

مؤسسة محمد بن راشد للتنمية
المشاريع الصغيرة والمتوسطة
DUBAI SME



An Agency of the Department of Economic
Development – **Government of Dubai**

SMEs Business Optimism Survey

Q1 - 2012

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AT A GLANCE

- The composite Business Confidence Index for Dubai for the first quarter of 2012 stood at over 112 points, indicating overall positive SME outlook for the coming quarter (Q2, 2012).
- The overall outlook on sales is positive, with 86% of the SMEs expecting either an increase or no change in their sales for the next quarter. In terms of economic activity, expectations are the highest among manufacturing firms followed by services and trading firms
- The severity of challenges, as perceived by businesses, has changed from the previous quarter (Q4, 2011). In the current quarter (Q1, 2012), government fees have been reported as the most important challenge, up from the third position in the last quarter. Insufficient demand is the next most severe challenge - top most challenge in last quarter - followed by frequent changes in government regulations - ranked number 5 in the previous quarter - and competition from local and international players which was perceived as the second biggest challenge in the previous quarter.
- Compared to the previous quarter, no change is reported in investment plans over a twelve-month time horizon, with 42% of businesses planning to upgrade technology and 55% intending to expand capacity.



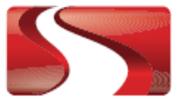
The Department of Economic Development (DED) has been mandated to help achieve the key strategic objectives of fostering ‘Sustainable Economic Development’ and strengthening the ‘Competitiveness of Dubai’. In order to gauge the perceptions of the business community, DED has launched Dubai’s Quarterly Business Surveys with the key objective to providing a snapshot of Dubai’s current economic activity and the outlook for the following quarter.

This document presents a summary of the survey conducted in the 1st Quarter of 2012 and highlights the future expectations of SME businesses in Dubai. The survey was administered to 475 SME businesses in Dubai. In addition, the survey also examines key challenges hindering the growth and development of SME businesses and summarizes their investment outlook over the coming twelve months.

METHODOLOGY

The quarterly business survey for Q1, 2012¹ was conducted on a total of 500 companies across the Emirate of Dubai. The sample included a mix of small, medium and large enterprises and ensured an adequate representation from the Manufacturing, Trading and Services sectors, in the same proportions as their respective contributions to Dubai GDP.

¹ For the purpose of the survey, each quarter is defined as follows: Q1 is the period between January and March, Q2 is the period between April and June, Q3 is the period between July and September, and Q4 is the period between October and December of each year.



Distribution of survey respondents across industry groups						
	Trading (160)		Manufacturing (60)		Services (255)	
	Employees	Turnover	Employees	Turnover	Employees	Turnover
Micro	<= 9	& <= AED 9 mn	<= 20	& <= AED 10 mn	<= 20	& <= AED 3 mn
Small	<= 35	& <= AED 50 mn	<= 100	& <= AED 100 mn	<= 100	& <= AED 25 mn
Medium	<= 75	& <= AED 250 mn	<= 250	& <= AED 250 mn	<= 250	& <= AED 150 mn

● Number of Respondents

From the perspective of tapping ‘business outlook’ or expectations, the survey focused on key indicators, such as *sales, selling prices, volumes sold, profits and No. 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



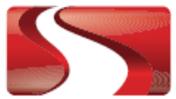
average Index score. The SME composite index score is finally rebased so that Q2, 2011 = 100.

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*

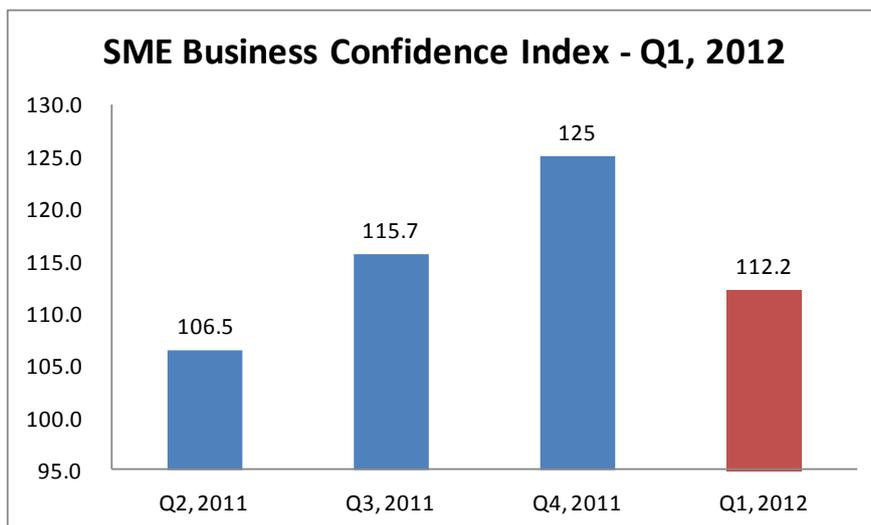
When expressed with reference to the base quarter Q2-2011, the following interpretations hold (t and t-1 referring to two consecutive quarters):

- *BCI(t) < BCI(t-1): business expectations are declining*
- *BCI(t) = BCI(t-1): business expectations are stable*
- *BCI(t) > BCI(t-1): business expectations are rising*



SME BUSINESS CONFIDENCE INDEX – Q1, 2012

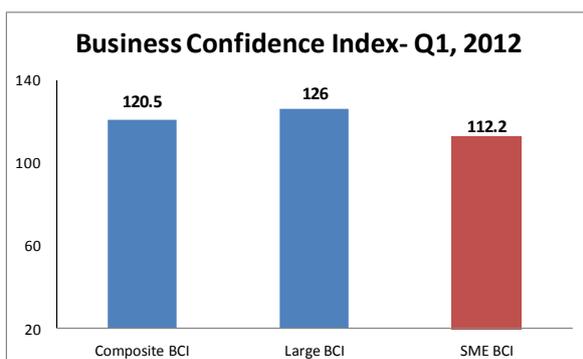
The composite confidence index in Q1, 2012 stood at 112.2 points, indicating a positive overall business outlook for the 2nd quarter, 2012. (a score of 100 indicates neutral sentiments).



(Base Quarter, Q2, 2011)

However, a quarter-on-quarter comparison shows a seasonal dip of around 10% in overall optimism of SMEs as compared to Q4, 2011 which is due to the combined effect of reduced tourism activity in the upcoming summer months, and the onset of family vacations and school holidays.

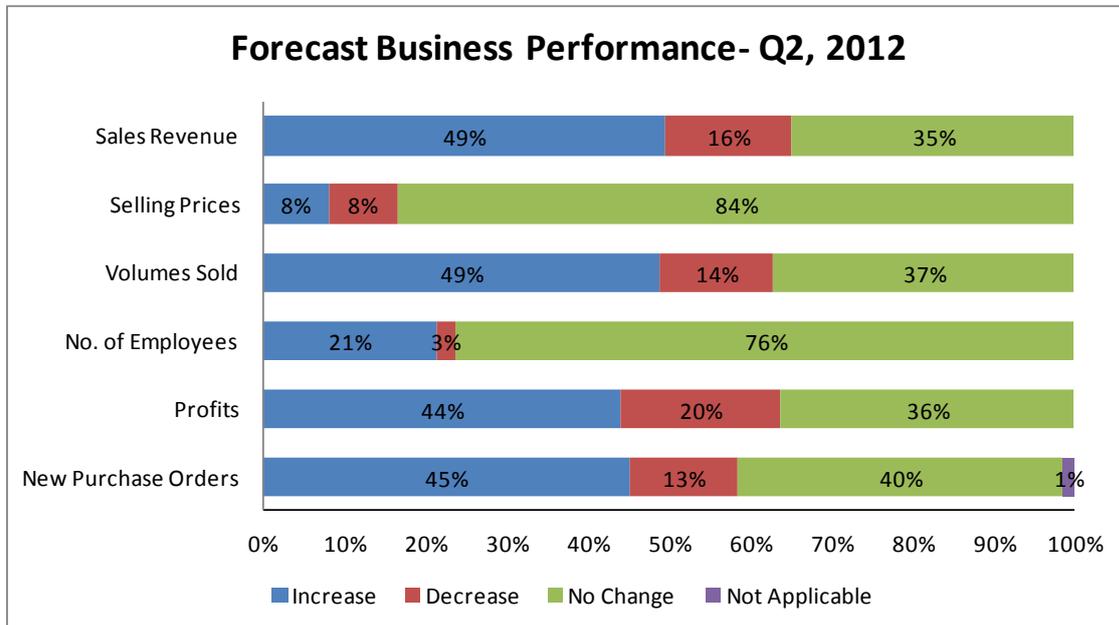
Although optimism is widely shared among all the firms, expectations are more upbeat



among large businesses than among SMEs, as shown in their respective index scores of 112 and 126. This higher confidence among large companies is primarily due to a more optimistic outlook on future selling prices and profits. This is similar to Q4, 2011 finding according to which large companies

were relatively more optimistic than SMEs on the account of higher profit expectations.

SME BUSINESS OUTLOOK – Q2, 2012

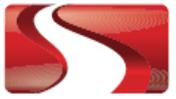


Reflecting the expectations of the overall business community, the survey reveals positive outlook for the coming quarter; with 49% of the SMEs expecting an improvement in sales revenue and 35% foreseeing no change in Q2, 2012.

Continuing the trends of the last few quarters, optimistic sales expectations are driven by an increasing real business activity (sales volumes) as prices will continue to remain largely stable. However, a few (10%) companies intend to raise their selling prices due to rising prices of raw materials which are determined on global market prices (fuel, plastic resins, metals, food & beverage ingredients and building materials).

A comparison between large companies and SMEs shows that the former are moderately more optimistic about sales revenues than the latter, with a positive net balance² of 40% and 33% respectively.

² Net Balance = % of respondents citing an increase - % of respondents citing a decrease



The overall optimistic SME sentiments are driven by the upbeat expectations of the manufacturing SMEs on all key parameters (sales volume, selling prices, profits, employees), closely followed by SMEs in the service & trading sectors. In contrast, expectations for large companies are driven by the trading sector), followed by manufacturing and service sector companies.

Within the manufacturing sector, sales volumes expectations are high for SMEs engaged in metal fabrication, manufacturing of plastics and furniture. In contrast, SMEs in food & beverage (F&B), cement, and glass manufacturing sub-sectors are expecting a decrease in their sales volume in the coming quarter.

The positive outlook for the service sector SMEs is driven by sub-sectors like professional services, transportation, IT & telecom; which are expecting a significant increase in their sales in the coming quarter.

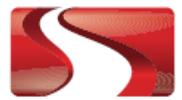
SMEs in the Transportation sector are also having a positive outlook for Q2 2012 with shipping, cargo and logistics companies expecting a seasonal rise in activity as traders tend to stock goods prior to summer holidays & Ramadan.

Companies in construction have pointed to some recovery in the next quarter, with 47% of the respondents expecting an increase in orders from existing projects that had previously been put on hold. This trend is reaffirmed by the positive sentiments of many architecture & engineering firms who also expect some of the stalled projects to be revived in the coming quarter.

However, SMEs in Tourism & Hospitality foresee decline in business performance for the coming quarter. With the advent of the summer season, inbound tourism is likely to decline in the next quarter. Resultantly, hotels and hotel apartments are expecting a decline in sales volume in Q2, 2012, due to expected lower occupancy rates. However, SMEs in other activities, such as car rental companies and travel agencies and tour operators, have indicated a relatively stable outlook for the next quarter primarily driven by existing service contracts.

Although positive, the outlook for SMEs in the trading sector is lower as compared to manufacturing and service sectors. In addition, expectations are shaped by the optimism of retail oriented businesses.

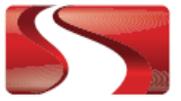
SMEs trading in sub-sectors such as jewellery, footwear, cosmetics, garments, pharmacy, electronics and auto-parts foresee positive performance in the next quarter owing to rising exports.



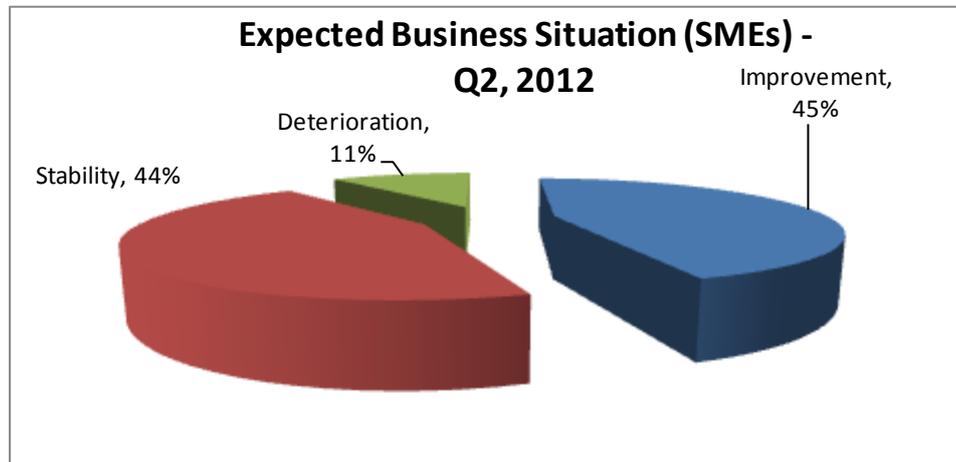
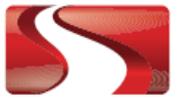
- The fashion-oriented SMEs (jewellery, footwear & cosmetics trading) are bullish on their expected sales volume due to higher optimism on export sales as well as plans for stock clearance through promotions & discounts.
- SMEs engaged in Garment trading also expect higher sales in the next quarter, as the demand for summer wear is likely to increase from retailers who often tend to buy / procure stock from wholesalers before the upcoming shopping festival - Dubai Summer Surprises (DSS) - and the festive Ramadan season.
- Sales of electronics & computer trading SMEs are expected to be higher on account of new orders from institutional buyers in local market as well as growth in re-export business.
- Food & beverage trading SMEs engaged in re-exports, have higher optimism on their sales performance.

In line with the positive outlook on sales, the percentage of companies planning to increase their purchase orders has remained largely stable (40% in Q2), as many companies plan to replenish stocks for the upcoming Dubai Summer Surprises & Ramadan season. A look at the different sectors reveals that manufacturing firms (57% of firms) are the keenest to raise their new purchase orders in the next quarter, followed by trading (48%) and services (41%) firms. Compared to SMEs, large companies are more optimistic on new purchase orders with 50% of the respondents expecting an increase in the next quarter.

As for employment,, the outlook remains stable with 76% of SMEs expecting 'no change' in their employee count in Q2, 2012. Manufacturing & service SMEs are slightly more inclined to hire additional workers in the coming quarter as compared to trading firms. However, the proportion of SMEs planning to increase their workforce has marginally declined from 28% in Q1 to 21% in Q2, 2012. In contrast, large companies are relatively more optimistic than SMEs on hiring new employees with 31% of them planning to hire additional workers in Q2, 2012.



Given the overall positive outlook on sales, profits are generally expected to rise or at least to remain stable with 44% of SMEs expecting higher profits in the next quarter while less than 20% think their profits will decline. However, large companies are more optimistic than SMEs about Q2 profits, with a net positive balance of 31% for large companies against 24% for SMEs.



According to SMEs' overall assessment, the business outlook for Q2, 2012 remains positive, with 89% of the SME respondents reporting either improvement or stability in comparison with Q1 of this year.



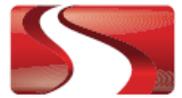
SME PERFORMANCE – Q1, 2012

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 of SMEs from one quarter to another.

Compared with the previous quarter (Q4, 2011), business for SMEs was relatively slower in Q1, 2012 as a higher number of SMEs reported a decrease rather than an increase in sales volumes. However, it is interesting to note that SMEs in tourism and manufacturing reported an improvement in sales volumes in Q1, 2012 in comparison with the preceding quarter (Q4, 2011). In addition, large companies reported positive business performance in the current quarter with a positive net balance of 28% as compared to the positive net balance of 8% in Q4, 2011.

Selling prices remained largely stable in Q1, 2012 with almost 53% of the SME respondents reporting 'no change'. However, 35% reported a reduction in their prices in order to attract and retain customers in sectors that have experienced increasing competition and reduced demand. The activities reporting price reduction are cement & plastics manufacturing, architectural & engineering, construction & contracting, and trading in computer & electronics, textiles & garments.

- Echoing last quarter trends, manufacturing SMEs performed better than their services and trading counterparts.
- The positive performance of SMEs in manufacturing seems to be driven by plastics, chemicals and food & beverages. However, firms producing or dealing in cement and metals faced challenges due to the continuing slowdown in construction activity. This is also reflected in their capacity utilization which averaged 35 to 50% against 70% for plastics, chemicals and food & beverages.
- The main factors accounting for a negative net balance for SMEs in the trading sector are the decline in sales in textiles - high competition from local & international players,



furniture due to reduced local demand, groceries & foodstuff because of high competition from supermarkets & hypermarkets, auto parts - due to high competition from Chinese players, and building & construction for lack of new projects.

- The performance of SMEs in services was pulled down by the slowdown of transportation, contracting, architectural and professional services firms even though a few contracting companies reported increased sales which were prompted by price discounts offered to win new work contracts on existing construction projects. In contrast, SMEs in tourism & hospitality (car rental, hotels, restaurants, travel agencies & tour operators) outperformed other types of services, driven by high demand in the peak tourist season of the first quarter of this year which resulted in high hotel occupancy rates varying between 80 and 90%.
- SMEs operating in the IT & telecom services sector also bagged new contracts from Government & multinational companies. In contrast SMEs in transportation sector continued to suffer in Q1, 2012, owing to lower orders from Europe, reduced cargo movements to Iran due to recent trade restrictions, reduced movements of construction material due to low local demand, and further reduction in the value of orders from existing customers.

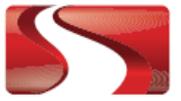
Hiring was by and large stable in Q1, 2012, although a proportion of SMEs reported new hiring as shown in a positive net balance of 11%. A majority of firms (67%) reported indeed 'no change' in their employee count for this quarter. Hiring was more prevalent in the services & manufacturing sector with a positive net balance of 13% each, followed by SMEs in trading (positive net balance of 4%). A majority of companies that reported a decline in workforce were from the contracting services and transportation sector. However, a higher proportion of large companies reported an increase in their employee count as compared to SMEs, 28% for the former against 22% for the latter.



- Mirroring the overall performance of the SMEs on sales volumes, new purchase orders also declined in this quarter, as reflected by a negative net balance of 5%. Around 48% of respondents in trading reported a decline in new purchase orders against 34% and 28% of the SMEs in services & manufacturing sectors respectively. In comparison, large companies have reported a positive performance on new purchase orders as reflected by the positive Net Balance of 16% in Q1, 2012.
- Following last quarter behavior, the cost of labor remained relatively stable in Q1, 2012 with 67% of SMEs reporting no change in unit labor costs and only 29% reporting an increase imputed to annual increments & bonuses provided to employees at the beginning of the year (January).

The cost of raw materials, a growing cause of concern for most SMEs, increased for 42% of the respondents in Q1, 2012. The impact of such costs was even higher for large companies with 63% of the companies reporting an increase in raw material costs in Q1, 2012. Rising costs related to fuel (diesel) had, as expected, a strong impact on transportation activity while rising cost of clinker, food ingredients & flavors, plastic & petrochemical products, metals (aluminum & steel), wood and chemicals adversely affected manufacturing. In addition, rising prices of tiles, marble, cement, electrical items and paints are reported to be the main cause of concern for construction related businesses.

Rental costs remained stable in Q1, 2012 for 73% of the SMEs, resonating findings from the last quarter which showed that for 79% of SME respondents rents didn't change. However, for a few respondents (14%), rents increased in the last quarter following the annual renewal of rent contracts with an approximate increase of 5% to 10%. Likewise, large companies also reported stability in rental prices.



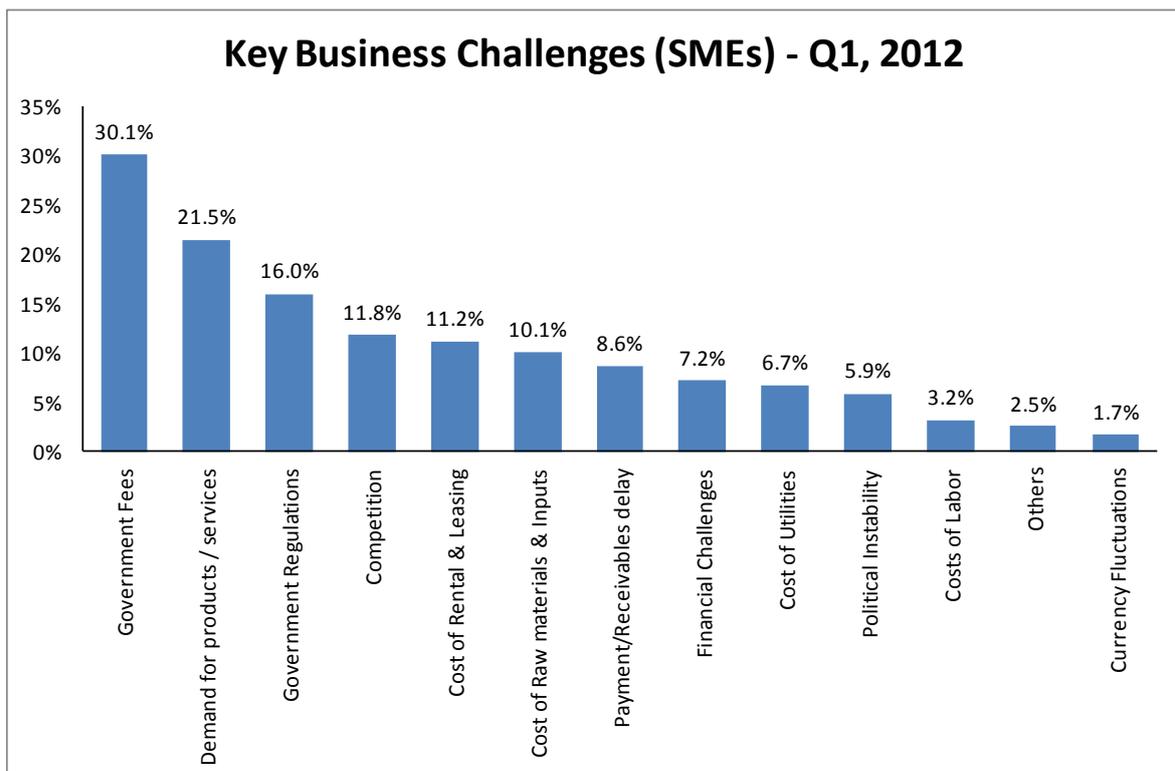
The current quarter survey also revealed that around 29% of SMEs used bank finance out of which 75% reported no changes in the cost of finance and 16% reported an increase in this cost. In terms of sectoral disparities, manufacturing SMEs made more recourse to bank finance (37%) than trading (14%) and services firms (9%).

The combination of the slowdown in sales and rising costs (mainly of raw materials) led to lower profits with 57% of SMEs reporting a decline in Q1, 2012 as compared to Q4, 2011. However, large companies have reported a positive performance on profits in Q1, 2012 as compared to the SMEs with 50% of the respondents indicating an increase in business profits in the last quarter.



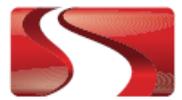
KEY BUSINESS CHALLENGES IN DUBAI

The survey also addressed key challenges faced, as perceived by SMEs at the end of Q1, 2012. It is interesting to note that 23% of the SMEs cited no business challenges which is a significant change compared to Q4, 2011 findings (11%).



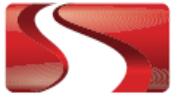
The following are found to be the major challenges impacting the business in Dubai:

1. Government fees - cited by almost 30% of respondents - have been reported as the most serious challenge. Main reasons cited are the high cost of trade license renewal and the increase in employee visa fees (on account of reduction in tenure of visa from 3 to 2 years, mandatory Emirates ID requirement etc). Transportation firms also reported rising port handling charges and municipality fees.
2. Relatively low demand for products and services (cited by 21% of the respondents). Insufficient demand constrained SME businesses in the construction sector (including cement, glass and metal manufacturing companies), due to the slow recovery of the real



estate sector and the scarcity of new projects. SMEs in the transportation industry also experienced a dip in demand due to the economic climate in US and Europe, economic and trade sanctions against Iran and stiff competition from local and international companies.

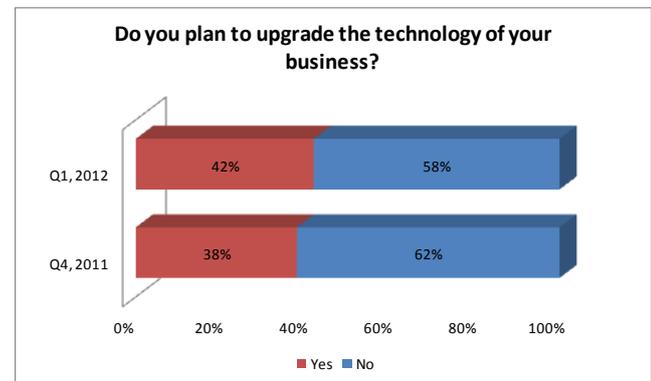
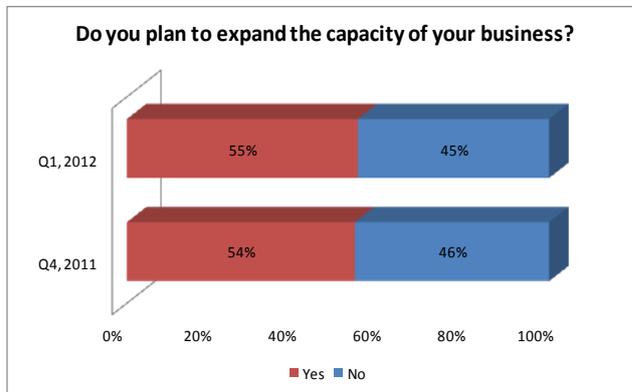
3. The third most important business challenge is government regulations (cited by 16% of the respondents). Frequent changes in business regulations (*relating to business licensing procedures, import-export procedures, municipality and traffic rules*), coupled with a lack of communication of such changes, are considered the third largest challenge.
4. Competition (*cited by ~12% of respondents*): Competition from local and international players is the fourth most serious challenge. SMEs in transportation, manufacturing (cement, plastics and food & beverage) and trading (construction material) seem to be the most affected by this challenge. For instance, food & beverage manufacturing SMEs cited intense competition from companies in Saudi Arabia - supplying to the UAE - which are strongly supported by the Saudi government.
5. High cost of rentals & leasing was reported as an important challenge by businesses who had to renew their leases at higher rentals. These respondents stated that in spite of the business slowdown, rents increased by 5-10%. This challenge was felt to be more pronounced among Free Zone companies.
6. SMEs have also been adversely affected by fluctuating and increasing costs of key raw materials and some other inputs. Rising costs of clinker, food ingredients & flavors, plastic & petrochemical products, metals (aluminum & steel), wood, chemicals, and commercial fuel had an adverse impact on manufacturing firms while rising prices of tiles, marble, cement, electrical items, paints were a cause of concern for construction related businesses.
7. Delays in payment receivables were reported by 8% of respondents: collecting money from customers, making timely payments to suppliers and negotiating better credit terms. In addition, respondents expressed the need for more transparency and stringent laws for enforcing contracts and collection of debts.



In terms of differences across business categories, the main challenges reported by SMEs were more or less the same as those faced by other firms. However, large companies have a different ranking of these challenges: competition first, followed by uncertainty in government regulations, then by increasing government fees.



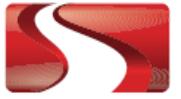
INVESTMENT OUTLOOK



The survey reveals that companies are more willing to expand the capacity of their business (55%) as compared to upgrading technology (42%). Compared to the previous quarter, capital investment plans over a twelve-month horizon are steady; with 55% planning to expand their capacity (vs. 54% of businesses as per the Q4 survey) and 42% of firms planning to upgrade technology (vs. 38% of businesses as per the Q4 survey).

Primary reasons cited by businesses not willing to expand their capacity in the coming quarter are unfavorable market conditions, lack of clarity in the improvement of business situation in the upcoming quarter, investments already undertaken in expanding the capacity and under utilization of existing capacity of the business. Key sub-sectors not planning to expand capacity are construction & contracting and transportation sectors with 58% and 40% respondents within the respective sectors not planning to add capacity in the next 12 months.

- From a sectoral perspective, service sector SMEs are the most optimistic about investing in capacity expansion, with approximately 58% expressing intent to invest in capacity expansion. In comparison, manufacturing SMEs are more inclined to increase investments in technology upgradation followed by services and trading SMEs.
- From a business size perspective, large businesses are more inclined to upgrade technology while SME businesses are more willing to invest in expanding the capacity of their business.



- With regards to the export orientation of SME businesses, both domestic and export oriented firms are more optimistic on expanding the capacity of their business.
- Further, the survey reveals that there is no significant difference in capacity expansion and technology upgradation plans of SMEs registered in the Dubai mainland and Free zones.



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