UAE Competitiveness for the Third Millennium: The Role of Government

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United Arab Emirates
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What is Competitiveness?

• Competitiveness depends on the **productivity** with which a nation uses its human, capital, and natural resources.
  – Productivity **sets the sustainable standard of living** (wages, returns on capital, returns on natural resources)
  – It is not **what** industries a nation competes in that matters for prosperity, but **how productively** it competes in those industries
  – Productivity in a national economy arises from a **combination of domestic and foreign firms**
  – The productivity of “**local” or domestic industries** is fundamental to competitiveness, not just that of export industries
  – Relentless **innovation** in technology, products, and organizational methods is necessary to **drive productivity growth** and a rising standard of living

• Nations compete to offer the **most productive environment for business**

• The public and private sectors play **different but interrelated roles** in creating a productive economy
### Sources of Prosperity

#### Inherited Prosperity
- Prosperity is derived from selling **inherited natural resources**
- Prosperity is **constrained** by the limited amount of resources available
- Dutch disease and macroeconomic volatility **undermine** the non-resource economy
- Focus gravitates towards the **distribution of wealth** as interest groups seek a bigger share of the pie

- **Government** is the central actor in the economy as the owner and distributor of wealth
- Resource revenues allow **unproductive policies and practices** to persist
- Resource revenues support **distortive subsidies**

#### Created Prosperity
- Prosperity is derived from **creating valuable products and services**
- Prosperity can only be created by **firms**
- Prosperity is **unlimited**, based only by the innovativeness and productivity of companies and subsidiaries operating in the economy
- Creating the **conditions for productivity and innovation** is the central policy challenge for government

- **Companies** are the central actors in the economy
- Government’s role is to create the **enabling conditions** to foster private sector development
UAE’s Long-Term Economic Performance

Note: 2009 GDP figures are IMF estimates. 2009 Jan-Nov 2009 spot oil price used.
Source: BEA, IMF (2009), Groningen Growth and Development Centre (2009), EIU (2009)

Index Values, 1980 = 1.00

- Total Real GDP
- Real GDP per capita
- Real Oil Price
- Labor Productivity

GDP per Capita
CAGR: -4.56%
CAGR: -0.58%
CAGR: +2.58%

Note: 2009 GDP figures are IMF estimates. 2009 Jan-Nov 2009 spot oil price used.
Source: BEA, IMF (2009), Groningen Growth and Development Centre (2009), EIU (2009)
Determinants of Competitiveness

Natural Endowments
Natural Endowments in the UAE

**Location**
- Position on the trade route between Europe and Asia and access point to the Gulf economies
- Natural basis for a trading hub
- Competing locations with similar advantages
- Infrastructure needed to leverage location

**Natural Resources**
- Large reserves of oil
- Significant financial resources
- Potential for Dutch disease and weak institutions

**Size**
- Small local population and moderate local market
- Mobilize for consensus and action
- Limited ‘natural attraction’ for foreign companies

- Natural endowments create **opportunities or challenges**; the actual **outcomes** depend on the policy choices that countries or regions take in response
Determinants of Competitiveness

- Macroeconomic Competitiveness
  - Social Infrastructure and Political Institutions
  - Macroeconomic Policies

- Natural Endowments
Determinants of Competitiveness

- Macroeconomic Competitiveness
  - Macroeconomic Policies
  - Social Infrastructure and Political Institutions

- Macroeconomic Policy
  - Fiscal policy: public spending aligned with revenues over time
  - Monetary policy: low levels of inflation
  - Macroeconomic management: avoiding structural imbalances and cyclical overheating
Macroeconomic Policy in the UAE
Observations

• The inflationary pressure prior to the crisis revealed the challenges for monetary policy in the context of the US Dollar-peg and the absence of a domestic bond market
  – Monetary policy is one of the few policy areas unambiguously controlled by the UAE level through the Central Bank

• The UAE benefited from responsible management of large oil revenues, but the simultaneous accumulation of foreign debt indicates the challenges for managing fiscal policy
  – Recently created Federal Council to Coordinate Fiscal Policy is a step in the right direction

• Macroeconomic management was effective in stabilizing the UAE financial system in the midst of the crisis, but failed to avert pre-crisis overheating and overleveraging

• A key challenge for the UAE is the institutional architecture in macroeconomic policy
Determinants of Competitiveness

- **Human Development**: basic education and health care
- **Rule of Law**: property rights and due process
- **Political Institutions**: stable and effective political and governmental organizations and processes
# Human Development

## Selected Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>GDP per capita (PPP US$), 2007</th>
<th>GDP per capita</th>
<th>Human Development Index (HDI)</th>
<th>Life Expectancy Index</th>
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Source: World Bank, Human Development Index 2009

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Human Development in the UAE

Observations

Primary and Secondary Education

• **Free provision** of primary and secondary education to all citizens

• High and rising primary and secondary education **completion rates** among the school age population

• **Illiteracy rates** in the UAE are still relatively high
  – A large segment of the expatriate labor force has low levels of education
  – Older generations are significantly less well educated
  – Variations across emirates and gender, with males falling behind

• Little internationally comparable **data** on education quality across the UAE, though some local efforts

• Relative **roles and responsibilities** of government agencies at the UAE and the emirates’ level are unclear

Health Care

• **Free provision** of services to all citizens

• Growing health concerns related to rising prosperity (diabetes, etc.)
### Political Institutions

#### Governance Indicators

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<tr>
<th>Country</th>
<th>GDP per capita (PPP US$)</th>
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Note: Sorted left to right by decreasing average value across all indicators. The ‘zero’ horizontal line corresponds to the median country’s average value across all indicators. Source: World Bank (2009)
Political Institutions and Rule of Law
Observations

- **Solid overall ranking** on rule of law and many indicators of political institutions

- The UAE and its emirates have sought to improve the **legal environment** for business

**However**

- The system of **legal rights** and **government decision making** is often unclear, ad-hoc, and fragmented

- The **dialogue** between government leaders and the private sector exists but lacks openness and supporting institutions

- Existing problems are usually resolved by one-off decisions that **circumvent root causes** instead of addressing them

- This approach was sufficient in the growth period, but has had **significant costs** in the downturn
Determinants of Competitiveness

- Macroeconomic competitiveness creates the potential for high productivity, but is not sufficient.
- Productivity ultimately depends on improving the microeconomic capability of the economy and the sophistication of local competition.
Determinants of Competitiveness

- The external conditions that affect company productivity and the rate of innovation

**Quality of the National Business Environment**

**Macroeconomic Competitiveness**
- Quality of the National Business Environment
- State of Cluster Development
- Sophistication of Company Operations and Strategy

**Microeconomic Competitiveness**
- Social Infrastructure and Political Institutions
- Macroeconomic Policies

**Natural Endowments**
Quality of the Business Environment

Context for Firm Strategy and Rivalry

- Open and vigorous local competition
  - Openness to foreign competition
  - Competition laws
- Local rules and incentives that encourage investment and productivity
  - e.g. incentives for capital investment, intellectual property protection, corporate governance standards

Demand Conditions

- Sophisticated and demanding local customers and needs
  - e.g., Strict quality, safety, and environmental standards
  - Consumer protection laws

Factor (Input) Conditions

- Efficient access to high quality business inputs
  - Efficient utilization of natural endowments
  - Human resources
  - Capital availability
  - Physical infrastructure
  - Administrative and information infrastructure (e.g. registration, permitting, transparency)
  - Scientific and technological infrastructure

Related and Supporting Industries

- Availability of suppliers, supporting industries and institutions, and firms in related fields

- Many things matter for competitiveness
- Successful economic development is a process of successive upgrading, in which the business environment improves to enable increasingly sophisticated ways of competing
# Factor (Input) Conditions

## UAE’s Relative Position 2009

<table>
<thead>
<tr>
<th>Competitive Advantages Relative to GDP per Capita</th>
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<tr>
<td><strong>Communication infrastructure</strong></td>
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<td>Mobile telephone subscribers</td>
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<tr>
<td><strong>Logistical infrastructure</strong></td>
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<tr>
<td>Quality of air transport infrastructure</td>
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<tr>
<td>Quality of roads</td>
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<td>Quality of port infrastructure</td>
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<td><strong>Administrative infrastructure</strong></td>
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<tr>
<td>Burden of customs procedures</td>
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<td>Burden of government regulation</td>
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<tr>
<td><strong>Capital market conditions</strong></td>
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<tr>
<td>Ease of access to loans</td>
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<td>Venture capital availability</td>
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<td>Financing through local equity market</td>
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<td>Protection of minority shareholders’ interests</td>
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<table>
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<th>Competitive Disadvantages Relative to GDP per Capita</th>
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<td>Ease of starting a new business</td>
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<td>Domestic credit to private sector</td>
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<td>Financial market sophistication</td>
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<td>Tertiary enrollment</td>
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<td>Quality of management schools</td>
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<td>Availability of scientists and engineers</td>
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<td><strong>Innovation infrastructure</strong></td>
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<td>Utility patents per million population</td>
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<td>Quality of scientific research institutions</td>
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<td>University-industry research collaboration</td>
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Note: Rank versus 133 countries; overall, UAE ranks 14th in 2008 PPP adjusted GDP per capita and 20th in Global Competitiveness

Logistical Performance Index

Ranking of Financial Centers

Financial Center Score, 2008

Dubai
Rank 24 (=0)

Bahrain
Rank 39 (+10)

Qatar
Rank 47 (+3)

Note: figures in parentheses are change in rank between 2008 and 2007
Source: Global Financial Center Ranking (2008), author’s analysis.
## Doing Business

### Selected Countries

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<tr>
<th>Economy</th>
<th>Ease of Doing Business</th>
<th>Starting a Business</th>
<th>Dealing with Licenses</th>
<th>Employing Workers</th>
<th>Registering Property</th>
<th>Getting Credit</th>
<th>Protecting Investors</th>
<th>Paying Taxes</th>
<th>Trading Across Borders</th>
<th>Enforcing Contracts</th>
<th>Closing a Business</th>
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</table>

Rank out of 178 countries.

## Context for Strategy and Rivalry
### UAE’s Relative Position 2009

### Competitive Advantages
Relative to GDP per Capita

<table>
<thead>
<tr>
<th>Category</th>
<th>Rank</th>
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<tr>
<td><strong>Incentives</strong></td>
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<td>Impact of taxation on incentives to work and invest</td>
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<td>Distortive effect of taxes and subsidies on competition</td>
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<tr>
<td><strong>Openness</strong></td>
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<tr>
<td>Prevalence of trade barriers</td>
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<td>Restrictions on capital flows</td>
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<tr>
<td><strong>Nature of competition</strong></td>
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<td>Intensity of local competition</td>
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<td>Intellectual property protection</td>
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<td><strong>Labor markets</strong></td>
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<td>Pay and productivity</td>
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<tr>
<td>Low rigidity of employment</td>
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### Competitive Disadvantages
Relative to GDP per Capita

<table>
<thead>
<tr>
<th>Category</th>
<th>Rank</th>
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</thead>
<tbody>
<tr>
<td><strong>Nature of competition</strong></td>
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<tr>
<td>Regulatory quality</td>
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<td>Market disruption from state-owned enterprises</td>
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<td>Quality of competition in the ISP sector</td>
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<td>Effectiveness of antitrust policy</td>
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<tr>
<td><strong>Openness</strong></td>
<td></td>
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<tr>
<td>Strength of investor protection</td>
<td>71</td>
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<tr>
<td>Prevalence of foreign ownership</td>
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<tr>
<td><strong>Corporate governance</strong></td>
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<tr>
<td>Strength of auditing and reporting standards</td>
<td>28</td>
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<tr>
<td>Efficacy of corporate boards</td>
<td>17</td>
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</tbody>
</table>

---

Note: Rank versus 133 countries; overall, UAE ranks 14th in 2008 PPP adjusted GDP per capita and 20th in Global Competitiveness

Determinants of Competitiveness

- **Microeconomic Competitiveness**
  - Quality of the National Business Environment
  - State of Cluster Development
  - Sophistication of Company Operations and Strategy

- **Macroeconomic Competitiveness**
  - Social Infrastructure and Political Institutions
  - Macroeconomic Policies

- **Natural Endowments**

- **Sophistication of Company Operations and Strategy**

- The *internal skills*, capabilities, and management practices driving company productivity and the vitality of SMEs and entrepreneurship
Company Sophistication in the UAE
Observations

• The traditional local sector is **weak**
  – Old family groups focusing on retail/wholesale trade, often as local partner of multinationals subject to limits on foreign ownership
• **Entrepreneurship** and new firms play a very limited role
• GLCs are the **dominant** local companies
  – Created recently with a combination of petrodollars and expatriate management
  – Compete largely on operational efficiency and ability to serve to growing local demand, not on strategic positioning
• Foreign companies are focused on **serving local demand**
  – Serve the growing local market
  – Or use UAE as a headquarters to serve the Gulf region due to relatively attractive living conditions for foreign expatriates
  – Virtually no activities serving the broader global market
Determinants of Competitiveness

- The presence of a **critical mass of firms in particular fields**, together with specialized skills, infrastructure, and institutions, that enable productivity through externalities across related firms and supporting services.
# Related and Supporting Industries

## UAE’s Relative Position 2009

### Competitive Advantages Relative to GDP per Capita

- **Depth of clusters**
  - Availability of latest technologies: 8
  - Local supplier quantity: 8
  - Local availability of process machinery: 13

- **Cluster Policy**
  - Extent of cluster policy: 6

### Competitive Disadvantages Relative to GDP per Capita

- **Effectiveness of clusters**
  - State of cluster development: 27
  - Extent of collaboration in clusters: 19

- **Depth of clusters**
  - Local supplier quality: 23
  - Local availability of specialized research and training services: 20

---

Note: Rank versus 133 countries; overall, UAE ranks 14th in 2008 PPP adjusted GDP per capita and 20th in Global Competitiveness

Enhancing Cluster Development
Tourism Cluster in Cairns, Australia

Sources: HBS student team research (2003) - Peter Tynan, Chai McConnell, Alexandra West, Jean Hayden
The Evolution of Regional Economies

San Diego

- Climate and Geography
- U.S. Military

1910
- Bioscience Research Centers

1930
- Hospitality and Tourism
- Transportation and Logistics

1950
- Power Generation
- Aerospace Vehicles and Defense
- Analytical Instruments

1970
- Communications Equipment
- Education and Knowledge Creation

1990
- Sporting Goods
- Information Technology
- Medical Devices
- Biotech / Pharmaceuticals
Clusters and Economic Diversification
Linkages Across Clusters

Note: Clusters with overlapping borders or identical shading have at least 20% overlap (by number of industries) in both directions.
Cluster Development
UAE’s National Cluster Export Portfolio, 1997 to 2007

Change in UAE’s world export market share, 1997 to 2007

UAE’s Average World Export Share: 0.71%

Exports of US$13 Billion =

Change in UAE’s overall world export share: +0.27%

Oil and Gas (4.26%)
$78.3 billion (72% of total)

Jewelry, Precious Metals and Collectibles (2.51%)

Construction Materials

Prefabricated Enclosures and Structures

Motor Driven Products

Aerospace Engines

Metal, Mining and Manufacturing

Marine Equipment

Heavy Machinery

Chemicals

Textiles

Motor-Driven Products

Apparel

Biopharmaceuticals

Automotive

Agriculture Products

Processed Foods

Plastics

Fish and Fish Products

Building Fixtures and Equipment

Entertainment and Reproduction Equipment

Production Technology

Lighting and Electrical Equipment

Footwear / Leather and Related Products

Information Technology

The Dubai Logistics Cluster Map

- Container maintenance
- Ship maintenance
- Aircraft maintenance
- Educational Institutions
- Logistics Services
  - Land transport
  - Handling agents
  - Logistics providers
  - Storage & Warehousing
- Port Operations
- Airport Cargo Operations
- Shipping Lines
- Airlines
- Tourism
- Finance
- Manufacturing (Free Zones)
- Construction
- Cluster Organizations
  - Emirates Freight Forwarders Assoc., Dubai Shipping Assoc.
  - Jebel Ali and Dubai Airport FZ Authorities
  - UAE Customs, other gov. agencies
History of the Dubai Logistics Cluster
Key Developments and Institutions

1959
Dubai International Airport established

1967
Port Rashid build

1975/76
Port Hamriya build

1979
Dubai Dry Dock opened

1983
Jebel Ali port opened

1985
Emirates SkyCargo established

1991
Dubai Ports Authority created

1999
Dubai Ports International created

2006
DP World acquires P&O terminals

2008
Dubai Airport Expansion

Dubai World Central

Expansion

Anchor companies

Infrastructure
Clusters in the UAE
Observations

• Clusters and cluster development efforts exist at the level of individual emirates

• There is significant overlap between cluster efforts within the UAE; collaboration is very limited

• Current UAE’s clusters build on natural endowments, infrastructure investments, and the attraction of foreign firms and talent

• Despite aggressive government efforts, success in creating clusters in areas outside traditional fields has been limited

• Dialogue and active collaboration within clusters is limited, even where there is a significant degree of co-location of activities

• The UAE has made more progress in cluster-based economic diversification than many other oil-driven economies

• However, building a broader portfolio of dynamic, sustainable clusters remains a major priority
The Need for an Economic Strategy

- Implementing **best practices** in each policy area
- There are a **huge number** of policy areas that matter
- No country can or should try to make **progress in all areas** simultaneously

- A prioritized agenda to create a **unique competitive position** for a country or region
Defining an Economic Strategy

National Value Proposition

- What are the distinctive competitive assets of the nation’s economy given its location, legacy, rate of progress, existing strengths and potential strengths?
  - What unique value as a business location?
  - In what types of fields/clusters?
  - What roles with neighbors, the region, and the broader world?

Developing Unique Strengths

- What elements of institutional context and the business environment can be unique strengths relative to peers/neighbors?
- What existing and emerging clusters can be built upon?

Addressing Crucial Constraints

- What are the crucial weaknesses and constraints that must be addressed to achieve parity with peer countries and allow the country to move to the next level?

- Priorities and sequencing are a necessity in economic development
Economic Strategy in the UAE

• The UAE government has in early 2007 announced the government strategy for the coming years, outlining activities and ambitions

• Different emirates have developed their own economic strategies, e.g., Abu Dhabi Economic Vision 2030 and Dubai Strategic Plan 2015

• For economies that are in the process of economic transformation such documents are particularly important as they outline new qualities to be achieved

• These documents also provide important orientation to coordinate the activities of new government agencies that are emerging

• Current strategies focus on aspirations and particular policies, not on specific competitive advantages to be created

• There is insufficient integration of strategies and policies at different levels of government
Geographic Influences on UAE Competitiveness

- Neighboring Countries (GCC)
- UAE
- Emirates
Regions and Competitiveness

• Economic performance **varies significantly** across sub-national regions (e.g., provinces, states, metropolitan areas)

• Many essential levers of competitiveness reside at the **regional level**

• Rules and regulations ensuring open, effective competition, e.g., trade policy, general rules and regulations for business, are best coordinated **across regions**

• Region’s **specialize** in different sets of clusters

• **Cluster strength** directly impacts regional performance

• Each region requires its own distinctive **competitiveness agenda**

• **National policies and investments** can help all regions to be more effective in the competitiveness efforts

• Improving competitiveness requires **effective policy collaboration** between regions and the national government

• Neighboring regions have to find a productive **balance of competition and collaboration** to avoid zero-sum rivalry
Regions and Competitiveness in the UAE

• The large **heterogeneity** in economic size, profile, and performance across the Emirates of the UAE is not untypical

• In terms of economic development, more **cooperation** and coordination across the individual Emirates is required

• Competitiveness-related rules, regulations, and policies are **less aligned** across the UAE than in most other countries

• The federal government needs to strengthen the regulatory and legislation frameworks

• The UAE needs to significantly increase the **transparency of roles and responsibilities** (legal as well as actual) across different levels of government

• The UAE needs to focus more on **coordination** and **integration** across different levels of government
Economic Integration Among Neighboring Countries
UAE’s Neighborhood

- Economic coordination among neighboring countries can significantly enhance competitiveness
- Integration offers greater opportunities than participation in broader economic forums (e.g., EU)
Competitiveness and the Neighborhood

• A nation’s most natural trading and investment partners are its neighbors

• A nation’s competitiveness can be significantly enhanced by economic coordination with neighbors
  – Capturing spillovers in policy and infrastructure
  – Facilitating internationalizing of local firms
  – Specialization in the value chain
  – Attracting FDI
  – Clout in international negotiations

• Economic collaboration among the neighborhood can enhance the effectiveness of domestic competitiveness efforts by helping to overcome domestic political and economic barriers
Regional Collaboration within the GCC

• The Gulf Cooperation Council has made some progress in enhancing regional collaboration

• However, too often policy action has remained significantly behind an ambitious rhetoric that did not acknowledge differences in interests
  – GCC member countries compete in a number of economic development efforts head on (finance, logistics, etc.)

• The traditional approach focused on market integration and is generating decreasing returns

• An effective regional agenda focuses on areas where joint action can enhance national efforts to improve competitiveness
  – Transparent rules and regulations
  – Skill development
  – Data infrastructure
  – Etc.
The Process of Economic Development

Shifting Roles and Responsibilities

Old Model

- The central government drives economic development through policy decisions, spending and incentives

New Model

- Economic development is a collaborative process involving government at multiple levels, companies, educational and research institutions, and private sector organizations

- Competitiveness must be a bottom-up process in which many individuals, companies, and institutions take responsibility and act
Appropriate Roles of Government in Economic Development

1. Establish a **stable and predictable** macroeconomic and political environment

2. Improve the availability, quality, and efficiency of **general purpose inputs, infrastructure and institutions**

3. Establish overall **rules and incentives** governing competition that encourage productivity growth

4. Facilitate **cluster development and upgrading**

5. Convene and actively support a long-term **process for economic upgrading** which informs and mobilizes government at all levels, the private sector, educational and other institutions, and civil society.
Strategic Issues for UAE Competitiveness

Action

• Enhance public availability of data for fact-based policy making
• Upgrade administrative capacity and coordination across government
• Strengthen macroeconomic policy coordination and management
• Leverage clusters to organize economic policy delivery, coordinate government action, and direct diversification efforts
Cluster and Policy Implementation

- Clusters provide a framework for **organizing the implementation** of public policy and public investments towards economic development.
Clusters and Economic Diversification

- Upgrade Existing Export Products and Services
- Turn Products Into Clusters
- Deepen Existing Clusters
- Develop Related Clusters

- Local firms
- MNCs
Strategic Issues for UAE Competitiveness

Action

• Enhance public availability of data for fact-based policy making
• Upgrade administrative capacity and coordination across government
• Strengthen macroeconomic policy coordination and management
• Leverage clusters to organize economic policy delivery, coordinate government action, and direct diversification efforts
• Address remaining weaknesses in the rules and regulations affecting business
• Strengthen the governance of government-linked companies
Transforming the Role of Government

Policy maker, regulator, owner, competitor

Policy Maker

Regulator

Owner

Competitor
Strategic Issues for UAE Competitiveness

Action
- Enhance public availability of data for fact-based policy making
- Upgrade administrative capacity and coordination across government
- Strengthen macroeconomic policy coordination and management
- Leverage clusters to organize economic policy delivery, coordinate government action, and direct diversification efforts
- Address remaining weaknesses in the rules and regulations affecting business
- Strengthen the governance of government-linked companies
- Launch an aggressive effort to enhance private entrepreneurship
- Focus on skill development for the local population, addressing both the supply and demand for high-quality education

Process
- Clarify the role and responsibilities of the different levels of government within the UAE
- Improve transparency of the policy process and legal system
- Strengthen platforms for public-private dialogue and give them a clear role in the policy process
UAE Competitiveness: Entering the Next Stage

• Within less than one generation, the UAE has transformed its economy and competitiveness

• The UAE’s competitiveness agenda reflects the new demands at the level of development reached

• The crisis exposed some of the structural weaknesses that threaten further development; it is not a sign that past progress was an illusion

• At this junction, the UAE needs a new set of policies and institutional structures to succeed