

SMEs Business Optimism Survey

Q2, 2018

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AT A GLANCE

- The SME Composite BCI has gained on a yearly basis from 107.3 points in Q2, 2017 to 109.9 points in Q2, 2018.
- A comparison of the outlook on a q-o-q basis shows that the SME Composite BCI was marginally lower by 0.70 points on account of intense competition, slowing business conditions and lack of demand for products/services.
- Large companies continue to be more optimistic than SMEs with respect to their business outlook, with Composite BCI scores of 114.6 points and 109.9 points, respectively. Large companies are more confident than SMEs about their outlook with respect to volumes, hiring, profitability and new purchase orders. SMEs have displayed a better forecast for revenues and selling prices.
- Dubai's SMEs expect the business situation to weaken in Q3, 2018 than that in the previous quarter. The proportion of firms that anticipate an improvement in the business environment stands at 44% for Q3, 2018 compared to 50% for Q2, 2018. Additionally, 45% of the survey respondents do not anticipate any obstacles in their business operations during Q2, 2018.
- Key challenges faced by SMEs continue to be VAT implementation and competition.
- Plans to expand capacity have strengthened over the quarter, while plans to upgrade technology are weak on a quarterly basis.

The Department of Economic Development (DED) is a Dubai Government entity 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 conducts a quarterly business survey to assess the level of current economic activity and the outlook of businesses for the next quarter.

This document presents a summary of the survey conducted in the second quarter of 2018.

In addition, the survey elicits feedback from businesses on challenges that may impact growth and development and assesses their investment outlook for the coming twelve months.

METHODOLOGY

The quarterly business survey for Q2, 2018 was conducted for 500 businesses in 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’s GDP.

The survey was administered to 442 Small & Medium Enterprises (SMEs) in Dubai.

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

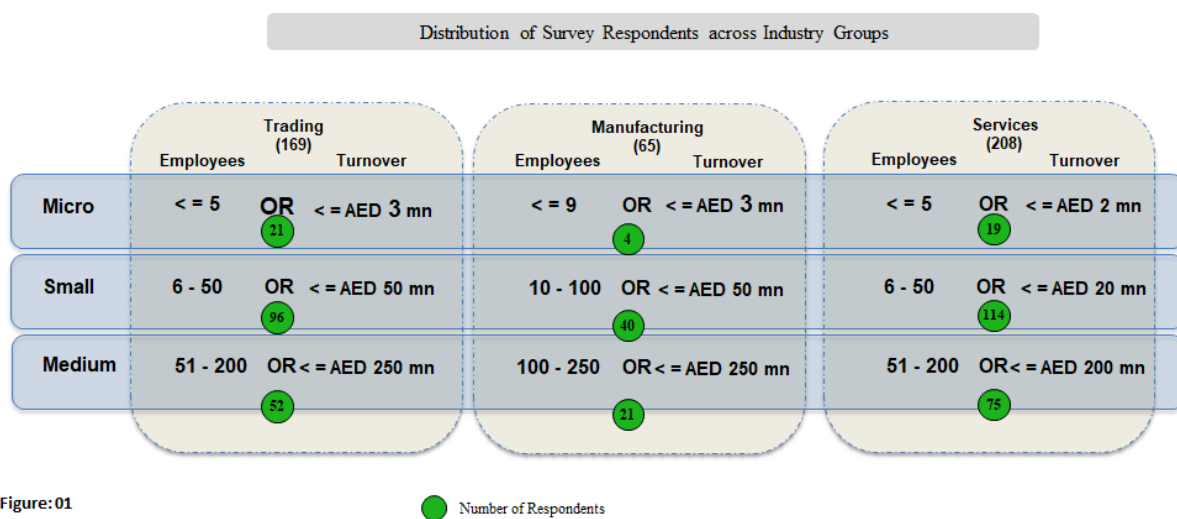


Figure:01



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.

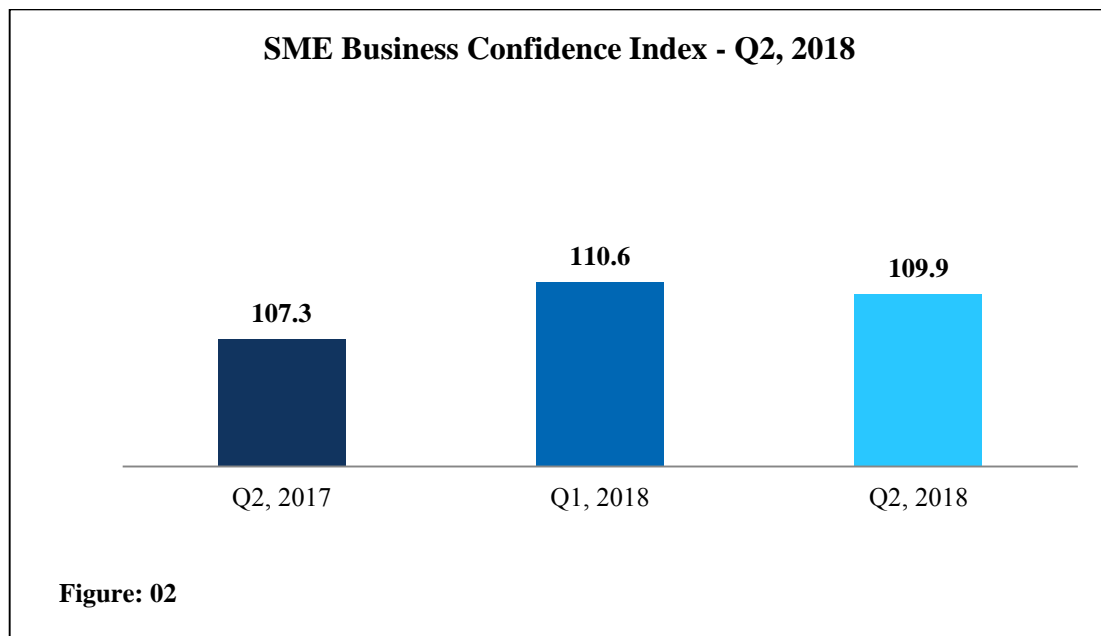
BCI scores are classified in the following three groups:

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

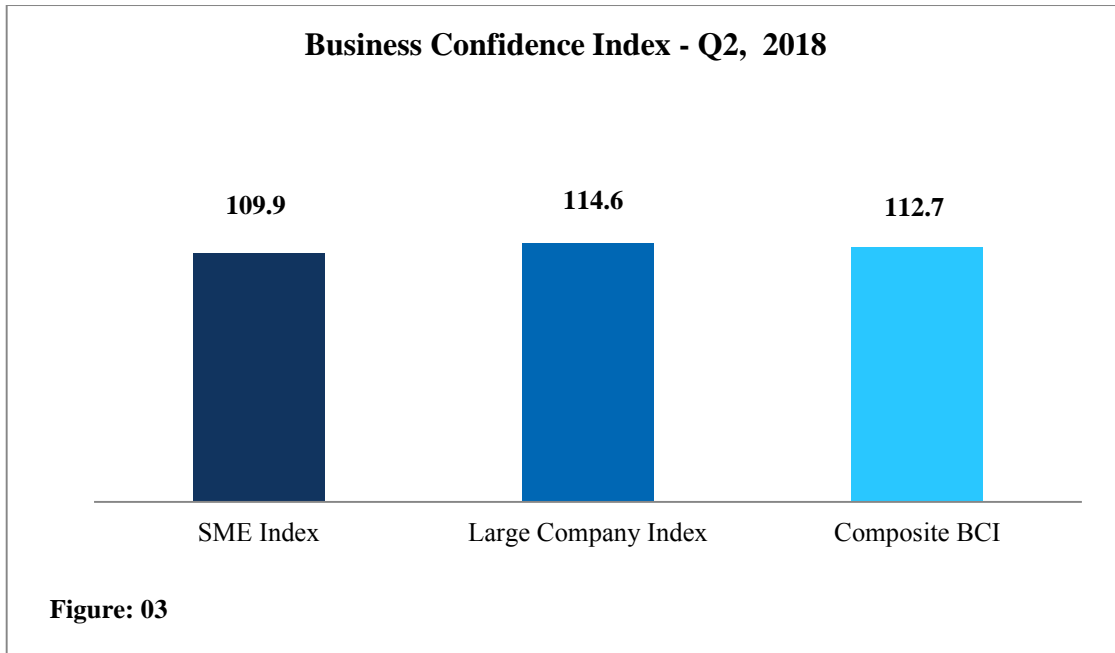


SME BUSINESS CONFIDENCE INDEX - Q3, 2018

Dubai's GDP is expected to grow at 4.2% in 2019, according to the International Monetary Fund (IMF), from a 3.4% pace this year, driven by government infrastructure spending ahead of Expo 2020. In line with this positive view, the UAE Central Bank added that the growth of the economy will be primarily driven by recovering oil prices, an expansionary fiscal stance and an upswing in investment ahead of Expo 2020. Meanwhile, the IMF has pencilled in that VAT is expected to raise revenues by 1.5% of GDP in the long term. Dubai's SMEs have a steady outlook for Q2, 2018 with the Composite Business Confidence Index (BCI) at 109.9 points (a score of 100 indicates stable/neutral sentiments).



The Composite BCI has strengthened on an annual basis from 107.3 points in Q2, 2017 to 109.9 points in Q2, 2018. A comparison of the Composite BCI on a q-o-q basis shows a decline on account of intense competition, slowing business conditions and lack of demand for products/services.



Large companies continue to be more optimistic than SMEs with respect to the business outlook, with Composite BCI scores of 114.6 points and 109.9 points, respectively. Large companies are more confident than SMEs about their outlook with respect to volumes, hiring, profitability and new purchase orders. SMEs have displayed a better forecast for revenues and selling prices.

SME BUSINESS OUTLOOK - Q3, 2018

SMEs account for a dominant share in Dubai's total business composition, 442 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.

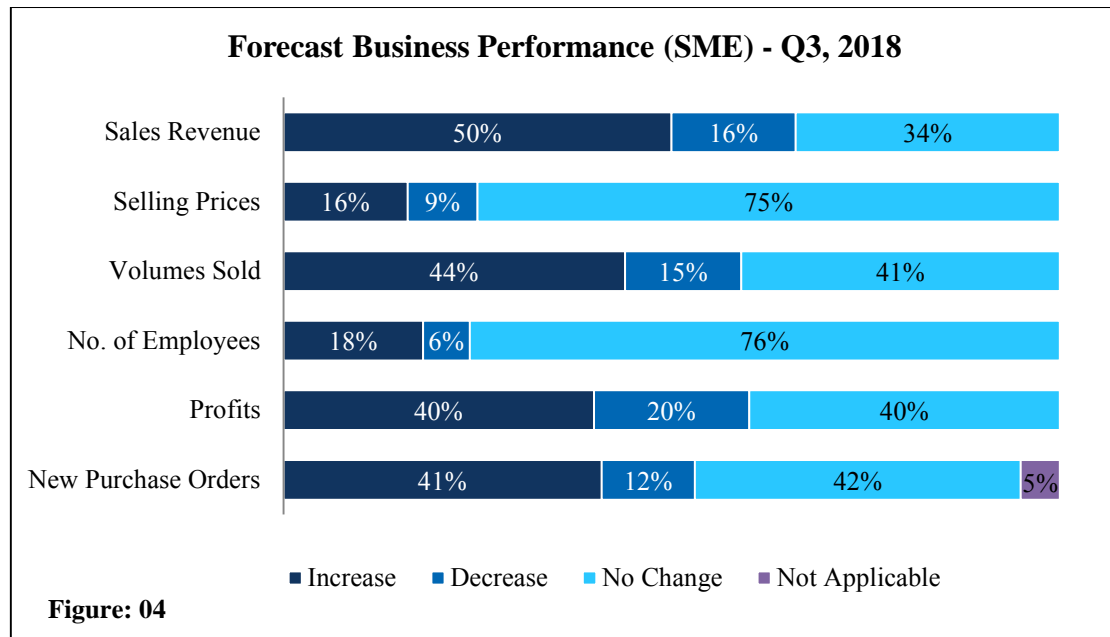
Table: 01

Forecast Business Performance (SMEs) - Q3, 2018

Parameter	Q3, 2017				Q2, 2018				Q3, 2018			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	43%	14%	43%	29%	54%	18%	28%	36%	50%	16%	34%	34%
Selling Prices	8%	11%	81%	-3%	13%	11%	76%	2%	16%	9%	75%	7%
Volumes Sold	45%	15%	40%	30%	51%	17%	32%	34%	44%	15%	41%	29%
No. of Employees	16%	7%	77%	9%	18%	6%	76%	12%	18%	6%	76%	12%
Profits	39%	18%	43%	21%	43%	20%	37%	23%	40%	20%	40%	20%
New Purchase Orders	43%	13%	44%	30%	47%	15%	36%	32%	41%	12%	42%	29%

*Note: Increase % + Decrease % + % No Change = 100%

In an event it does not add up to 100%, the balance percentage is the Not Applicable figure.



- The forecast for Q3, 2018 is weaker than that for Q2, 2018 for most parameters. Key reasons cited by respondents for this softer forecast include slow demand, fewer projects/orders and growing competition.
- SMEs are more optimistic than large companies with respect to revenues and selling prices, but are less confident about volumes, hiring, profits and new purchase orders.
- On a quarterly basis, the forecast for sales volumes has weakened, with the net balance decreasing from 34% for Q2, 2018 to 29% for Q3, 2018. However, 44% of the respondents anticipate an increase in their volumes in Q3, 2018 as they hope to get new projects/orders or expect market conditions to improve. The net balance for volumes for large firms stands at 33%, relatively low as compared to SMEs
- The manufacturing sector holds the firmest forecast for volumes for Q3, 2018, followed by the services sector, while trading SMEs are the least optimistic.
- Most (75%) SMEs anticipate that their selling prices will remain unchanged in Q3, 2018. 16% of the respondents expect to increase their prices owing to higher expenses, rise in the cost of raw materials or because of higher demand for their products.
- SMEs forecast for net profits have weakened q-o-q in line with the weakening sentiments with respect to sales volumes.
- The outlook for hiring has firmed q-o-q and is slightly stronger on a y-o-y basis as SMEs expect more business volumes.



- 51% of manufacturers and 34% of services firms forecast an increase in their capacity utilization rates for Q3, 2018.
- SMEs anticipate moderation in the business situation in Q3, 2018. The proportion of firms that have forecast an improvement for Q3, 2017 stands at 44%, lower than the proportion of 50% in Q2, 2018. A lower proportion of firms (10%) anticipate deterioration in Q3, 2018 versus 11% in Q2, 2018 while the number of businesses anticipating stability has firmed up from 39% in Q2, 2018 to 46% in Q3, 2018.

Manufacturing SMEs

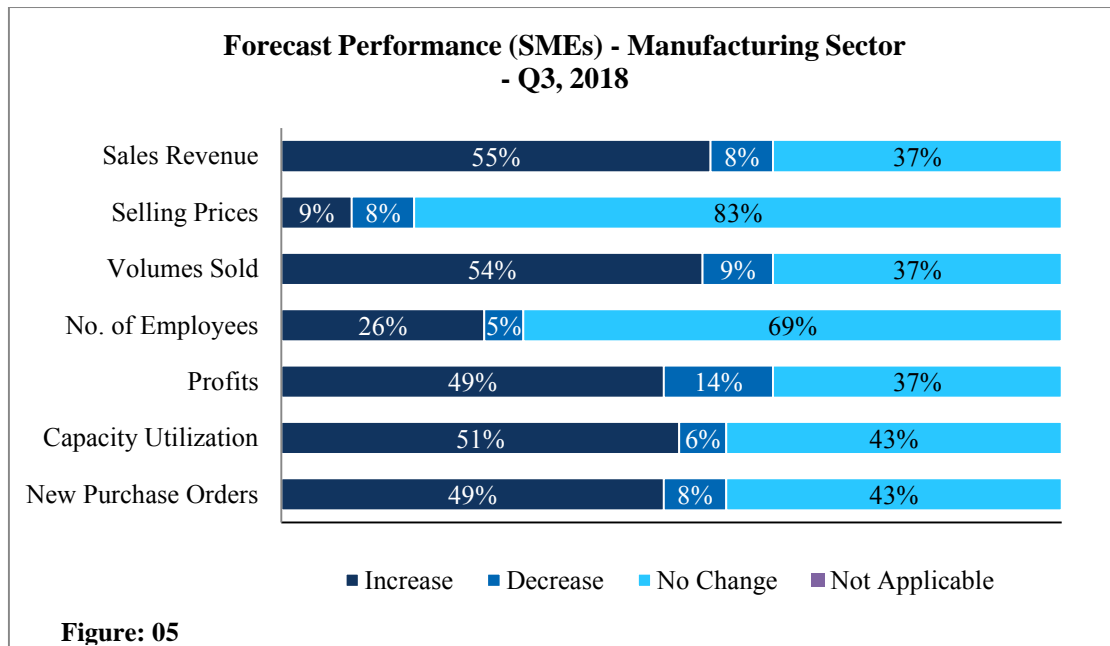
Table: 02

Forecast Business Performance (Manufacturing SMEs) - Q3, 2018

Parameter	Q3, 2017				Q2, 2018				Q3, 2018			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	64%	11%	25%	53%	44%	19%	37%	25%	55%	8%	37%	47%
Selling Prices	8%	11%	81%	-3%	13%	11%	76%	2%	9%	8%	83%	1%
Volumes Sold	56%	9%	35%	47%	51%	20%	29%	31%	54%	9%	37%	45%
No. of Employees	27%	5%	68%	22%	19%	7%	74%	12%	26%	5%	69%	21%
Profits	52%	13%	35%	39%	40%	23%	37%	17%	49%	14%	37%	35%
New Purchase Orders	56%	6%	38%	50%	46%	13%	41%	33%	49%	8%	43%	41%

*Note: Increase % + Decrease % + % No Change = 100%

In an event it does not add up to 100%, the balance percentage is the Not Applicable figure.



- Respondents in the manufacturing sector are confident about their volumes for Q3, 2018 than they were for the previous quarter backed by expectations of new projects, more customers and higher demand during the summer season. 54% of all manufacturers expect that their volumes will increase in Q3, 2018.
- Manufacturing sub-segments most optimistic about their volumes for Q3, 2018 are food and metal products manufacturers.

Trading SMEs

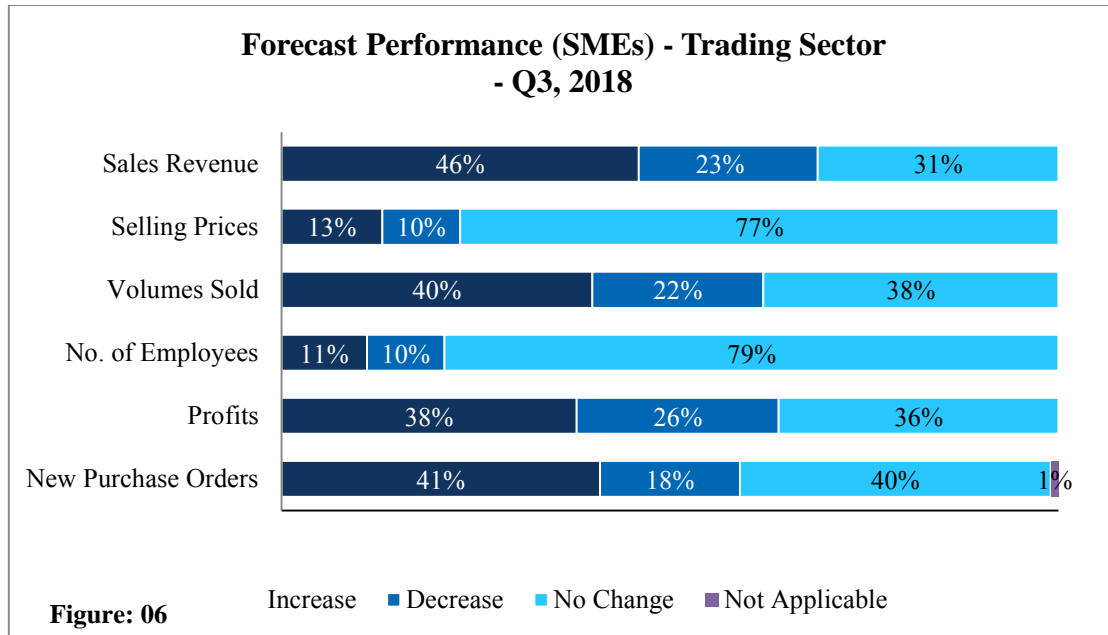
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Forecast Business Performance (Trading SMEs) - Q3, 2018

Parameter	Q3, 2017				Q2, 2018				Q3, 2018			
	No Change	Net Balance	Increase	No Change	Net Balance	Increase	No Change	Net Balance	Increase	No Change	Net Balance	Increase
Sales Revenue	41%	20%	39%	21%	54%	15%	31%	39%	46%	23%	31%	23%
Selling Prices	8%	11%	81%	-3%	13%	10%	77%	3%	13%	10%	77%	3%
Volumes Sold	37%	22%	41%	15%	52%	15%	33%	37%	40%	22%	38%	18%
No. of Employees	10%	8%	82%	2%	12%	5%	83%	7%	11%	10%	79%	1%
Profits	28%	25%	47%	3%	44%	19%	37%	25%	38%	26%	36%	12%
New Purchase Orders	34%	19%	47%	15%	50%	13%	37%	37%	41%	18%	40%	23%

*Note: Increase % + Decrease % + % No Change = 100%

In an event it does not add up to 100%, the balance percentage is the Not Applicable figure.



- Sentiments with reference to sales volumes in the trading sector have moderated on a q-o-q basis but have strengthened on a y-o-y basis. 40% of the traders anticipate a rise in volumes in Q3, 2018, versus 52% in Q2, 2018 and 37% for Q3, 2017. Among the three main sectors, trading firms hold the weakest outlook for most parameters in the survey.
- Key sectors optimistic of higher demand over the next quarter are the food & beverage and electronics traders.

Services SMEs

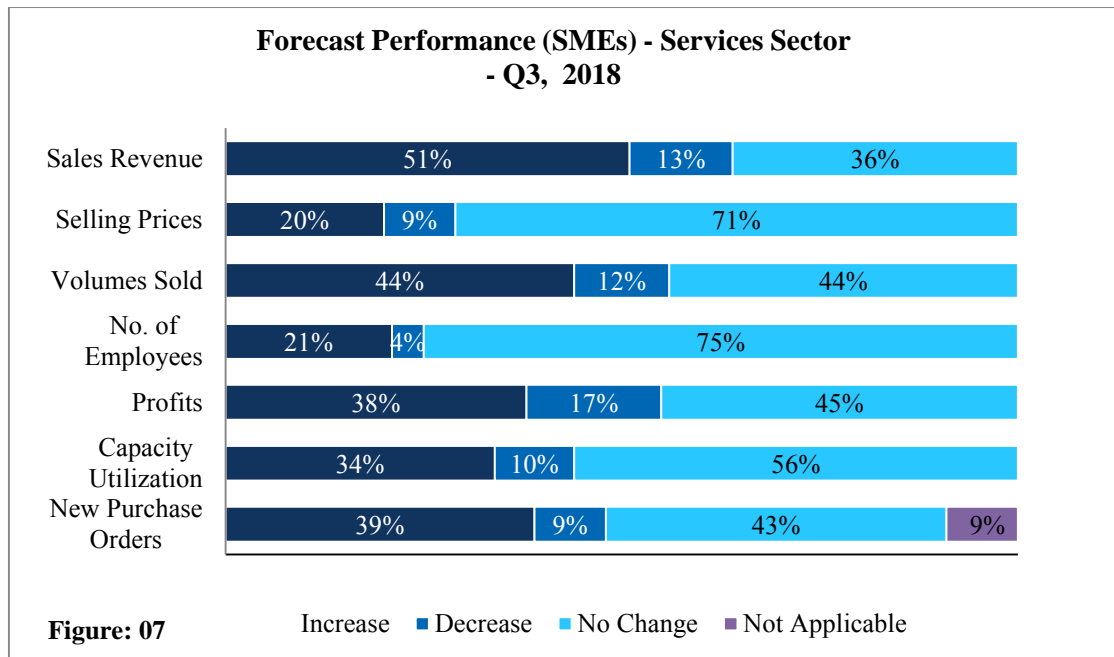
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Forecast Business Performance (Services SMEs) - Q3, 2018

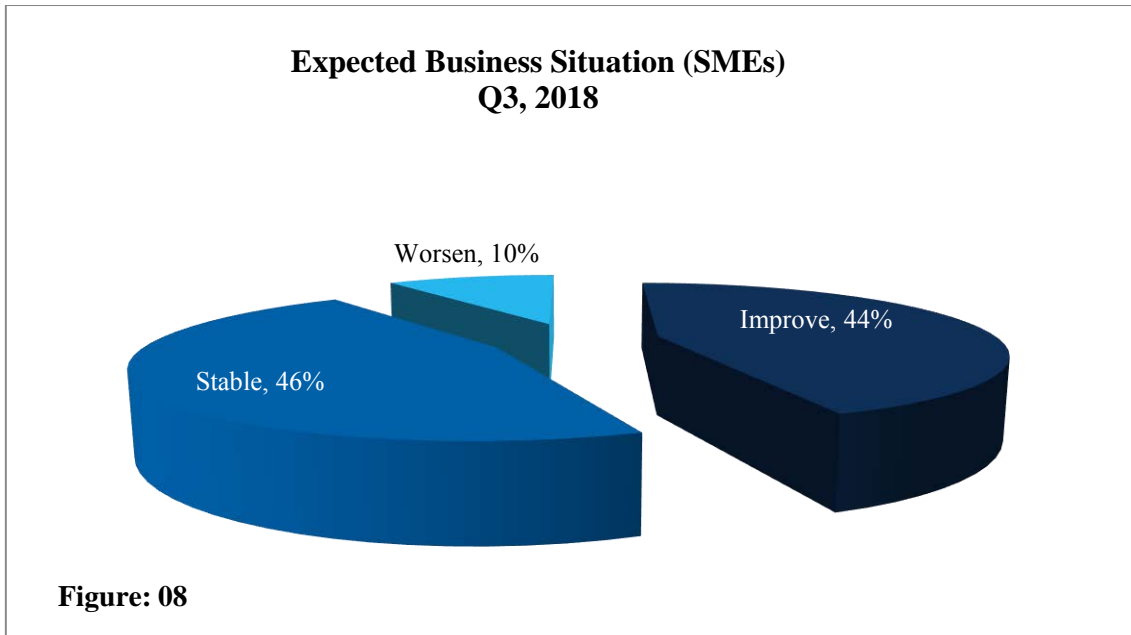
Parameter	Q3, 2017				Q2, 2018				Q3, 2018			
	No Change	Net Balance	Increase	No Change	Net Balance	Increase	No Change	Net Balance	Increase	No Change	Net Balance	Increase
Sales Revenue	39%	10%	51%	29%	57%	20%	23%	37%	51%	13%	36%	38%
Selling Prices	9%	10%	81%	-1%	12%	12%	76%	0%	20%	9%	71%	11%
Volumes Sold	48%	12%	40%	36%	50%	18%	32%	32%	44%	12%	44%	32%
No. of Employees	18%	6%	76%	12%	23%	6%	71%	17%	21%	4%	75%	17%
Profits	44%	14%	42%	30%	44%	21%	35%	23%	38%	17%	45%	21%
New Purchase Orders	47%	10%	43%	37%	45%	17%	33%	28%	39%	9%	43%	30%

*Note: Increase % + Decrease % + % No Change = 100%

In an event it does not add up to 100%, the balance percentage is the Not Applicable figure.



- According to the survey, the forecast for volumes is steady over the quarter but is weak on a y-o-y basis. The relatively firm forecast over the quarter is due to respondents' expectations of getting new orders/tenders/projects/contracts.
- Within the services sector, the hotels & restaurants are the most optimistic about their volumes in Q3, 2018 (net balance of 53%). Among construction, architecture & real estate firms, 48% expect an increase in volumes in Q3, 2018 as these respondents expect to get more projects or new orders in the third quarter, while 11% anticipate a decline, resulting in a net balance of 37%. In the transportation segment, 51% of the firms hope to see higher volumes in Q3, 2018, while an 8% anticipate a decrease.



44% of SMEs expect an improvement in the business situation in Q3, 2018; the corresponding proportion is higher for large companies at 52%.

DUBAI SME OUTPUT - Q2, 2018

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, 2018

Parameter	Q2, 2017				Q1, 2018				Q2, 2018			
	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance	Increase	Decrease	No Change	Net Balance
Sales Revenue	17%	41%	42%	-24%	16%	48%	36%	-32%	19%	44%	37%	-25%
Selling Prices	10%	24%	66%	-14%	20%	22%	58%	-2%	11%	26%	63%	-15%
Volumes Sold	20%	38%	42%	-18%	16%	46%	38%	-30%	19%	45%	36%	-26%
No. of Employees	15%	19%	66%	-4%	13%	19%	68%	-6%	12%	16%	72%	-4%
Profits	17%	45%	38%	-28%	12%	52%	36%	-40%	13%	53%	34%	-40%
New Purchase Orders	19%	33%	48%	-14%	17%	40%	41%	-23%	17%	35%	44%	-18%

*Note: Increase % + Decrease % + % No Change = 100%

In an event it does not add up to 100%, the balance percentage is the Not Applicable figure.

- For the sales volume parameter, SMEs' achieved a slight uptick in Q2, 2018 over the quarter but was weaker than that in Q2, 2017. The net balance for volumes sold in Q2, 2018 was negative 26% (19% of respondents reporting an increase in their volumes and 45% registering a decline). The decrease in volumes was a result of slow market conditions and lack of demand.
- Large companies reported better economic performance than SMEs with respect to most parameters in the survey: revenues, volumes, hiring, profits and new purchase orders.
- A majority (63%) of the SMEs reported that their selling prices were steady in Q2, 2018, while 26% had to lower their prices mainly due to competition and poor market conditions.



- 72% of the respondents kept their employee numbers unchanged in Q2, 2018, while 12% had to hire additional staff to address business requirements.
- Performance with respect to net profits in Q2, 2018 weakened on an annual basis but was steady over the quarter.
- 18% each of the manufacturing and services SMEs reported an increase in their capacity utilisation rates for Q2, 2018.
- 41% of the firms experienced an increase in the cost of labor due to a rise in the cost of living and hikes in wages & salaries, but it remained unchanged for 56% of the firms.
- 25% of the respondents were impacted by the rising cost of raw materials, while 36% reported no change in the parameter. Among large companies, 34% reported an increase in such costs.
- Rental costs increased for 20% of the SMEs and 24% of the large firms.

KEY SME CHALLENGES IN DUBAI

The survey also highlighted key challenges perceived by businesses at the end of Q2, 2018 that may impact near term business growth and development. 45% of the survey participants do not expect to face any hurdles in their business operations in Q2, 2018 versus 50% in the previous quarter.



Key SME Business Challenges - Q1, 2018

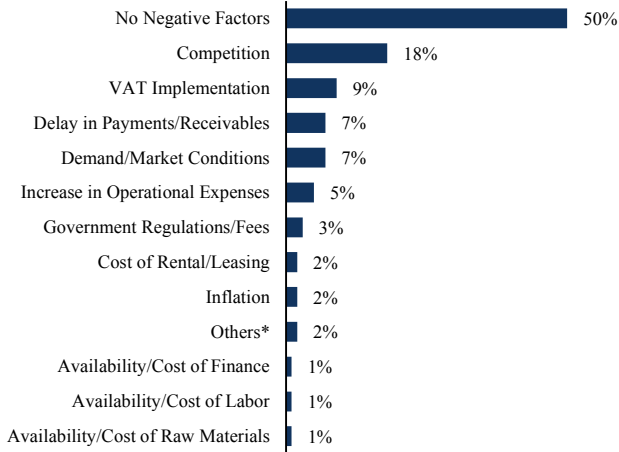


Figure: 09

Key SME Business Challenges - Q2, 2018

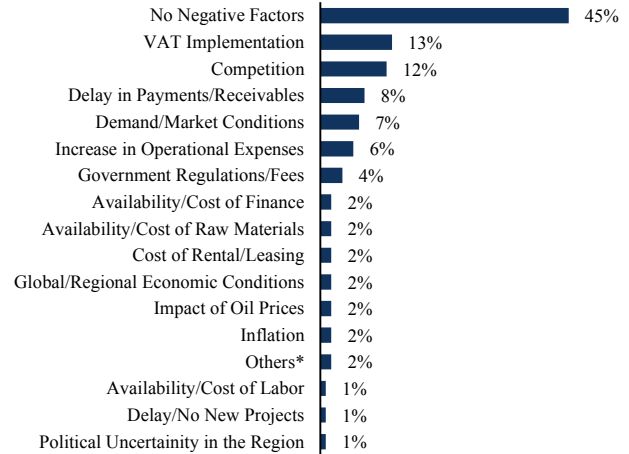


Figure: 10

*Others include purchasing power of customers, challenges surrounding pricing strategy and government policies of other countries

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

1. **VAT Implementation:** This is an obstacle to 13% of the respondents, with 53% of them anticipating worsening of the factor.
2. **Competition:** 12% of Dubai's SMEs face competition as an impediment to their business operations.
3. **Delay in Payments/Receivables:** 8% of the firms face this as a challenge.
4. **Demand/Market Conditions:** This is an impediment to 7% of the firms.
5. **Increase in Operational Expenses:** 6% of the survey participants have identified this as a factor challenging them.

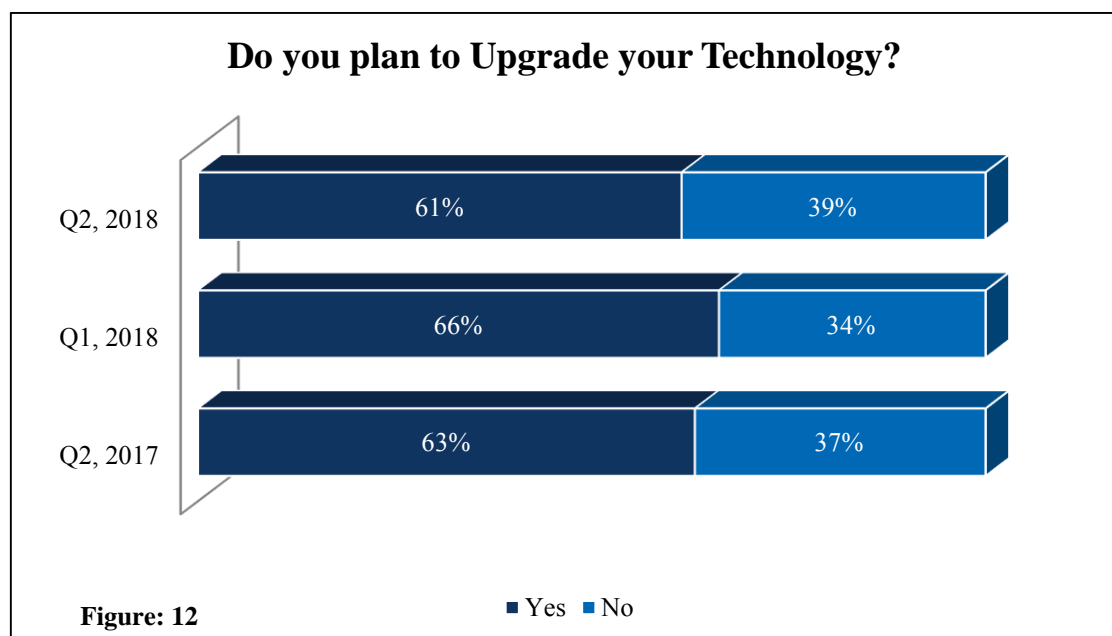
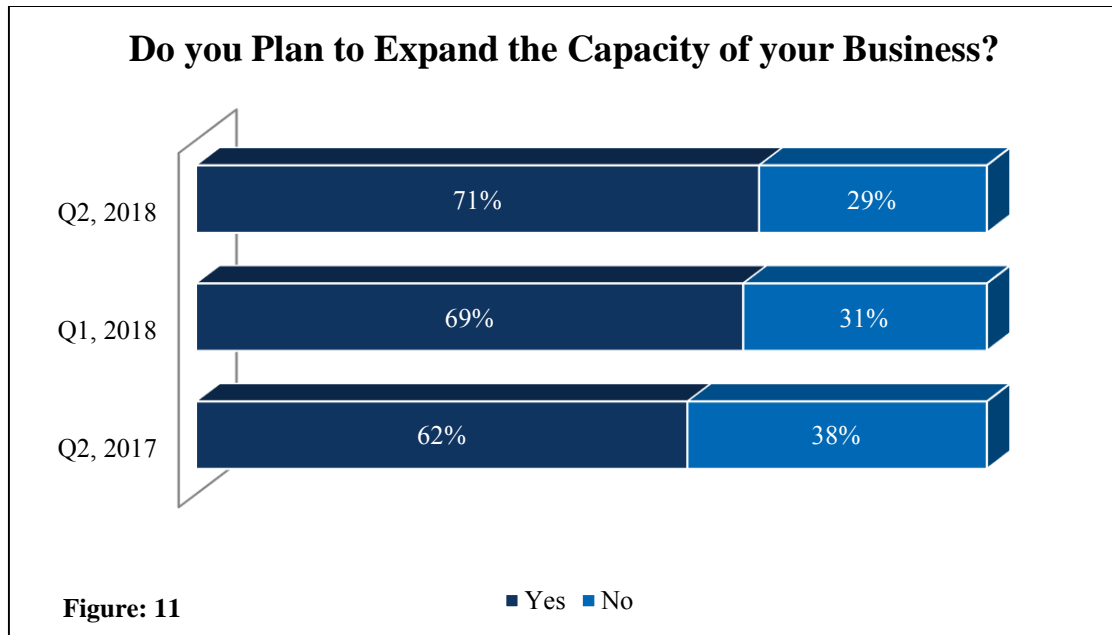
The remaining concerns impacted 4% or fewer of the participants.

The important challenges reported by large companies were competition, the impact of VAT on business and poor market/demand conditions.



INVESTMENT OUTLOOK

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



- Capacity expansion plans are bullish on a quarterly and annual basis. 71% intended to expand capacity in Q2, 2018 and 69% in Q1, 2018 versus 62% in Q2, 2017. However, plans



to upgrade technology are less bullish; the proportion of respondents intended to upgrade technology is recorded at 61% for Q2, 2018, 66% for Q1, 2018 and 63% for Q2, 2017.

- Key reasons cited by respondents for not considering expanding business capacity include lack of business demand, poor market conditions and no plans to expand business for now.
- 73% of trading companies versus 63% of manufacturing and 72% of services firms have capacity expansion plans. On the other hand, 64% of services companies are optimistic about technology plans as compared to 60% of manufacturing and 59% of trading SMEs.
- Large companies are more confident than SMEs about investments in technology upgrades.