Dubai Model of Economic Diversification and Development

High-Level IMF-Ministry of Finance of Kuwait Conference on Economic Development, Diversification and the Role of the State

KUWAIT, April 30th-May 1st, 2014
Outline

- Why diversification?
- Initial conditions in Dubai
- How diversified is Dubai’s economy? Growth experience
- What policies account for diversification in Dubai?
- Challenges of diversification
Why Diversification?

Benefits of diversification:

- Reduce volatility due to external or internal shocks and ensure sustainability

- Grow faster: Empirical evidence that growth and diversification are positively correlated, at least for a wide range of per capita income

- Widen the range of skills in the country

- Secure stable revenue for the Government to spend on Government services, build infrastructure and eventually provide social subsidies, particularly if the natural resource base is narrow
Initial conditions

- Very little natural resources
- Very small population
- Poor infrastructure
- However, a leadership well aware of these unfavorable conditions and keen to catch up
- A tradition favorable to trade and movements of persons
- However, a strategic location, a region well endowed in natural reserves and oil wealth, rapidly growing trade partners, and access to a wide pool of labor, skilled and unskilled at very low cost for the latter
Growth and diversification in Dubai’s economy

- Growth performance

2000-2007: 14.7% per annum, with fastest growing sectors: trade, construction and real estate, transportation and logistics, finance

2008-2010: 1.2% per annum, with resilience of manufacturing and logistics and transportation

2011-2013: 4.3% per annum, with tourism leading the recovery

2000-2013: 8.9% per annum.
GDP in 2013: about US$90 billion which is three times as high as in 2000
Changes in GDP Composition

- Net increase in the shares of transportation and logistics and financial services

- Sharp decline in the shares of construction and real estate

- Dominance of wholesale and retail trade
Sources of Growth in Dubai

Investment:
- 2001-2004: about 23%
- 2005-2008: over 36% on the average with a peak of 44% in 2007
- Return to 24% in 2011-2012

% Investment to GDP Ratio in Dubai (2001-2012)

Source: Dubai Statistics Center, DED
- Excessive share of real estate in 2006-2008: a third of total investment, 40% with construction.

- Large drop in real estate in 2011-2012 to 19%, 28% with construction. Transportation and Logistics and Trade account for about a third of total investment.
**Government Revenue:**

- Economic diversification has led to radical change in the composition of Government revenue without losing regional competitiveness.

- The share of oil dropped from over 53% in 2000 to less than 17% in 2010.

- Revenue from fees has become the main source of Government revenue: about 55%.
Policies of Diversification: Developmental State

- Openness to trade, capital and labor flows (long tradition)
  - Beginning 1900s: removal of customs fees and licenses for vessels
  - Dubai became long ago a trade hub, responding to new demand for re-exports due to trade restrictions in the wider region (notably India after independence)

- Building a modern infrastructure that accommodates increasing flows of goods and services and an expanding population

- Business-friendly environment and regulation (Reforms to address regulatory restrictions and expand opportunities: ex of FZs and Free hold real estate)

- Historical events (...): Overcoming adverse changes, sizing on opportunities and building on experience
Some large energy-intensive projects were launched in the late seventies, early 80s: Dubai Aluminum (DUBAL) in 1979, a liquefied gas plant (DUGAS) (1980), Dubai Cabling Company (DUCAB) in 1981 and other manufacturing companies later.

Two major airports, one already among the largest and a second expected to be the largest in the world.

Early seventies: Decision to build a second new deep water port in Jebel Ali, opened in 1979 which has become one of the largest in the world.

World Trade Centre: opened in 1979 (exhibitions, ...)

Launching of Emirates Airlines in 1985 with leasing of a number of planes from Pakistan Airlines. Today it is one of the biggest in the world.

Hospitality: The first hotel was built in Dubai in 1960 to support the newly opened airport. Today Dub has more than 500 hotels and a hosting capacity of more than 80000 units, one of the most endowed cities in the world.
A tenfold increase in the value of total imports, from about USD$20 billion in 2000 to 200 billion in 2012.

Similarly for re-exports: from 11 to 95 billion USD$.
Challenges

- Rapid increase in total employment: 13% per year on the average over the period 2000-2012, sharp drop in recent years: 2.6% during 2009-2012

- Highly volatile productivity with no gains over the period 2000-2012

- Decline in productivity during the construction/real estate boom

Productivity: No gains

Explanation:
- Low productivity sectors
- Dual economy argument: perfectly elastic supply of labor
- Lack of export diversification: Gold and jewelry dominate

- Insufficient engagement of nationals in the diversified economy: 85% are employed in the public sector, which distorts the education and employment incentives system

- Excessive expansion of the real estate sector in the past (real estate bubble in the period 2006-2009): avoid a new bubble

- Debt challenge: the huge investment in infrastructure –but also in other activities- couldn’t have been financed by domestic saving alone. Today GRSs are healthy and are expected to service their debts
THANK YOU