

## **UAE Economy Outlook**

While the seven emirates—Abu Dhabi, Dubai, Sharjah, Umm al-Qaiwan, Ajman, Ras al-Khaimah and Fujairah—retain a significant degree of autonomy within their own territories, recent events are likely to cement Abu Dhabi as the central controlling force within the country. Abu Dhabi, with its oil wealth and previously conservative outlook in relation to diversification, is now seen as a key financial support to Dubai, which has undertaken a more radical approach to economic expansion and is now seen as more vulnerable under prevailing international financial conditions. Abu Dhabi now effectively controls the central budget, rather than sharing that role with Dubai. The UAE's marked degree of cohesion within such a (still) relatively loose federal structure is unlikely to be compromised by global events. Moreover, the cosmopolitan and polyglot nature of society is unlikely to unravel, although more low key dissension is likely against a background of weaker job prospects. Relatively large per capita incomes and supportive state action to alleviate any stresses in society will limit internal unrest. President Sheikh Khalifa bin Zayed al-Nahyan is unlikely to face a political challenge to his leadership, particularly as he is emir of Abu Dhabi and therefore his personal status within the ruling families has been enhanced by recent events. A significant redirection of diplomatic, political or economic policies is unlikely.

Regionally, the UAE is a founding member of the Gulf Co-operation Council (GCC) and that grouping is likely to become closer as a united front is sought against a more difficult external economic and financial environment. However, plans for a common currency by 2010 remain optimistic. Although relations with Iran will remain uneasy, there is little to indicate that regional disputes will become destabilising. Foreign policy will remain generally pro-Western and, largely for that reason, terrorist attacks cannot be discounted.

**GDP Growth:** As the UAE is a relatively open economy (exports are equivalent to around 100% of GDP) and its key wealth generator is output of oil and gas (over 30% of GDP), the country is

vulnerable to downturns in the global economy and to declining commodity prices. To that extent, prevailing global economic and financial conditions, which are likely to remain through 2009, provide a serious challenge to the country's resource management.

Annual real GDP growth averaged 6.3% between 1987 and 2006 and we estimate economic expansion of 7% in 2007, buoyed by high oil prices and increased hydrocarbon production to meet global demand pressures. GDP growth this year is also likely to register around 7% but this figure has been revised downwards because of the weaker global environment. Until recently, growth in the nonhydrocarbon sectors had been strong and supplemented that resulting from increased output of oil and gas. Financial services, tourism (despite regional uncertainties) and construction (reflecting Dubai's large expenditure programme in establishing commercial and financial offices and related buildings) had all boosted growth through to the latter part of 2008. However, with a rapid slowdown in the global economy and associated lower demand for energy supplies, we now forecast that overall growth will slow to only 3% in 2009.

**Policy:** Despite weaker oil prices in 2009, we expect the UAE's consolidated budget balance—a combination of federal and individual emirate fiscal activity, combined with investment income derived from Abu Dhabi Investment Authority (ADIA)—to remain firmly positive. However, we forecast that the consolidated fiscal surplus, which reached over 26% of GDP in 2006-08, will decline to less than 9% of GDP next year. Neither the federal nor the individual emirate governments have significant domestic debt stocks and these largely comprise ST credit facilities with local banks.

Monetary policy will continue to centre on a fixed exchange rate between the dirham and the US dollar, which has been pegged at USD1=AED3.67 since 1980. Interest rates will therefore trend downwards in line with rate cuts in the United States, although a positive differential in favour of the UAE will be retained. Plans for a full monetary union within the GCC with a common currency by 2010 are likely to be revised, particularly as Oman has already declared that it will not be ready at that stage.

**External Balance:** The external sector account generally tracks movements in hydrocarbon revenues—the sector provides over 46% of total export revenues—and therefore in oil prices.

Accordingly, substantial trade-driven current account surpluses, equivalent to around 20% of GDP, have been recorded in recent years. These surpluses have been used to augment the country's net foreign asset base (principally through ADIA holdings), rather than solely build up FX reserves.

Official data indicating the value of sovereign wealth funds (SWF) are limited but we estimate them

currently to be around USD850bn, compared with GDP of around USD220bn. Most of the UAE's external debt has historically been short term (payable within a year) and trade-related, largely reflecting Dubai's import needs for its re-export trade. Medium- and long-term debt, in the public sector only, is traditionally small. Dubai accounts for the largest share of external debt, which is estimated at around 30-40% of both GDP and of export receipts. The debt service ratio will remain low, at around 3.5% in 2009. Moreover, although fiscal and current account surpluses will be much lower in 2009 and SWFs may need to be drawn on, there is only a very moderate risk that the UAE will not fulfil its international obligations and it is likely to retain its net creditor position.

The ruling regime is not seriously challenged and the political system, though not completely transparent, is relatively stable. Despite some unease with its proximity to Iran, regional relations, particularly through the auspices of the Gulf Co-operation Council (GCC), are generally good. The UAE is of strategic importance, particularly in relation to its proximity to the Straits of Hormuz through which global oil shipments are transported. The sustained period of high oil prices between 2006 and Q3 2008 resulted in large fiscal and current account surpluses and further build-up of foreign assets. To that extent, the economy appears more resilient and robust than many developing economies and in a relatively comfortable financial position to withstand a global economic downturn, even one that is both severe and protracted. Liquidity and solvency ratios will deteriorate in 2009 but are likely to remain generally better than those recorded by many emerging markets.

Nevertheless, business conditions in the UAE will be significantly tighter in 2009 and the domestic and global economic slowdowns suggest that business failures and the number of insolvencies are likely to increase markedly.

### **Industry Outlook - Pharmaceuticals**

One of the healthcare sector's most important third party logistics providers is preparing for sky-high pharmaceutical sales in the medium to long term, and has invested significantly in infrastructure as a result.

Dubai-based Pharma World Holdings is predicting 50% compound year-on-year growth until 2013 due to current sales and expected market share for the firm, which is one of the few 3PL service providers to the

healthcare sector in the region. International consultancies have forecast that drug sales in the Middle East will raise from US\$5 billion to \$9 billion over the next five-year period.

### **Industry Outlook – Transport**

UK-based transport and logistics consultancy Transport Intelligence has released the result of its First Global Logistics Business Confidence Index for February 2009. The survey is designed to provide an insight into the health of the various sectors of the transport industry by asking executives in differing regions and industries how they see business prospects in the short and medium term.

With any result above the 0 level being rated as positive – the boundaries each way being +100 and -100 – the present state of the industry was viewed as remaining positive (+6.4), according to the survey’s respondents.

However, the view was markedly different when respondents considered the next three months, in comparison to the previous three-month period; the score was -29.6. The 12-month outlook was rated at a marginally improved -26.5.

From the geographical perspective, China was rated as the most positive market currently, with North America being the most negative. India was seen as being the most positive sector over both the three-month and 12-month period.

Intermodal was rated as being most positive, while road freight and express were the least positive.

“Our new Business Confidence Index shows that although there is a lot of negative sentiment in the market regarding its future prospects, on a global basis the industry is still just about keeping its head above water,” said John Manners-Bell, Transport Intelligence’s chief executive.

“Our survey has shown that some sectors are doing much better than others, such as

Intermodal and Pharma logistics. Developing markets such as China and India are also still good places to be doing business. The Index will provide a monthly update on the state of the industry, allowing companies an insight into the markets, sectors and segments in which they operate," Manners-Bell added.

### **Shipping Outlook – boxfleet**

The number of idled containerships has increased to 392, aggregating 1,100,000 TEUs, or 8.8 per cent of the cellular box fleet, according to a report.

Big ships continue to pile up at Asian anchorages as they end rotations after the expected resurgence orders from China after its New Year did not materialise. Indeed, the prospects dimmed with analysts predicting exports falling by a further 15-20 per cent over 3 months.

This is far worse than the 3.2 per cent of ships laid up in March 2002—the height of the last downturn—said the report, pointing out that this was the worst state of affairs in containership history, more serious than the 5 per cent laid up in 1986 when the entire US Lines fleet, with the world's biggest boxships at the time, was frozen in bankruptcy.

The report also said that an average annual growth of 15 per cent in the container trades over three years would be needed to bring the supply and demand back into balance in 2013.

A more pessimistic view reckons on a 10 per cent annual growth to see normalcy only in 2014.

### **Port Outlook – Middle East**

The speakers list at the recent MEED Middle East Port Development 2009 Conference read like a who's who of the regional port industry and over the two days the delegates were informed of exciting new port developments as well as being given progress reports on current projects by some key players from the industry. Other speakers offered ideas on how to weather the current global financial crisis while being in a good position to take advantage of the inevitable upturn.

Addressing the delegates, MEED conference chairman Edmund O'Sullivan said Gulf Co-operation Council (GCC) countries had to brace themselves for a "short sharp

shock" and that their economies would most likely rebound in 2010 when oil prices rise, international demand increases and the world claws itself out of recession. "It's a bit of a shock, but the region's banks are still prepared to invest in long-term finance," O'Sullivan argued.

The keynote speech was made by DP World's senior vice president for corporate strategy Anwar Wajdi. Wajdi gave a typically bullish address and seemed confident the region's largest port operator would still show growth in 2009. He told the conference that Jebel Ali in Dubai, the company's flagship port, would continue to expand with Terminal 2 coming on stream by the end of February, providing an extra 5 million TEU of capacity and raising the overall port capacity to 14 million TEU.

"We have to tread carefully to see if volumes grow. I'm confident growth will continue even if it's not as big as five years ago, but it could still be in the region of 9 to 10%," said Wajdi. "If we see volumes are holding up, then we will go full throttle, but if things slow down then we will be cautious."

The story of the conference came with the announcement of the new port in Doha by Colin Rudd, vice president of transportation for Cansult Maunsell Limited, the consultants. The project looks set to be one of the largest infrastructure projects in the Middle East over the next decade and a half and with an estimated cost of around US\$7 billion.

Gulftainer's commercial manager Keith Nuttall's presentation provided an overview of the expansion and technical upgrades at Gulftainer-operated Khorfakkan Container Terminal as well as discussing how efficient practices are driving growth, and how working with the supply chain can ensure efficient and effective service for port users. "Lines are using larger container ships of 10,000 and above in order to consolidate shipments and cut down on costs," said Nuttall. "The Middle East region is a major importer, the 'real economy' is sound and infrastructure development is continuing throughout the region, so volumes in the Gulf will continue in 2009 and beyond, although the rate of growth will slow somewhat."

One of the conference's more unusual addresses came from Mahammad Ali Hassenzadeh, the head of investment office ports and maritime organisation Iran. Hassenzadeh called upon the delegates to consider forming partnerships to counter the threats posed by other methods of moving cargo, quoting the success of a similar partnership scheme employed by the ports of Malmo and Copenhagen.

The Red Sea ports dominated the second day of the conference, with guest speakers including Lye Seng Tang from Jeddah Islamic Port in Saudi Arabia and Corne Hulst from DP World's Sokhna terminal in Egypt.

The one disappointment from the conference was the sudden withdrawal of Amer Abdul Jabbar Ismail, the transportation minister from Iraq, who was going to address the conference on the country's infrastructure policy.

### **Piracy update**

The Middle East's biggest story of 2009 so far has to be the release of the Vela owned supertanker the Sirius Star. The images taken by the US Navy of a plane parachuting in a reported US\$3 million ransom were shown across world and again reminded us of the perils currently facing the maritime industry in the Gulf of Aden. The resultant chaos that ensued when six of the Somalian pirates drowned as they made their getaway with the money may have elicited a certain amount of schadenfreude in some quarters, but this only underlines the dangers crews are being exposed to. Ask yourself the question – would you like to be caught in the crossfire when desperate men armed with AK47's are fighting over their share of US\$3 million? What also needs to be remembered is that although it is welcome news that the crew of the Sirius Star is safe and reunited with their respective families, the release of the ship also brought a sharp focus to the many vessels still held in Somalia whose crews aren't quite so lucky. Let's hope that the next couple of months bring a swift resolution that sees all of the ships released and all crews safe and reunited with their loved ones.

**Brain teaser**

If:

$$1 = 5$$

$$2 = 25$$

$$3 = 325$$

$$4 = 4325$$

$$5 = ?$$

Come back with your answers or check the next issue!!.

Pls feedback any views or reactions to Prabhu Williams <dxbgene@owl.ae>