The role of diversification strategies in the economic development for oil-depended countries: - The case of UAE

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Abstract

Diversification strategies adopted by oil-depended economies' played an important role in the economic development in these countries, which rely heavily on oil exports. UAE as an oil-dependency economy has the type of strategy to diversify the sources of its national income and reduce its dependence on oil to counter the instability in global oil prices.

This paper seek to investigate whether the diversification strategies adopted by (UAE) is adequate to manage its economic development. The methodology employed in this study is to examine the contribution of diversified sectors based on the country's GDP especially during and after the global financial crisis (2008-2012) using statistical analysis procedure. The results confirm that investment in different sectors rather than oil would have substantially improved the performance UAE economy.

1. Introduction

The United Arab Emirates has witnessed substantial development in its economic performance since 1970, despite of the fluctuation of oil price in the last two decades & global financial crises in 2008. The UAE's Minister of Economy – Sultan Al-Mansouri said that the UAE's strategy of diversifying income has helped the country reduce its dependence on oil, & he expected the UAE's GDP to have grown at its forecast rate of 4.5 percent in 2014 (Gulf News Jan.2015). In 2012, UAE experienced considerable improvement in economic performance, which has become more stable in the diversity phase led by a number of Non-oil sectors such as tourism, foreign trade, financial service, and telecommunications sector. Such factors have been reflected positively on the overall growth of GDP and achieved GDP growth by 4.4% in 2012 to reach 280$ billion in 2011.

Non -oil-sectors contributed to the growth in 2012 by about 3.4% to rise from 182$ billion in 2011 to 188$ billion in 2012 and accounted for 67.3% of GDP 2012 (Annual Economic Report 2012) UAE adopted strategy called UAE 2021vision. The aim of this strategy in the economy sector is to build a high competitive knowledge economy, which is divided into 12 national key performance indicators, the first indicator focus on non-oil real GDP growth, the indicator that measures the real annual growth of all sectors expect oil. The target of this indicator is to achieve 5% GDP growth by 2021 (UAE vision 2021).

This study examines the relationship between the economic diversification strategies adopted by (UAE) and its economic development.

2. Related Literature

An economic diversification strategy is regarded as one of the most important strategies that is used to support economic and business aspects and increases their competitive advantages. Diversification reduces the risks of focusing on a single economic sector or business area which contribute in maintaining the stability even in hard times, and consider as a great tool for business & economic development.

2.1 **Economic Diversification Strategies**

Nowadays diversification strategies are considered as a significant tool for economics to reduce risks. (Heydreich 2012) said that "Research results between 1992 and 2003, have shown that economic diversification based on economic variables can lead to superior geographic diversification" and in order to use the diversification strategies effectively (Al-Hashemi &etal,2012) stated that the diversification of the economy towards non-oil and gas industries is a challenging task that would require cluster based, collaborated and liberalized approach for development between government, industries and foreign investors, in the oil depended economy country, the economic diversification strategy mainly considered developing non-oil sectors and lowering oil financial dependency by creating a viable non-oil modern economy that can sustain a relatively high level of income (Fasano 2003) moreover added that the diversification is important to reduce or spread the risk as well as to promote economic development.

(Hvidt 2013) on the other hand identified three factors "income from hydrocarbons is finite, fluctuates and is practically the only source of the wealth "have placed the issue of economic diversification on the political agenda in the Gulf countries since oil was discovered.

In many cases the objectives & benefits of diversification are under debate. Many authors think that the reasons for diversification include achieving conglomerate power, not meeting of objectives with current portfolio of product / business and responding to opportunities outside of current business, spreading of risks, having excess cash of having slack resources (Akpinar 2009), While in other hand (Nelson and Nelson2003) argued that "The primary purpose of any diversification strategy is to reduce non-systematic risk".

The way to form diversification takes different forms (widest – or narrow) (Armstrong 2008) argued, "The portfolio with the widest diversification will have the lowest risk."

As things stand most of the GCC countries have tried different forms of diversification as a tool of economic development (Karolak 2014) stated that "The beginning of 21st century marked a crucial turn since governments of the GCC countries made a commitment to a sustainable development independent from oil resources and to competitiveness as requirements for future growth of the GCC region overall."

The GCC countries diversified their economics in different sectors, with a major focus key tourism. "The path of economic diversification through development of tourism has proved its success in the United Arab Emirates, especially in Dubai. Statistics indicate that in 2012 tourism accounted for 14% of UAE GDP and 31% of Dubai GDP alone. As a result, UAE has become a global leader in the higher-end leisure market" (WTTC, 2011).

The Gulf States also embarked on large scale economic diversification programs in 1990s and 2000s these created new integrative linkages with the global economy (ULRICHSEN 2011) moreover he added that the GCC states became world leading center of production for a variety of industries ranging from petrochemicals and aluminum to cements and construction products, according to (Porter 2010) the most competitive issue facing the GCC countries as a whole is increasing economic diversification.

According to (World Bank Report 2013) the oil exporting countries must continue to make reforms that accelerate the pace of Economic Diversification, and invest more in infrastructure to improve the business climate.

2.2 Economic Development

There has been many published studies that focused on economic development (Porter 2003) said that the responsibility for economic development shifted from the old model "the government drives economic development through policy decision and incentives" to the new model "Economic development is a collaborative process involving government at multiple levels, companies, teaching and research institutions",

While others think that the best way to achieve high economic development should be done through economic diversification. (Shihab) states that the successful implementation of human development policy in the UAE hand, to hand with industrialization, urbanization, and modernization, is one of the rare example of a country which has successfully used income from huge natural resources for its long-term development over a short period of time(from early 1970s to late 1990s)

Other approaches find that there is a link between three concepts at which relying on economic diversification enhances competitiveness of countries which finally enables economic development. (Maskell & et al 1998) describe that the economic prosperity of regions or countries is associated with their ability to generate or attract economic activities which are able to increase the income by performing well in the market.

The UAE's National Strategic Goals driven from the VISION 2021"To enable the UAE to become one of the most competitive countries in the world."Through knowledge economy supported by sustainable and diversified economy.

3. Data and methodology

For examining the relationship between the economic diversification adapted by UAE and economic development, the following area of development has been evaluated.

1- The contribution of the different diversified sectors in the GDP.
2- Value of non-oil sectors comparatively to oil sector during the period (2008 – 2012) through analysis other data obtained from the ministry of Economic and national business of statistics, UAE
3- The contribution of the non-oil sector in the Gross Fixed Capital Formation

3-1 The UAE Experience of Economic Diversification

3–1–1 Historical Background

The UAE is a federation of seven Emirates was constituted on December 2. 1971. The seven Emirates are Abu Dhabi (The capital), Dubai. Sharjah, Ajman, Fujairah, Ras Al-Khaimah, and Umm Al Quwain. The following table (3-1) showed the population and area of UAE in (2009)

Table (3 – 1): Population and Area of UAE (2009)

Emirates	Population (Persons)	Area in Sq. Km.	Population Density (persons / sq.Km)
Dubai	1.722.000	3.885	443
Abu Dhabi	1.628.000	67.340	24
Sharjah	1.017.000	2.590	393
Ajman	250.000	259	965
Ras Al-Khaimah	241.000	1.684	143
Fujairah	152.000	1.166	130
Umm Al-Quwain	56.000	777	72
Total	5.066.000	77.701	2170

Source & National Bureau of Statistics – Abu Dhabi - UAE

Oil was discovered in Abu Dhabi in the early 1960s and first exported oil in 1962, this dramatically shifted the focus of economy of the UAE and enabled the country to initiate enormous development programs in short period of time.

UAE is considered one of the richest countries in the world and the richest in the Middle East with a high per capita income reaching $ 44, 952 in 2012(World Bank Report 2013).

Table (3-2)
GDP - per capita (US$)

Country	2008	2009	2010	2011	2012
UAE	45,431	44,873	43,234	43,952	44,440

Source: World Bank Report 2013

According to (IMF 2012) UAE's debt to GDP ratio is the third lowest in the world following Norway and Libya. Currently standing at -93% whilst the world average at 64%

With regard to the oil production now UAE is considered as the Fourth oil producer in the world with 2.5 million barrels a day insert the group.

It is one of the oil producing countries whose economy is mainly based on oil products (Ministry of Energy). UAE leaders have adopted economic diversification as a means of reducing dependence on oil and committed to economic diversification earlier since the oil shock of the 1970s (Horyo Pestomo & et al 2011).

Table (3-3)
UAE crude oil production (2008-2012)

Year	Production	Change
2008	2,681.02	3.01 %
2009	2,412.55	-10.01 %
2010	2,414.66	0.09 %
2011	2,679.18	10.95 %
2012	2,803.61	4.64 %

Source: US Energy Information Administration

During 1970s and 1980s, diversification has been based on the development of capital – and energy – intensive industries as well as the physical and social infrastructure (Fasano 2003) and development of the productive sectors and heavy industry at that time Dubai Aluminum started in 1980 & the other sector diversified in 1980s is the service sector, the creation of free zones in Dubai since the Mid 1980s (beginning with Jabel Ali free zone). (Porter 2003) identified that the 1980s and 1990 the composition of UAE economy change over time and the shareof GDP divided by different sectors such as construction, manufacturing, government, services as well as oil, the UAE has reduced its dependence on the oil sector significantly.

The contribution of non-oil sector to GDP from 36.7% in 1980 to 57% 1991(UAE Economic Report 1992)

In the last decade the major aim for UAE government has been to enhance its competitiveness through leverage clusters to organize economic policy, delivery, coordinate government action, and direct diversification efforts (Porter 2010). During the first decade in the third millennium the UAE government has established a strategy named *Vision 2021* which divided into six national priorities, the third one is concentrating on how to build the competitive knowledge economy, and the first indicator is used to measure non-oil real GDP growth, actual results for 2012 for this indicator was 3.5% and the 2021 target will be 5% (UAE *Vision 2021*).

(Shackmurove2004) argued that UAE, although of its energy resources are expected to last for more than 100 years of current rate of production, is recognizing the need for diversification. Currently the UAE is focusing on the development of its service sector and non-oil industrial base. Different emirates have developed their own economic strategies, e.g. Abu Dhabi Economic vision 2030 (Porter 2010).

The Government of Abu Dhabi considers the year 2030 will represent an important mile stone for the Emirate of Abu Dhabi. Baseline growth assumptions reveal that Abu Dhabi could achieve tangible levels of economic diversification by the time (the Abu Dhabi Economic vision 2030- 2008). (Lancaster 2011) states that Abu Dhabi, the largest of the UAE's seven Emirates and its most prosperous owing 95% and 92% of the country's considerable oil and gas wealth, is moving into a new era of economic diversification and he added"vision 2030 is essentially a road map for greater diversification away from the country hydrocarbon-dominated economy. Mubadala Development Company, the strategic investment arm of Abu Dhabi government, continues to play a major role in the region's industrial development, including a wide range of projects, among them commerce, finance, energy and leisure."

In December 2014 Dubai launching its plan 2021 to begin a new phase of sustainable and systematic development in all vital sectors in the Emirate of Dubai (Gulf News Dec. 2014). The Dubai plan aims to align itself with UAE vision 2021 and the national agenda key performance indicators and complement Dubai strategic plan 2015 (WAM Dec. 2014).

This paper examines the relationship between the economic diversification strategies adopted by UAE and economic development. The methodology used in this study to examine the contribution of selected diversified sectors (construction, manufacturing, service, and tourism and Non-oil sectors) based on the country's GDP especially during and after the Global financial crisis (2008 – 2012) using statistical analysis procedures.

3-1-2 contribution of oil & non-oil sectors to GDP (2008 – 2012)

The information for this analysis appearing in the following table (3-4) shows such information needed to evaluate the contribution of oil and non-oil sectors to (GDP) during the period (2008-2012).

Table (3-4)

Contribution of oil & Non-oil sectors to GDP (2008 – 2012) (in million AED)

Sector	2008	2009	2010	2011	2012	average
Total GDP	977.4	930.5	946.4	982.7	1.025.6	977.52
Non-oil sector GDP	664.6	645.6	650.2	667.3	690.3	663.68
Contribution of oil sector to GDP	312.8	284.9	295.8	315.4	335.3	308.84
Contribution of Non-oil sector to GDP %	68.0%	69.4%	69.5%	67.9%	67.3%	68.42
Contribution of oil sector to GDP %	32.0%	30.6%	30.5%	32.1%	32.7%	31.58

Source: National bureau of statistics

In 2009 the GDP rate of growth for (UAE) reduced to 4% due to the global financial crisis and the decrease of oil price from $ 91.48 in 2009 to 53.48 in 2009. Although the non-oil sectors contribution increased from 68% to 69.4% in 2009 and 69.5 in 2010 respectively indicating that the non–oil sector plays an important role in the economic development of (UAE).

In 2011 and 2012 the contribution of non-oil sectors witnessed a small decrease to the 67.9% and 67.3% respectively while the oil sector contribution to the GDP increased from 32.1% in 2011 to the 32.7% in 2012 due to the increase of oil price from 53.48% in 2009 to the 71.21 in 2010 & 87.04 in 2012, and 88.95 in 2012 (inflation data.com November 2014).

From the above data in table (3-4) non-oil sectors maintain approximately the same high level of contribution to the GDP during and after Global financial crisis and it was not affected by the decrease and increase of oil price at the period of analysis, as an average in the period of study (2008 – 2012) the non-oil sector contributes to the UAE's GDP by 68.42.

3-1-3 Sectors Contribution to UAE's GDP (2008 – 2012)

As far as the information about the sectors contribution to UAE's GDP during the period of the study (2008-2012) is considered, the analysis of data is concern about evaluating the contribution of each sector to the overall UAE's GDP and identify the major players. Table (3-5) shows the sectors contribution to UAE's GDP (2008-2012)

Table (3-5)
Sector Contribution to UAE's GDP (2008 – 2012) (in million AED)

Sector	2008	2009	2010	2011	2012	average
Oil & natural gas	32.0%	30.6%	30.5%	32.1%	32.7%	31.58
Agriculture, Livestock & Fishing	0.9	0.9	0.8	0.7	0.7	0.8
Mining and quarrying	0.3	0.3	0.3	0.3	0.3	0.3
Manufacturing	8.6	8.5	8.8	9.2	8.9	9
Electricity, gas and water	2.5	2.5	2.5	2.7	2.7	2.58
Construction	11.1	11.2	11.1	10.4	10	10.8
Whole sale and retail trade and repairing service	13.2	13.3	13.4	13	12.5	13
Restaurant and hotels	1.8	1.9	1.8	1.9	1.9	1.86
Transport, storage and communications	9.4	9.4	9.2	9.3	9	9.26
Real estate & business service	10.2	10.6	10.2	10.2	10.5	10.34
Social & personal services	2.2	2.2	2.2	2.3	2.5	2.28
Financial corporations	6.3	7.4	6.2	6.7	7	7.1
Government services	4.6	4.7	4.6	4.7	5.5	4.82
Domestic level of household	0.5	0.4	0.4	0.4	0.4	0.42
Less imputed bank service	3.6	3.9	2.4	3.9	4.6	4.14
Total	100%	100%	100%	100%	100%	100%

Source: National bureau of statistics – Abu Dhabi – UAE

From table (3-5) it can be observed that the oil and gas sector contributed to UAE's GDP by an average of 31.58 in the period of analysis (2008 – 2012), while the non-oil sector contributed by 68.42 during the same period divided into different sectors, which reflects a measure of the effectiveness of economic diversification strategies adopted by UAE.

The wholesale and retail trade and repairing service sector has the higher share among the other sectors (13%), followed by construction sector by about (11%), then the real estate and business service by about (10.5%).

The transport, storage and communication contribution rate reached about (9%), manufacturing contributed by some rate (9%).

Also we can observe that the service sector (whole sale and retail trade and repairing, real estate and business service, transport, storage and communications, social and personal services, and hotel and restaurant). All together achieved the highest contribution to GDP by about (37%) comparing to other non-oil sectors.

a. Construction (11%)
b. Manufacturing (09%)
c. Financial Corporation (07%)
d. Government Service (05%)

e. Electricity, Gas & Water (03%)
f. Agriculture, Live Stock & Fishing (0.8%)
g. Mining Quarrying (0.3%)

The highest contribution of the service sector was affected by the movement of financial resources to the service sector specially the tourism by building many tourism infrastructures such as (Khalifa Tower, World Tallest Building, Dubai Mall, The Mall of Emirates, Yas Island which include Ferrari world & Yas water world and Formula 1 Circuit Abu Dhabi).

To meet the increased demand for the tourism services, a lot of branded hotels and restaurants have been developed; in 2010 alone there were 10 million visitors to Dubai, and Dubai's strategic plan is to increase the number of tourists to 15 million by 2015 (MEED)

According to the travel and tourism competitiveness report issued in World Economic Forum by in 2014 the UAE was placed in the 28 rank among the countries covered by the report (140 countries) and at the First rank among GCC countries, the following table (3-6) illustrate this information.

Table (3-6)
The Travel & Tourism Competitiveness Report (GCC Countries)

Country	2013 Ranking
UAE	28
Qatar	41
Bahrain	55
Oman	57
Saudi Arabia	62
Kuwait	101

Source: World Economic Forum report 2014

Construction is the highest contributor for the rest of the non-oil sector, this is because of the development of tourism infrastructure (shopping malls, hotels, leisure, and sport complexes) and real estate sector. Dubai & Abu Dhabi observing the highest rate of construction projects in UAE followed by Sharjah, Ajman, Ras Al-Khaimah, Fujairah, and umm Al-Quiwain respectively. There are more than 6.000 construction companies operating in UAE, but the major market key players are:

- Nakheel, Emmar, and Dubai properties and Damac in Dubai.
- AlDar properties and Sorouh Real Estate in Abu Dhabi.
- Al Hanoo holding company and Burooj properties in Sharjah.

The drivers for increasing growth of this sector is the highest demand for the real estate units due to the growing expatriate population,an ideal investment climate with high degree of flexibility and attractiveness and effective economic and investment policies attracts multi-national companies to expand their business in UAE

The second contributor in the non-oil sector rather than service is the manufacturing sector which contributes by about (9%) as an average rate during the period of (2008-2012).
Manufacturing sector includes a lot of industries areas such as; petrochemicals, metals, pharmaceuticals, as well as aviation industry. Financial corporations contribute about (7%), there are 50 banks in the UAE, about half of them domestic and half are foreign (Ministry of Economy2014) and in addition to that, UAE hosts two stock exchanges: the NASADAQ DUBAI, and ABU AHABI Securities Market (ADSM).

The agricultural, livestock and fishing sectors are small and their contribution to the GDP with Mining & Quarrying by (0.8%) and (0.3%) respectively. Although the agriculture industry in the UAE is diversifying quickly, it is still at the lowest level of contribution to GDP – its main exports include dates fish, vegetables, eggs, and dairy products.

3-1-4 Gross Fixed Capital Formation by the Economic Activities

This section used to analyze the structure of the investment distributed among the different diversified sectors, it is noticed that the non-oil sector played the major role of the constitution of Gross Fixed Formation which consistent with the contribution of these sector to GDP

Table (3-7) shows the Gross Fixed Capital Formation by Economic Activities (2009 – 2012)

Table (3-7)
Gross Fixed Capital Formation by Economic Activities
(2009 – 2012)* (in million AED)

Sector	2009	2010	2011	2012	Average Annual growth 2009-2012	Contribution %
Non – Financial Corporation	206.937	215.873	234.154	257.185	7.5%	83%
Agricultural, livestock, fishing	918	775	837	927	0.3%	0.3%
Mining & Quarrying Activies	38.078	38.047	30.480	34.261	-3.5%	11%
* Oil & Gas	37.826	37.690	30.111	33.875	-3.6%	10.9%
* Quarrying	252	357	369	386	0.15%	0.1%
Manufacturing Activity	35.695	40.336	40.809	45.583	10.6%	14.7%
Electricity, Water, and Gas	28.272	22.736	22.575	42.336	-4.9%	7.9%
Construction	11.438	13.718	11.965	12.503	3%	4%
Wholesale, and retail trade, advertising Service	10.396	12.340	12.817	13.548	9.2%	4.4%
Restaurant and Hotels	4.661	4.097	4.270	4.847	1.3%	1.7%
Transport, Storage and Communication	29.754	32.068	44.421	49.974	18.9%	16%
*Transport, Storage other Communication	24.845	28.636	37.382	42.656	19.7%	13.8%
* telecommunication	4.909	3.432	7.039	7.609	15.7%	2.5%
Real Estate & Business Service	41.911	43.190	52.086	55.159	9.6%	17.8%
Social & Personal Service	5.814	8.567	13.893	16.046	40.3%	5%
Financial Corporation	5.011	7.472	5.298	5.695	4.4%	1.8%
Government Service	57.276	39.230	42.238	46.293	-6.7%	15%
Total	269.224	262.575	281.690	309.173	4.7	

Source: National bureau of statistics – Abu Dhabi – UAE
*2008: N / A

Table (3-7) reveals that gross fixed capital formation grew by annual average of 5% during the period (2009 – 2012), whereas increased from 269.224 million dirhams in 2009 to 309.173 in 2012.

Also we can observe from the table above that the oil-sector contributed to the gross fixed capital formation by only (11%) in 2012 while the investment has been concentrated in four sectors of economic diversification by (64%) including :

- Real Estate (18%)
- Transport and Storage (16%)
- Manufacturing (15%)

- Government Service (15%)

3-2 UAE Economic Development

This part of the study provides insights into the area of the UAE economic development based on analysis of the competitiveness as a framework for economic development. As a result of the successful economic diversification strategies adopted by the UAE which concentrate "to enable the UAE to become one of the most competitive countries in the world" (UAE Vision 2021) the United Arab Emirates was ranked in the advance places in different classification, a report issued by the World Economic Forum for the year 2009-2010, the mid period of the study, ranks UAE comparatively to the Arab World and Worldwide as the following:

- First, among Arab counties in terms of economic liberalization
- First, in the classification of countries most integrated in globalized economy
- Third, in the world in terms of the appropriate economic climate for entrepreneurs

Statistics issued by a report on Doing Business in 2010 indicated that the UAE has occupied the following ranks:

- The 44th for the year 2010, in (project startup) after having been ranked 118th in 2009.
- The 33rd for the year 2010, in (Doing Business), compared to 47th in 2009.
- The 5th for the year 2010, in (cross-border trade), compared to 13th in 2009

UAE has achieved recently high standard rates of overall development in various fields, putting it at the top centers in the reports of the regional and international specialized institutions, especially in the indices of global competitiveness reports, which were classified in the best developed countries in the world lists ranked all most, as the first among Arab Countries, the following table (3-8) shows some of the recent standing (2013-2014)

Table (3-8)
UAE current Standing (2013-2014)

Report name	Global Ranking	Regional Ranking	Report Date	Published By
The World Competitiveness Yearbook	8 ▲	1 —	2014	World Economic Forum
World Happiness Report	14 ▲	1 —	2013	Earth Institute/Columbia University
The Global Competitiveness Report	12 ▲	1 ▲	2014	World Economic Forum
The Global Information Technology Report	24 ▲	2 —	2014	World Economic Forum
Doing Business Report	23 ▲	1 ▲	2014	World Bank
The Travel and Tourism Competitiveness Report	28 ▲	1 —	2013	World Economic Forum
Prosperity Index	28 ▲	1 —	2013	Legatum Institute
The Global Enabling Trade Report	16 ▲	1 —	2014	World Economic Forum

Source: Emirates Competitiveness Council Dubai, United Arab Emirates

4. Conclusions

Based on the data analysis of the contribution of diversified sector (Non-oil sector) at UAE's GDP and gross fixed capital formation, we can conclude that the UAE government realizes that it is important for the economic development to have other income source rather than oil. Despite the global financial crisis and the fluctuation of oil price during the study period (2008 – 2012), the UAE managed to overcome the negative impact through emphasizing more economic diversifications which support the country's economic development and the competitiveness, which put the UAE in the first rank in its region.

It is evident that the non-oil sector contributes to UAE's GDP by around 70% and four sectors from the diversified sector contribute to the gross fixed capital formation by around 64%. It is also clear that the UAE development and competitiveness continuously enhanced according to the international competitiveness measure. It can be observed that some sectors achieved a smaller contribution to the UAE economy such as agriculture, livestock & fishing which contributed by less than 1%, Mining and Querying 0.3%.

It is recommended that, the government should invest more in these less contributing sectors to increase their role in the UAE economy.

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