

**Report for the Arab Supply Chain Impact Initiative of the  
World Economic Forum's MENA Regional Business Council**

# **STRENGTHENING THE MENA REGION'S SME ECOSYSTEM**

**A CASE STUDY ON INCREASING PROCUREMENT FROM SMEs**

**November 2017**

## Case Study: Strengthening the MENA region's SME ecosystem

*Crescent Enterprises ("CE") is a multinational company headquartered in the UAE with diversified global businesses under three verticals—operating businesses, strategic investments and new business incubation spanning sectors including ports and logistics, power and engineering, business aviation, healthcare and entertainment. Crescent Enterprises employs over 4,500 people in 20 countries across five continents.*

### Introduction

In March 2015, the Executive Committee of CE ("CE ExCom") decided to proactively plan and direct more procurement from small and medium enterprises (SMEs) and initiated a pilot programme awarding three key contracts to SME vendors. Based on the positive results of the pilot programme, in July 2015, the CE ExCom set a target to award 20 percent of all procurement across CE through SMEs by the end of 2018, and this initiative was internally code named "**Challenge: 20 by '18**". The key objective was to increase the SME participation in CE's overall procurement in order to **benefit from the ability of SMEs to offer more flexible solutions, better customer responsiveness and more innovative product and service offerings at competitive commercial terms**. However, it was essential to ensure that contracts were awarded on solely the commercial and technical merits, and without compromising on the quality of products and services procured. **Beyond the clear business case, Challenge: 20 by '18 was also in line with CE's sustainability roadmap and ongoing initiatives towards advancing the UN Sustainable Development Goals.**

#### **Key business drivers for CE to pursue a deeper engagement with SMEs:**

- **Flexible solutions:** *As some of its long-standing large vendors were unable to customise their offerings, CE sought bespoke solutions that SMEs were keen to offer.*
- **Customer responsiveness:** *SMEs can usually devote more individual attention to their customers, and hence are more agile, achieve shorter turnaround times, and better service levels.*
- **Innovative solutions:** *CE found that SMEs can offer significantly more innovative solutions, while continuously adapting and improving on their offerings at a faster pace.*
- **Specialisation:** *CE wanted to engage specialist vendors for some of its contracts to benefit from the depth of the product or service offering.*

**SMEs:** The definition of SME varies among countries. CE uses the Government of Dubai Department of Economic Development's definition of SME, which is as below:

|               | Trading   |              | Manufacturing |              | Services  |              |
|---------------|-----------|--------------|---------------|--------------|-----------|--------------|
|               | Employees | Turnover     | Employees     | Turnover     | Employees | Turnover     |
| <b>Micro</b>  | <= 9      | <= AED 9mn   | <= 20         | <= AED 10mn  | <= 20     | <= AED 10mn  |
| <b>Small</b>  | <= 35     | <= AED 50mn  | <= 100        | <= AED 100mn | <= 100    | <= AED 100mn |
| <b>Medium</b> | <= 75     | <= AED 250mn | <= 250        | <= AED 250mn | <= 250    | <= AED 250mn |

## Background

SMEs generate about 70 percent of employment on average in the developed economies and 45 percent of the total employment in the emerging economies.<sup>1</sup> They serve as key engines of job creation and economic growth in emerging economies. However, in the Middle East and North Africa (MENA) region, SMEs are estimated to account for only 30.2 percent of all private sector employment.<sup>2</sup>

SMEs play an important role in promoting competitiveness and introducing new products and services to the ever-changing market dynamics. With technological innovations, the importance of economies of scale has reduced, offering SMEs an opportunity to further increase their contribution to the economy. However, many of the fundamental challenges that SMEs encounter, such as lack of financing, constrained managerial capabilities, and regulatory requirements, also become more acute in a globalised, technology-driven environment.

Realising the vast potential of the SMEs and the possible benefits to CE, the CE ExCom decided to set a target of increasing SME contribution in the CE procurement programme to 20 percent by 2018, with a quarterly review of the SME vendors' performance and an annual assessment of the ExCom target.

## Implementing “Challenge: 20 by ‘18”

In 2014, SMEs accounted for 7 percent of CE's total procurement. Therefore, achieving the target of 20 percent warranted structural changes to the procurement process due to the challenges large corporates face while dealing with SMEs. CE's procurement team had to ensure that the SME vendors were financially capable of delivering on the contracts while complying with deadlines and quality requirements. Due to their size, many SMEs are able to only provide solutions that are local or focused on a niche area. Hence, SMEs are usually unable to offer a comprehensive solution, and the CE procurement team would have to manage several vendors providing different products or services.

- *Globally, SMEs are **key engines of job creation and economic growth**. SMEs account for 55 percent of the GDP of the European Union, whereas SMEs' contribution to the GDP across the GCC varies between 14 percent and 30 percent.<sup>3</sup>*
- *Youth unemployment rates in the MENA region are higher than any other region in the world. In developed economies, SMEs provide more than 70 percent of local employment.<sup>4</sup> A boost to SMEs is a way **to increase youth employment in the region**.*

### **Challenges of dealing with SMEs**

- *Managing multiple small vendors*
- *Vendor's financial ability to deliver*
- *Ability to honour deadlines*
- *Lack of quality assurance*
- *SMEs' inability to offer comprehensive solutions*

<sup>1</sup> “Enhancing the Contributions of SMEs in a Global and Digitalised Economy”, OECD, June 2017

<sup>2</sup> “SME Contributions to Employment, Job Creation, and Growth in the Arab World”, World Bank, 2013

<sup>3</sup> “Not all SMEs are Created Equal”, AT Kearney, 2014

<sup>4</sup> “Enhancing the Contributions of SMEs in a Global and Digitalised Economy”, OECD, June 2017

CE conducted a survey among its key existing SME vendors to understand their challenges before drawing up the implementation roadmap for the Challenge: 20 by '18. Taking this feedback (see Figure 1 below) into account and after studying global best practices, CE made some structural changes to its procurement policies.

**Figure 1: Results of CE's survey of 163 SME vendors in the UAE**

### Comments from SME vendors

- *“My biggest challenge is managing working capital. Customers in the region often delay payments. Large corporates can manage this easily, but for us, payment delays constrain us from bidding for large contracts, leading to slowing down or, worse, stopping our growth.”*
- *“Balancing our margins whilst ensuring high quality standards is the biggest challenge. Our suppliers often prioritise their large customers before us because of order size. Thus, we often struggle to deliver quality output within the deadline at adequate profit margins.”*

### Major concerns of SME businesses



\*RfQ: Request for Quotation; RfP: Request for Proposal

\*\* KYC: Know Your Client

## CE's initiatives to increase procurement from SMEs

Understanding the myriad of challenges that SMEs face while dealing with large corporates, CE's management undertook the following policy initiatives:

- **Boosting participation:** CE decided to have at least one bid/quote from an SME out of the minimum of three bids/quotes required for every procurement order, to ensure increased participation from SMEs in CE's procurement programme. This required increasing outreach and broadening CE's SME database by engaging with the regional chambers of commerce and industry, SME industry groups, and business forums to ensure that there was adequate SME participation in each product/service category.

- Wider roll-out of e-procurement:** While CE was using e-procurement for large contracts, a wider rollout was implemented to simplify the process and alleviate SMEs' concerns on cumbersome pre-qualification, KYC, and bidding procedures. The system created standard and more fit-for-purpose templates regarding CE's quality and delivery requirements, supply contracts, bid evaluation criteria, and invoicing requirements for each category of procurement tenders. Prospective vendors benefited through shorter purchasing cycles and costs associated with bid submission. SMEs could track the status of the bid submission and evaluation process in real time and plan their work better thanks to enhanced visibility on future tenders. The broader use of the e-procurement system also helped CE reduce administrative costs, eliminating unnecessary paperwork and increasing productivity of the procurement team.
  - Dividing large contacts:** CE's e-procurement system allowed bidders to bid for smaller components of a large contract as well as for the whole contract. This enabled CE to receive a higher response rate from SMEs—as it is often challenging for SMEs to bid for large contracts—while enabling CE to choose the most competitive bid/s: either a single vendor that offers a comprehensive solution or multiple vendors that offer complementary solutions for specialised parts.
  - Working capital management:** Access to finance is a key challenge that SMEs encounter, especially in the MENA region where nearly 63 percent<sup>5</sup> of SMEs lack access to working capital facilities. CE's undertook to reduce the working capital cycles associated with the CE procurement process, enabling SMEs to better manage their financial resources to compete with larger organisations. While providing better payment terms incurs additional costs to CE, as SMEs have a significantly higher cost of capital, the enhancement allows SMEs to submit more competitive commercial terms and hence results in a net positive gain for CE. CE also introduced SME vendors to its banking relationships, helping them access such financial products as bill discounting at a lower cost.
  - Integration into the CE supply chain:** CE also sought to integrate the SME vendors into its larger supply chain by offering them the opportunity to extend their services across the wider CE's companies. SMEs could gain from CE's diversified business interests across geographies.
- Boost SME participation** by having at least one bid/quote from an SME for the minimum of three bid/quotes invites for every procurement order
  - Wider rollout of **e-procurement**
  - Offer **better payment terms** to all bidders to ensure a more level playing field
  - Divide large contracts in to smaller pieces** to enable specialist SME firms to bid
  - Integrate the SME vendors** in the organisation's larger supply chain complete solution

<sup>5</sup> "Overcoming Constraints to SME Development in MENA Countries and Enhancing Access to Finance", IFC, 2017

While the above structural changes to CE's procurement policies aimed to provide a level playing field for SMEs and simplify their business dealings with CE, the cardinal principle was that all bids shall be evaluated impartially and assessed purely on the specified commercial and technical criteria.

### Regular reviews and process improvement

The CE procurement team conducted quarterly reviews of the performance of SME vendors that the company selected for its Challenge: 20 by '18. SME vendors were assessed on cost and performance metrics such as compliance with quality standards, adherence to deadlines, customer responsiveness and the ability to customise products (where needed) and provide innovative solutions.

CE adopted a collaborative approach of working with SME vendors for them to clearly understand the performance requirements from the outset, and provided regular feedback on where vendors were falling short. As part of these quarterly reviews, CE also asked SMEs to submit standardised feedback forms through the online platform to help it understand what process elements needed improvement, and how they could be enhanced. Accordingly, CE implemented changes and improvements to the process, where required. This regular review and feedback cycle helped SMEs improve their performance and in turn enabled CE to improve its procurement process.

### Impact of CE's procurement programme

CE rolled out its procurement programme across its countries of operations. However, the initial focus of implementation was on the UAE, Saudi Arabia, and Iraq because these countries had the highest contribution to CE's overall procurement. Going forward, CE is looking to further expand implementation within across other countries of operations.

The new procurement programme attracted significant interest from SMEs. **The number of SME vendors within CE's procurement programme tripled from 343 in 2014 to 1,040 in 2016 across CE's countries of operations. The share of SMEs within CE's total procurement increased by 86 percent in 2015 vs. 2014, and by 117 percent in 2016 vs. 2015.**

CE found numerous SME bids to be more cost competitive, with better customer responsiveness, and offering solutions tailored to its requirements. Most SMEs showed a greater drive and willingness to expand business with CE. The winning SME bids were often from companies that had developed niche product offerings.

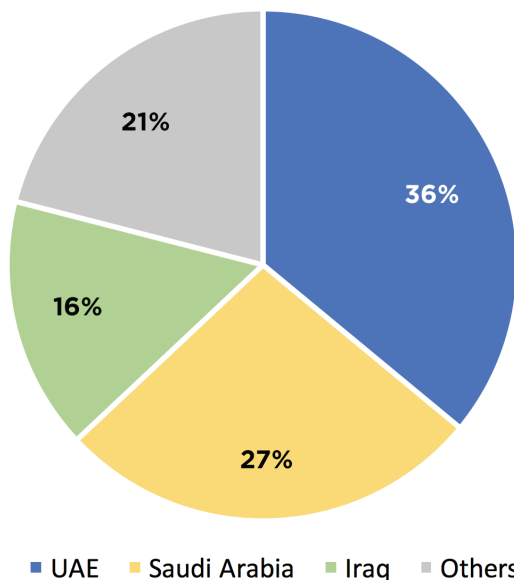
#### Impact & Results

- *SME participation increased from seven percent of CE's total procurement in 2014 to 29 percent in 2016*
- *Number of SME vendors grew by 203 percent from 343 in 2014 to 1,040 in 2016*

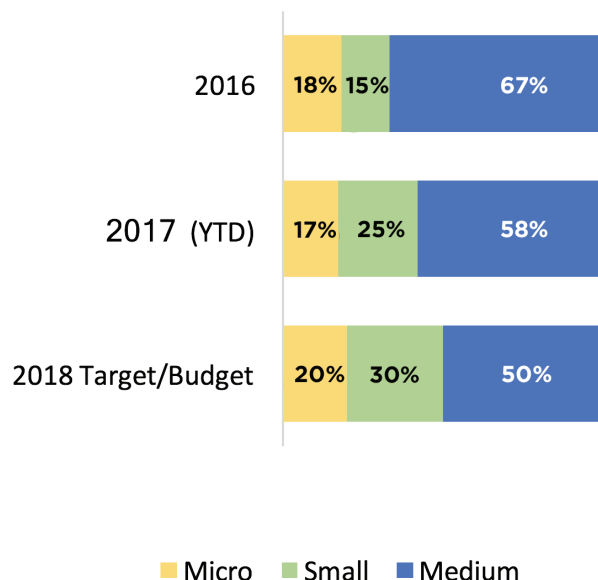
However, the CE procurement team had to proactively coordinate with several SMEs vendors for smaller portions of a large contract, instead of having one large vendor fulfilling the entire contract. While this led to more administrative work for the procurement team, it brought the significant advantage of more competitive pricing and hence lowered the overall costs.

The implementation of CE’s policy initiatives and new procurement programme increased the share of SMEs in CE’s procurement programme to 29 percent of the total procurement, surpassing the “Challenge 20 by ‘18” target in 2016, two years ahead of the end of 2018 deadline. In January 2017, CE ExCom set a new target of 35% to be achieved by the end of 2018 and the plan is to maintain it at that level beyond 2018.

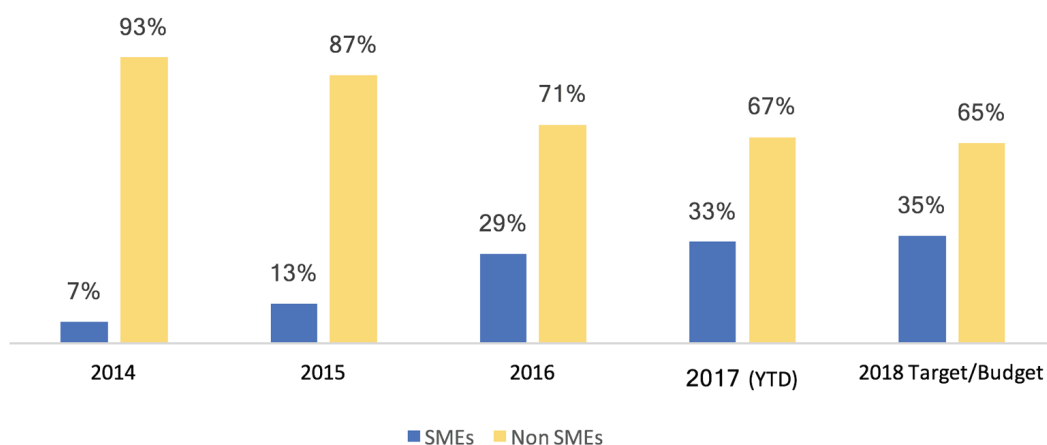
**Figure 2: SMEs’ participation across CE’s countries of operations (2016)**



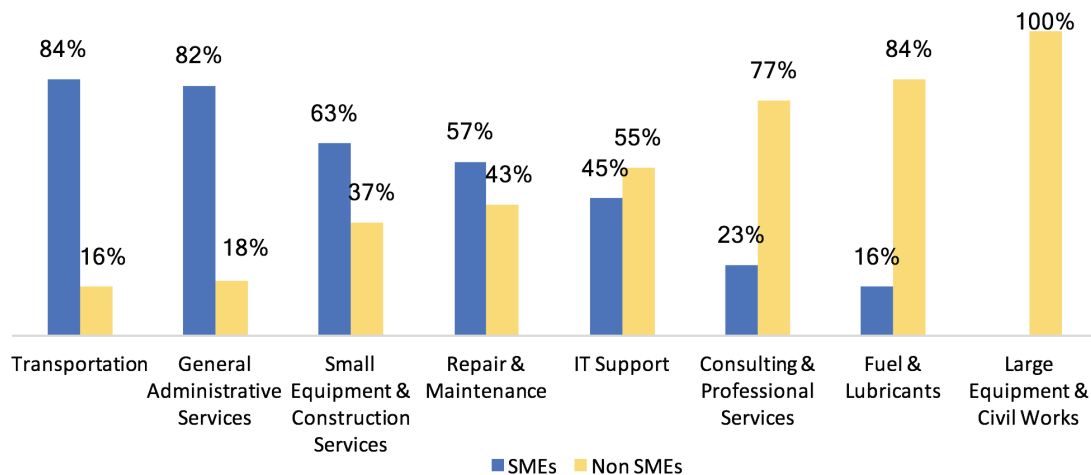
**Figure 3: Share of micro, small, and medium enterprises within CE’s SME procurement**



**Figure 4: Increasing share of SMEs in CE’s total procurement**



**Figure 5: SME participation across key product and service contracts (2016)**



## Results

### Advantages of working with SMEs

For large corporates seeking to integrate SMEs into their supply chain, SMEs offer significant advantages as follows.

- **Bespoke solutions:** SMEs are more flexible than large corporates and thus can offer customised solutions to meet the needs of their customers. For instance, an SME offered a customised solution for the financial reporting and analysis of CE's diverse strategic investments.
- **Agility and innovation:** As the renowned investment guru Jim Slater once said, "Never forget that elephants don't gallop". Large corporates are often slow to adapt and innovate. Due to their small size, SMEs are generally more agile and innovative.
- **Technologically advanced:** CE benefited from partnering with several SME vendors who used more advanced technologies and data analytics for varied tasks such as customer relationship management, and contract management.
- **Niche areas of specialisation:** To compete with larger organisations, SMEs tend to develop niche areas of specialisation that can be difficult to replicate.
- **Customer responsiveness:** SMEs can devote individual attention to their customers and are, on an average, more responsive and thus, offer a shorter turnaround time.

### Risks and mitigating factors:

Cognisant of the inherent challenges of working with SMEs, CE proactively managed and mitigated the risks.

- **Quality control:** Realising that the consistency of quality can be an issue with SMEs, CE, where deemed necessary, insisted upon more fit-for-purpose performance bonds that would get relaxed over time based on performance-as opposed to large and long duration performance bonds- which helped ensure



compliance with the required quality standards and delivery timelines. To help its SME vendors, CE facilitated their availing of such bonds on more competitive terms thanks to its banking relationships.

- **Financial capability:** In view of the limited financial capability of SMEs, CE's policy to offer better working capital cycles helped many SME vendors bid more competitively.
- **Business continuity:** In view of limited historical operating track record and financial capability, there is a much higher risk of business continuity with SMEs. CE conducts an adequately thorough assessment of each vendors' track record before registering the vendor. Performance bonds also help mitigate the business continuity risk, however, as mentioned above, CE requires for more fit-for-purpose performance bonds.
- **Lack of turnkey solutions:** SMEs are often only able to cover a limited local footprint and with a focus on a single niche area, many are unable to offer a comprehensive one-stop solution. Therefore, CE took the initiative to allow SMEs to bid for smaller portions of a large contract. This ultimately benefitted CE by lowering the overall procurement costs.
- **Ethical business practices:** As SMEs have limited corporate governance and compliance procedures, the risk of vendors' engaging in corrupt or other unethical business practices could be more acute compared to larger corporates. To address this challenge, CE has, besides the vendor KYC procedures, a 'Code of Conduct' that must be undertaken and complied with by all vendors and suppliers, and any breach of it directly results in the termination of a contract and a hefty penalty. The Code of Conduct is explained upfront to vendors at the time of onboarding and communicated through the online platform prior to each bid submission.

### Plans and areas for further development:

CE shall maintain its efforts to increase and expand SME participation in its procurement programme:

- **Targeting 35 percent SME participation by 2018:** CE is on track to increase SME participation from 29 percent in 2016 to 33 percent in 2017, and is targeting 35 percent by 2018, which is 15 percent above the original target set by the CE ExCom.
- **Broadening SME participation across product and service categories:** As seen in Figure 4, CE recorded higher SME participation in categories such as small equipment and construction services, transportation, and general administrative services, while categories such as fuel and lubricants, and large equipment and civil works saw minimal participation. CE is committed to developing more SME relationships in these under-penetrated categories to drive SME participation across all categories.

- ***Increasing the share of micro and small enterprises in overall SME procurement:*** In 2016, micro and small enterprises accounted for 33 percent of the total procurement from SMEs, with 67 percent from medium-sized enterprises. The share of micro and small enterprises has increased to 42 percent in 2017 (year-to-date) with CE targeting 50 percent in 2018.

## Conclusion

The CE procurement team successfully delivered on the ExCom’s “Challenge: 20 by ‘18”. The programme increased the total share of SMEs in CE’s procurement from seven percent in 2014 to 29 percent in 2016, and the number of SMEs working with CE tripling in just two years, CE is confident of achieving the revised target of 35 percent SME participation and increasing the participation across categories by 2018. While CE had to navigate through several short-term challenges along the way, the structural changes made to CE’s procurement policies laid a solid groundwork for smooth implementation.

- *The CE Executive Committee decided in 2015 to proactively plan and direct 20 percent of all procurement from SMEs by 2018.*
- *CE took certain policy initiatives that boosted participation by SMEs in CE’s procurement programme.*
- *Cognisant of the inherent challenges of working with SMEs, CE is working on managing and mitigating the risks.*
- *As a result, in 2016, ahead of the targeted year of 2018, SMEs constituted 29 percent (against the planned target of 20 percent) of CE’s total procurement.*

*“We had made a commitment to ourselves in 2015 to achieve a 20% target of SME participation in CE’s total procurement in 3 years. This has been a remarkable learning process for us. I am proud to see the results and the huge impact on our SME family, which we have already grown three-fold. With proper planning and the right policy changes to address the key challenges, the implementation has generally been smooth. We are working towards making further improvements and strengthening our SME vendor system.”*

***Head of Procurement and Contract Management at CE***

*“We had some initial problems when we first bid for a contract, especially on regulatory and compliance issues. But now, things are very streamlined. I know what CE contracts will be tendered and when. This helps me in planning and raising additional resources in anticipation of those contracts. The availability of ‘template contracts’ helps me avoid engaging with expensive lawyers and I can focus more on my business. Today, CE is my second largest client and makes up a significant part of my total annual turnover.”*

***Business Owner of a SME vendor providing equipment rental and maintenance services, reflected on his journey with CE***

## General Policy Recommendations

To build a strong SME ecosystem, large corporates and governments need to work together. Based on CE's experiences from the SME vendors, the following initiatives can boost the SMEs in the Arab world:

- **Public procurement:** Public or government procurement is a powerful tool to boost the SME ecosystem. For instance, the Government of the UK has set a target to increase SME procurement (directly or indirectly<sup>6</sup>) to 33 percent. Similarly, the UAE government announced in 2014 that at least 10 per cent of their federal procurement would be from SMEs. Governments across the MENA region can adopt similar minimum targets for SME procurement.
- **E-procurement:** Implementation of e-procurement systems across the procurement process could be initially challenging, but there are significant cost-savings and efficiency benefits. Additionally, documentation required for bidding can be considerably streamlined. For public institutions, e-procurement brings more transparency. E-procurement also enables information related to all future tender opportunities ahead of time, leading to higher SME participation rates.
- **SME financing:** While regional governments and various multilateral organizations have launched several initiatives to boost SME financing, SMEs still face severe challenges in raising working capital debt from banks and other financial institutions at a viable cost. A viable option is to classify SME financing, especially in low-risk sectors, as a 'priority lending sector' by governments.
- **Capacity building:** Most SMEs are founder-driven and are constantly challenged on the management and team's bandwidth to manage multiple projects simultaneously. Regional business forums and governments can promote knowledge sharing by organising workshops and establishing shared resource centres to support in building SME capacity. Further, the WEF MENA Regional Business Council is very well placed to facilitate creation of a central database of highly-rated SME vendors that members can all tap in to for their procurement requirements.
- **Enhancing corporate governance within SMEs:** Whilst corporate governance is often associated with large businesses, there is a huge opportunity to help SMEs realise the considerable benefits that stronger governance practices bring, including strengthening the SME's credibility and alleviating compliance related issues. To this end, the Pearl Initiative, a business-led non-profit organisation founded in 2010 to advocate the adoption of higher standards in corporate accountability, transparency and governance, launched a 'Governance in SMEs' programme across the Gulf, which has so far engaged with over 2,000 SMEs. It is imperative to enhance corporate governance within SMEs through more engagement and programmes similar to the Pearl Initiative.

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<sup>6</sup> Indirect SME procurement refers to contracts through the supply chain that ends with SMEs.

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