

## **JETRO's FY2015 Survey on Business Conditions of Japanese-Affiliated Firms in the Middle East**

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Middle East and Africa Division

Overseas Research Department

Japan External Trade Organization (JETRO)

# Key Points of Survey Results



## Japanese-affiliated companies in the Middle East

**Despite public security risks and low oil prices, the majority of Japanese-affiliated companies post a surplus and have an incentive to expand their business.**

1

**In 2015, the majority of companies posted a surplus.** In terms of operating profit forecasts for 2015, 56.2% of companies replied that they would post a surplus. The percentage of those which replied that they would suffer a loss remained at 15.7%. By country, the percentage of companies in the black in the UAE was largest, at 64.3%. Meanwhile, about 30% of companies in Saudi Arabia replied that they would suffer a loss, suggesting that they operated in a harsh business environment.

2

**The business sentiment for 2016 indicated that a little over 40% of companies expected their business to improve.** Asked about prospects for 2016, 44.1% of companies expected their operating profits to improve, indicating that more companies had brighter prospects of profitability than in the previous year. The largest reason for improvement was “sales increase in local markets” (74.0%), followed by “sales increase due to increased exports” (51.9%).

3

**Seventy-percent of companies were having an incentive to expand their future business.** As to business development policy for the next one to two years, about 70% of companies in each country and territory replied that they planned to expand their business. The two greatest reasons for expansion were “high growth potential” (68.3%) and “increasing sales” (67.5%), and many of them (75.6%) intended to expand their sales functions.

4

**In order to localize management, companies aimed to hire more employees locally rather than bring them from Japan.** Cited as major initiatives to localize management were “strengthen systems to train/cultivate local human resources” (54.0%), “encourage mid-level hiring activities to obtain competent local staff” (44.4%), and “assign local staff to a general manager/manager position” (40.6%), but “insufficient performance/awareness among local staff” (43.2%) and “difficulty in recruiting local candidates for executive positions” (39.3%) were cited as issues to be addressed. An overwhelming percentage of companies (about 70%) replied that in the future the number of Japanese employees would remain at almost the same level, but the percentage of companies that expected to hire more local employees in the years to come was high, at about 60%.

5

**UAE’s investment environment was beneficial in terms of taxation and free zoning, but the challenge was growing costs.** Many companies considered UAE’s investment environment as attractive because of “merits of tax systems (no corporate tax and no income tax)” (78.2%), “free zones (no regulation for foreign investment and one-stop service)” (70.6%), and “political/social stability” (63.0%), but many of them cited soaring costs such as real estate rent, personnel expenses, and handling fees as issues to be addressed.

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# Survey Overview

## Objective

- To grasp the actual condition of Japanese-affiliated companies' business activities in the Middle East (United Arab Emirates (UAE), Saudi Arabia, and Turkey) and provide the results to the public

## Companies Surveyed

- A questionnaire survey was locally conducted for Japanese-affiliated companies operating in the Middle East.
- Valid replies were received from 191 companies (120 from UAE, 36 from Saudi Arabia, and 35 from Turkey)

## Period

- September 28 to October 22, 2015

## Response Rate

- The response rate was 46.6% (questionnaires were distributed to 410 companies, and valid replies were received from 191 of them).
- By country, the response rate was 49.2% for UAE (120 of 244 companies), 50.7% for Saudi Arabia (36 of 71), and 36.8% for Turkey (35 of 95).

## Remarks

- This was the third survey for UAE and the second for Saudi Arabia. For Turkey, it was the first survey that covered all industries; the previous ones targeted only the manufacturing industry.
- JETRO informed companies to be surveyed of the URL for the questionnaire and asked them to complete and return it or sent them questionnaires written in Japanese by email.

## Notes

- All response rates are shown in percentages (%). The response rate was rounded to the second decimal place. As a result, some total figures do not amount to 100%.
- "N" stands for the number of valid responses.

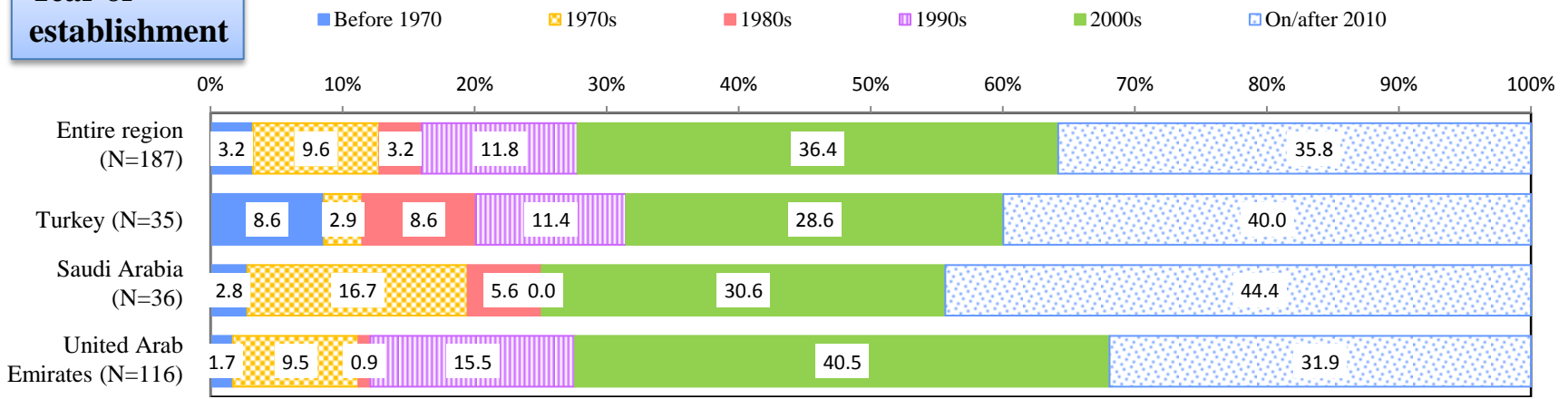
## Map of the Middle East



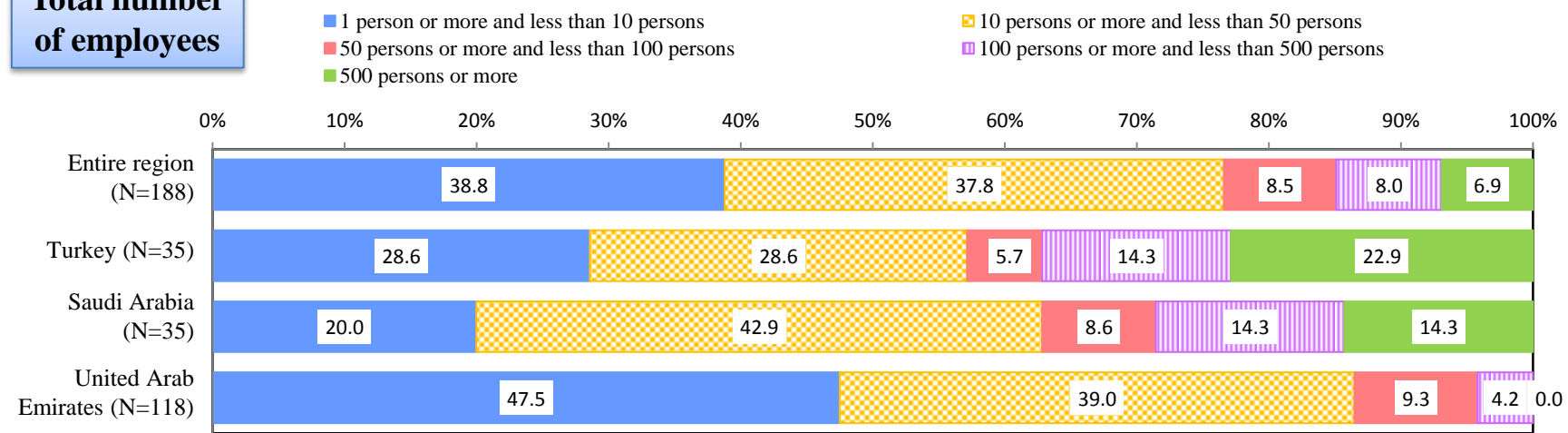


# Figure 1. Company Profile

## Year of establishment

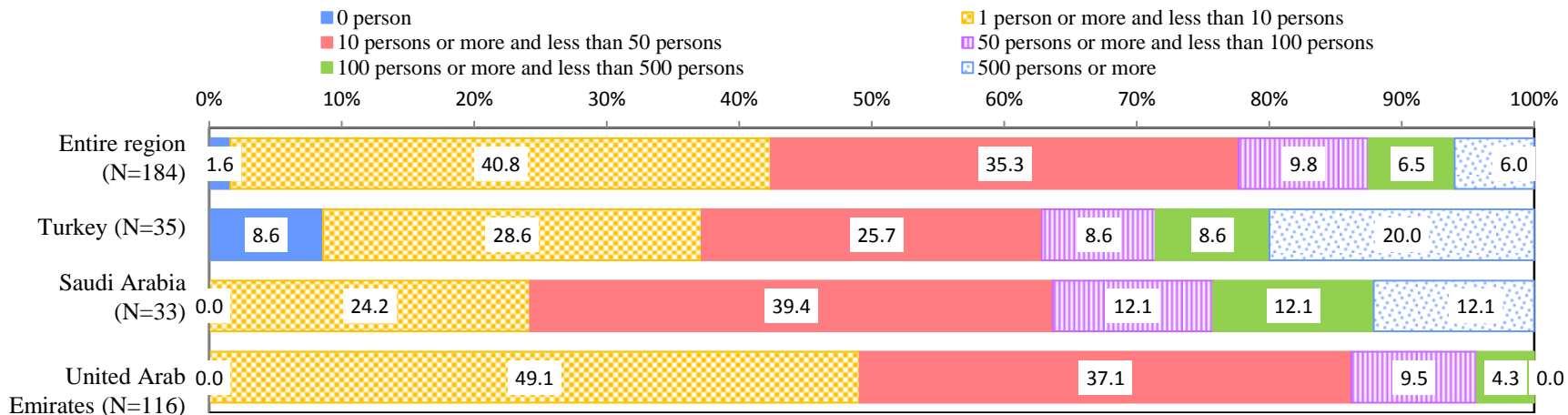


## Total number of employees

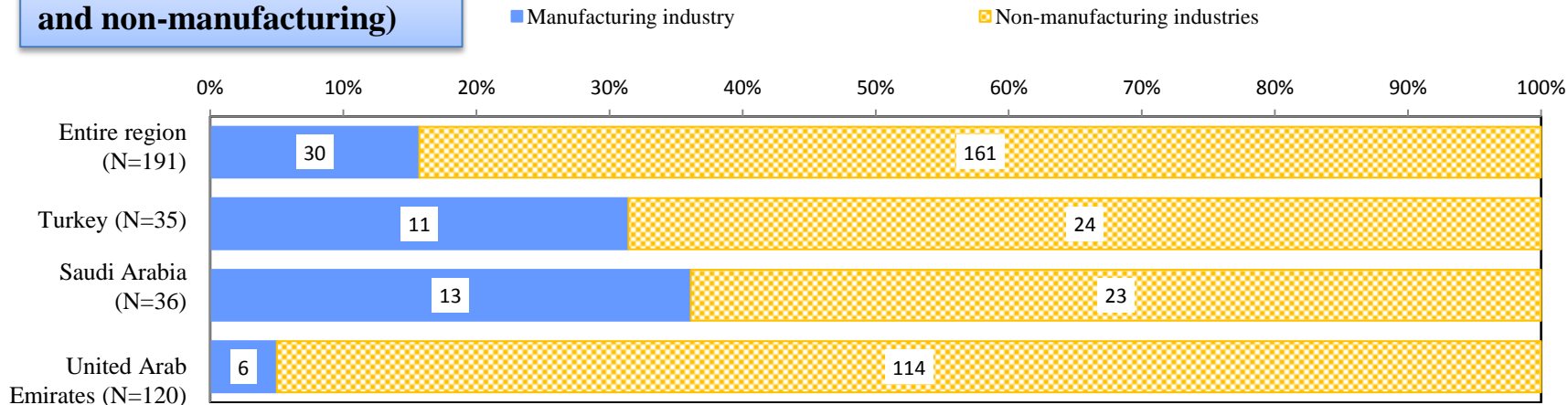


# Figure 2. Company Profile

## Number of regular employees



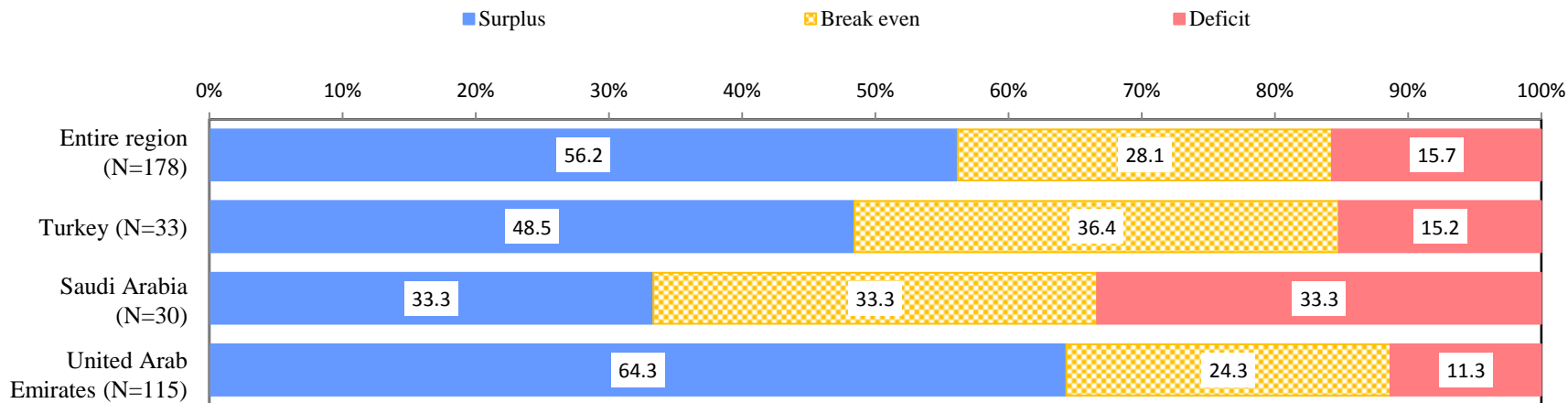
## Industry (manufacturing and non-manufacturing)



Note: The figures in the graph refer to the numbers of the companies.

# Figure 3. Operating Profit Estimate (1)

## Operating Profit Estimate for 2015

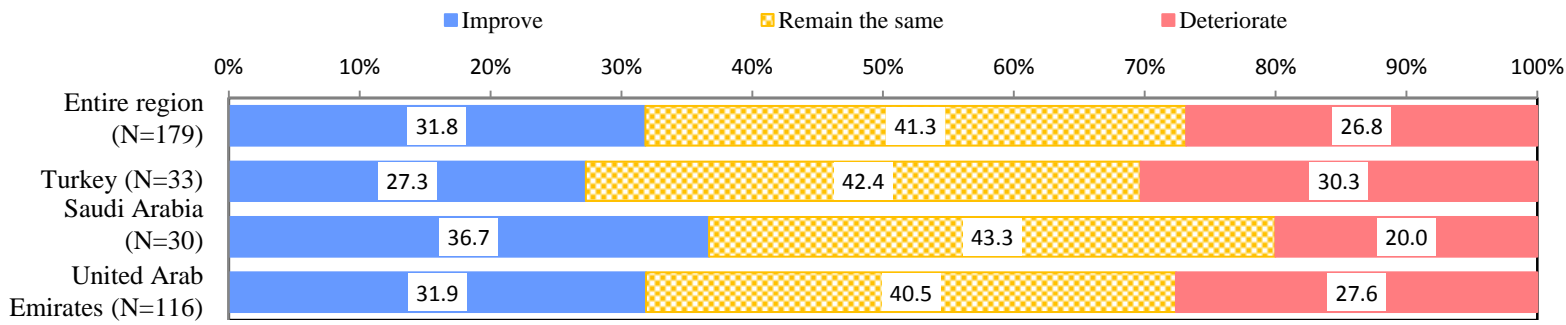


- A look at operating profit forecasts for the entire Middle East in 2015 indicated that the majority of companies replied that they had posted a surplus and that the percentage of those which replied that they had suffered a loss was only 15.7%.
- By country, the percentage of companies that answered, “Surplus,” in UAE was largest, at over 60%, followed by Turkey, where it was also high, at a little less than 50%, but that for Saudi Arabia was low, at 30%. Meanwhile, the percentage of companies that answered, “Deficit” was largest in Saudi Arabia, at 30%, suggesting that the Saudi business environment was relatively harsh.
- A comparison with the previous year showed that the percentage of companies operating at a profit declined from 65.4% to 64.3% in UAE and from 41.9% to 33.3% in Saudi Arabia. On the other hand, the percentage of loss-making companies in UAE and Saudi Arabia also dropped, from 12.8% to 11.3% in UAE and from 35.5% to 33.3% in Saudi Arabia. The percentage of companies that answered, “Break even” increased compared to the previous year.

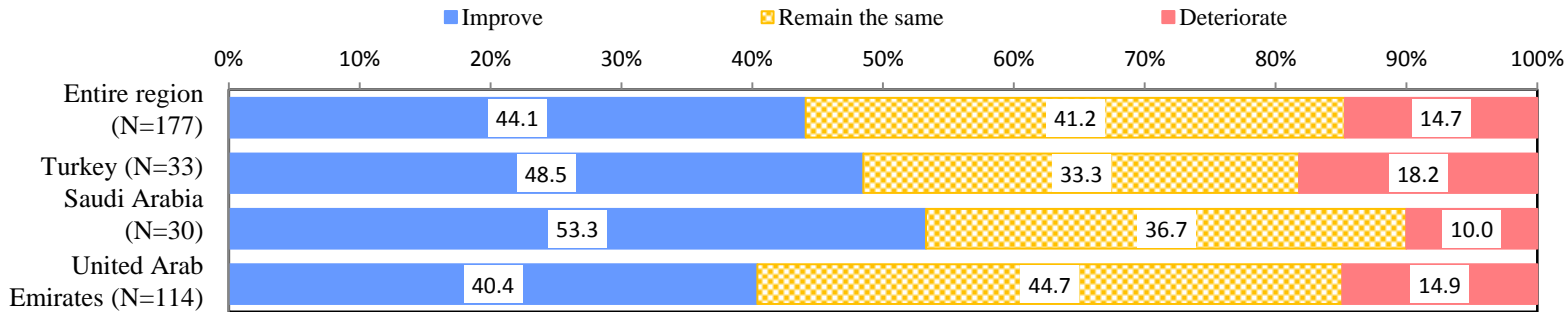


# Figure 4. Operating Profit Estimate (2)

## 2015 operating profit forecast (compared to 2014)



## 2016 operating profit forecast (compared to 2015)



- A look at operating profit forecast for the entire Middle East showed that in 2016 the percentage of companies replying that the forecast would improve compared to the previous year increased from 31.8% to 44.1%, while the percentage of companies replying that it would deteriorate decreased from 26.8% to 14.7%. Overall, for 2016, an increasing percentage of companies had a brighter operating profit forecast than in the previous year.
- By country, the percentage of companies replying that in 2016 the forecast would improve compared to the previous year was largest in Saudi Arabia, at 53.3%, followed by Turkey, where it was also high, at 48.5%. The percentage for UAE was relatively low, at 40.4%. On the other hand, the percentage of companies in Turkey replying that it would deteriorate compared to the previous year was largest, 18.2%, followed by UAE, at 14.9%, and that for Saudi Arabia was lowest, at 10.0%.
- A comparison with the previous year indicated that the percentage of companies that expected operating profit to improve increased in all countries, from 36.7% to 53.3% in Saudi Arabia, from 27.3% to 48.5% in Turkey, and from 31.9% to 40.4% in UAE. On the other hand, the percentage of those which expected it to deteriorate nearly halved, from 20.0% to 10.0% in Saudi Arabia, from 27.6% to 14.9% in UAE, and from 30.3% to 18.2% in Turkey. In all countries, the operating profit forecast change for the better.

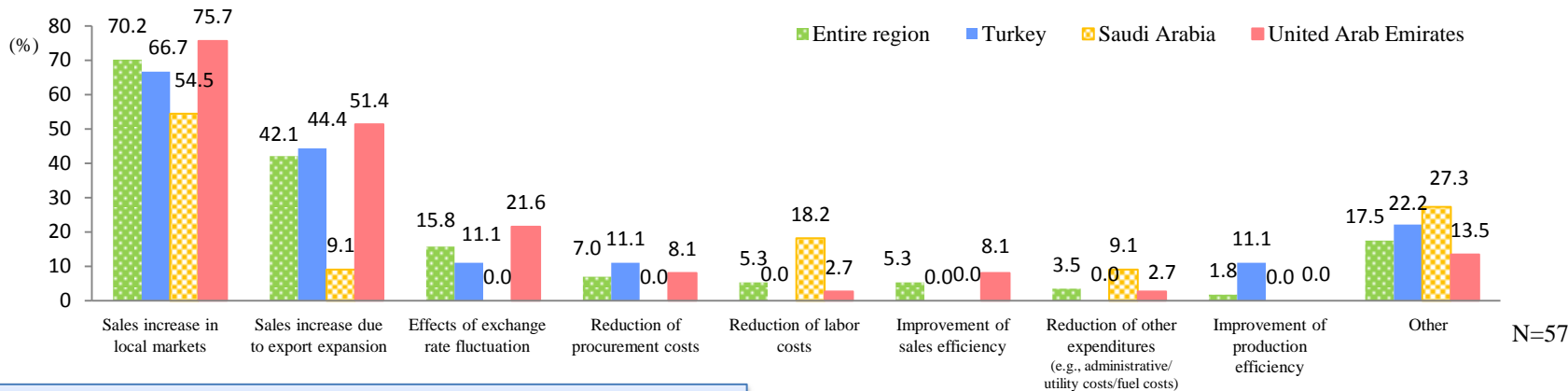




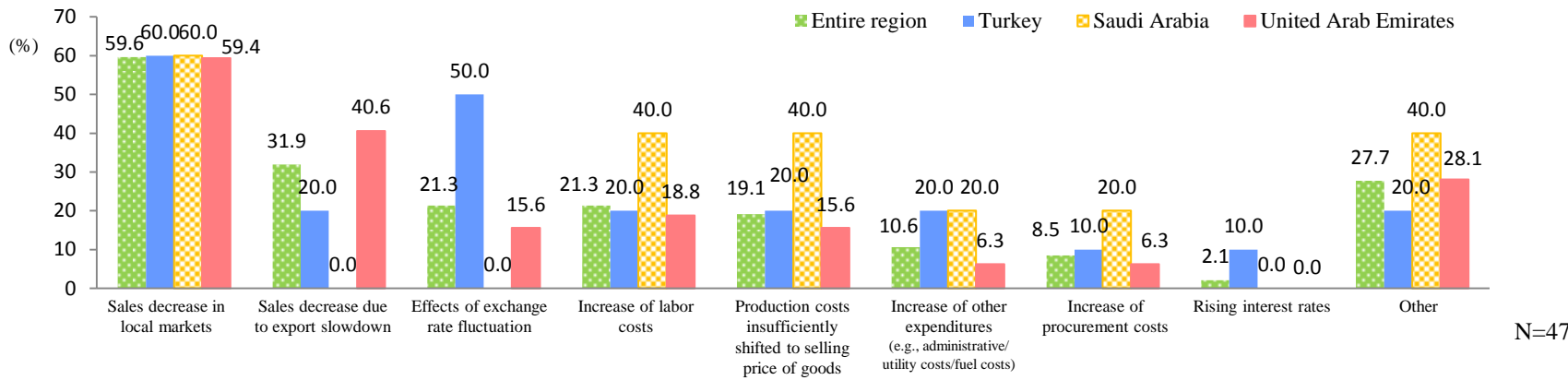
# Figure 5. Operating Profit Estimate (3)

Multiple answers allowed

## Reasons 2015 operating profit forecasts



## Reasons 2015 operating profit forecasts deteriorate



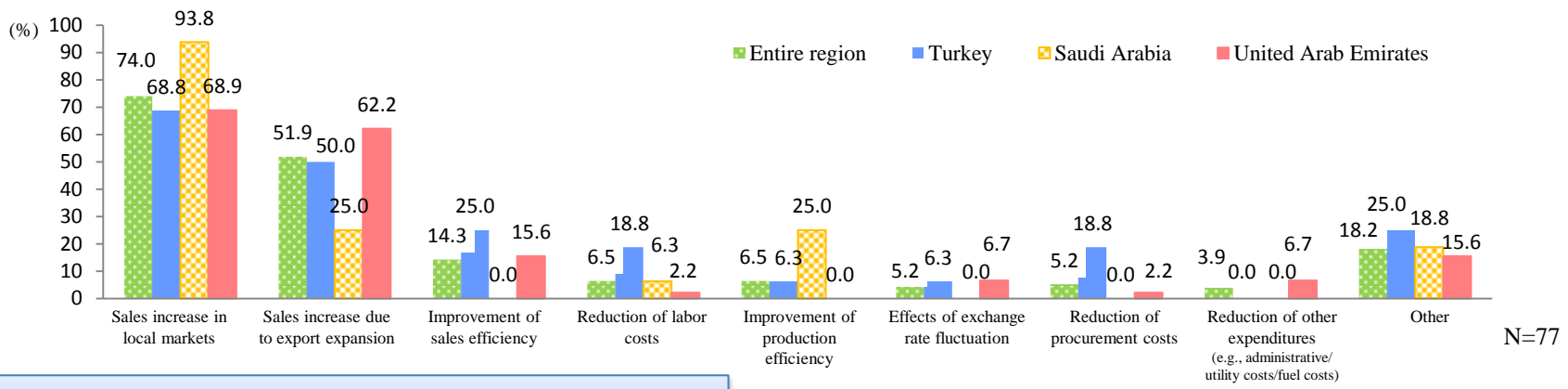
- A look at operating profit forecast for 2015 showed that in all countries the percentage of companies that cited “sales increase in local markets” as the main reason the forecast improved was largest, at 50-70%, followed by companies that mentioned “sales increase due to export expansion” (over 40%) except for Saudi Arabia. In Saudi Arabia, on the other hand, a large percentage of companies cited “reduction of labor costs” as the reason for improvement (a little less than 20%) with the percentage of “sales increase due to export expansion” being low, at less than 10%.
- In all countries, the percentage of companies that cited “sales decrease in local markets” as the reason for deterioration was largest, at about 60%. In the entire region, the second largest reason was “sales decrease due to export slowdown,” which accounted for a little more than 30%, but by country, the reasons were varied, with half of the companies in Turkey citing “effects of exchange rate fluctuation,” 40% of those in Saudi Arabia mentioning “increase of labor costs” and “production costs insufficiently shifted to selling price of goods,” and the same percentage of those in UAE choosing “sales decrease due to export slowdown.”



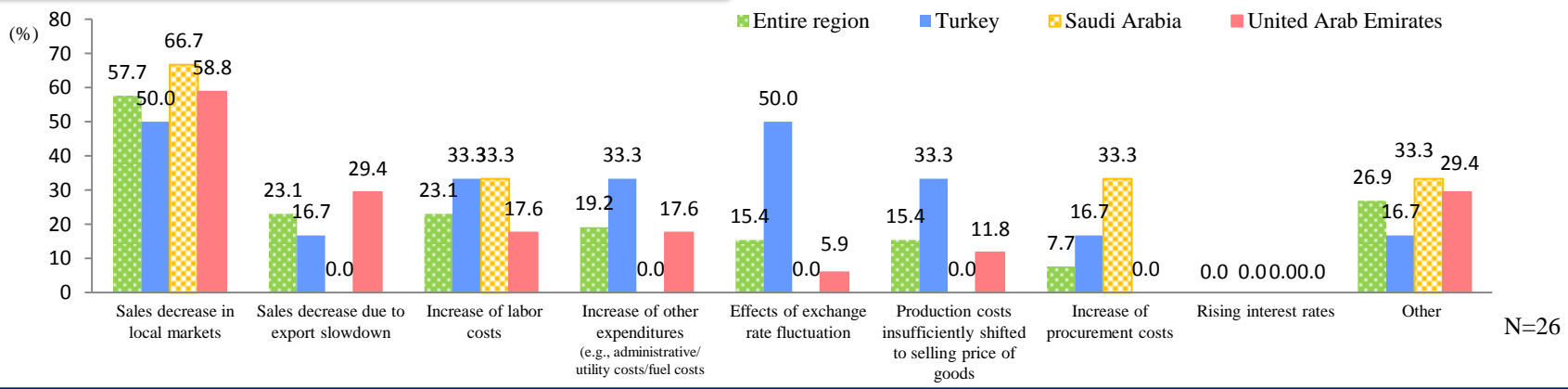
Multiple answers allowed

# Figure 6. Operating Profit Estimate (4)

## Reasons 2016 operating profit forecasts improve



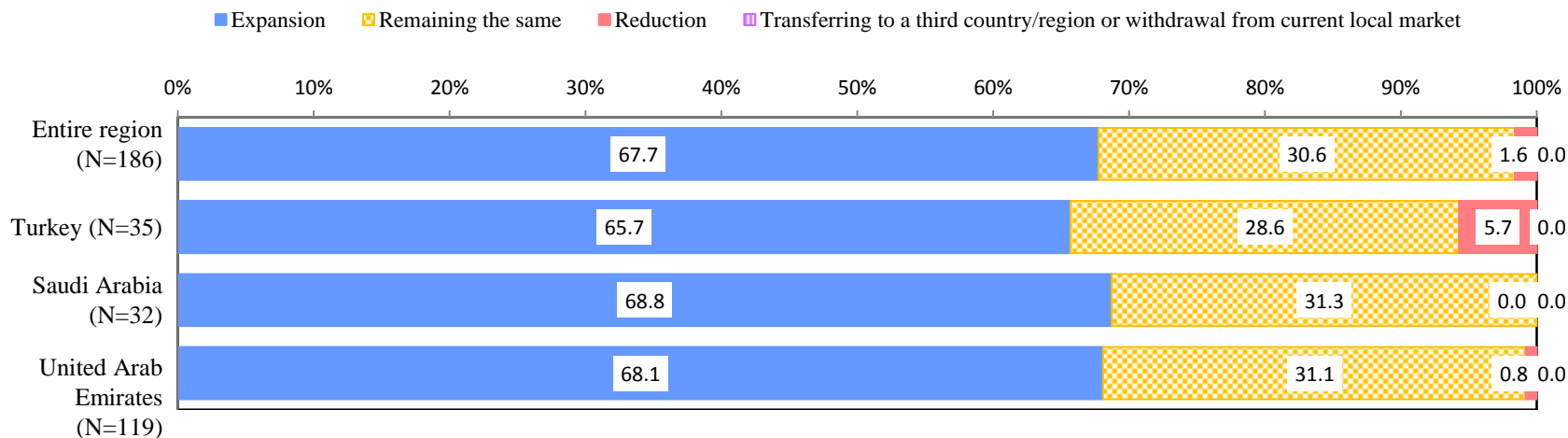
## Reasons 2016 operating profit forecasts deteriorate



- A look at operating profit forecast for 2016 indicated that in all countries 70-90% of companies cited “sales increase in local markets” as the largest reason operating profit improved. The second reason was “sales increase due to export expansion.” However, in countries other than Saudi Arabia, 50-60% of companies mentioned “export expansion” as the reason for improvement, but in Saudi Arabia, the percentage of such companies was low, at a little less than 30%, and the percentage of companies that cited “improvement of production efficiency” was also high, at 50-60%.
- In all countries, the largest reason for deterioration cited was “sales decrease in local markets” (57.7% for the entire region). The second reasons were “sales decrease due to export slowdown” and “increase of labor costs” for the entire region (a little more than 20% for both), but by country, the reasons were varied, with 50% of companies in Turkey citing “effects of exchange rate fluctuation,” 33.3% of those in Saudi Arabia mentioning “increase of labor costs” and “increase of procurement costs,” and 29.4% of those in UAE choosing “sales decrease due to export slowdown.”

# Figure 7. Business Expansion in the Next One or Two Years (1)

## Business operations in the next one or two years

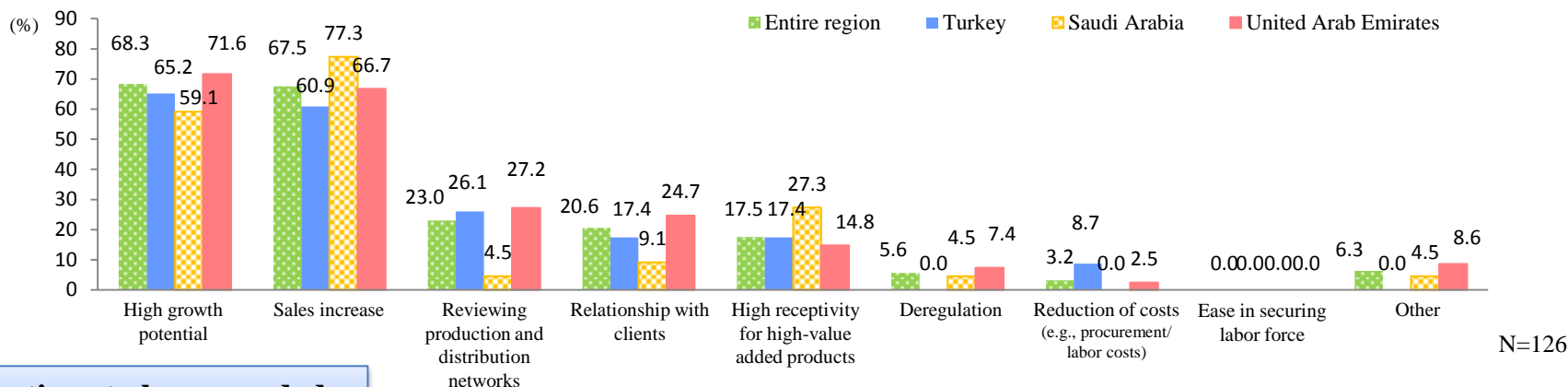


- Asking about their approach to business development over the next one to two years from 2015, more than 60% of companies in each country replied that they planned to expand their business. If companies that replied that they would maintain the status quo (about 30%) are included, almost all companies expected that they planned to expand their business or maintain the status quo. However, 5.7% of companies in Turkey chose to reduce their business, highlighting the difference between Turkey and other countries.

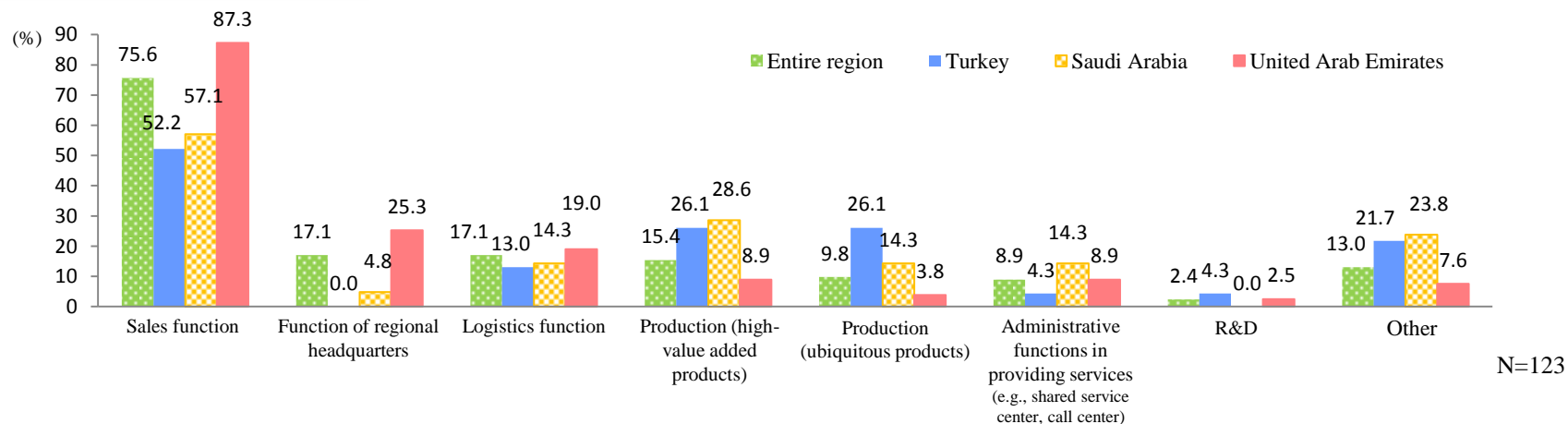
# Figure 8. Business Expansion in the Next One or Two Years (2)

Multiple answers allowed

## Reasons for expansion



## Functions to be expanded

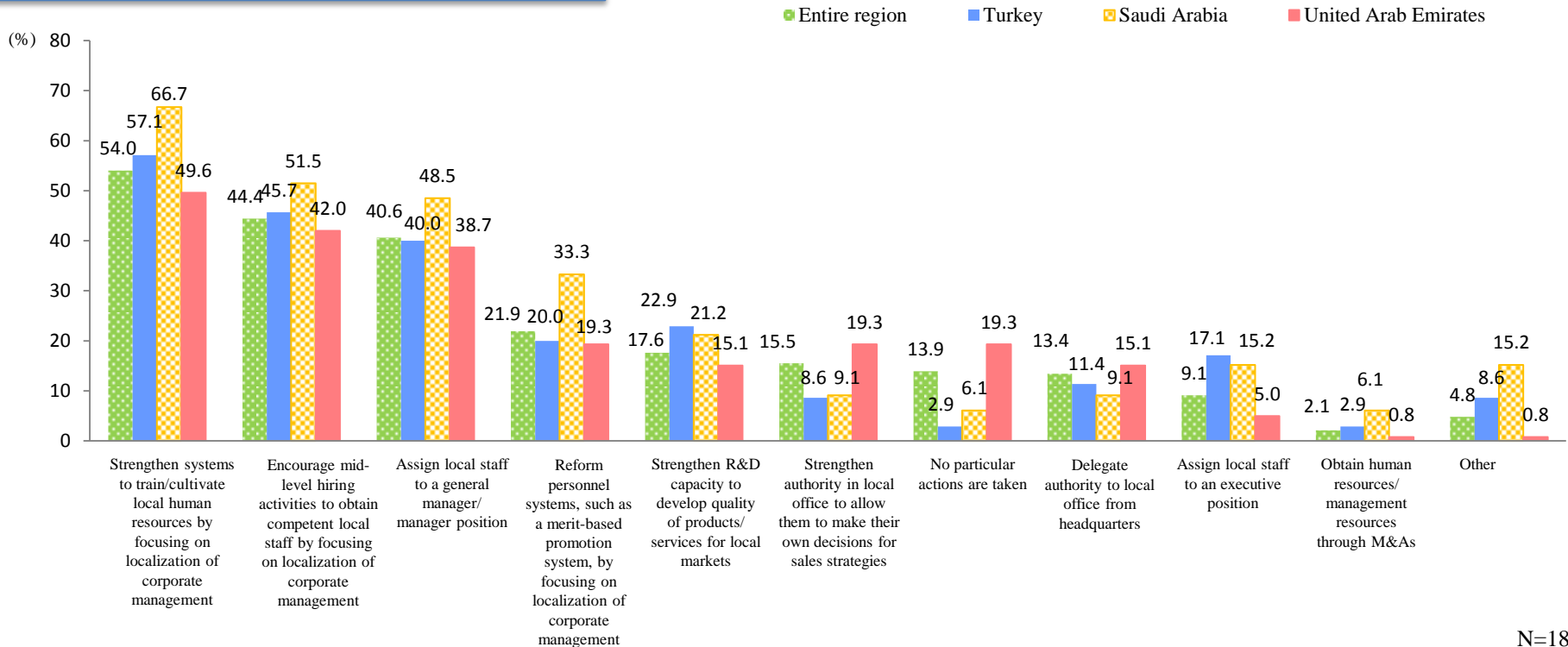


- The two major reasons for expansion were “high growth potential” and “sales increase,” each of which accounted for 60-70% of the companies surveyed. The third largest reason for many companies was “reviewing production and distribution networks” for Turkey and UAE and “high receptivity for high-value added products” for Saudi Arabia.
- An overwhelming percentage of companies planned to expand their “sales function” (50% to a little less than 90%). By country, the second and lower reasons were “production (high-value added products)” and “production (ubiquitous products)” for Turkey (26.1% each), “production (high-value added products)” for Saudi Arabia (28.6%), and “function of regional headquarters” for UAE (25.3%), indicating that the reasons varied from one country to another.

# Figure 9. Management Localization (1)

Multiple answers allowed

## Approaches to management localization



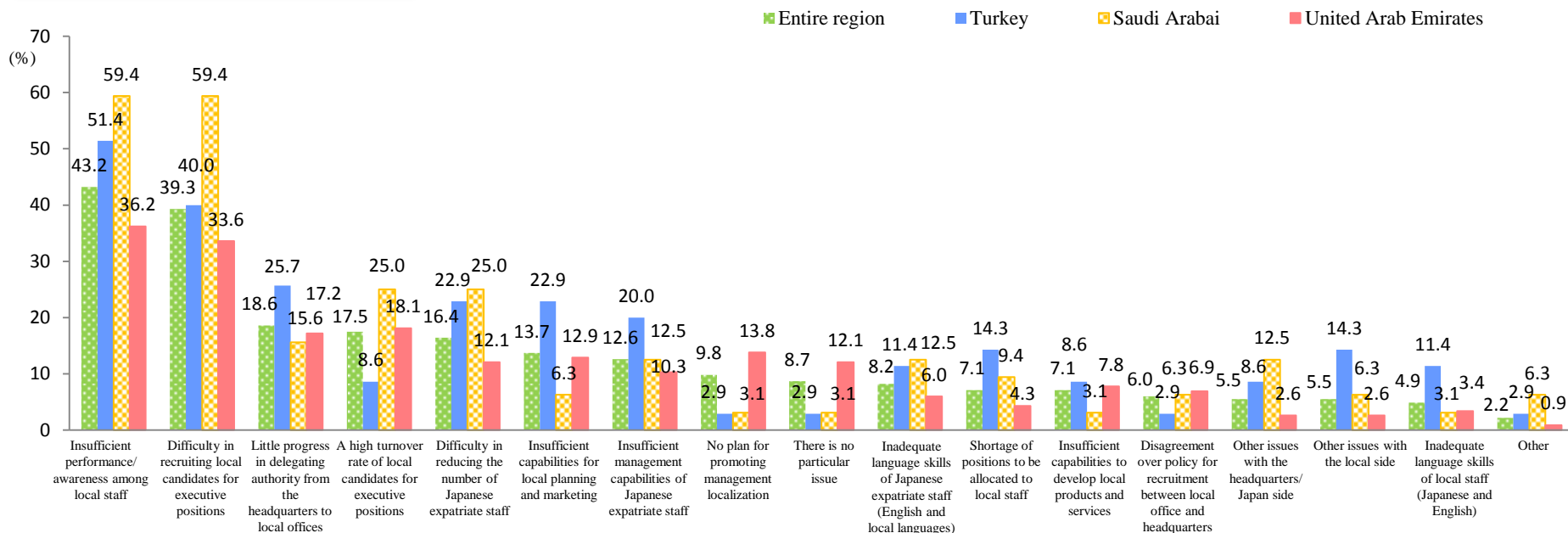
N=187

- In terms of approaches to management localization, the percentages of three replies were largest in all countries: “strengthen systems to train/cultivate local human resources” (54.0% for the entire region), “encourage mid-level hiring activities to obtain competent local staff” (44.4%), and “assign local staff to a general manager/manager position” (40.6%).
- The percentages of the top three approaches were high in all countries, but those of approaches in lower ranks varied from one country to another. A look at the characteristics of each country indicated that while in Saudi Arabia the percentage of “reform personnel systems, such as a merit-based promotion system by focusing on localization of corporate management” was high (33.3%) compared to other countries, the replies of companies in UAE reflected the degree to which the duty to employ people of the country was imposed, as they cited “strengthen authority in local office to allow them to make their own decisions for sales strategies” and “no particular actions are taken” (19.3% each).

# Figure 10. Management Localization (2)

Multiple answers allowed

## Challenges in localization



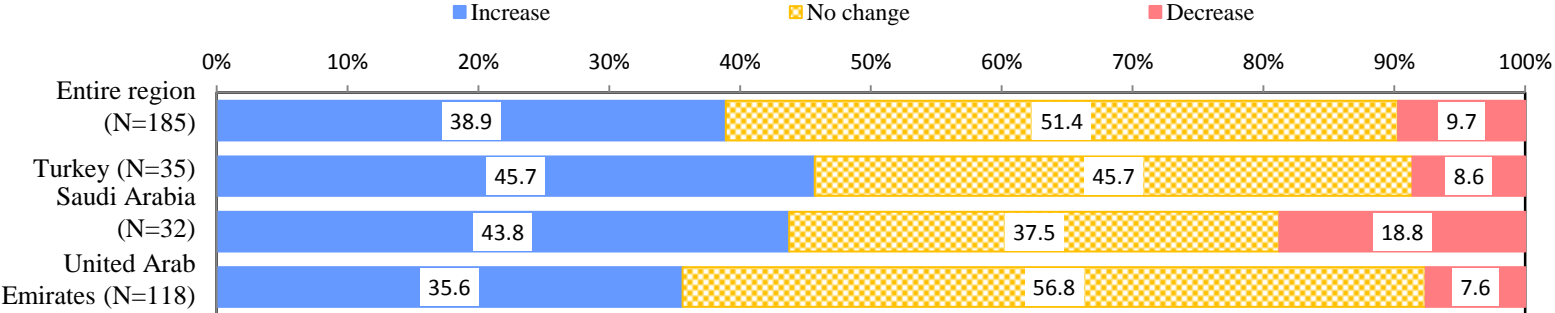
N=183

- Asked about challenges in management localization, the largest percentage of companies cited “insufficient performance/awareness among local staff” (43.2% for the entire region), followed by companies that mentioned “difficulty in recruiting local candidates for executive positions” (39.3%). In Saudi Arabia, however, the percentage of companies that chose the two answers was as high as about 60% (59.4%), suggesting that they were the challenges shared by companies that operated in the country.
- Apart from the top two challenges, a look at the characteristics of each country showed that in Turkey the percentage of “little progress in delegating authority from the headquarters to local offices” was high, at 25.7%, and in Saudi Arabia that of “a high turnover rate of local candidates for executive positions” and “difficulty in reducing the number of Japanese expatriate staff” was high, at 25.0% each. One characteristic of UAE is that the percentages of all replies except the top two were equalized, as none of them exceeded 20%.

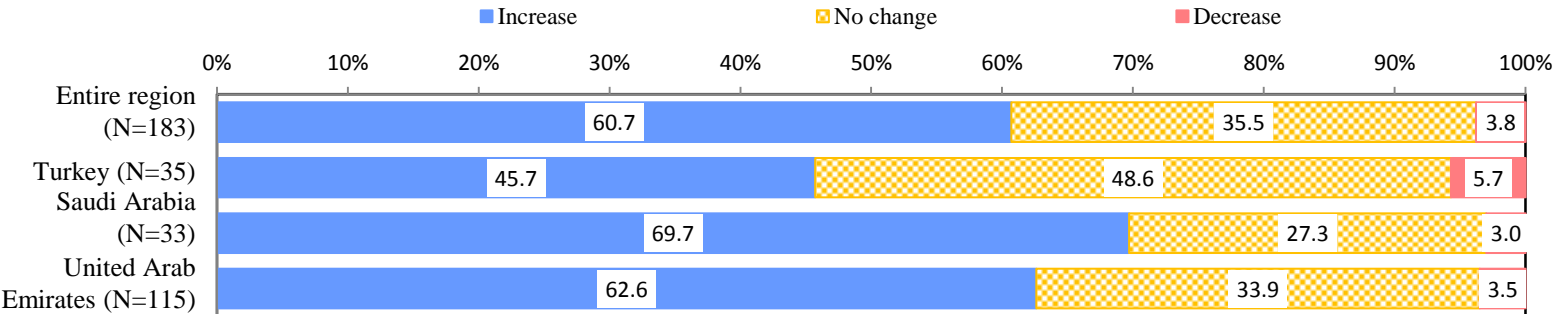


# Figure 11. Changes in Human Resource Structures (1)

## Changes in the number of local employees over the past year



## Future plans

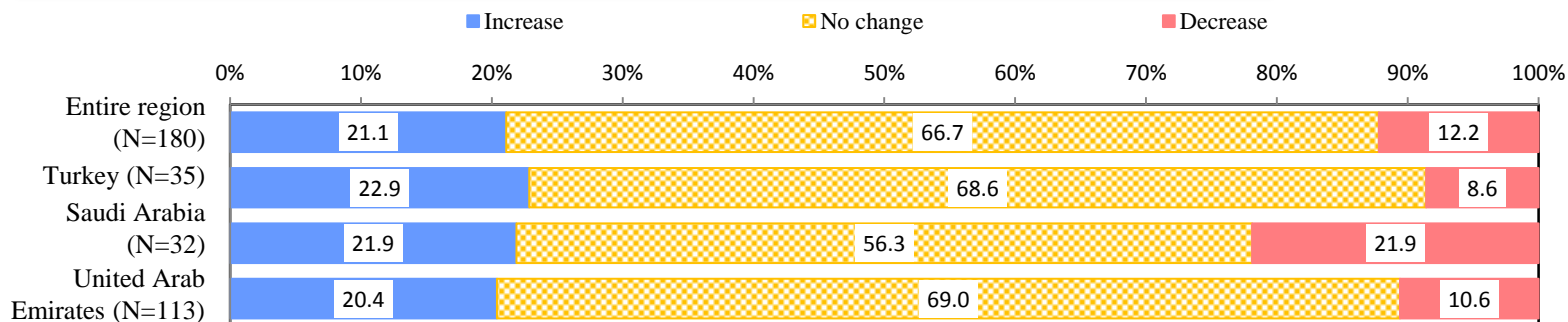


- A look at the changes in the number of local employees during the past year showed that the percentage of companies that had seen the number increase was 38.9% and that of those whose number had remained at almost the same level was 51.4%. By country, while more than 40% of companies in Turkey and Saudi Arabia replied that the number had increased, the percentage of such companies in UAE remained at 35.6%. In Saudi Arabia, on the other hand, the percentage of companies replying that the number had decreased was 18.8%, more than double that for Turkey (8.6%) and UAE (7.6%).
- In terms of future plans, the percentage of “increase” (60.7%) exceeded that of “no change” (35.5%) with that of “decrease” being small, at 3.8%. By country, the percentage of companies in Saudi Arabia that answered, “Increase,” was largest among the three countries, at about 70%, and that of companies that answered, “Decrease,” was smallest among the three, at 3.0%. On the other hand, the percentage of “increase” for Turkey (45.7%) was smallest among the three, and that of “decrease” (5.7%) was largest. This indicated that in the future, companies in Saudi Arabia would be most active in hiring local employees and that those in Turkey would be relatively cautious.

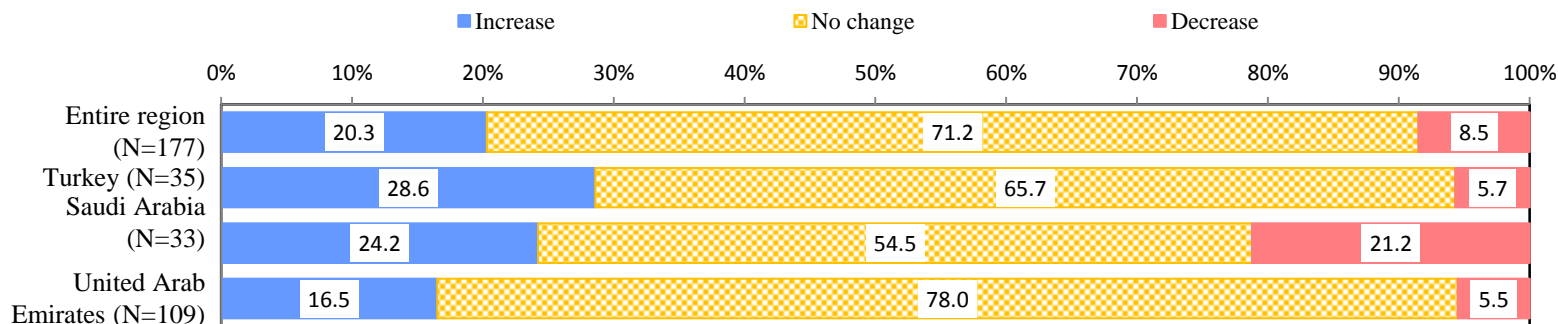


# Figure 12. Changes in Human Resource Structures (2)

## Changes in the number of Japanese expatriate employees over the past year



## Future plans



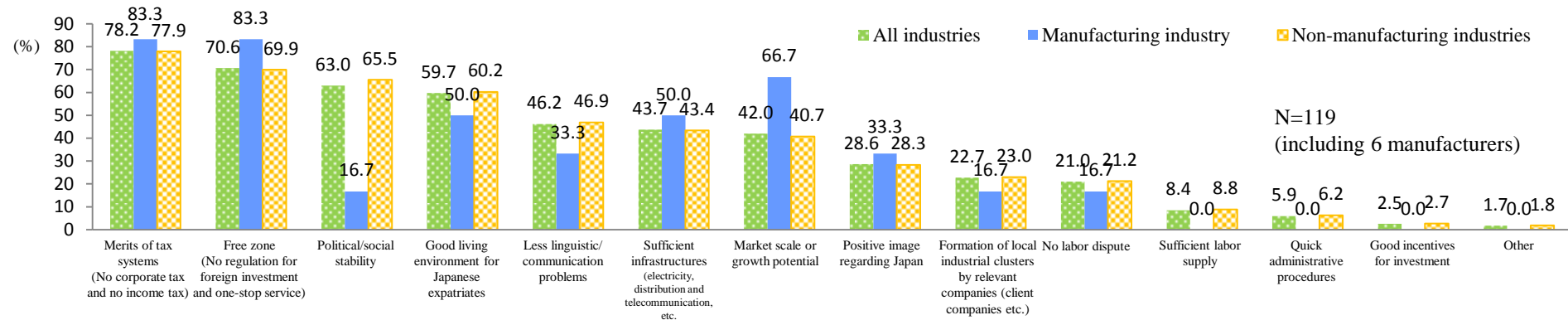
- At look at the changes in the number of Japanese expatriate employees during the past year showed that the percentage of “no change” was 66.7%, that of “increase” was 21.1%, and that of “decrease” was 12.2%. By country, in terms of the percentage of companies replying that the number had increased, there was no major difference among the three as the percentage stood at a little more than 20% in each, but the percentage of companies in Saudi Arabia replying that the number had decreased was largest, at 21.9%, followed by UAE (10.6%) and Turkey (8.6%), and this highlighted a greater decrease for Saudi Arabia.
- Asked about future plans, 71.2% of companies answered, “No change,” 20.3% replied, “Increase,” and 8.5% said, “Decrease.” By country, the percentage of companies in Turkey replying that they planned to increase the number of Japanese expatriate employees was largest, at 28.6%, followed by Saudi Arabia (24.2%) and UAE (16.5%). On the other hand, the percentage of companies in Saudi Arabia replying that they planned to decrease the number was largest, 21.2%, four times that for Turkey (5.7%) and UAE (5.5%). In particular, for Saudi Arabia, the percentage of companies replying that they planned to decrease Japanese expatriate employees was remarkably high.



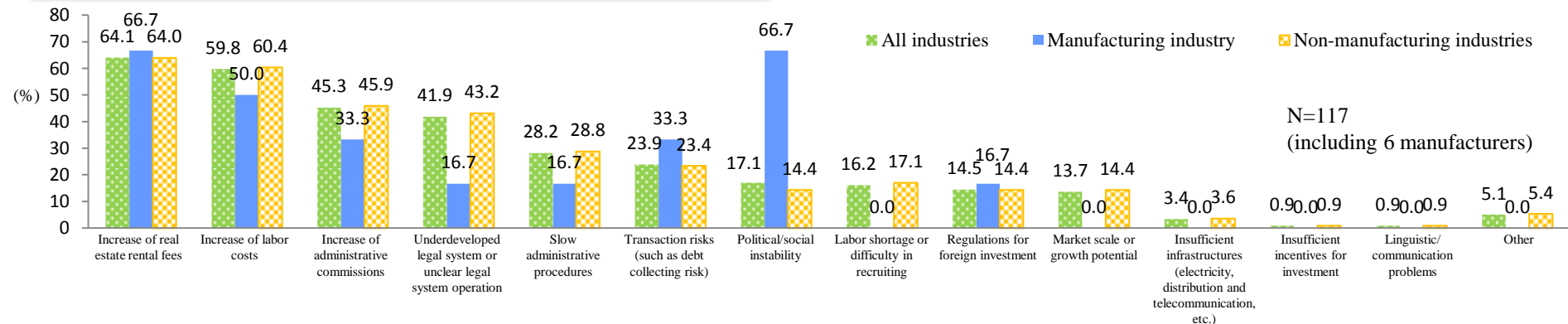
# Figure 13. Investment Environment (United Arab Emirates Only)

Multiple answers allowed

## Advantages of the investment environment in UAE



## Disadvantages of the investment environment in UAE



- Overall, more than half of companies cited as the advantages of the investment environment in UAE “merits of tax systems (no corporate tax and no income tax)” (78.2%), “free zone (no regulation for foreign investment and one-stop service)” (70.6%), “political/social stability” (63.0%), and “good living environment for Japanese expatriates” (59.7%). In the non-manufacturing industries, companies generally gave almost the same replies as mentioned above, but manufacturers favorably evaluated “market scale or growth potential” (66.7%) and “sufficient infrastructures (electricity, distribution and telecommunication, etc.)” (50.0%) while the percentage of companies that chose “political/social stability” was low, at only 16.7%.
- A large percentage of companies cited “increase of real estate rental fees” (64.1%) and “increase of labor costs” (59.8%) as the disadvantages of the investment environment in UAE, irrespective of whether they were in the manufacturing or non-manufacturing industries. One characteristic of manufacturers was that the percentage of those which mentioned “political/social instability” was high, at 66.7%. In the manufacturing industry, “transaction risks (such as debt collecting risk)” (33.3%) and “regulations for foreign investment” (16.7%) were also cited by many firms as problematic.
- (Note) (1) This survey was carried out only for companies operating in UAE. (2) Since non-manufacturing industries account for an extremely high percentage of all industries in UAE, the survey results generally indicate the same trends as for the non-manufacturing industries.



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