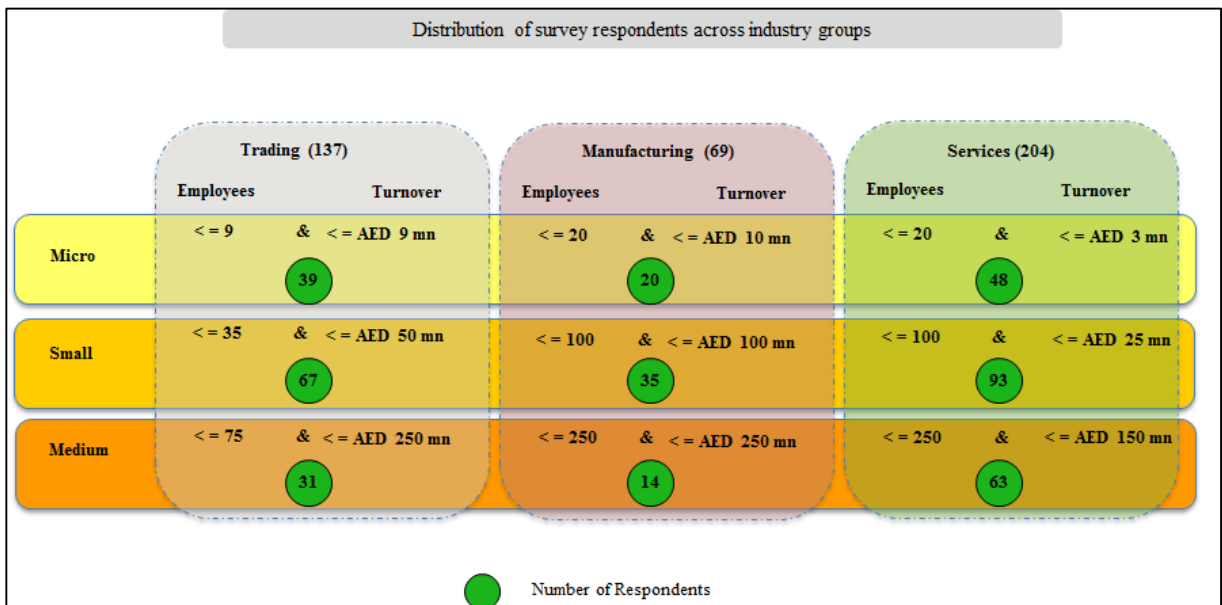


Figure: 01

In order to tap ‘business outlook’ or expectations, the survey focused on key indicators, *such as sales, selling prices, volumes sold, profits and number of employees*. Respondents were asked to indicate if they expect an ‘increase’, ‘decrease’ or ‘no change’ in these indicators.

SME Business Confidence Index Calculations

The SME Business Confidence Index (BCI) is calculated as a weighted average score of the following 'business outlook' indicators:

- Selling Prices
- Volumes Sold
- Number of Employees
- Profits

For each indicator, 'Resultant scores' are calculated using the net balances method:

$(\% \text{ of positive responses} - \% \text{ of negative responses}) + 100$

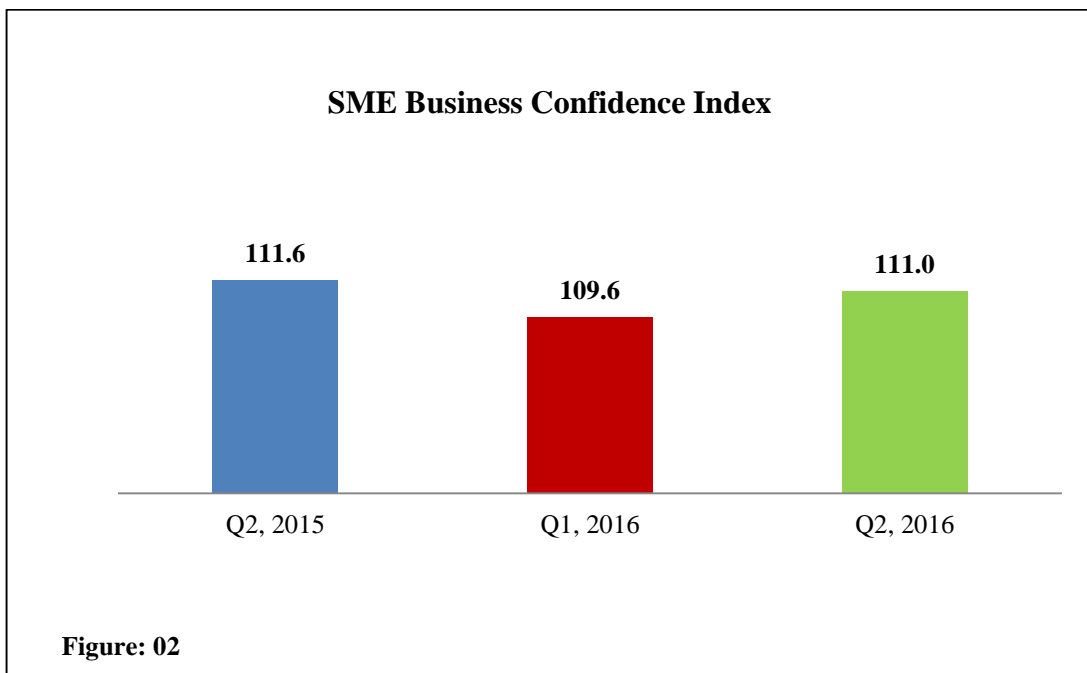
For calculating the SME Composite Business Confidence Index for Dubai, the resultant scores are multiplied with their corresponding parameter weights to arrive at a weighted average Index score. The SME Composite Index score is finally rebased so that Q2, 2011 = 100.

BCI scores are classified in the following three groups:

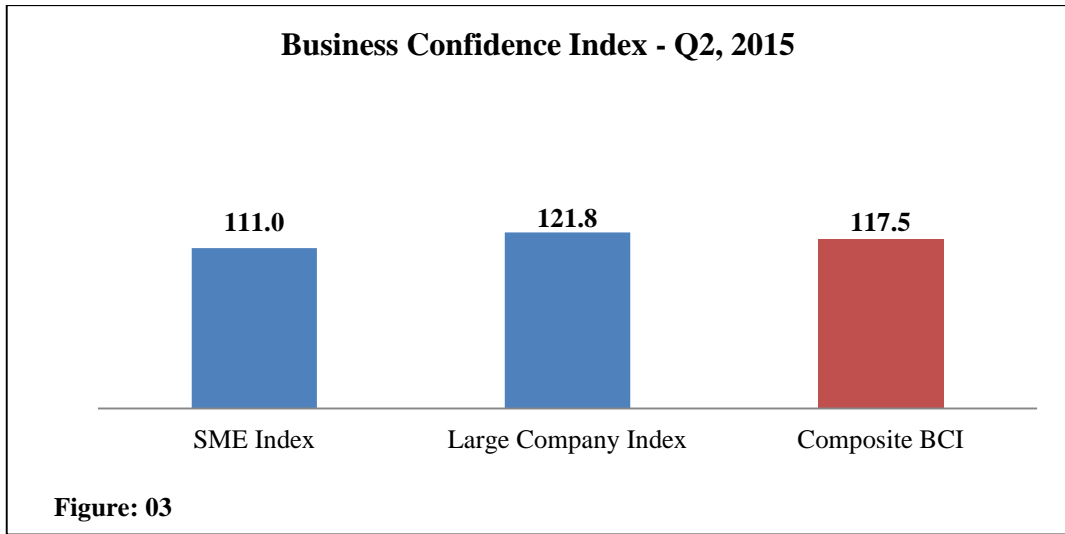
- ***BCI < 100, business expectations are negative***
- ***BCI = 100, business expectations are stable***
- ***BCI > 100, business expectations are positive***

SME BUSINESS CONFIDENCE INDEX – Q2, 2016

According to the IMF, despite headwinds posed by lower oil revenues, Dubai is poised to record 3.7% growth in 2016, up from 3.6% last year due to the diversified nature of its economy. Dubai's growth is expected to far exceed the average GCC growth forecast of 1.8% for 2016. The current survey shows that the Composite Business Confidence Index for Dubai's SMEs for Q2, 2016 is recorded at 111.0 points (A score of 100 indicates stable/neutral sentiments), reflecting a positive outlook.



The Composite BCI has edged up by 1.4 points over the previous quarter's reading, moving from 109.6 points in Q1, 2016 to 111.0 points in Q2, 2016. A y-o-y comparison shows that the Composite BCI in Q2, 2016 is at par with the index in Q2, 2015, supported by expectations of getting new projects/orders, suitable market conditions and robust demand due to the festival season and new customers.



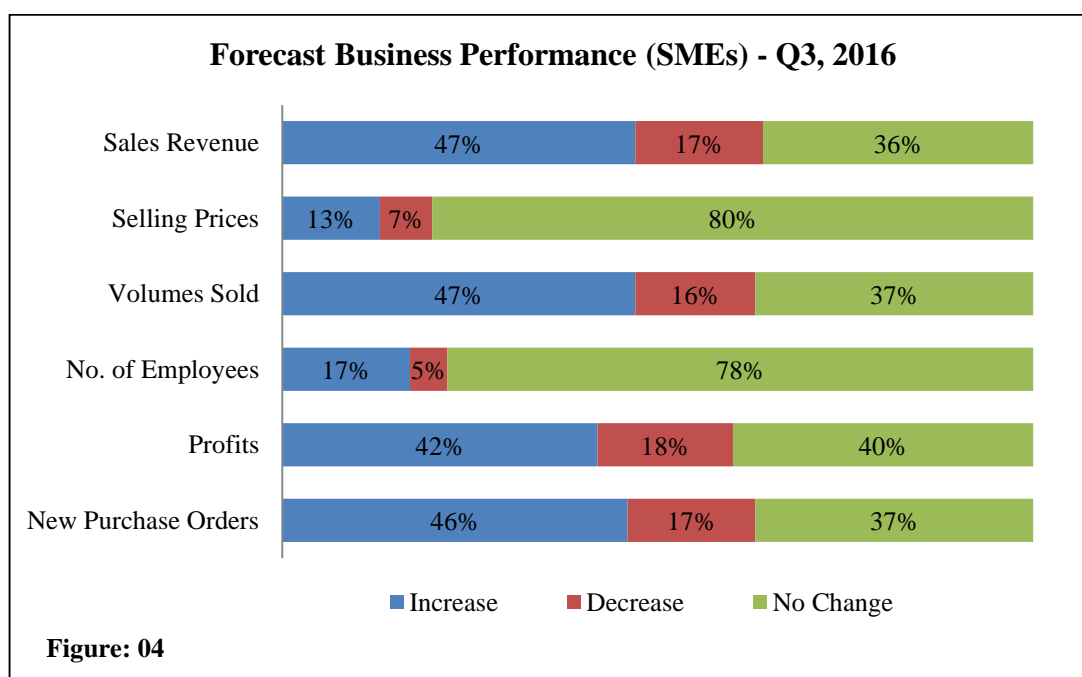
The current survey also shows that large companies continue to maintain a more optimistic stance compared to SMEs with composite BCI scores of 121.8 and 111.0 points respectively. Large companies have indicated a stronger outlook for revenues, volumes, hiring, profitability and purchase orders. SMEs are however modestly more optimistic about their selling prices.

SME BUSINESS OUTLOOK – Q3, 2016

SMEs account for a dominant share in Dubai’s total business composition (95% of the total number of firms), 410 of the 500 firms that were interviewed as part of the survey were SMEs. These included micro, small, and medium enterprises as per Dubai’s SME definition.

Table: 01
Forecast Business Performance (SMEs) – Q3, 2016

Parameter	Q3, 2015				Q2, 2016				Q3, 2016			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	48%	17%	35%	31%	47%	14%	39%	33%	47%	17%	36%	30%
Selling Prices	12%	9%	79%	3%	11%	11%	78%	0%	13%	7%	80%	6%
Volumes Sold	49%	20%	31%	29%	44%	14%	42%	30%	47%	16%	37%	31%
No. of Employees	20%	4%	76%	16%	18%	6%	76%	12%	17%	5%	78%	12%
Profits	48%	20%	32%	28%	41%	16%	43%	25%	42%	18%	40%	24%
New Purchase Orders	49%	19%	32%	30%	37%	11%	52%	26%	46%	17%	37%	29%

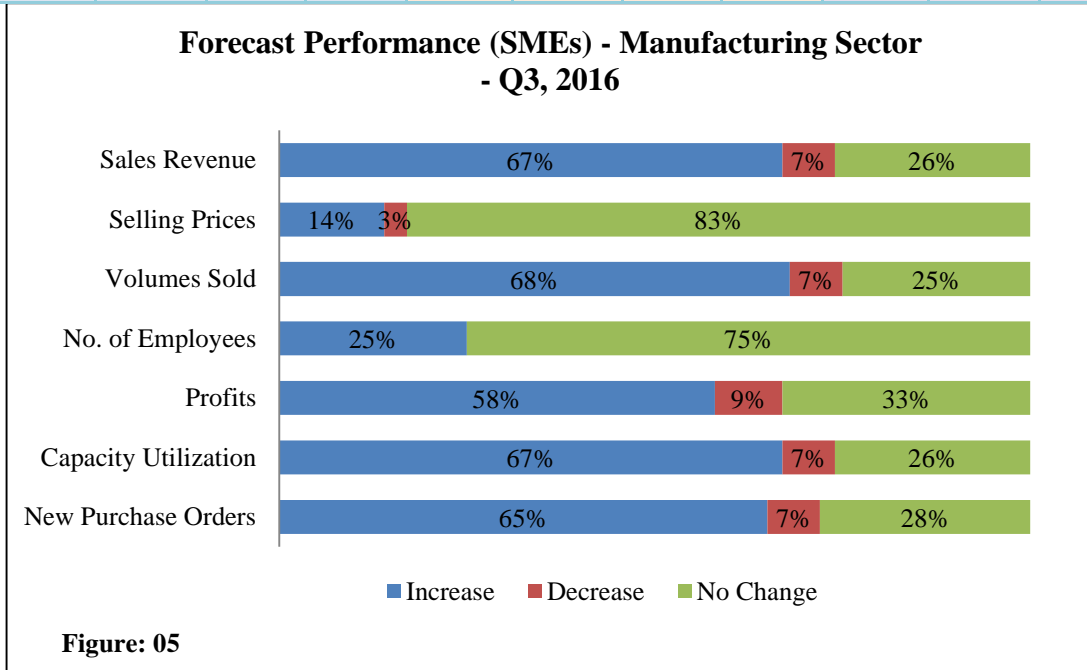


- Optimism levels for volumes, employment and profits for Q3, 2016 are at par with last quarter's outlook.
- The net balance for volume of sales for SMEs is at 31% compared to 41% for large companies.
- Manufacturing SMEs have shown a quarterly surge in sentiments for volumes (net balance has increased from 28% to 61%) for Q3, 2016, while the trading sector (net balance of 35% for both quarters) has a stable outlook and the services sector (net balance has dropped from 26% to 17%) has registered a decline.
- The outlook for selling prices for Q3, 2016 has firmed up in comparison to the forecast for Q2, 2016 as firms expect an increase in the price of raw materials and have projected stronger demand.
- The employment and profitability forecast for Q3, 2016 is similar to that for Q2, 2016, but modestly weaker than that for Q3, 2015.
- 67% of manufacturing firms and 39% of services firms expect to increase their capacity utilization rates during Q3, 2016.
- The proportion of respondents that expect the business situation to improve stands at 43%, which is higher than the 37% in the last quarter; another 44% anticipate stability, while the remaining 13% of the firms have forecast deterioration.

Manufacturing SMEs

Table: 02
Forecast Business Performance (Manufacturing) – Q3, 2016

Parameter	Q3, 2015				Q2, 2016				Q3, 2016			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	60%	16%	24%	44%	46%	18%	36%	28%	67%	7%	26%	60%
Selling Prices	16%	7%	77%	9%	7%	19%	74%	-12%	14%	3%	83%	11%
Volumes Sold	61%	17%	22%	44%	46%	18%	36%	28%	68%	7%	25%	61%
No. of Employees	19%	1%	80%	18%	19%	10%	71%	9%	25%	0%	75%	25%
Profits	59%	17%	24%	42%	44%	18%	38%	26%	58%	9%	33%	49%
New Purchase Orders	60%	19%	21%	41%	44%	17%	39%	27%	65%	7%	28%	58%



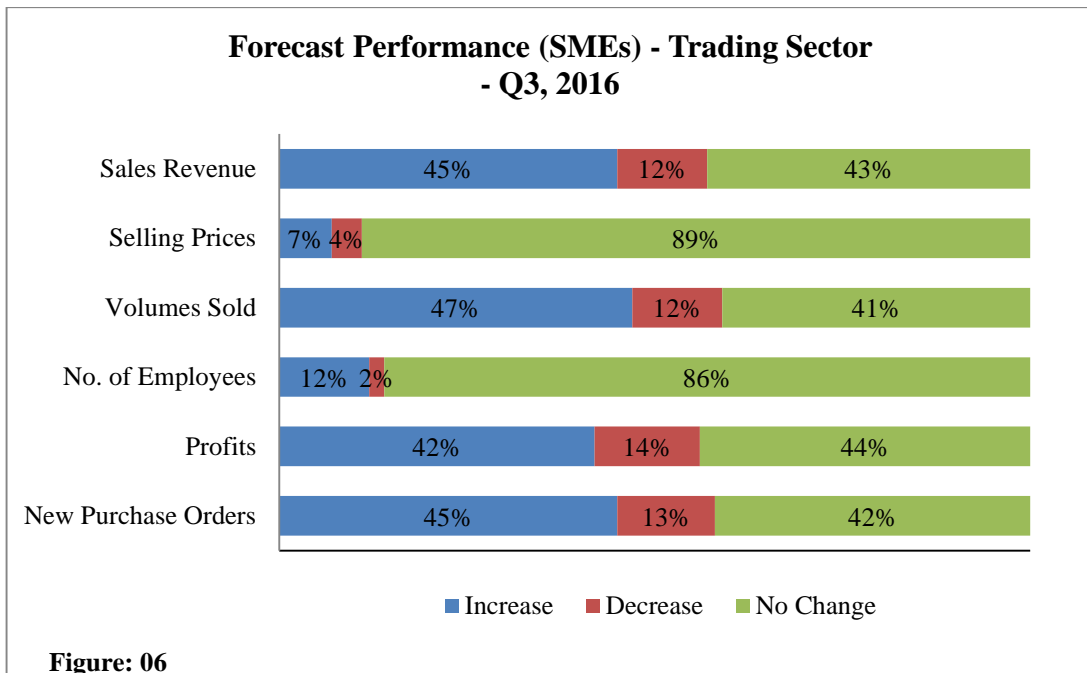
- 68% of the surveyed manufacturers expect an increase in their volumes during Q3, 2016 based on hopes of receiving new orders/contracts/projects both from the government and private sectors and an increase in demand for their products. 7% of the manufacturing firms anticipate a decline in volumes due to the summer season and Ramadan, leading to a net balance of 61%. The outlook for Q3, 2016 is much stronger in comparison to that for Q2, 2016 (net balance of 28%) and Q3, 2015 (net balance of 44%).

- Within the manufacturing sector, furniture and plastics manufacturers hold the strongest outlook for volumes.

Trading SMEs

Table: 03
Forecast Business Performance (Trading) – Q3, 2016

Parameter	Q3, 2015				Q2, 2016				Q3, 2016			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	43%	23%	34%	20%	52%	8%	40%	44%	45%	12%	43%	33%
Selling Prices	9%	11%	80%	-2%	8%	8%	84%	0%	7%	4%	89%	3%
Volumes Sold	45%	28%	27%	17%	43%	8%	49%	35%	47%	12%	41%	35%
No. of Employees	14%	5%	81%	9%	13%	4%	83%	9%	12%	2%	86%	10%
Profits	44%	28%	28%	16%	39%	11%	50%	28%	42%	14%	44%	28%
New Purchase Orders	45%	25%	30%	20%	43%	8%	49%	35%	45%	13%	42%	32%

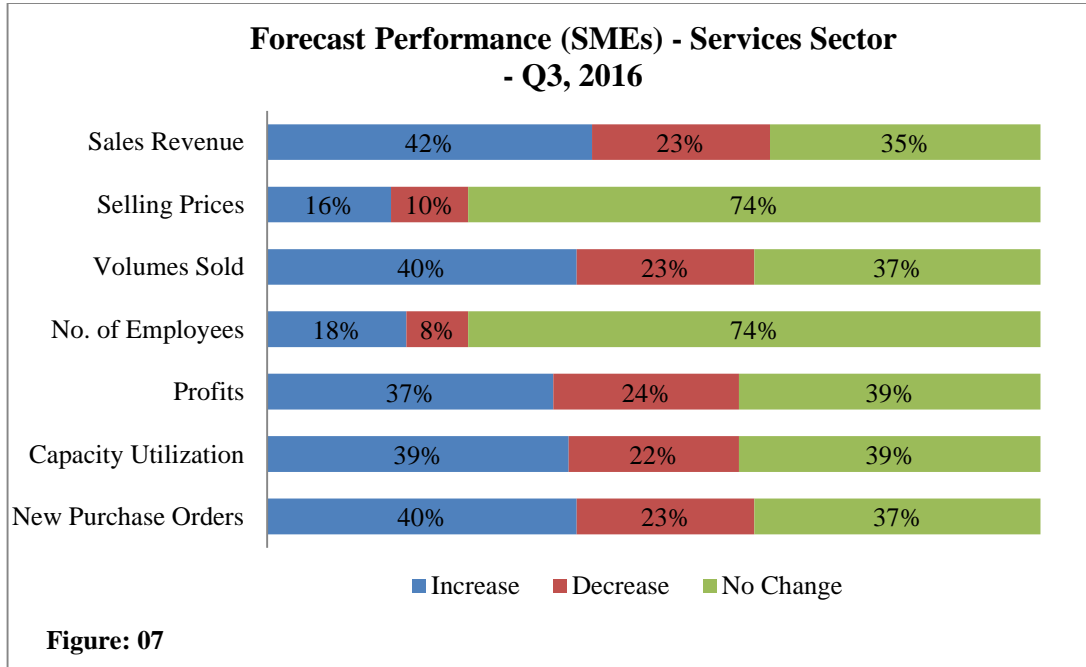


- With respect to sales volumes, the trading sector is less optimistic than manufacturing, but more confident than services. The outlook for volumes for Q3, 2016 is at par with the previous quarter's forecast, but much stronger than the forecast for Q3, 2015. 45% of participants expect an increase in revenues versus 12% that anticipate a decline. The remaining 43% expect stability.
- Key sectors optimistic of higher demand over the next quarter include the following: computers, construction traders, food & beverages and auto traders are hopeful of an increase in volumes during Q3, 2016.

Services SMEs

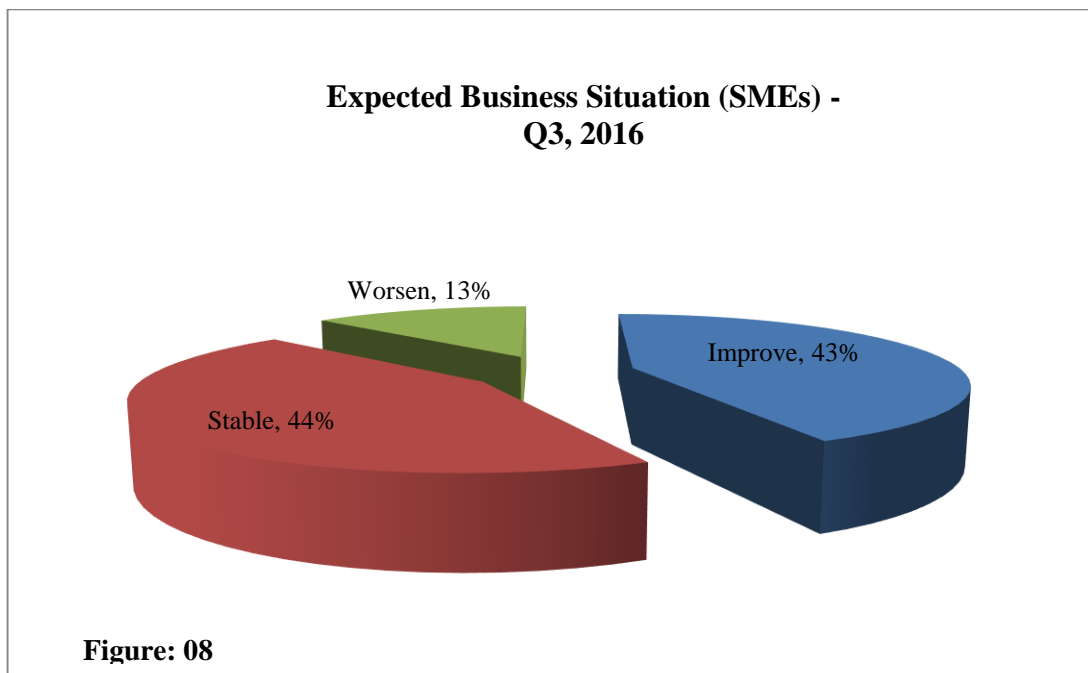
Table: 04
Forecast Business Performance (Services) – Q3, 2016

Parameter	Q3, 2015				Q2, 2016				Q3, 2016			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	48%	14%	38%	34%	44%	17%	39%	27%	42%	23%	35%	19%
Selling Prices	12%	8%	80%	4%	16%	10%	74%	6%	16%	10%	74%	6%
Volumes Sold	48%	15%	37%	33%	43%	17%	40%	26%	40%	23%	37%	17%
No. of Employees	24%	4%	72%	20%	22%	7%	71%	15%	18%	8%	74%	10%
Profits	47%	16%	37%	31%	40%	18%	42%	22%	37%	24%	39%	13%
New Purchase Orders	48%	14%	38%	34%	29%	13%	58%	16%	40%	23%	37%	17%



- The services sector is less optimistic for Q3, 2016 than it was for Q2, 2016 and Q3, 2015. The q-o-q and y-o-y decline is underlined by sharp drops in the forecast for the tourism & hospitality and construction sub-segments. The transportation segment has however recorded more bullish sentiments for Q3, 2016 compared to last quarter and last year.

- Within the travel & hospitality sector, car rentals & travel companies have displayed a bearish stance for Q3, 2016 (net balance of negative 22%) due to expectations of fewer tourists and lower demand during the summer season. Hotels & restaurants are modestly optimistic with 33% of the participants anticipating an improvement in volumes and 24% expecting a decrease, resulting in a net balance of 9%.



43% of SMEs and 50% of large companies expect the business situation to improve in Q3, 2016.

DUBAI SME OUTPUT – Q2, 2016

Although the main purpose of the survey is to gauge business expectations for future activity, it also tries to capture the actual changes in business performance from one quarter to another.

Table: 05
Overall Business Performance (SMEs) – Q2, 2016

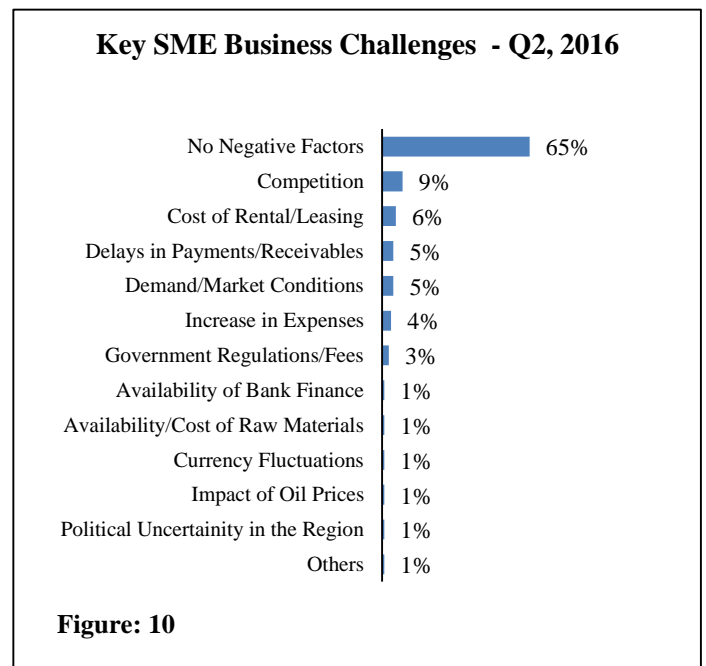
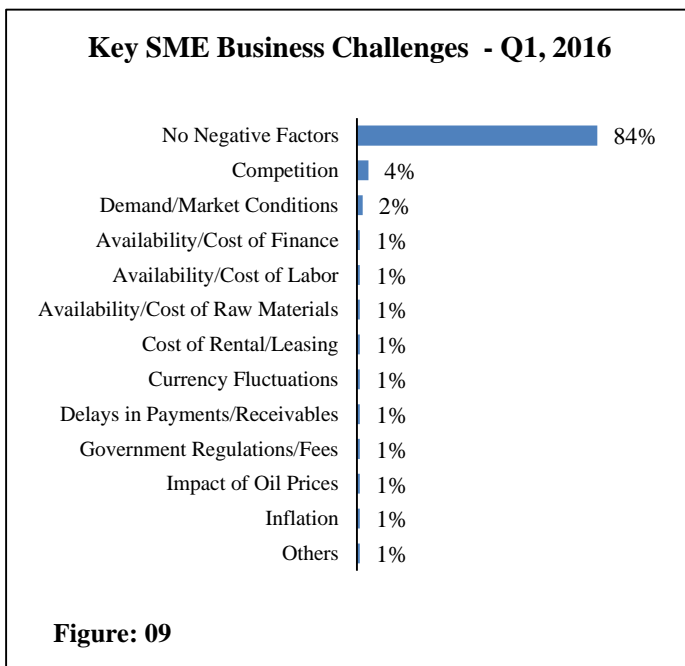
Parameter	Q2, 2015				Q1, 2016				Q2, 2016			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	27%	29%	44%	-2%	16%	35%	49%	-19%	20%	28%	52%	-8%
Selling Prices	12%	22%	66%	-10%	9%	24%	67%	-15%	9%	22%	69%	-13%
Volumes Sold	30%	31%	39%	-1%	16%	36%	48%	-20%	21%	27%	52%	-6%
No. of Employees	17%	10%	73%	7%	10%	14%	76%	-4%	12%	10%	78%	2%
Profits	28%	35%	37%	-7%	14%	38%	48%	-24%	18%	30%	52%	-12%
New Purchase Orders	30%	30%	40%	0%	15%	27%	58%	-12%	20%	27%	53%	-7%

- While 21% of the firms recorded an increase in their volumes in Q2, 2016, 27% registered a decrease due to lack of projects, poor market conditions, seasonal downturn in summer, competition and slow growth in export markets.
- Large companies had a stronger quarter (Q2, 2016) with respect to all the parameters: revenues, selling prices, volumes, hiring, profits and purchase orders.
- 22% of the survey participants indicated that they had to reduce their selling prices in Q2, 2016 due to competition or poor market conditions. However, 69% of the firms maintained their selling prices.
- 78% of the firms were able to maintain their workforce size, while 12% hired new employees to support their businesses. SMEs employment increased in Q2, 2016 compared to the previous quarter.
- Weak sales volumes were reflected in purchase orders.
- Capacity utilization rates improved on a quarterly basis for both manufacturing and services firms.

- The unit cost of labor increased for 38% of the firms due to an increase in wages, rise in the cost of living, high visa costs, increments given, higher government fees and higher rates of rental.
- Cost of raw materials increased for 16% of the companies but remained unchanged for 64% of the firms. Among large companies, such costs increased for 10% of the firms.
- Rental costs increased for 47% of the respondents during Q2, 2016. Among large companies, 51% of the respondents reported an appreciation in such costs.

KEY SME CHALLENGES IN DUBAI

The survey also addressed key challenges perceived by businesses at the end of Q2, 2016 that may impact near term business growth and development. The survey shows that 65% of the surveyed businesses do not expect to face any hurdles in their business operations; the corresponding proportion in the previous quarter was 84%.



A summary of the major challenges facing Dubai's SME community are as follows:

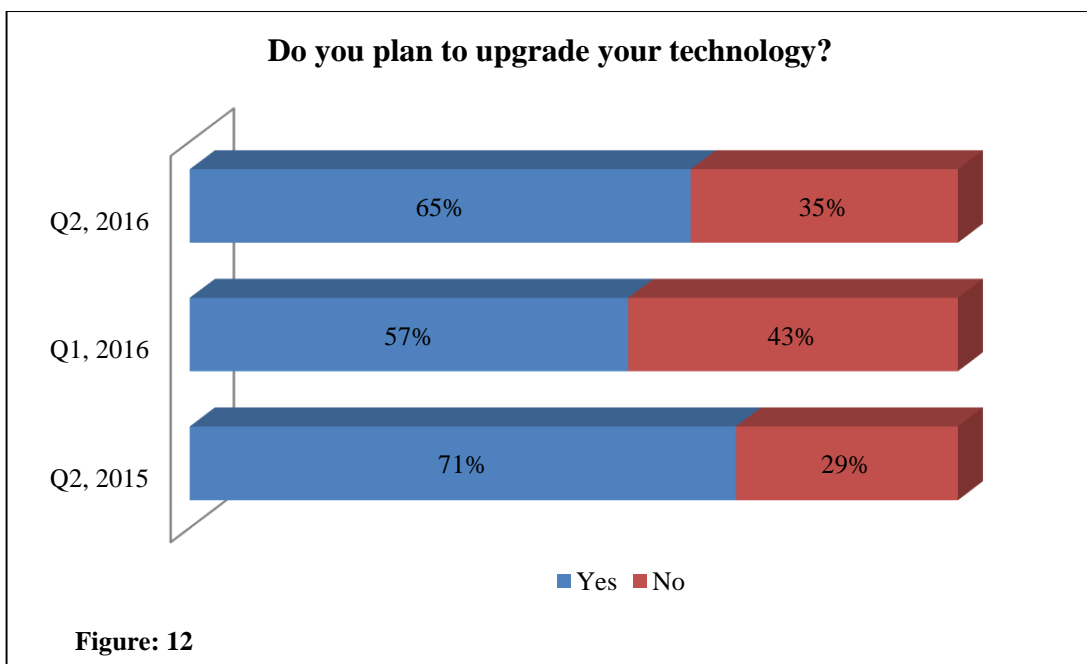
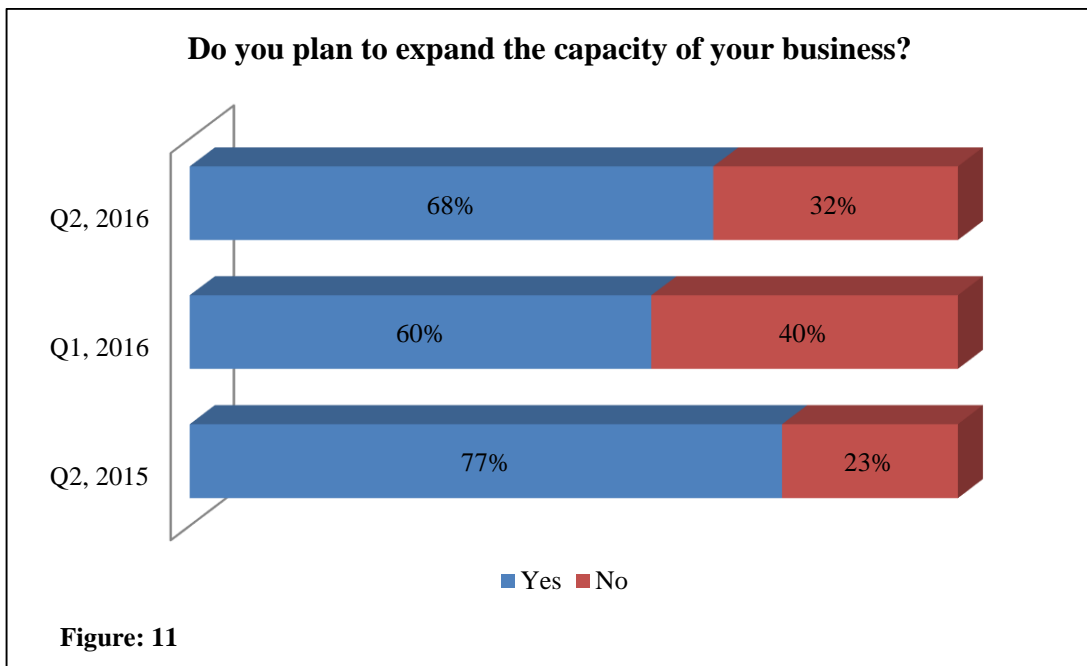
1. Competition: 9% of the firms have indicated that competition will be an obstacle. 45% of them expect that competition will intensify.
2. Cost of rental/leasing: Issues related to the rising costs of rental/leasing will hamper 6% of the participants. 74% of these SMEs anticipate an increase in severity for this factor.
3. Delays in payments/receivables: This is a hurdle for 5% of the SMEs in Dubai.
4. Demand/market conditions: 5% of Dubai's SMEs are concerned about the impact of poor market conditions on their operations.

The remaining concerns were similar in importance and each impacted fewer than 5% of the participants.

For large companies, the key concerns were the same as the overall sample: competition, poor demand/market conditions and delays in payments/receivables. For SMEs, the leading obstacles are competition, cost of rental/leasing and delays in payments/receivables.

INVESTMENT OUTLOOK

The survey also gauges the business community's investment outlook with respect to capacity expansion and technology upgrade plans over the coming twelve-month horizon.



- The proportion of businesses that intend to invest in capacity expansion and technology upgrades has increased in Q2, 2016 compared to the previous quarter; 68% of the SMEs plan to invest in expansion of capacity in Q2, 2016 versus 60% in Q1, 2016 and 65% intend to upgrade technology in Q2, 2016 versus 57% in Q1, 2016.
- Companies planning capacity expansion are willing to undertake capital investment for expansion of their current office premises and acquisition of fixed assets (such as, factories, warehouses, machinery, and vehicles). Key reasons cited by respondents for not considering expanding business capacity include satisfaction amongst applicable respondents related to size and scale of their current operations and/or prioritization towards achieving stability and profitability, over and above market expansion.
- A comparison among sectors shows that the trading sector is most optimistic towards capacity expansion (72% in trading versus 71% in manufacturing and 65% in services intend to invest in expansion), while manufacturers are more inclined towards technology upgrades (70% in manufacturing against 65% in services and 64% in trading plan to invest in upgrading technology).
- Large firms are more inclined than SMEs with respect to investment in technology upgrades and capacity expansion.

INNOVATION ORIENTATION

Survey participants were also asked if they were making any innovations in their businesses, the objective for such innovations and also the amount of provisions being made for R&D.

Have you implemented any type of Innovation in your business?

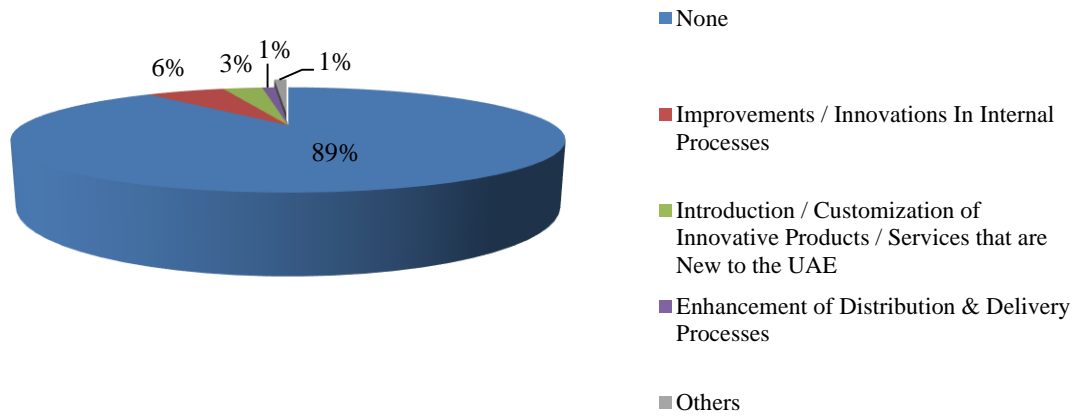


Figure: 13

89% of the SMEs did not implement any type of innovation in their businesses. Of the remaining, 6% implemented innovations in internal processes, 3% introduced products/services that were new to the UAE and 1% enhanced the distribution & delivery processes.

Innovation implementation was similar irrespective of size of firms: 89% of SMEs did not innovate compared to 88% of large firms. While large firms were more inclined towards introduction / customization of innovative products / services that are new to the UAE, SMEs were more inclined towards improvements / innovations in internal processes.

Key Objectives for Implementing Innovation

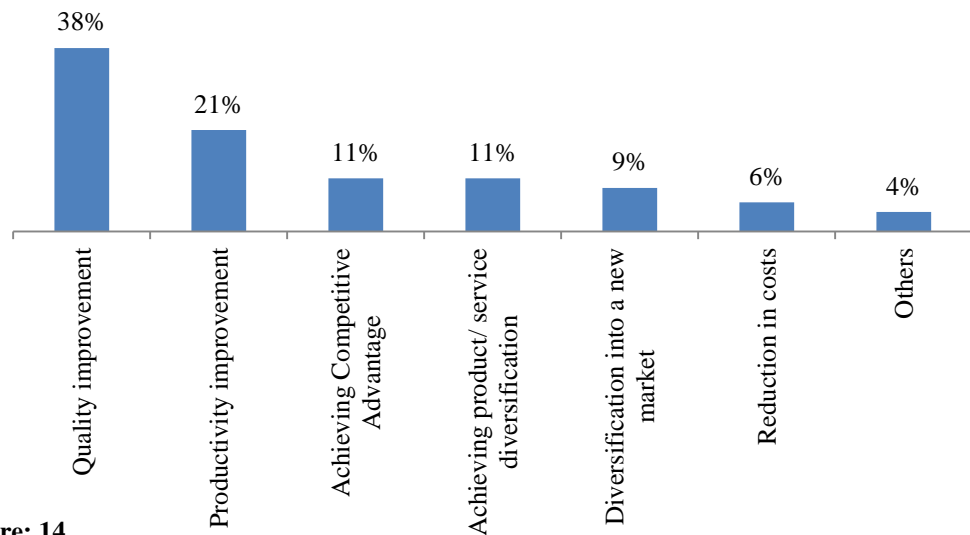
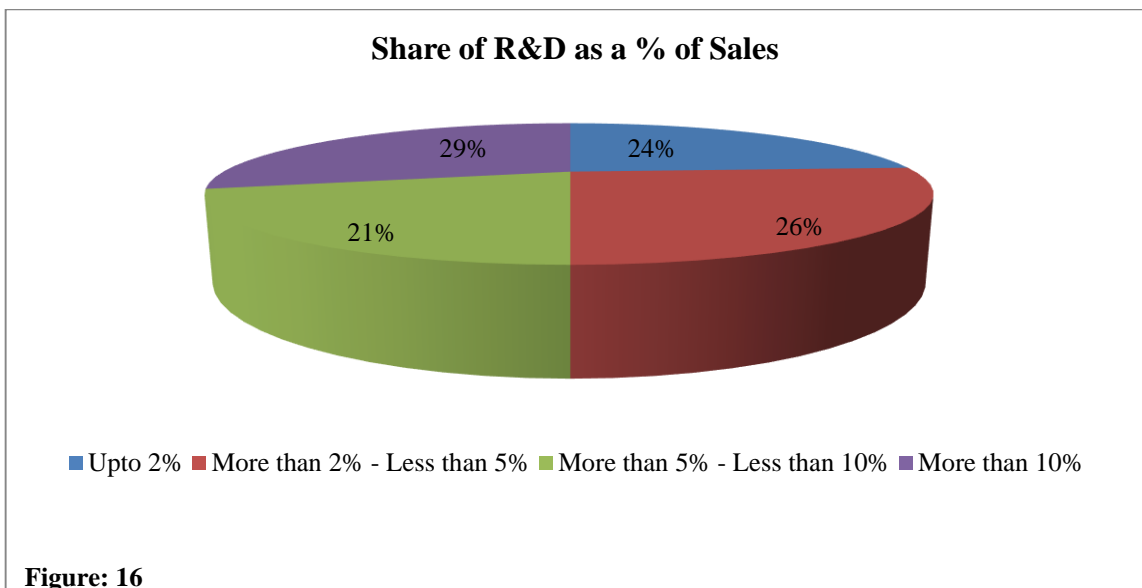
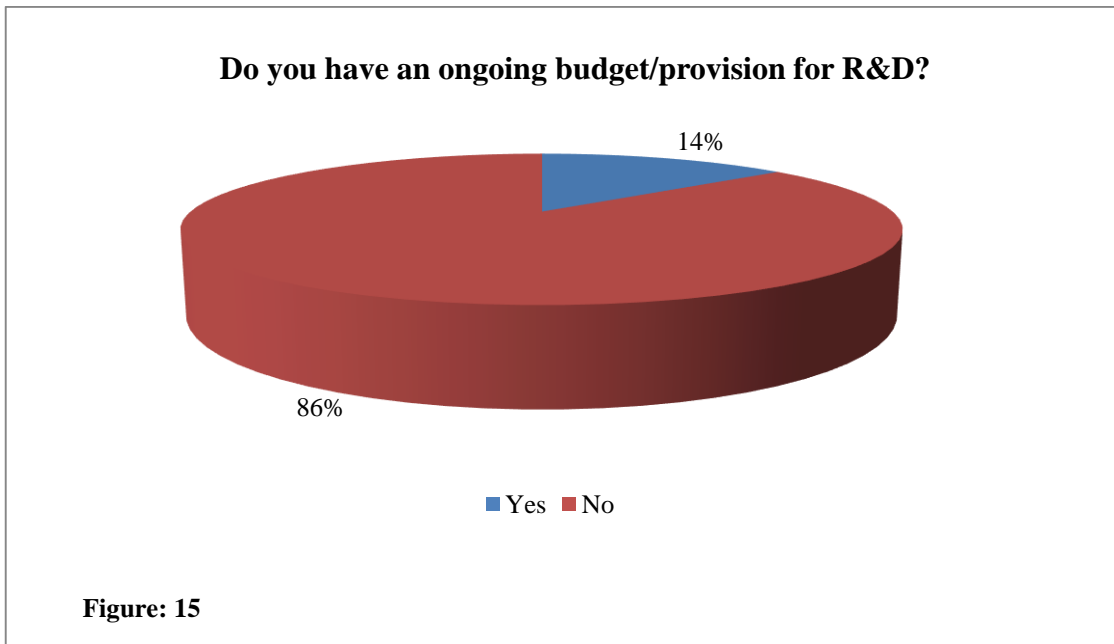


Figure: 14

The key objectives for implementing innovation were quality improvement (38%), productivity improvement (21%), achieving competitive advantage (11%) and achieving product/service diversification (11%).

For large firms, the key objectives are quality improvement and achieving competitive advantage and for SMEs, the reasons are the same as the overall survey.



86% of the firms did not have any provision for R&D. Of the 14% that had an ongoing budget or made provisions for R&D, 29% had budgeted more than 10% of their sales for R&D.