

Standard Chartered Hong Kong SME Leading Business Index Report

First Quarter 2013

Release Date: 10th January 2013

Executive Summary

The third survey of the Standard Chartered Hong Kong SME Leading Business Index (Standard Chartered SME Index) was conducted in December 2012. Top management of 810 SMEs were surveyed to gauge their views on the outlook of the overall business environment and regional economic changes in the 1st quarter of 2013.

The Standard Chartered SME Index is registered at 49.5 for the 1st quarter of 2013, a slight increase of 3.2 points from last quarter's reading of 46.3, indicating an improvement in SMEs' sentiments for the second consecutive quarter. As the reading gets closer to the 50.0 no-change mark, SMEs are less pessimistic about the overall business environment and regional economies in the 1st quarter of 2013.

Key findings of the survey are as follows:

- 1) The 1st quarter 2013 index slightly increases and is closer to the 50.0 no-change mark, which implies SMEs' sentiments have improved. The result is consistent with other recently released market indices and economic statistics. The improvement in sentiments is mainly brought by the increase of the Sales Amount Sub-Index and Investments Sub-Index.
- 2) The Retail Industry Sub-Index is registered at 51.9, the first time to exceed the 50.0 no-change mark, indicating optimistic sentiments in overall business environment for this quarter.
- 3) The sentiments of both manufacturing industry and the import/export trade and wholesale industry show improvement, but the Sub-Indices are still below the 50.0 no-change mark, indicating pessimistic sentiments in overall business environment for this quarter.
- 4) Majority of respondents expect the major cost components to rise for this quarter. Percentages of expected rent and employee salary expenses to the overall total cost increase, while that of raw materials maintains at 29%. Rent constitutes about 30% of the total cost of the retail industry, which is 4 percentage points higher than the ratio in the last quarter.
- 5) The SMEs are surveyed on their expectations on the 2013-14 policy address. 25% respondents want the government to offer tax relief or tax credit, 20% want more effective control measures on property market/rent and 17% need government's support in financing and loan guarantee.

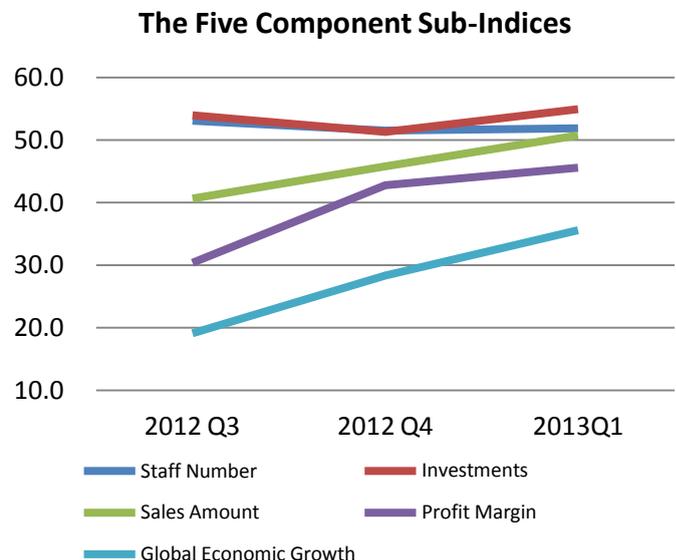
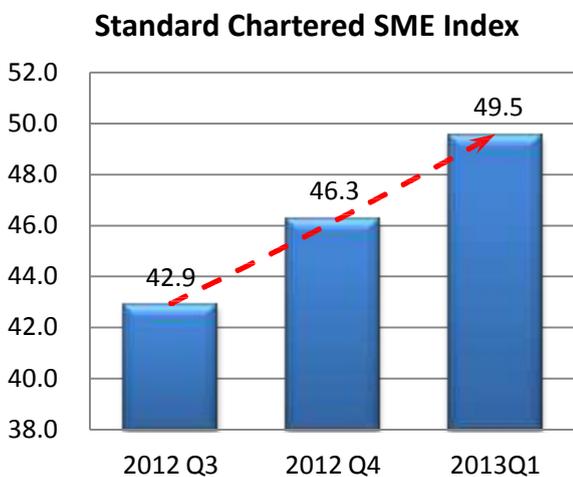


Year 2013 1st Quarter Index up slightly to 49.5, increases for the second consecutive quarter

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Each of the five Sub-Indices increases by a different magnitude in this quarter. Sales Amount Sub-Index rises to 50.7 from last quarter's reading of 45.8, marginally above the 50.0 no-change mark, indicating better sentiments in this aspect. Investments Sub-Index is registered at 54.9, increased by 3.6 from last quarter's reading, showing optimistic sentiments in investments for the third consecutive quarter. To increase production capacity and raw materials inventory, as well as the set up of new offices, factories and retail stores are the three major areas of investments cited. Staff Number Sub-Index slightly increases to 51.9, indicating optimistic sentiments in this aspect.

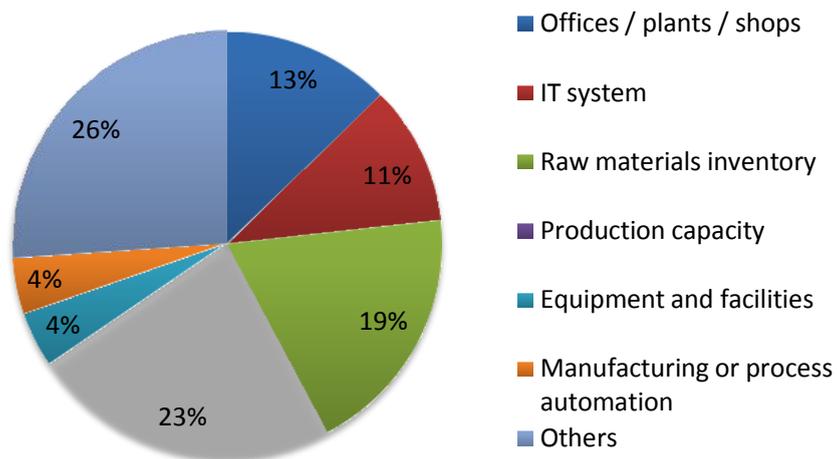
Although SMEs have optimistic sentiments in sales, the Profit Margin Sub-Index is still below 50.0 no-change mark. The main reason behind the situation could be the rising trend of major types of cost. Lastly, Global Economic Growth Sub-Index is still below 50.0 no-change mark, but is 7.3 higher than last quarter's reading.



Standard Chartered SME Index Summary

	2013 Q1		2012 Q4		2012 Q3
Overall Index	49.5	+3.2	46.3	+3.4	42.9
Staff Number	51.9	+0.4	51.5	-1.6	53.1
Investments	54.9	+3.6	51.3	-2.7	54.0
Sales Amount	50.7	+4.9	45.8	+5.1	40.7
Profit Margin	45.6	+2.8	42.8	+12.4	30.4
Global Economic Growth	35.6	+7.3	28.3	+9.2	19.1

Change of Area of Investment

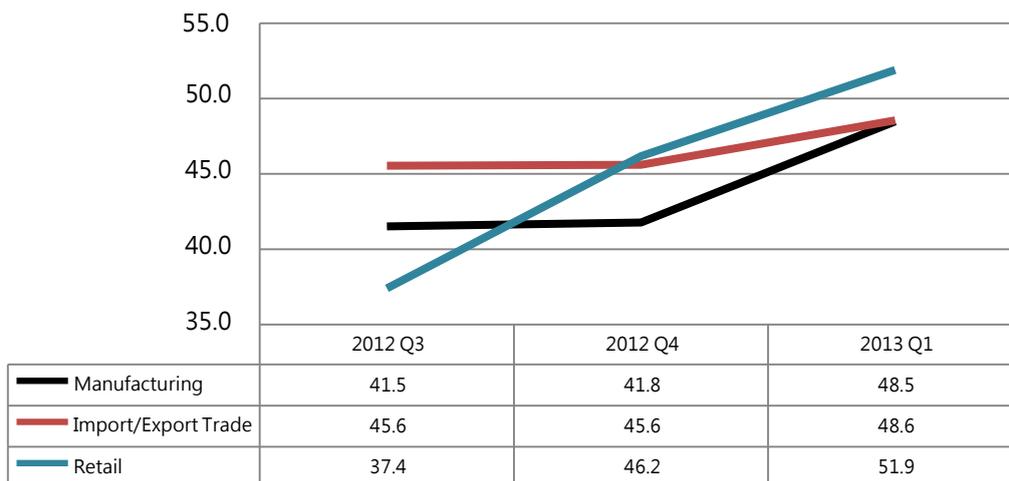


Retail Industry Sub-Index exceeds the 50.0 no-change mark

All of the three Industry Sub-Indices increase for the second consecutive quarter. The Retail Industry Sub-Index is registered at 51.9 in the 1st quarter of 2013, the first time to exceed the 50.0 no-change mark, indicating optimistic sentiments in overall business environment for this quarter. The sentiments of the retail industry show the biggest improvement among the three industries. The reading rises from 37.4 in the 3rd quarter of 2012 (the lowest among the three industries), to 46.2 in the 4th quarter of 2012 and to 51.9 of this quarter (the highest among the three industries).

The Manufacturing Sub-Index is registered at 48.5, increased by 6.7 points from last quarter's reading. The Import/Export Trade and Wholesale Industry Sub-Index is registered at 48.6, slightly increased by 3.0 points from the last quarter. The two Industry Sub-Indices are still below the 50.0 no-change mark, indicating pessimistic sentiments in overall business environment for this quarter.

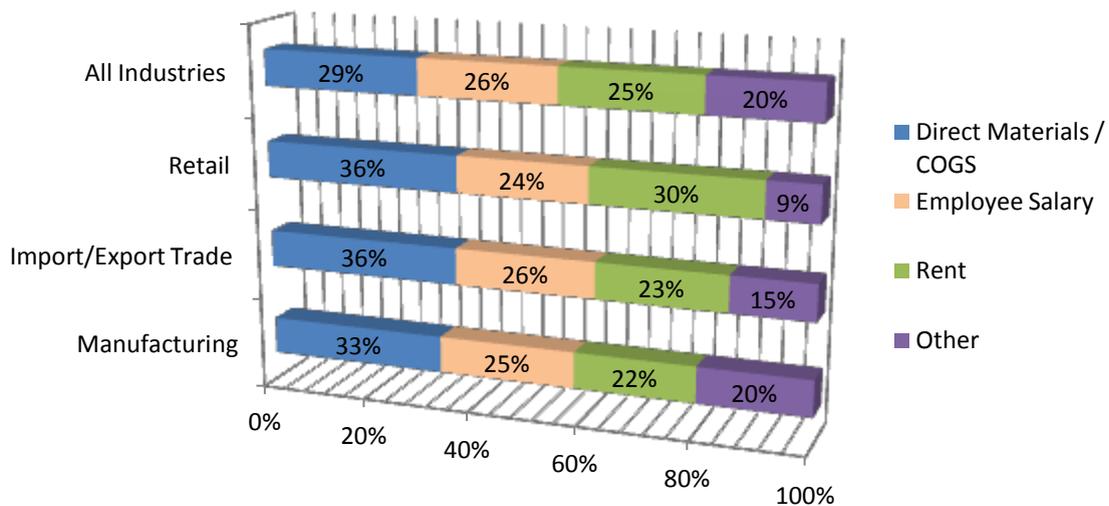
Standard Chartered SME Index by Industry



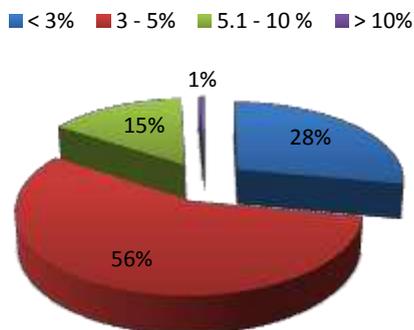
Rent constitutes 30% of the Total Cost of SMEs in the Retail Industry

Majority of respondents expect the major cost components to rise for this quarter. The ratio of direct materials/ cost of goods sold to overall total cost maintains at 29%. The ratio of employee salary expense has slightly increased and the weighted average of the salary increment percentage is 3.5 – 4%. The ratio of rent expense has also slightly increased, while over 50% of respondents expect rent will rise in the coming quarter. Rent constitutes about 30% of the total cost for the retail industry, which is 4 percentage points higher than last quarter’s ratio and is the highest among the three industries.

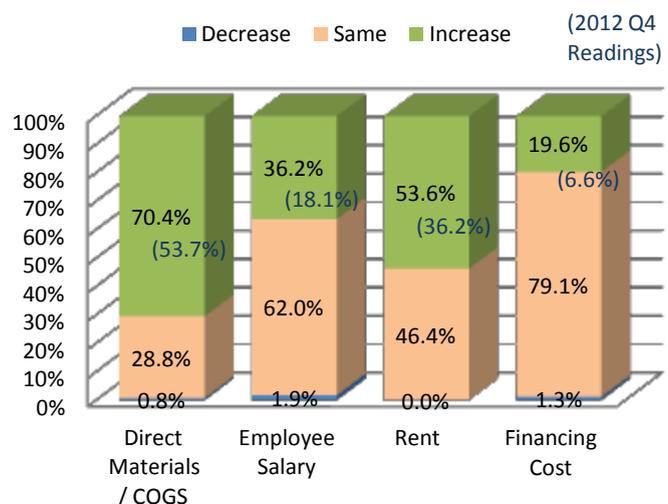
Cost Distribution by Industry



Employee Salary Increment Percentage

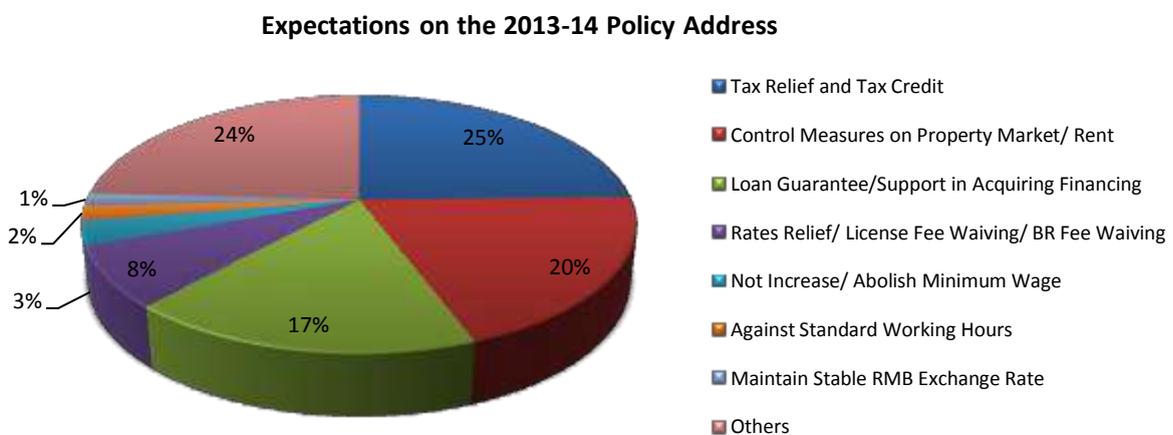


Change of Major Cost Components



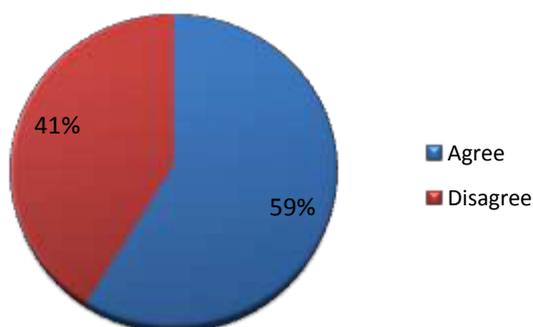
Expectations on 2013-14 Policy Address

The SMEs are surveyed on their expectations on the 2013-14 policy address. The top three most frequently mentioned items include: Tax relief and tax credit (25%), government control measures or property market/ rent (20%) and government loan guarantee/ support in acquiring financing (17%). Only 3% respondents want the government to maintain minimum wage at the current level or totally abolish minimum wage, while 2% oppose to implement standard working hours. The results imply that SMEs are relatively more concerned about the rising rent and financing, while minimum wage and standard working hours are not the major challenges facing SMEs.

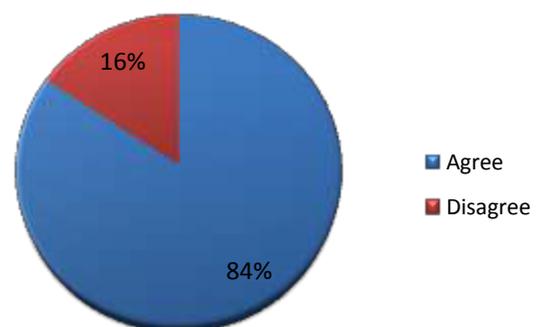


Almost 60% respondents support the legislation of standard working hours. This implies that implementing standard working hours in Hong Kong is not a big impact on most SMEs. In addition, over 80% respondents support to implement paid paternity leaves in Hong Kong.

Legislation of Standard Working Hours



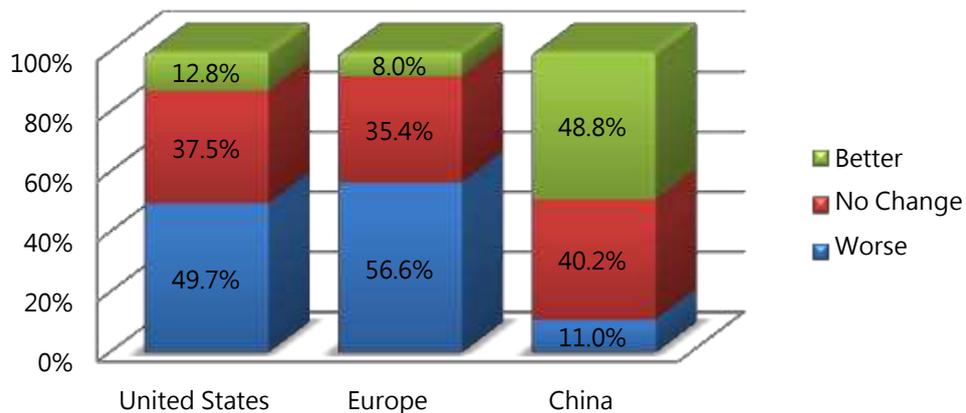
Paid Paternity Leaves



Sentiments of Market Performance

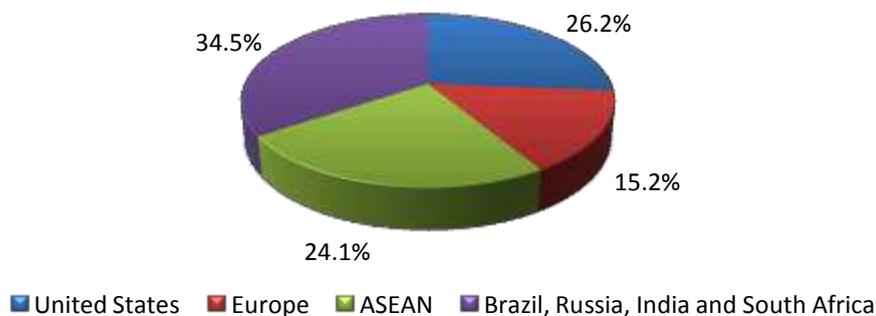
SMEs are pessimistic about the performance of U.S. and European markets in this quarter. Most of them expect the two markets will get worse or remain the same condition. Only a slight proportion of respondents expect the two markets will improve in this quarter. On the contrary, nearly 50% of respondents expect better performance in the China market.

Expectation on Market Performance



When SMEs are surveyed on their plan in market expansion, not surprisingly China is the top priority for most of them. Apart from the Mainland China, around 35% of SMEs choose emerging markets like Brazil, Russia, India and South Africa as their top priority for market expansion, higher than both United States (26%) and Europe (15%), which are large demand markets in the past. Finally, 24% of SMEs are targeting ASEAN markets (Association of Southeast Asian Nations), which includes Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam.

Market Expansion Plan



Supplementary Information

Sample Distribution

Data are collected from over 800 SMEs using publicly available SME directories and HKSAR Census database. The sample is stratified by the Hong Kong Standard Industrial Classification (HSIC) version 2.0, and based on the number of SME establishments in Hong Kong. The stratified sample covers nine categories namely: 1) Manufacturing, 2) Import/Export Trade and Wholesale, 3) Retail, 4) Accommodation and Catering Services, 5) Information and Communications, 6) Finance & Insurance, 7) Professional and Business Services (include Legal, Accounting, Consultancy, Advertising, Interior Design), 8) Real Estate (include Property Agent, Property Management and Maintenance), and 9) Miscellaneous category (include Construction, Transportation, Courier Services, Human Health Activities, Entertainment, and Domestic Personnel such as maids, cooks, gardeners, caretakers; exclude non-commercial activity such as primary school).

Index Calculation

Standard Chartered SME Index is a composite index based on the diffusion indices of the five surveyed areas with the following weights:

$$\text{Staff Number} \times 0.25 + \text{Investments} \times 0.25 + \text{Sales Amount} \times 0.2 + \\ \text{Profit Margin} \times 0.2 + \text{Global Economic Growth} \times 0.1$$

Respondents indicated the change of business sentiments in three ways: Increase, same or decline. Each diffusion index is calculated using the following formula:

$$\text{Increase \%} \times 100 + \text{No Change \%} \times 50 + \text{Decline \%} \times 0$$

Diffusion indices, which have been broadly used as leading indicators, are convenient summary measures indicating the prevailing direction of change in business sentiments. An index above the 50 no-change mark generally indicates optimistic business sentiment, while that below 50 indicates pessimistic business sentiment. A reading at 50 indicates neutral business sentiment.

Report Release

The Standard Chartered SME Index is released in January, April, July and October every year. Full reports can be downloaded at www.smeone.org, and the next report will be published in early April 2013.

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