مؤسسة محمد بن راشد لتنمية
المشاريع الصغيرة والمتوسطة
DUBAI SME

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

SMEs Business Optimism Survey

Q4 - 2012

AT A GLANCE

- The composite Business Confidence Index for the SME sector in Q4, 2012 is at 127.8 points with a y-o-y gain of 2.8 points and a q-o-q gain of 3.1 points indicating that the overall business outlook for the coming quarter (Q1, 2013) is positive and rising.
- A bullish sales outlook reflects expansion in business activity, with 94% 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 trading firms followed by services and manufacturing firms.
- 31% of companies in the sample reported no business challenge this quarter (vs. 45% in Q3), reflecting a weakening 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 lower than large companies
- Large companies remain more optimistic in their investment outlook over the next 12 months compared to SMEs

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 4th Quarter of 2012 and highlights the future expectations of SME businesses in Dubai. The survey was administered to 446 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 Q4, 2012[1] was conducted on a total of 501 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 (159)			Manufacturing (70)			Services (217)		
	Employees		Turnover	Employees		Turnover	Employees		Turnover
Micro	< = 9	&	< = AED 9 mn	< = 20	&	< = AED 10 mn	< = 20	&	< = AED 3 mn
		73			22			81	
Small	< = 35	&	< = AED 50 mn	< = 100	&	< = AED 100 mn	< = 100	&	< = AED 25 mn
		64			34			95	
Medium	< = 75	&	< = AED 250 mn	< = 250	&	< = AED 250 mn	< = 250	&	< = AED 150 mn
		22			14			41	

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:

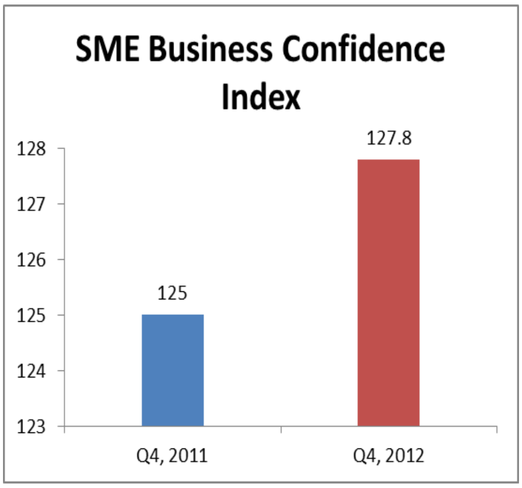
- ***BCI < 100, business expectations are negative***
- ***BCI = 100, business expectations are stable***
- ***BCI > 100, business expectations are positive***

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 – Q4, 2012

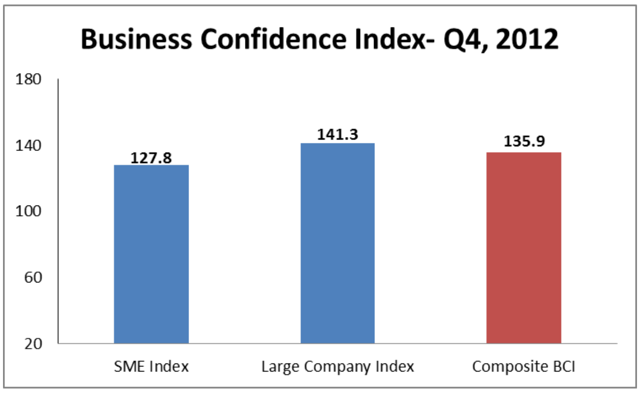
During 2012, the global economy continued to struggle with post crisis adjustments and growth weakened. Several developed economies fell into recession and the spillover effects from these countries was partly responsible for the slowdown in growth in many emerging and developing countries. Contrasting trends are found in Western Asia, where most oil-exporting countries experienced robust growth supported by record-high oil revenues and government spending.



(Base Quarter, Q2, 2011)

Dubai's economy looks set to sustain its growth momentum, as investor confidence has returned and some core sectors such as construction, real estate and tourism are rebounding. This is reflected in the rising business confidence index, which at 127.8 points, shows that the overall business outlook for SMEs in Dubai is positive and rising for the first quarter of 2013. (A score of 100 indicates stable/neutral sentiments).

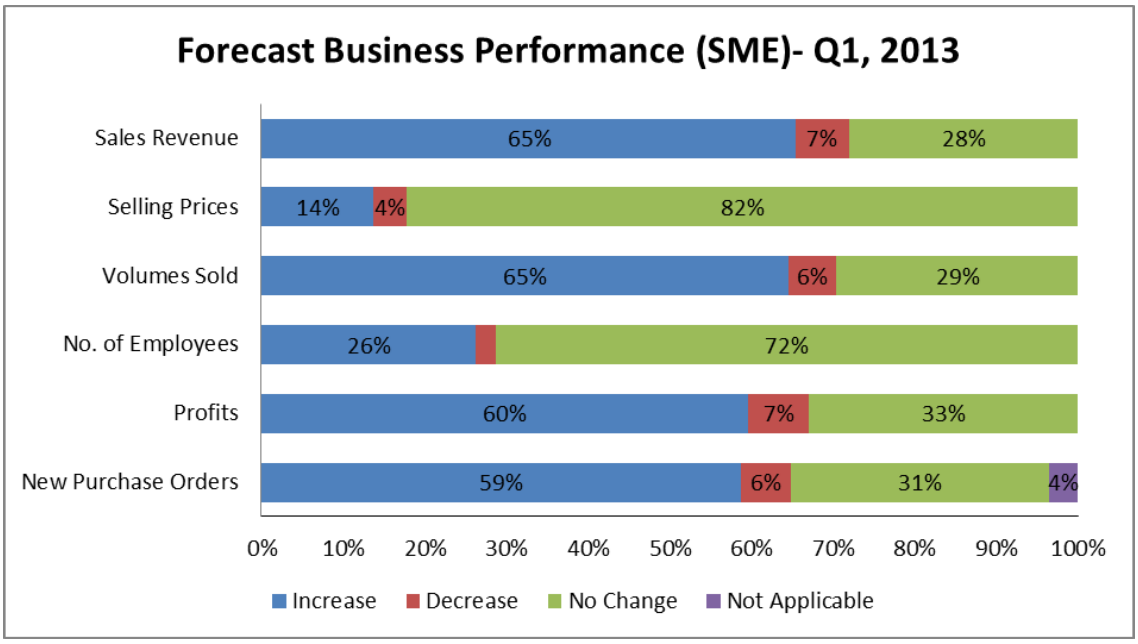
Quarter-on-quarter comparison shows that the current quarter composite index is 3.1 points higher than the index in the previous quarter. This is mainly due to higher optimism for profits, volumes and number of employees in the coming quarter. A year-on-year comparison reveals an increase of 2.8 points over the index value during the same period in 2011.



A comparison between large companies and SMEs shows a reversal of trend from the previous two quarters; large businesses are observed to be more optimistic than SMEs in this quarter, as shown by their respective index scores of 141.3 and 127.8. The higher confidence among large businesses is due to their more optimistic outlook with respect to sales revenue, volumes sold and profits.

The UAE Purchasing Managers' Index rose to the highest level in 19 months in December on external demand and rising public spending, reflecting that business conditions in the UAE’s non-oil producing private sector improved solidly. At 55.6, up from 53.7 in November, the PMI pointed to the strongest improvement in operating conditions in 19 months. The survey also suggests that Dubai’s export-orientated service sector has led the way, completing what has been a year of strong economic recovery for the emirate.

SME BUSINESS OUTLOOK – Q1, 2013



Reflecting the expectations of the overall business community, the survey reveals strong expectations for the coming quarter; with 65% of the companies expecting an improvement in their sales revenue (compared to 70% in the previous quarter) and 28% expecting no change in Q1, 2013. The net balance for sales revenues expectations stands at positive 58% for Q1, 2013 compared to positive 61% in the previous quarter.

Following the trend in the past quarters, the optimistic sales forecast in this quarter is driven by optimistic expectations for volumes (the net balance on sales volumes stands at positive 59% compared to positive 61% for Q4, 2012). Outlook for sales volumes in Q1, 2013 is also higher when compared with the same period in 2012, with a net balance of positive 59% this year versus positive 55% last year.

A comparison between SMEs and large companies shows a reversal of trend from the previous two quarters; large businesses are observed to be more optimistic than SMEs in this quarter with respect to sales revenues, as shown by their respective net balance scores of positive 69% and positive 58%. The higher optimism in SMEs is driven by a more optimistic outlook with respect to volumes, since expectations regarding selling prices are very similar.

The overall business sentiments are driven by the upbeat expectations across all sectors. While businesses in the services and trading sectors are more optimistic with respect to volumes sold, manufacturing firms have higher optimism for hiring and prices. Also, while the outlook for the trading sector has improved that for the manufacturing sector has edged lower. As in the previous quarters, expectations for volumes sold among large companies continue to be driven by the trading sector, followed by manufacturing and service sector companies.

In line with the overall business outlook, services and trading SMEs are more optimistic in terms of expected sales volumes for Q1, 2013, compared to manufacturing SMEs (positive net balance of 60% for services and trading SMEs and 51% for manufacturing SMEs)

Within the manufacturing sector, the outlook for companies engaged in the manufacture of cement, garments and glass is very optimistic, while those in the paper and plastic sub-sectors are the least optimistic. Within the manufacturing sector, 56% of the respondents expect their volumes to increase (compared to 79% in the previous quarter), while 40% anticipate no change. A marginal 4% 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 shopping festival season in the coming quarter.

The outlook for the overall service sector remains steady in Q1, 2013, compared to the last quarter. Year-on-year comparison for the overall service sector reveals a gain in the outlook for volumes sold (net balance of positive 60% in Q1 2013 and net balance of positive 54% in Q1 2012). Within the service sector, firms engaged in advertising, architecture and the tourism and hospitality segments are most optimistic followed by firms engaged in other sub-sectors such as professional services, printing, education, real estate and construction.

Among the service sub-sectors, advertising firms anticipate strong business in the first quarter of 2013, due to the upcoming Dubai shopping festive season (wherein the demand for advertisements and promotions increases), increase in capacity utilization and expansion plans. Architecture firms are upbeat about Q1 since they have new projects or have expansion plans in new markets such as Africa and India. Two-thirds of the companies in construction are expecting new projects in the local as well as regional markets or are expecting to restart stalled projects, which would lead to an increase in their business activity.

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 expect to get new orders during the festival season, have expansion plans and also because of expectations of higher demand in the first quarter as companies are refilling their stock and more business is happening during the New Year season.

Hotels and restaurants are quite optimistic as well on their business performance in the next quarter with 70% expecting an increase in volumes. Respondents have mentioned that the increased tourist inflow during the shopping festival will drive their business. Also since many events and exhibitions take place during this time, the increased tourist flow results in higher demand for their businesses.

The survey reveals that optimism in the trading sector is at a six quarter high in Q1, 2013. The net balance during Q1 stands at positive 60%, with 67% of the respondents anticipating an increase in volumes during the first quarter. Another 25% of the respondents do not anticipate any change in volumes in Q1. Key sub-sectors expecting an increase in demand in the next quarter include the following:

- Sales of electronics trading businesses are expected to be higher during the Dubai shopping festival, which will boost their business with the greater inflow of tourists. Those engaged in exports are expecting higher demand from the international markets.
- Food & beverage trading businesses including supermarkets and groceries have higher optimism on their sales performance due to increase in demand for food items during the winter season. Traders have mentioned that the demand for food products is steady during the period (October – March) as fewer residents tend to travel outside UAE for vacations. Exporters in this sub-sector are optimistic on higher levels of exports to Africa and the Middle East.
- Pharmacists are anticipating strong sales based on introduction of new products, impact of promotions and advertising as well as an increase in the number of tourists during the shopping festival.
- Jewelry and precious gems traders are very bullish on their expected sales volume as they expect to benefit from high demand during the Dubai shopping festival season in Q1 as well as from the increase in international orders.
- Footwear traders have also cited increased demand due to the shopping festival in the first quarter as well as planned sales promotions and advertising of their products. Select respondent also cited anticipation of higher export sales.
- Traders of computers & equipment, expect higher sales during Q1, on the back of an increase in tourist inflow during the next 3 months

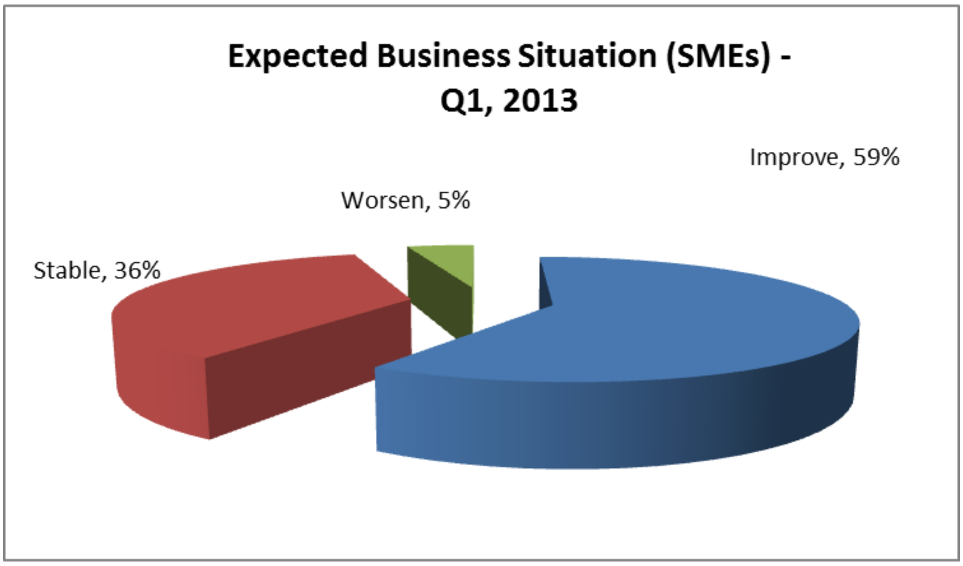
Sales prices will continue to remain stable in the coming quarter as well with 82% of the respondents expecting no change in the selling prices of their products and services, compared to 92% in the previous quarter. However, 14% of the companies intend to increase their selling prices in the next quarter either to cover for the rising cost of raw materials or improve their profit margins by taking advantage of the seasonal high demand during Q1 2013. Trading SMEs (net balance of positive 13%) are more optimistic than the service SMEs (net balance of positive 6%), but less optimistic than manufacturing SMEs (net balance of positive 16%) with respect to their selling prices.

Reflecting the strong expectations on sales, 59% 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 or because some prefer to stock on a regular basis in order to always be in a position to take orders whenever required. 31% of the businesses which are planning to maintain the same level of purchase orders have said that they have made their purchases in the previous quarters and currently have sufficient stocks. Trading SMEs hold a more optimistic outlook compared to services and manufacturing SMEs for new purchase orders in Q1. Large companies hold a more optimistic outlook on new purchase orders with 67% of the large companies expecting an increase in the next quarter.

The outlook on hiring has improved significantly over the previous quarter, with 26% of the SMEs expecting to increase their employee count in Q1, 2013 compared to just 7% in Q4, 2012. 71% of the SMEs expect to hold their employee count stable in Q1, 2013. Manufacturing and service sector firms are more optimistic with respect to hiring compared to trading firms, with 36% in manufacturing, 30% in services and 16% in trading expecting to increase in their employee count in Q1. The survey also revealed that a marginal 2% of the businesses expect to decrease their workforce in the next quarter. Reversing last quarter's trend, SMEs are observed to be slightly less optimistic than large companies on hiring new employees with 33% of the large companies planning to hire additional workers in Q1, 2013.

With respect to capacity utilization, SMEs in manufacturing and services are less optimistic than large companies (net balance of positive 57% for SMEs versus a net balance of positive 69% for large companies). In the previous quarter, SMEs had a much better outlook for capacity utilization compared to large companies.

The strong optimism on sales activity is also reflected in the profitability expectations of SMEs in Dubai, with 60% of the respondents expecting an increase in the next quarter. Businesses are expecting to make more profits as some are looking to get new projects or contracts, while some companies are undertaking cost cutting measures to increase their margins. Some firms foresee a big rise in demand for their products on account of the DSF. Sector-wise comparison reveals that services and trading firms are most optimistic on profitability (61% and 60% respectively reporting an increase in Q1, 2013) compared to manufacturing firms (56%). Also, reversing last quarter's trend, SMEs are less optimistic than large companies about Q1 profits, with a net positive balance of 53% for SMEs against 60% for large companies.



According to the firms' overall assessment, the business outlook for Q1, 2013 remains steady, with 95% of the respondents reporting either an improvement or stability in business conditions, (similar outlook as in Q4, 2012). A comparison between large companies and SMEs shows that the former are more optimistic about the business situation during Q1, 2013. 69% of the large companies anticipate the business situation to improve in Q1, compared to 59% of SMEs. Over two-thirds of the companies that expect the business environment to worsen have said that lack of demand is a factor for the current business situation.

SME PERFORMANCE – Q4, 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 Q4, 2012 was stronger compared to the previous quarter as a higher number of respondents reported an increase rather than a decrease in sales volumes**.** The manufacturing and services sectors reported a positive performance with respect to volumes sold in Q4, with a net balance at positive 14% and positive 16% respectively, while the trading sector reported a net balance of negative 18%. In addition, large companies reported a much better business performance in the current quarter with a positive net balance of 27% compared to the positive net balance of 3% for SMEs.

- The positive performance of manufacturing was driven by cement, food & beverages, glass and metals sub-sectors. However, firms producing or dealing in chemicals, furniture, garments, paper and plastics manufacturing faced a slowdown in activity due to liquidity crunch, increased competition, 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 auto parts (declining demand), building & construction (delayed payments and less demand), computers and electronics (slow demand, availability of cheap substitutes and slow business due to the festival season), cosmetics (impact of war in Syria), footwear (cheap substitutes), furniture (market has a large number of Chinese traders that sell goods at a much cheaper price), garments and textiles (no new orders or cheap substitutes from China) and grocers (slow business due to unrest in the region).
- The positive performance of services in Q4 was led by an increase in activity in the following sectors: advertising (increase in demand), architecture and construction (increase in number of contracts), education (new students), printers (GITEX), real

estate (increase in number of foreigners, improving business climate, Dubai is safer for investment compared to other countries in the region), hospitality (increase in tourists due to festive seasons and trade shows) and transport (booming business conditions have led to increasing number of people coming to Dubai, festive season).

Selling prices remained largely stable in Q4, 2012 with 68% of the respondents reporting 'no change'. However, 21% of the respondents reported a reduction in their prices in order to boost sales in sectors that have experienced increasing competition and reduced demand.

Workforce numbers improved during Q4, 2012 with 18% of the businesses reporting that they increased their workforce during the quarter. A majority of firms (70%) however reported 'no change' in their employee count for this quarter. Firms in the services and manufacturing sectors were more optimistic with 23% of the respondents in each sector reporting an increase in workforce compared to 10% in the trading sector. Also, a higher proportion of large companies (31%) compared to SMEs reported an increase in their employee count.

Replicating the overall performance of the business community on sales volumes, new purchase orders also increased during Q4, 2012, as reflected by a positive net balance of 5%. Among the key sectors, services and manufacturing firms reported a positive performance with a positive net balance of 14% and 13% respectively. On the other hand trading 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 31% in Q4, 2012.

As in the last quarter, the unit cost of labor to businesses remained relatively stable in Q4, 2012 with 71% of the businesses reporting no change in unit labor costs. However, 27% of businesses reported an increase in labor costs and cited the following reasons – revision of salaries, increments, increase in labor accommodation rent as well as increase in other costs of living and demand for higher salaries due to inflation.

The cost of raw materials, which has been a cause for concern for several businesses, increased for 44% of the SMEs in Q4, 2012, and it was 12 percentage points higher than in Q3, 2012 findings. Comparison between the three sectors shows that raw material costs impacted manufacturing firms the most, with 57% of the respondents indicating an increase in Q4. The corresponding number for the services sector is 40% and 45% for the trading sector. The impact of such costs was similar for large companies with 45% of the companies reporting an increase in raw material costs in Q4, 2012.

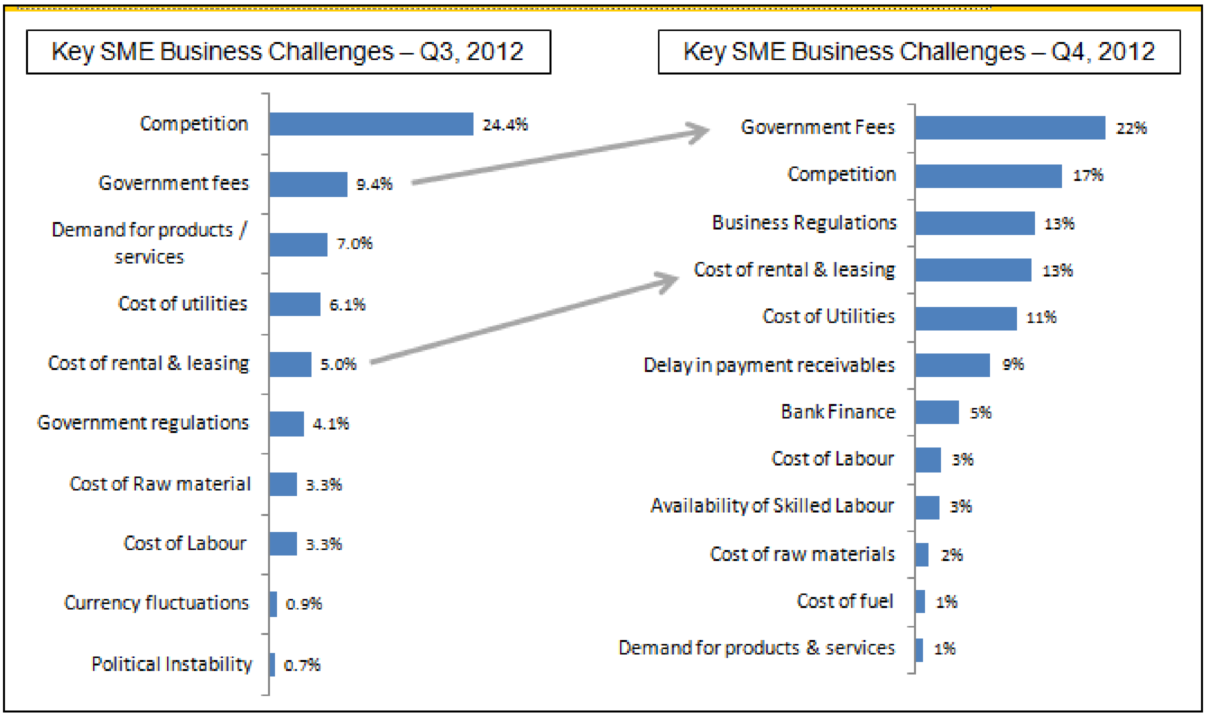
Rental costs remained stable in Q4, 2012 for 68% of the respondents, which was much lower from the last quarter which showed that for 92% of respondents rents didn't change. However, for 24% of the respondents rents increased mainly due to their annual increase in rents charged by the landlords. The impact of rental costs increases was much higher for manufacturing companies. 81% of the manufacturing companies reported an increase in rents in Q4 compared to 19% for trading SMEs and 9% for services SMEs. With respect to large companies, 76% reported an increase in rental costs in Q4.

The current quarter survey also revealed that around 24% of the SMEs availed bank finance out of which 77% reported no changes in the cost of finance and 22% reported an increase in this cost. The top reasons cited by respondents for not availing bank finance remained the perception of high interest rates & charges and challenges with collateral / guarantees. Among the large companies, 44% availed of bank finance, of which 79% reported no change in costs, while the remaining reported an increase.

The survey revealed that 50% of the respondents reported an increase or no change in their profit levels during Q4, 2012. Manufacturing firms reported better performance with respect to profits (net balance of negative 9%) compared to service (net balance of negative 12%) and trading firms (net balance of negative 41%). Following the trend in the last quarter, large companies have reported a better performance on profits in Q4, 2012 compared to SMEs with 64% 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 Q4, 2012. The survey shows that 31% of the SME businesses cited no challenges, indicating the ease of doing business in Dubai in the current quarter.



A comparison with the last quarter reveals that top 2 business challenges in Q4, 2012 are similar to those faced in Q3, 2012. However, there has been an interchange in the intensity of the challenge between competition and government fees. The following are found to be the major challenges impacting SMEs in Dubai:

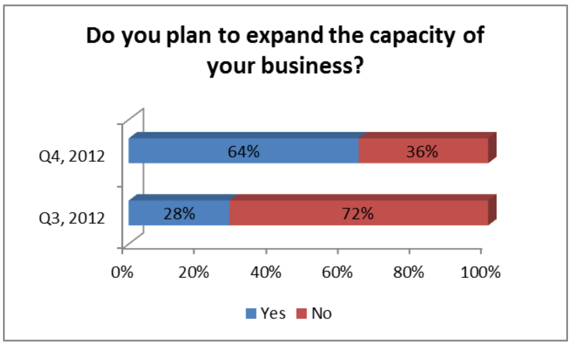
The following are found to be the major challenges impacting businesses in Dubai:

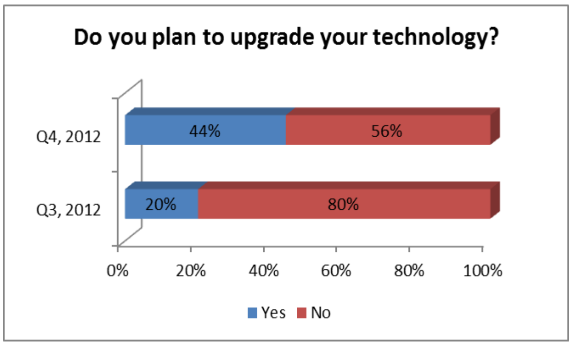
1. Government fees (*cited by 22% of the respondents):* This has been reported as the top most serious challenge in Q4; moving up a place as it was ranked second in the previous quarter. The main reasons cited are the high cost of trade license renewal and visa fees. Among the respondents that have cited this as a challenge, 59% have said the severity of this challenge had increased in the current quarter

2. Competition *(cited by 17% of the respondents):* Competition from local and international players is the top most challenge facing Dubai businesses. Also, (42%) 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 (cement, food & beverage, garments), services (construction & travel) and trading (auto parts, computers) seem to be the most affected by this challenge.
3. High cost of rentals & leasing *(cited by 13% 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 51% of the respondents citing it as a challenge.
4. Business regulations *(cited by 13% of the respondents):* Frequent changes in business regulations (relating to business licensing procedures, import-export procedures, municipality and traffic rules). 41% of the respondents that cited business regulation as a challenge think that its severity has increased in the last quarter.
5. Cost of utilities *(cited by 11% of the respondents):* This challenge has increased in severity for 48% of the respondents that cited it as an important factor
6. Delay in payment/receivables *(cited by 9% of the respondents):* Among the respondents that cited this factor as a challenge, 58% of them said that the severity of this factor had increased in Q4, 2012.

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. On the other hand, cost of utilities is the topmost challenge affecting large companies.

INVESTMENT OUTLOOK





In comparison with findings from the last quarter survey, the outlook of businesses with respect to future expansion plans has improved significantly in Q4, 2012. Also, compared to the last quarter, current survey findings show that a much higher number of businesses have cited plans to invest in technology upgrade. 64% of the respondents are planning to expand their capacity (vs. 28% of businesses in Q3) and 44% of firms are planning to upgrade technology (vs. 20% of the businesses in Q3). Also, companies are more willing to expand (64%) compared to upgrading technology (44%)

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.

Businesses with no expansion plans seem to be satisfied with the current scale of their operations or are looking for stability and profitability before adding to costs.

Sector wise comparison shows that services (65%) and manufacturing (64%) companies are slightly more optimistic about investing in capacity expansion compared to trading firms (62%). With respect to upgrade of technology, manufacturing firms (50%) are more optimistic followed by trading companies (44%) and service firms (41%).

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