

STUDYING THE CASE OF THE UAE IN ECONOMIC DIVERSIFICATION AND NON-OIL EXPORT GROWTH: PUBLIC POLICY LESSONS FOR AZERBAIJAN

BAHRUZ BABAYEV¹

¹ Azerbaijan State University of Economics (UNEC)

Email: bahruzbabayevs@gmail.com; Tel: (+994 55) 981 06 15

Received 15 February 2019; accepted 24 May 2019; published online 27 December 2019

ABSTRACT

This paper aims to study the experience of the UAE to achieve economic diversification and non-oil export growth for offering public policy recommendations for Azerbaijan based on the following structure. Firstly, it presents the case of the UAE and its success story. Then, it proposes policy recommendations for Azerbaijan. The main finding of this paper is to explain the role of holistic state policies of the UEA in economic success. Along with oil revenues, the economic success in the UAE has been achieved due to economic model chosen by the government of the UAE and public investments in the non-oil sector. It discusses if the same economic policies can bolster non-oil export growth in Azerbaijan. In conclusion, the paper summarizes the main findings.

Key words: Economic diversification, non-oil export, UAE, development, policies, growth.

JEL classification: F00, F01, F55, 038.

INTRODUCTION

Located in the Arabian Peninsula on the Persian Gulf, the UAE is one of the wealthiest and the most economically diversified countries in the world. It is a federation of seven small Gulf States which include Abu Dhabi, Dubai, Fujairah, Ras Al Khaimah, Sharjah and Umm Al Quwain. The country received its independence from the British Protectorate in 1971. Before the discovery of oil in 1958, located on the desert, the Emirates was a disadvantaged country with limited resources (Elhiraika and Hamed, 2002: 2). Traditionally, people in the UAE were engaged in fishing, small trading, pearling extraction and agriculture even though overseas trading was controlled when the country was a part of the British Empire (Elhiraika and Hamed, 2002: 2). As a result, thanks to oil exports, the government of

the UAE could hugely invest in constructing the economy and building the infrastructure.

However, the UEA had a strong reliance on oil exports before the 1980s (Elhiraika and Hamed, 2002: 2). Due to declining and fluctuating oil prices that started in the 1980s, the UAE has started its efforts towards achieving economic diversification and supporting non-oil exports since 1980s (Elhiraika and Hamed, 2002: 2). Since then, the government has started to invest continuously in manufacturing and development of other economic sectors to bolster economic diversification. As of today, the UAE is one of the most diversified economies in the Arabian Peninsula with advanced infrastructure and innovation-based knowledge economy. It is also recognized a great regional centre of transportation, tourism, real estate, entertainment, and shopping (Grant, Golawala, McKechnie, 2007: 507).

In 2020, the UAE diversified its revenues from non-oil exports which cover a diverse range of sectors such as transportation, tourism, construction and manufacturing of semi-processed products. Main non-oil exports of the country include gold, jewellery, diamond, raw aluminium, and cigarettes. The emirates also possess a robust re-export policy. The value of non-oil trade in the UAE was about Dh1.63 trillion in 2018 (Gulf News, 2019). 25 per cent of non-oil exports are gold which has been followed by aluminium and cigarettes (Gulf News, 2019). The Emirates has also chosen a path toward innovation and knowledge-based economy for 2021 and onwards.

Dubai which is a part of the UAE remains a great hub of foreign investment, world-class real estate development projects as well as one of the premier destinations of tourists. Davidson (2005: 5) mentions that the Emirates have suddenly become a “development miracle” due to oil exports. Today, “strategic location, strong financial reserves, large sovereign wealth fund, promising investor home economies, consistent government spending, the progressive policy of economic diversification, free zones and increased foreign direct investment contribute to the UAE’s robust economy” (Government of UAE, no date). Furthermore, it is important to note that oil exports have not been the only factor behind almost all aspects of advancement and development in the region (Davidson, 2005: 5). Also, it was prudent policies, the chosen development model as well as business ties with the Western countries that played a significant role in the diversified economy in the UAE.

THE UAE’S CASE OF ECONOMIC SUCCESS

As mentioned earlier, the UAE is remaining the world’s “eighth biggest oil producer” (Shayah, 2015: 735). “The UAE is an oil-rich nation; 80% of the nation's

revenues were derived from oil sources” (Grant, Golawala, McKechnie, 2007:508). Furthermore, it is one of the most diversified and developed economies in the world. Even though oil exports have played an important role in wealth accumulation in the UAE, non-oil exports have a vital role in economic diversification. Tourism, logistics and transportation, food manufacturing, raw aluminium and gold exports, real estate projects are key non-oil sectors which contribute to the overall well-being and sustainability of the economy. The economy of the UAE is characterized with its openness with a huge annual trade surplus (Shayah, 2015: 736). To understand the factors of success in the development of the economy in the UAE, it is important to analyze its economic development from a historical perspective and review the development policies of its government which resulted in success.

The UAE became independent in 1971. When it gained its independence, the country was suffering from underdevelopment and poverty. In 1968, the country had just 180,000 inhabitants, and main economic engagement of its people was pearling extraction, agriculture, fishing, and controlled foreign trading (Delgado, 2016: 17). Before 1971, the Emirates was a part of the British Empire, and it “was known to the World as the Trucial States” (Delgado, 2016: 23). However, the discovery of oil in the 1950s permitted the UAE to invest the revenues from oil exports in the development of the economy and infrastructure of poor emirates. It was an obvious fact that without the discovery of oil, it would be very hard for the UAE to develop other sectors of the economy. Oil and gas extraction played a crucial role in the rapid development of the economy in the UAE.

Furthermore, Delgado (2016: 32) writes that the progressive development of the economy of the UAE has been associated “with the boom in oil prices between 1973 and 1984” which create an opportunity for the government to increase public savings thereby directing them to the development of infrastructure and diversification of the economy. Furthermore, Delgado (2016: 32) mentions that the UAE did not have to pass through the stages of economic development, but it leapt these stages.

In 2016, the UAE made 298.7 bn USD of the oil and non-oil exports (Societe General, no date). The analysis of the components of these exports in 2016 shows how the UAE successfully diversified its exports. The country received only 12% of revenues from the export of oil and gas. The rest of income of the country is provided with the export of gold products (5.5%), diamonds, (4.3%), jewellery (4.0%), motor cars and other motor vehicles (4.3) and powered aircraft (3.1%) (Societe General, no date). The emirates also receive its national revenues from the export of cigars and cigarettes, unwrought aluminium.

As shown in the official website of the government of the UAE “(By the year 2021), the UAE will benefit from a sustainable and diversified economy, flexible in adopting new economic models, and capitalizing on global economic partnerships to guarantee long-term prosperity for current and future generations of Emiratis” (Government of UAE, no date). The government intends to build knowledge and innovation-based economy in 2021 and onwards with the special focus on the development of a touristic sector and human capital. As it is seen, only 12% of export revenues of the UAE come from oil revenues, and 88% of revenues come from non-oil exports. As mentioned earlier, oil and gas extraction simply enables the government of the UAE to accumulate financial capital to finance the development of other sectors of the economy, but of course, development path chosen by the government also plays a vital role in the diversification of the revenues in the country.

Considering the above-mentioned argument, it is important to present the successful policies of the UAE in economic diversification and deduct public policy recommendations for Azerbaijan which is also recognized as a resource-based economy. It is important to note that “diversification is important to promote economic development, to create job opportunities for a rapidly growing local workforce, but also to reduce or spread the risk of a high economic concentration, which makes an economy vulnerable to external events, such as changes in the price of the dominant commodity” (Schilirò, 2013: 3). Economic diversification also requires the structural transformation of the economy as well as the correctly chosen development model. The following policies are being implemented by the government of the UAE to achieve economic diversification.

“The importance of the UAE in the global arena is a product of its strategic location connecting the east and the west, its liberal and competitive business environment, and the government focus on diversifying from its dependence on oil sources” (Grant, Golawala, McKechnie, 2007:507). It is extremely important to note that the following factors which contribute to the economic success of the state of the UAE is its model of economic development with which most authors in the economic literature agree. Of them, the first factor is the discovery of oil and revenues from energy resources, including oil and gas. Certainly, the revenues contribute to the policy of the government to invest in improving the socio-economic conditions of the population and perform robust infrastructure projects. The second highlighting factor is the adoption of the free market system.

Since gaining its independence, different to most developing economies the UAE has accepted a free market based on “freedom of investment and trade in all fields, and where the private sector plays a leading role in the national economy since the

government's role is limited to formulating macroeconomic policies that reflect the overall strategy of the free economy". It means that the national government maintains its minimal intervention in the economy while "demand and supply determine by prices and investments in the economy" (Omaira, 2001: 2). As a part of its economic diversification strategy of the UAE focuses on turning into one of the most competitive economies of the world (Ahmed, 2015: 55) which an essential component of integration to the world economy (Muradov, Hasanli and Hajiyev, 2019: 1170). "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" (Ahmed, 2015: 49).

Moreover, macroeconomic policies, including fiscal, monetary, trade and investment have played an essential role in the development of the economy of the UAE (Omaira, 2001: 2). The fiscal policy being performed in the UAE is based on rationalizing public spending rather than spending funds for general development, while monetary policy run is based on the strengthening and maintaining the stability of national currency thereby stimulating private and foreign investment (Omaira, 2001: 12-13). When it comes to trade policy, economic diversification policy of the UAE is primarily based on reducing the reliance on oil export, and therefore, the UAE's government have eliminated all tariff-related barriers on the export of non-oil products (Omaira, 2001: 14).

Liberalization of trade has always been a priority for the government of the UAE, and due to this reason, the UAE has joined the World Trade Organization since 1996 (Omaira, 2001: 14). "The leading partners for the UAE nonoil exports were India, Iran, Saudi Arabia, and China. Trade with India represented 21.5% of the nonoil exports and 15.7% of the imports. China imports were second (11.7%), Japan was third (9.8%), and the United States ranked fourth (8.3%)" (Grant, Golawala, McKechnie, 2007:513). Moreover, intending to achieve economic diversification, the government of the UAE encourages private sector investments by providing favourable investment environment, incentives for private investors through a wide range of investment incentives as well as through the establishment of free industrial and trade zones (Omaira, 2001: 14). Privatization is an important component of the economic policy of the UAE, as the state tries to minimize its participation in the main development and real estate construction projects (Omaira, 2001: 15).

Alongside with this, through public funding, the government has made investments in the tremendous development of local and national infrastructure to connect different sectors of the economy (Nyarka, 2010: 7). Thanks to oil revenues, building

an excellent infrastructure in Dubai, it was able to develop a great environment to attract many foreign companies (Nyarka, 2010: 8).

While summarizing all government policies of the UAE, it is important to note that one of the largest oil producers of the world could raise its earliest finance from oil revenues, however, the government policies of the UAE which include huge investments in infrastructure, the adoption of free-market system, its strategy for increasing competitiveness based on knowledge and innovation-based economy, as well as conduction of rational fiscal policy based on efficiency played a unavoidable role in the rapid development and diversification of the economy of the UAE. Coordinated monetary, trade and investment policies while the prioritization of the increasing the national competitiveness of the economy are all contributing factors to increasing non-oil exports of the UAE.

LESSONS LEARNT AND POLICY IMPLICATIONS FOR AZERBAIJAN

Studying the economic diversification policy of the UAE can be a good case study to deduct policy lessons for Azerbaijan. Both Azerbaijan and the UAE have several common similarities. Both countries have experienced rapid economic growth since their independence thanks to oil revenues (Suleymanov, Aliyev, 2015: 40). Both countries have their strategic location, and both countries have a dependence on the export of oil resources. The difference is that while the UAE has successfully experienced the economic diversification, 91% of Azerbaijan's national income still comes from the export of energy resources, even though economic diversification has been chosen as the main development strategy for Azerbaijan too (Azernews.az, 2018). Questionably, what kinds of policy lessons can be deducted for Azerbaijan based on the experience of the UAE on economic diversification, and can policy measures implemented in the UAE can be applied in the case of Azerbaijan.

PUBLIC INFRASTRUCTURE INVESTMENTS

The role infrastructure in economic development is very vital. “Without adequate infrastructure, modern commerce characterized by production specialization and exchange across markets would grind to a halt” (Azam and Abu Bakar, 2017: 630). One of the lessons which can be drawn from the UAE is the massive investments of the government in the development of tremendous infrastructure in the UAE. Investment in infrastructure is an important policy objective for the government of Azerbaijan too (Belt & Road News, no date). The president of the Republic of Azerbaijan Republic Ilham Aliyev has always "stressed that, in general, the creation of modern infrastructure is one of the Azerbaijani government's key goals" (Belt & Road News, no date). It is a good public policy lesson from the UAE too. Even though infrastructure support policy of Azerbaijan overlaps with the UAE, the

government should continue its investments in massive infrastructure projects which is prerequisite to the development of national economy and development.

ADOPTION OF THE FREE-MARKET ECONOMY

Adoption of the free-market economy is key theories of economic development on the eve of the Post-Washington consensus. However, developing countries are cautious about accepting this model as a threat that may destroy their infant industries. The approach also needs the development of technological superiority and business potentials of the country so that its firms and products can be resilient to the global competition. Accepting this model as a policy recommendation will be good for Azerbaijan in the long-run, as it will encourage firms in Azerbaijan to increase their global competitiveness through a quality-based transformation and technological advancements. The approach might be found risky for Azerbaijan as it might destroy local companies and financial system which lack competitiveness, but leads to development in the long-run growth (Baku Research Institute, no date). However, in spite of its riskiness, the approach must be accepted by the Azerbaijani government if it wants to stimulate its firms intending to engage in global trade with its non-oil exports. Furthermore, simplification of export standards must be applied, and all costs associated with the export of non-oil exports must be compensated on the part of the Azerbaijan government. Acceptance of free market model and increasing of competitiveness will facilitate the Azerbaijan's integration to the world economy (Muradov, Hasanli, Hajiyeve, 2019: 1170). Furthermore, it is worthy to note that competition increases the application of technologies and innovations. Almaz and Hajiyeve (2004: 4) argues that "Azerbaijan's economy would be better off if existing uncompetitive sectors could be replaced with competitive new sectors or the expansion of existing competitive ones".

FISCAL, MONETARY, TRADE AND INVESTMENT POLICIES

The free market economy requires not only rationalization and optimization of firm costs but also the optimal implementation of the government's fiscal policy. Funding of development of the sectors with a competitive advantage in Azerbaijan must be a part of fiscal policy in Azerbaijan, while the application of trade policy based on the elimination of all barriers for non-oil exports can be recommendable based on the case of the UAE. Policy lesson from the UAE can also be drawn from the investment policy of the UAE. Trust and simplicity of doing business are extremely important for western investors from the global point of view. Together with country branding, the creation of trust and simplicity of doing business both in its already created industrial zones as well as in the overall country can be very important from the point of view of effective trade and investment policy. Investments in the sectors of the national economy with comparative advantage of Azerbaijan can bolster the

capacity of national exports (agriculture, tourism, small and medium-sized entrepreneurship) in Azerbaijan (Hajiyev, Rasulova, Bakshaliyev and Rzayev, 2004: 2).

ECONOMIC DIVERSIFICATION THROUGH STRENGTHENING COMPETITIVENESS

Economic diversification is important. But, it is also important to strengthen the competitiveness of firms and non-oil export products. Without these firms and products will not be able to compete in the international markets dominated by advanced products and companies. “Under the condition of increasing of globalization and liberalization, raising the competitiveness of the country’s economy is the most important problem. In high globalized and competitive world markets, states have great role in increasing the competitiveness of products”. (Adalat, Hasanli, Hajiyev, 2019: 1070). Development of competitiveness also requires the implementation of institutional reforms, increasing the effectiveness of state bodies and financial openness in Azerbaijan (Babayev, 2015: 87). The development of competitiveness is crucial for the government of Azerbaijan too mentioned in most strategic development papers of Azerbaijan adopted in the recent years. Naturally, the development of competitiveness depends on the global openness of the economy.

DEVELOPMENT BASED ON INNOVATION AND KNOWLEDGE ECONOMY

Economics in the modern world is based on innovation and knowledge-based product development, as well as the development of an innovation base of the economy and research and development. Even though starting from recent years, building a knowledge economy remains important for Azerbaijan too, it is important to strengthen these policies and coordinate it in a more professional way. A well-coordinated state policy is required from this point of view. It must be mentioned that “the establishment of a favourable innovation ecosystem remains an essential policy priority for the government of Azerbaijan as a part of a global trend and requirement of a modern economic system” (Babayev and Hajiyev, 2019: 312, Babayev, 2019:1). However, the policies of the government of Azerbaijan have to be supported by the adaptation of relevant laws and working mechanism in this direction, and international experience must be learnt and applied.

CONCLUSIONS

As a conclusion, it can be deduced that the UAE is one of the countries which became successful in terms of economic diversification and the provision of balance between its non-oil and oil exports. It has been achieved as a result of oil revenues as well as correctly adopted policies of the government of the UAE. Azerbaijan has also enjoyed oil and gas revenues in the past decades. But, it is lagging for its economic diversification despite similar policy objectives are also must for

Azerbaijan. A number of policy implications are deducted for Azerbaijan based on the case of the UAE. Despite the fact that the application of the same policy recommendations cannot have the same consequences for Azerbaijan, but studying the diversification experience of the UAE is useful for the academia and policy-makers in Azerbaijan which the paper tries to highlight.

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