



Equity Markets for SMEs and Growth Companies

Launch of Dubai SME 100

Dr. Nasser Saidi,
Chief Economist & Head of External Relations, DIFC Authority
14th March 2011



Agenda

Regional Developments

Economic Importance of SMEs & FOEs

Global Financial Crisis: Challenges for SMEs & Policy Initiatives

Creating Equity Markets for SMEs & Growth Companies

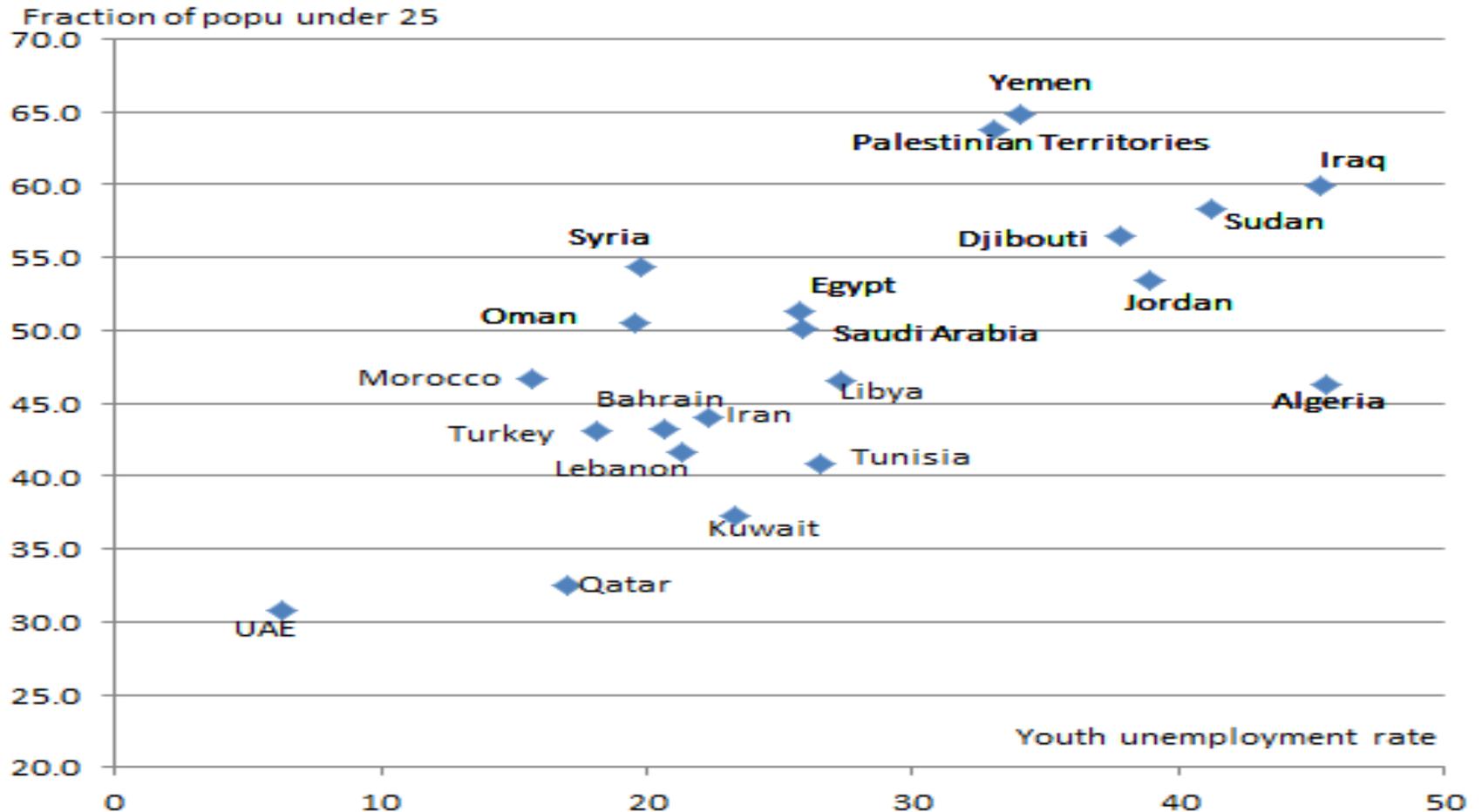
What Next?

Regional Developments

- Prior to recent events the **pace of economic activity was** set to continue to recover in the MENA & GCC region after the financial crisis. MENA Growth is expected at 4.7% in 2011 compared to 4.6% in 2010.
- However, other EMEs have recovered faster: Developing Asia is forecast to grow at 8.4% this year; Sub-Saharan Africa at 5.8%.
- Recent developments in the region highlights the need to ensure that economic growth is both inclusive and has a trickle-down impact.
- There is a need to **reduce chronically high unemployment and wide income disparities** with the countries and across the region.
- Job creation is a priority and this needs to come from the private sector for sustainable growth, innovation etc.
- Hence, there is a critical role for Family Owned Enterprises (FOEs) and Small & Medium Enterprises (SMEs) to engage in job creation and investment.
- Need to focus on: **structural reforms and developmental policies** (incl. infrastructure) that encourage private sector participation, tackle job creation and lift the economy to a higher growth trajectory over the longer term.

Youth Population vs. Youth Unemployment

Youth Population vs. Youth Unemployment



Economic Importance of SMEs/ FOEs

Establishment and encouragement of SMEs and FOEs will address the demographic and socio-economic challenges that are being highlighted in the recent turmoil.

- In GCC markets, SMEs and FOEs are the backbone of the corporate sector & account for the largest share of employment.
- SMEs profile in Dubai (*Source: Dubai Statistics Centre*)
 - a. SMEs count for **95%** of the total enterprise population in Dubai
 - b. SMEs employ around **42%** of Dubai's workforce
 - c. SMEs contribute to **40%** of Dubai's value added
- Within the GCC, **over 90% of all commercial activity** is estimated to be **controlled by family firms**. (*Source for GCC FOEs: Ithmar Capital*)
- These GCC FOE firms number over **5000**, hold **combined assets of more than \$500bn** and **employ 70% of the workforce**.
- Despite their importance, SMEs seem significantly **more financially constrained** than large firms in developing countries, especially in the GCC.

Realities of Banks' Lending Operations to SME/FOEs

Enterprise-level surveys conducted by the World Bank suggest that SMEs are particularly financially constrained in MENA countries:

- **Only 20% of MENA SMEs have a loan/ line of credit** - lower than any other region and
- **Only 10% of their investment expenditures are financed by a bank loan**, a share that is higher only to the one in Sub-Saharan Africa.

A WB - Union of Arab Banks survey (Jun 2010) initiative found that:

- MENA banks regard the SME segment as potentially profitable, and most banks are already engaged in SME lending to some degree.
- **Drivers that encourage SME lending:** potential profitability of SME market, saturation of the large corporate market, need to enhance returns & the desire to diversify risks.
- However, **lending volumes are not very impressive**. Share of SME lending in total lending is only 8% in MENA; 2% in the GCC; 14% in the non-GCC countries.
- **Drawbacks** for banks: the lack of SME transparency & weak financial infrastructure (weak credit information, weak creditor rights & collateral infrastructure), weak corporate governance

Pro-SME Environment Exists, But More Is Required

GCC SME segment is likely to contribute an additional \$100 bn to the region's GDP and create up to two million jobs in the coming years. (Source: A.T. Kearney, Apr 2010).

The UAE has launched a number of policy initiatives to support the private sector/ SMEs:

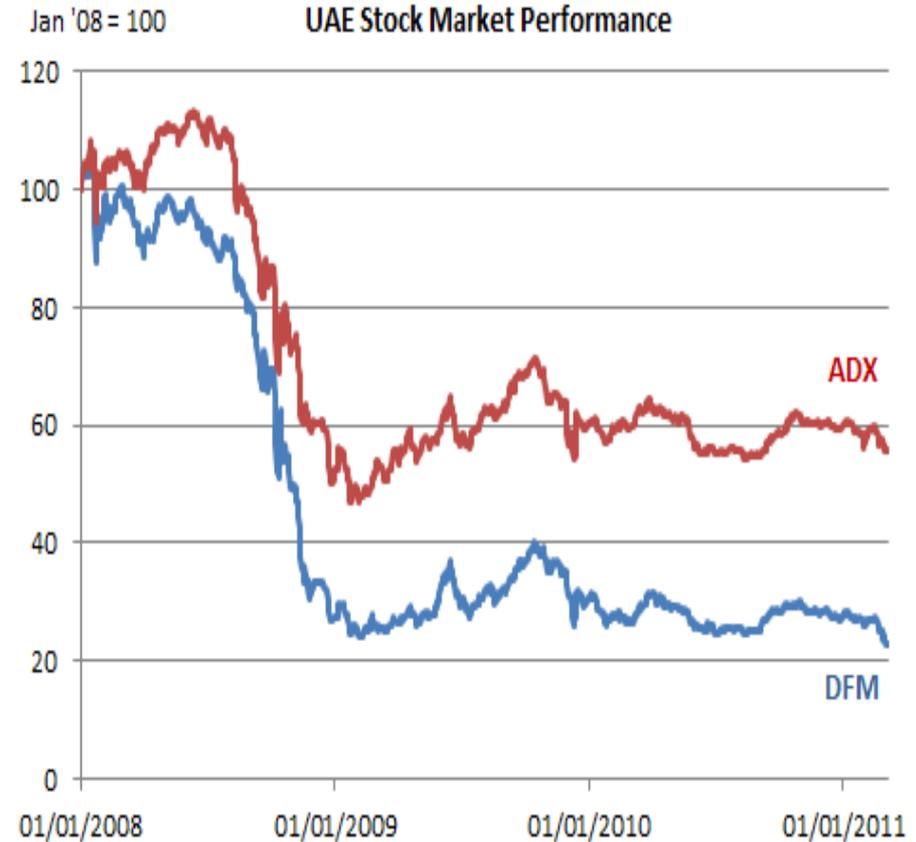
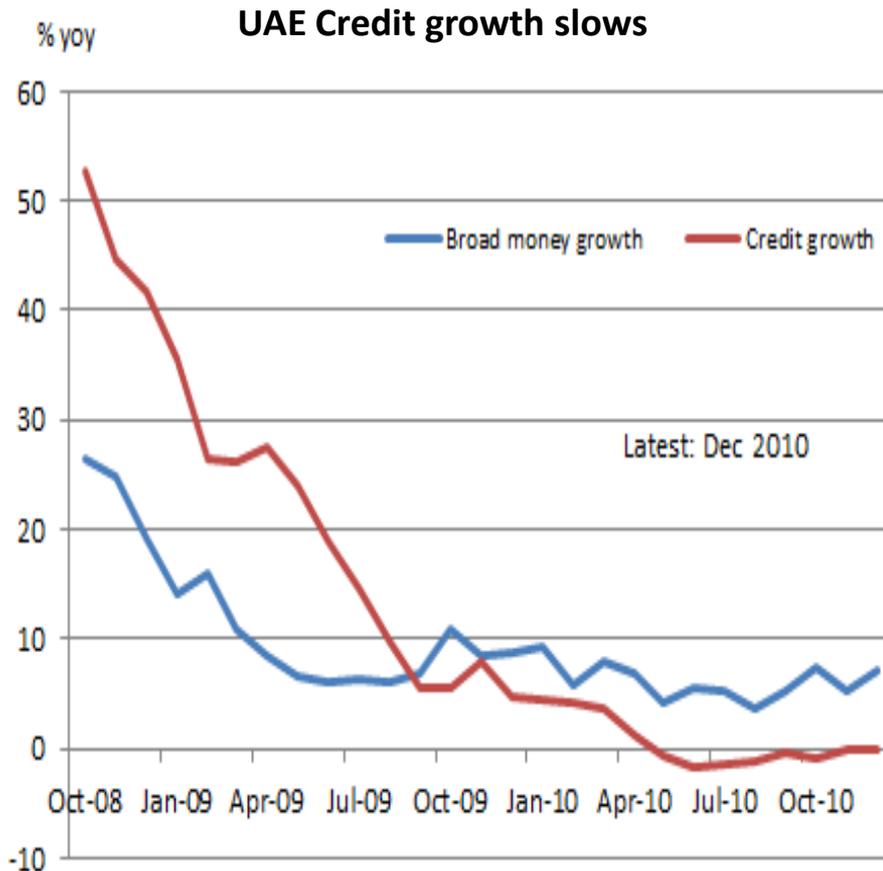
- Minimum capital requirement of AED 150k for the establishment of a limited liability company was removed in Aug 2009 - significantly **lowers the cost of doing business**.
- Ministry of Economy has signed a MoU with Tanmia to **provide sufficient training** to the national cadres to lead SMEs.
- Programs like the **Khalifa Fund for Enterprise Development & Mohammed Bin Rashed Establishment for SME Development (MBRE)**, while providing a helping hand to SMEs, does not provide sufficient capital to expand nor help eradicate financing challenges.
- During Dec '09, MBRE announced the first official definition for SMEs in Dubai.
- Private sector initiatives are growing: more private equity initiatives like Abraaj's **Riyada Enterprise Development & SME investment funds are required**
- ***However these initiatives all require an Exit for investors/promoters***

Need for an Exclusive Market to Cater to SMEs/ FOEs

- MENA capital markets are **dominated by bank assets and equities**: Debt securities make up just 11.1% of capital markets (GFSR Oct '10)
- Region's capital markets hardly cater to the needs of companies displaying a promising growth potential.
- **Financial crisis has exacerbated the challenges** - banks deleveraging & the region's equity markets have not recovered completely.
- Most regional stock markets have adopted a model best tailored for large, well established companies, with a long track record, operating in mature sectors (*i.e. banks, real estate, utilities, petrochemical sectors*).
- Newer, dynamic businesses and family enterprises may find listing & other regulatory requirements by larger established exchanges not only too burdensome but also as loss of control over their companies.
- They need capital to develop their innovations which obviously cannot produce a track record.
- Furthermore owners of such companies are reluctant to let a substantial part of their equity float on a market, and the same applies to FOEs.

Challenges in Access to Credit & Capital

In a nutshell: **THE MOST PROMISING ENTERPRISES DO NOT HAVE ADEQUATE ACCESS TO CREDIT & CAPITAL**



National/ Regional Equity Mkts for SMEs & Growth Co's

Stock exchange designed to meet the needs and the ambitions of this segment might become a key driver in the development of a liquid capital market

The market would target companies that are not ready or suitable for listing in a main equity market



It would be conceived as a “**stepping stone**” to the main market

These companies could benefit from **MORE FLEXIBLE:**

- *Forms of public quotation;*
- *Listing requirements;*
- *On-going reporting obligations;*
- *Tailor-made regulation.*

Comparison Across Other Second Tier Markets

AIM, PLUS, AMEX, ALTERNEXT, GEM and Novo Mercado are examples of successful second tier markets in the world

	MARKET CAP (bn. local ccy)			No. OF COMPANIES			AVG MKT CAP (mn. local ccy)		
	Main Market	2nd tier Market	Ratio of 2 nd tier to main mkt cap	Main Market	2nd tier Market	Ratio of 2 nd tier to main market	Main Market	2nd tier Market	Ratio of 2 nd tier to main market cap
LONDON	£ 1,952.20	£ 79.42	4.06%	1,068	1,194	111.80%	£ 1,827.90	£ 66.52	3.64%
EURONEXT	€ 2,070.52	€ 5.66	0.27%	1149	156	13.58%	€ 1,802.02	€ 36.29	2.01%
HONG KONG	HK\$ 20,936.80	HK\$ 134.67	0.64%	1365	169	12.38%	HK\$ 15,338.32	HK\$ 796.87	5.20%
BRAZIL	R\$ 2569.50	R\$ 269.7	10.50%	471	51	10.83%	R\$ 5,455.41	R\$ 5,288.23	9.69%
ITALY	€ 424.48	€ 0.36	0.14%	322	10	3.11%	€ 1,318.26	€ 36.00	2.73%

Arab Market Capitalisation, end-Feb 2011

Using the median values from the five existing 2nd tier markets (London, Euronext, Brazil, Hong Kong & Italy), we have roughly estimated the value of market cap & potential numbers of members in a fictional regional Arab SME market.

	Market Cap (USD mn)		No of companies		Average mkt cap (USD mn)	
	Main Market	Est. value of 2nd Tier Market	Main Market	Est. nos in 2nd Tier Market	Main Market	Est. value in 2nd Tier Market
Amman SE	28909.2	185.0	276	34	104.7	5.4
Bahrain SE	20458.6	130.9	50	6	409.2	21.2
Beirut SE	11308.9	72.4	24	3	471.2	24.4
Egypt SE	66907.1	428.2	216	27	309.8	16.0
Qatar SE	117621.2	752.8	43	5	2735.4	141.4
Kuwait SE	115592.5	739.8	217	27	532.7	27.5
Muscat SM	18960.5	121.3	123	15	154.2	8.0
Saudi SE	339004.5	2169.6	148	18	2290.6	118.4
UAE (DFM+ADX+Nasdaq Dubai)	130758.4	836.9	158	20	827.6	42.8
Regional Second tier mkt		5436.9		155		35.0

What Next?

- Access to Finance and Capital are critical at this stage of recovery => imperative for the growth of SMEs and FOEs
- Government policy initiatives are critical; however, there should also be clear exit policies e.g. sources of long-term finance & capital
- Private sector needs to be nurtured, with focus on SMEs & growth companies
- We advocate the set-up of a National & Regional Second Tier market for SMEs
- Provided an existing model is adopted, a near replication of successful markets, regulatory & trading infrastructure for 2nd tier markets could be established within 1 year

Thank You!