

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

Q3 - 2012

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AT A GLANCE

- The composite Business Confidence Index for the SME sector in Q3, 2012 is at 124.7 points with a y-o-y gain of 7.8% and a q-o-q gain of 16%, indicating that the overall business outlook for the coming quarter (Q4, 2012) is positive and rising.
- A bullish sales outlook reflects expansion in business activity, with 91% of the businesses expecting either an increase or no change in sales volume in the next quarter. Among the key sectors, expectations are the highest among manufacturing firms followed by service and trading firms.
- 45% of companies in the sample reported no business challenge this quarter, reflecting an improvement over the previous quarter in the ease of doing business in Dubai
- While key business expectations of SMEs is in line with the overall business community, however the overall optimism of SMEs is observed to be higher than large companies
- Large companies are more optimistic in their investment outlook over the next 12 months compared to SMEs
- Only 27% of the companies have availed bank finance; high interest rates & charges and challenges with collateral / guarantees are elicited as the key deterrents disabling access to bank finance

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 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 3rd Quarter of 2012 and highlights the future expectations of SME businesses in Dubai. The survey was administered to 459 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 Q3, 2012¹ was conducted on a total of 520 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.

Distribution of survey respondents across industry groups						
	Trading (169)		Manufacturing (68)		Services (222)	
	Employees	Turnover	Employees	Turnover	Employees	Turnover
Micro	<= 9	& <= AED 9 mn	<= 20	& <= AED 10 mn	<= 20	& <= AED 3 mn
		47		9		64
Small	<= 35	& <= AED 50 mn	<= 100	& <= AED 100 mn	<= 100	& <= AED 25 mn
		82		39		91
Medium	<= 75	& <= AED 250 mn	<= 250	& <= AED 250 mn	<= 250	& <= AED 150 mn
		40		20		67

● 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.

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.



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:

(% of positive responses - % 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*

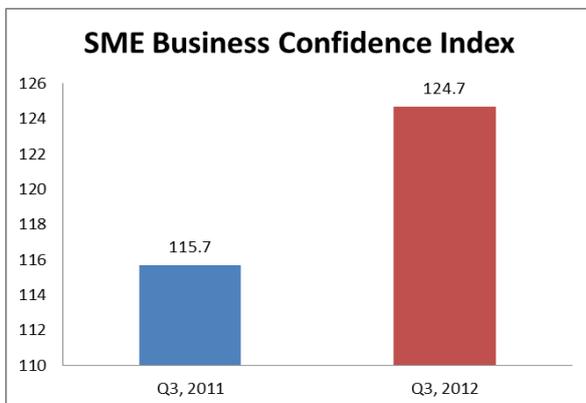
When expressed with reference to the base quarter Q2-2011, the following interpretations hold (t and t-1 referring to two consecutive quarters):

- *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 – Q3, 2012

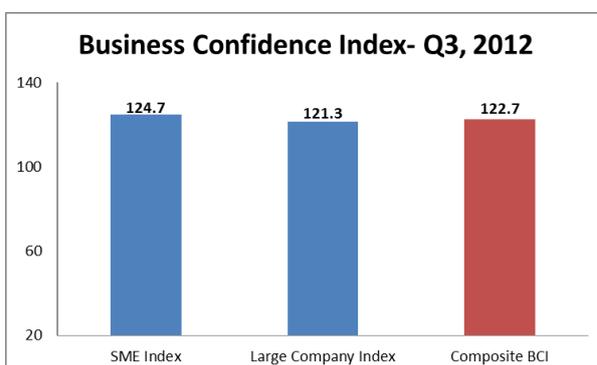
In its latest forecast, the IMF has said that the global economic slowdown was worsening, as it cut its growth forecast for the global economy to 3.3% in 2012. The Fund also said that the Euro area's debt crisis was a key threat and the risks to global financial stability had risen in the last six months. Risks from the Euro zone could also spill into emerging markets, where growth is already slowing. The IMF has estimated a growth of 4% for the UAE for the current year, supported by increased oil and NGL production and firm prices, as well as accommodative monetary and fiscal policies.



(Base Quarter, Q2, 2011)

Despite global uncertainty, Dubai's SME business confidence index reflects a rebound in economic activity in the next quarter. At 124.7 points, the overall business outlook for SMEs is positive for the fourth quarter of 2012. (A score of 100 indicates stable/neutral sentiments).

A year-on-year comparison reveals an increase of 9.0 points over the index value during the same period in 2011. This is due to the increased optimism on volumes sold and profits in Q3, 2012 compared to Q3, 2011. Moreover, a quarter-on-quarter comparison reflects that the confidence index has increased by more than 16% compared to Q2, 2012.

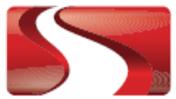


A comparison between large companies and SMEs shows a continuation of last quarter's trend with SMEs being slightly more upbeat than large companies in their expectations, as shown by their respective

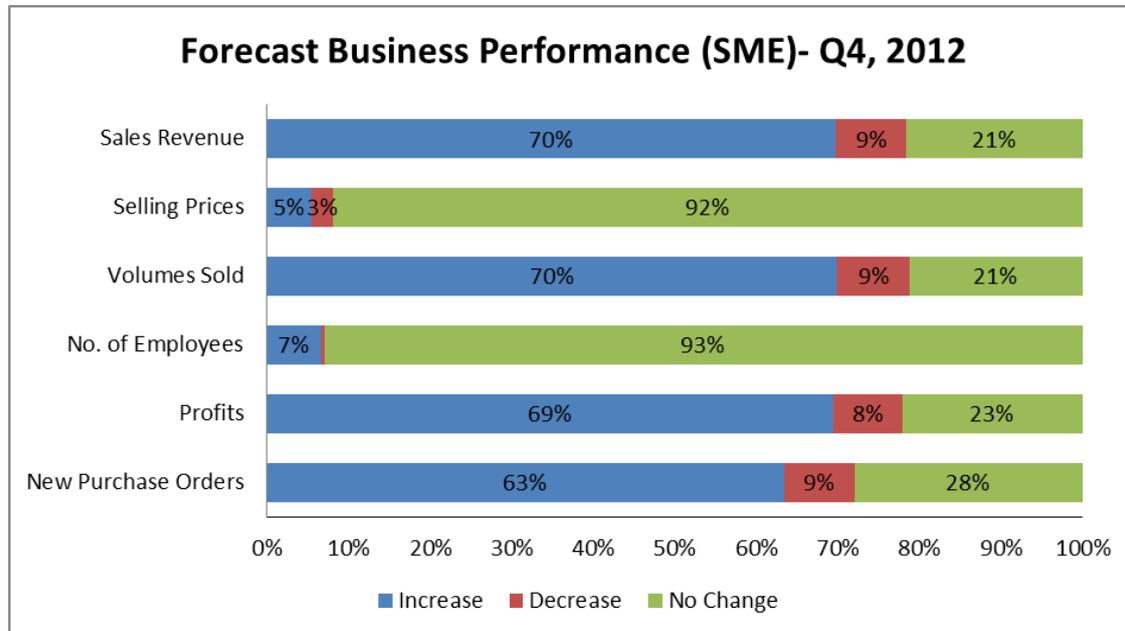


index scores of 124.7 and 121.3. The higher confidence among SMEs is due to their more optimistic outlook with respect to all four parameters: volumes sold, profits, hiring and selling prices.

The UAE Purchasing Managers' Index also rose in September to 53.8 points, up from 53.3 in the month before, reflecting the economy's steady pace of growth amid increasing signs of a global slowdown. The PMI also showed that new export orders increased for the 28th month in a row and staffing levels expanded during September as companies responded to greater production requirements.



SME BUSINESS OUTLOOK – Q3, 2012



Reflecting the expectations of the overall business community, the survey reveals rising expectations for the coming quarter; with 70% of the companies expecting an improvement in their sales revenue (an increase of 20% over the previous quarter) and 21% expecting no change in Q4, 2012. The net balance for sales revenues expectations stands at positive 61% for Q4, 2012 compared to positive 22% in the previous quarter.

Following the trend in the past quarters, the optimistic sales forecast in this quarter is driven by an expectation of higher volumes (net balance for outlook on sales volumes has improved from positive 22% in Q3, 2012 to positive 61% for Q4, 2012). Outlook for sales volumes in Q4, 2012 is also higher when compared with the same period in 2011, with a net balance of positive 61% this year versus positive 42% last year.

A comparison between SMEs and large companies shows that the former are more optimistic about sales revenues than the latter, with a positive net balance² of 61% and 43% respectively. The higher optimism in SMEs is driven by a more optimistic outlook with respect to volumes, since expectations regarding selling prices are very similar.

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



The overall business sentiments are driven by the upbeat expectations of the manufacturing sector on all key parameters (sales volume, profits, employees), followed by services and trading. The outlook for the service sector has shown a sharp improvement from the last quarter. As in the previous quarter, expectations for large companies continue to be driven by the trading sector, followed by manufacturing and service sector companies.

In line with the overall business outlook, manufacturing SMEs are more optimistic in terms of expected sales volumes for Q4, 2012, followed by service and then trading SMEs (positive net balance of 72% for manufacturing SMEs, 66% for services SMEs and 50% for trading SMEs)

Within the manufacturing sector, the outlook across all sub-sectors (especially companies in metals, food & beverage, paper & printing products and chemicals) is very optimistic, with 79% of the respondents expecting their volumes to increase (compared to 68% in the previous quarter), while 14% anticipate no change. A marginal 7% expects any decrease in volumes in the coming quarter. Key reasons cited include increase in demand from new projects, expansion in new markets and the onset of the tourist and festive season in the coming quarter.

The outlook for the overall service sector has also surged in Q4, 2012, compared to the last quarter. Year-on-year comparison for the overall service sector also reveals a gain in the outlook for volumes sold. Within the service sector, firms engaged in construction are most optimistic followed by firms engaged in other sub-sectors such as advertising, education etc.

Companies in construction are expecting new projects in the local as well as regional markets, which would lead to an increase in their business activity. Among the other service sub-sectors, advertising firms anticipate more business in the fourth quarter compared to the 2nd and 3rd quarters, due to the upcoming festive season wherein the



demand for advertisements and promotions increases. Education institutions are upbeat about Q4 since after the summer vacations, this is the time when new students seek admissions.

Driven by increased demand from all major sectors during this period, transportation service providers are also expecting an increase in business activity in the coming quarter. Transportation service providers offering services in regional / international markets are expecting better demand from their export markets.

Hotels and restaurants are also optimistic on their business performance in the next quarter with 73% expecting an increase in volumes. Respondents have mentioned that the increased tourist inflow during the winter season will drive their business. A few hotel respondents also cited plans to undertake promotional activities with the objective of maximizing their occupancy levels.

Although positive, the outlook for the Trading sector is less optimistic than Manufacturing and Services. The outlook for the Trading sector has shown a significant improvement over the last quarter with 64% of the respondents anticipating an increase in volumes during the fourth quarter. Another 22% of the respondents do not anticipate any change in volumes in Q4. Key sub-sectors expecting an increase in demand in the next quarter include the following:



- Jewelry and precious gems traders are very bullish on their expected sales volume as they will benefit from high demand during the festive season in Q4.
- Footwear traders have also cited increased demand due to the festivals in the fourth quarter.
- Garments and textile trading businesses also expect higher sales in the next quarter, as customers are back in town after their summer vacations and demand is expected to go up during the festival season.
- Traders of spare auto parts are optimistic about the coming quarter as they anticipate new projects, while some expect to have higher exports to Africa.
- Sales of electronics & computer trading businesses are expected to be higher on anticipation on increased demand as a result of aggressive marketing and new promotions for customers.
- Food & beverage trading businesses as well as grocers have higher optimism on their sales performance due to the festivals, while exporters in this sub-sector are optimistic on higher levels of exports to Africa.
- Furniture traders also anticipate higher demand as they expect to get new stock which will attract customers, while exporters are expecting to sell more in the MENA region.

Sales prices will continue to remain stable in the coming quarter as well with 92% of the respondents expecting no change in the selling prices of their products and services. However, a few companies (5%) intend to increase their selling prices in the next quarter either to cover for the rising cost of raw materials or improve their profit margins by taking advantage of the seasonal high demand during the fourth quarter of 2012. Trading SMEs (net balance of positive 5%) are more optimistic than service (net balance of positive 2%) and manufacturing SMEs (net balance of 0%) with respect to their selling prices.

Mirroring the rising expectation on sales, 63% of the SMEs are also planning to increase their new purchase orders in the next quarter, to supplement the need for raw materials for their business. 28% of the businesses which are planning to maintain the same level of

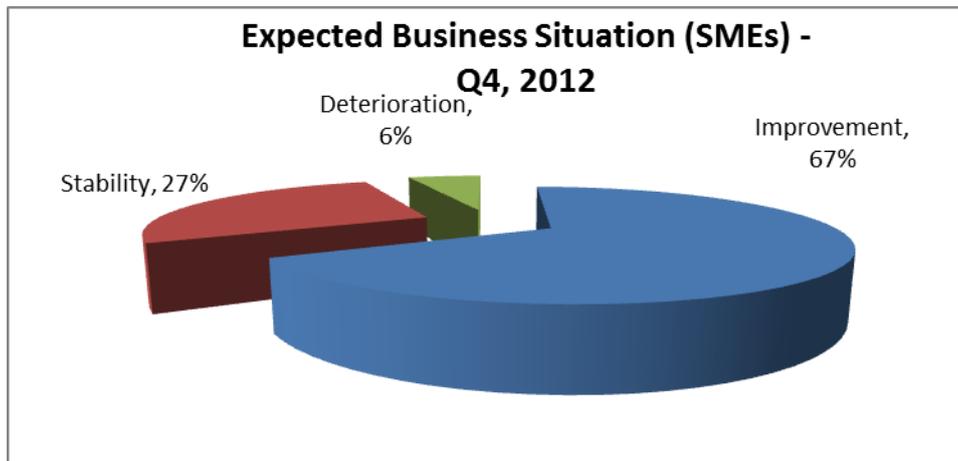


purchase orders are of the view that since the demand for their products is fluctuating, they would consider increasing their purchases based on market requirements. Manufacturing and service SMEs hold a more optimistic outlook compared to trading SMEs for new purchase orders in Q4. SMEs have a similar outlook as large companies on new purchase orders with 59% of the large companies expecting an increase in the next quarter.

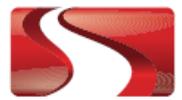
In line with the sentiments of the previous quarter, the outlook on hiring continues to remain stable, with 93% of businesses expecting 'no change' in their employee count in Q4, 2012. Firms across all sectors have reported a stable outlook in hiring. The survey also revealed that none of the businesses expect to decrease their workforce in the next quarter. Manufacturing and service sector firms are more optimistic on increasing their workforce (9% in each sector) in the coming quarter compared to trading sector firms (2% of the firms plan to increase their workforce). However, the proportion of SMEs planning to increase their workforce has declined from 12% in Q3, 2012 to 7% in Q4, 2012. SMEs remain slightly more optimistic than large companies on hiring new employees with just 3% of the large companies planning to hire additional workers in Q4, 2012.

With respect to capacity utilization, SMEs in manufacturing and services continue to be more optimistic than large companies (net balance of positive 59% for SMEs versus a net balance of positive 36% for large companies).

An increased optimism on sales activity is also reflected in the profitability expectations of companies in Dubai, with 69% of the respondents expecting an increase in the next quarter. Businesses are planning to take advantage of the high seasonal demand to increase their overall sales and profitability. Sector-wise comparison reveals that Manufacturing firms are most optimistic on profitability (78% reporting an increase in Q4, 2012) followed by Services (71%) and Trading (64%) firms. Also, following last quarter's trend, SMEs are more optimistic than large companies about Q4 profits, with a net positive balance of 61% for SMEs against 43% for large companies.



According to the firms' overall assessment, the business outlook for Q4, 2012 has become better, with 94% of the respondents reporting either an improvement or stability in comparison with Q3 of this year. A comparison between large companies and SMEs shows that the former expects a slightly better business situation during Q4. A marginal 2% of the large companies anticipate the business situation to deteriorate in Q4, compared to 6% of SMEs. A similar trend was observed in the last quarter where even though the confidence index of SMEs is higher than the large companies, the latter anticipate better business conditions in the Q4. Firms are anticipating an improvement in the coming quarter due to the following reasons: expectations of getting new projects, anticipation that the situation will be better in export markets, expansion of capacity, expectation of an improvement in global markets, seasonal demand improvement and higher sales in the fourth quarter due to the peak season for tourism and the onset of the festive season.



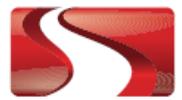
SME PERFORMANCE – Q3, 2012

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.

Business activity in Q3, 2012 was slightly weaker compared to the previous quarter as a higher number of respondents reported a decrease rather than an increase in sales volumes. This weakness was primarily in the service sector which reported a negative net balance of 16%, whereas the manufacturing and trading sectors reported a positive performance with respect to volumes sold in Q3, at positive 7% and positive 2% respectively. In addition, large companies reported a much better business performance in the current quarter with a positive net balance of 23% compared to the negative net balance of 6% for SMEs.

Selling prices remained largely stable in Q3, 2012 with 79% of the respondents reporting 'no change'. However, 14% of the respondents reported a reduction in their prices in order to boost sales in sectors that have experienced increasing competition and reduced demand. The activities reporting price reduction are cement and food & beverages manufacturing; transportation; and trading in electronics, food, footwear, and textiles.

- Echoing last quarter trends, manufacturing SMEs performed better than their services and trading counterparts.
- The positive performance of manufacturing was driven by aluminum, chemicals, A/C manufacturing, glass and furniture sub-sectors. However, firms producing or dealing in steel, concrete and packaging material and food & beverage manufacturing faced a slowdown in activity due to fewer projects and reduced consumer demand.
- The main factor accounting for a negative net balance for the trading sector was the decline in sales in textiles (summer vacations), industrial equipment (slow business due to Ramadan and summer vacations), marine suppliers, and stationery.

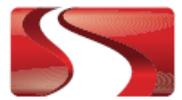


- The subdued performance of services in Q3 was led by a decline in activity in the following sectors: construction & architecture (lack of new projects, competition, decision makers were out of the country due to summer vacations), transportation (decrease in export sales, no new customers, decrease in demand as people were traveling, competition), advertising (off-season in Q2 and Q3 for exhibitions and conventions), equipment rental and other business services.

Workforce numbers remained mostly stable in Q3, 2012, with a majority of firms (90%) reporting 'no change' in their employee count for this quarter. Firms across all sectors reported no change in their hiring in Q3, 2012. Hiring was more prevalent in the manufacturing sector with a positive net balance of 4%, followed by services (positive net balance of 1%) and trading (negative net balance of 1%). Also, a similar proportion of large companies as well as SMEs reported an increase in their employee count at 5% for each group.

Replicating the overall performance of SMEs on sales volumes, new purchase orders also decreased during Q3, 2012, as reflected by a negative net balance of 5%. Among the key sectors, trading firms reported a positive performance with a positive net balance of 2%. On the other hand manufacturing firms recorded a negative net balance of 1% and service sector firms showed a negative net balance of 11% with respect to purchase orders. Large companies reported a much better performance on new purchase orders as reflected by the positive net balance of 26% in Q3, 2012.

As in the last quarter, the unit cost of labor to businesses remained relatively stable in Q3, 2012 with 87% of the businesses reporting no change in unit labor costs. 11% of businesses that reported an increase in labor costs cited the following reasons - higher salaries offered to new employees to remain competitive as employers, incentive given, increase in visa costs and government fees. Some companies faced higher costs as they were providing food, transportation & accommodation to their employees.



The cost of raw materials, which has been a cause for concern for several businesses, increased for 32% of the respondents in Q3, 2012, but it was 6 percentage points lower than in Q2, 2012 findings. The average increase in raw material costs ranged from 0-4%. Comparison between the three sectors shows that raw material costs impacted manufacturing firms the most, with 44% of the respondents indicating an increase in Q3. Within the manufacturing sector, the food & beverage, aluminum and glass sub-sectors were most impacted by the increase in raw materials. As in the previous quarter, the impact of such costs was lower for large companies with 18% of the companies reporting an increase in raw material costs in Q3, 2012.

Rental costs remained stable in Q3, 2012 for 92% of the respondents, resonating findings from the last quarter which showed that for 85% of respondents rents didn't change. However, for a few respondents (7%), rents increased mainly due to their annual increase in rents charged by the landlords. Rental costs increases were similar for all sectors. Likewise, large companies also reported stability in rental prices, with 98% of them reporting that there was no change in these costs in Q3.

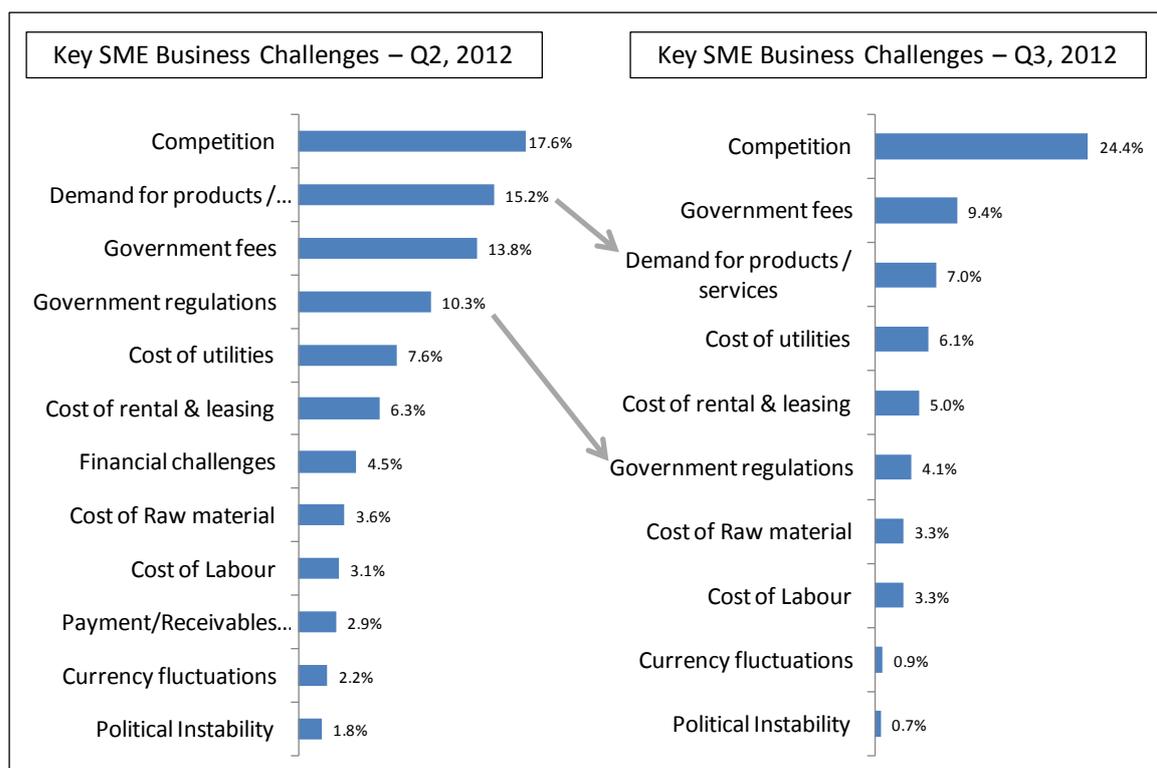
The current quarter survey also revealed that around 26% of the respondents availed bank finance out of which 75% reported no changes in the cost of finance and the remainder reported an increase in this cost. The top reason cited by respondents for not availing bank finance was the perception high interest rates & charges and challenges with collateral / guarantees. Among the large companies, 15% availed of bank finance, of which 78% reported no change in costs, while the remaining reported an increase.

The survey revealed that 58% of the respondents reported an increase or no change in their profit levels during Q3, 2012. Manufacturing firms reported better performance with respect to profits (net balance of positive 6%) compared to service (net balance of negative 15%) and trading firms (net balance of 0%). However, large companies have reported a better performance on profits in Q3, 2012 compared to SMEs with 72% of the respondents indicating an increase or no change in business profits in the last quarter.



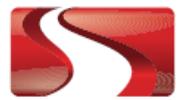
KEY BUSINESS CHALLENGES IN DUBAI

The survey also addressed key challenges faced, as perceived by businesses at the end of Q3, 2012. The survey shows that almost half (45%) of the businesses cited no challenges, which is a significant change compared to Q2, 2012 findings (31%). This indicates a marked improvement in the ease of doing business in Dubai in the current quarter.



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

1. Competition (*cited by 24% of the respondents*): Competition from local and international players is the top most challenge facing Dubai businesses. Also, most (93%) of the respondents that cited competition as a challenge, have said that the severity for this challenge had increased in the current quarter. This was common among all key sectors in the economy. Firms in manufacturing (aluminum, printing), services (construction & transportation) and trading (pharmacy) seem to be the most affected by this challenge.

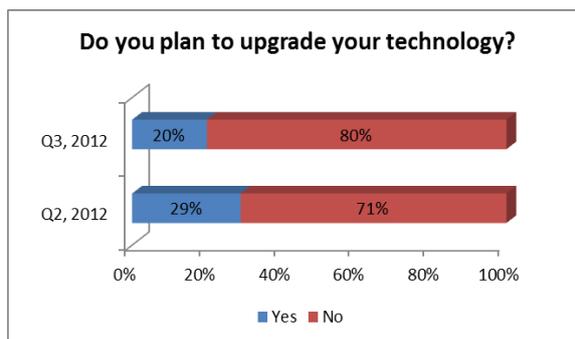
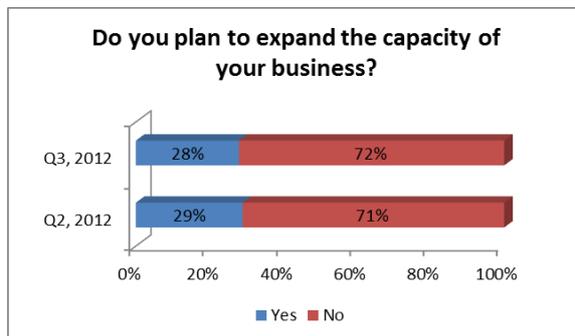


2. Government fees (*cited by 9% of the respondents*): This has been reported as the second most serious challenge in Q3; moving up a place as it was ranked third in the previous quarter. The main reasons cited are the high cost of trade license renewal and other government charges. Among the respondents that have cited this as a challenge, 89% have said the severity of this challenge had increased in the current quarter.
3. Insufficient demand for products and services (*cited by 7% of the respondents*): Among the respondents that cited low demand as a challenge, 69% of them said that the severity of this factor had increased in Q3, 2012.
4. Cost of utilities (*cited by over 6% of the respondents*): This challenge has increased in severity for 94% of the respondents that cited it as an important factor.
5. High cost of rentals & leasing (*cited by 5% of the respondents*): This was reported as an important challenge by businesses that had to renew their leases at higher rentals. Costs of rental and leasing increased for 88% of the respondents citing it as a challenge.
6. Government regulations (*cited by 4% of the respondents*): Frequent changes in business regulations (relating to business licensing procedures, import-export procedures, municipality and traffic rules). 81% of the respondents that cited government regulation as a challenge think that its severity has increased in the last quarter.

In terms of differences across business categories, it can also be observed that challenges cited by SMEs were similar to those faced by the overall business community. Whereas the top challenge remains the same for large companies, they cited insufficient demand as the next key challenge followed by cost of raw materials and government fees.



INVESTMENT OUTLOOK



In comparison with findings from the last quarter survey, the outlook of SMEs with respect to future expansion plans remains steady in Q3, 2012. However, compared to the last quarter, current survey findings show that a smaller number of businesses have cited plans to invest in technology upgrade. 28% of the respondents are planning to expand their capacity (vs. 29% of businesses in Q2) and 20% of firms planning to upgrade technology (vs. 29% of the businesses in Q2). Also, SMEs are slightly more willing to expand (28%) compared to upgrading technology (20%).

Businesses willing to expand capacity are planning to undertake capital investments such as expansion of the current office premises and investments in business assets such as factory, warehouse, machinery and vehicles. Also, several businesses are planning to expand capacity by opening a new branch office in UAE or in the GCC region.



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For businesses not willing to expand capacity, the primary reason cited is that they are satisfied with the current size or have no expansion plans at the current time. Unavailability of the required funds / capital investment and existing investments in building the current capacity have been cited as other reasons for not expanding capacity. Others have reported unfavorable or unstable market conditions due to which they not willing to undertake capacity expansion and are continuing operations with existing capacity

Sector wise comparison shows that service (31%) and manufacturing (31%) SMEs are slightly more optimistic about investing in capacity expansion compared to trading firms (22%). With respect to upgrade of technology, service SMEs (23%) are more optimistic followed by manufacturing SMEs (22%) and trading SMEs (15%).

From a business size perspective, large businesses are more inclined to upgrading technology as well expanding the capacity of their business compared to SMEs.

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