

The Business Model of the United Arab Emirates

Challenges and Opportunities

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The United Arab Emirates (UAE) are a young nation, gaining independence in 1971. Although it has only about 10 million inhabitants, the country is the eighth-largest petroleum producer worldwide, supplying about 4 percent of the world's oil, as well as the fifth-largest natural gas producer (although the country has been a net gas importer in recent years).

Economic Strategy

Post-Oil Transition

Oil and gas often lead to a “resource curse”, resulting in an overbearing mining industry, inflated public sector, low growth, high volatility, and low investment in human capital. The UAE started early to combat these problems and has fared comparatively better than most resource-rich countries. The federal government has strived for decades to move from a value-extraction economy to a value-creation economy by accelerating economic independence from natural resources and adapting successful models like the Singaporean and Chinese economic transitions.

Like other countries in the region, the government has announced its policy plans in various “Visions”, most prominently in the [UAE “Vision 2021”](#), built around massive infrastructure investments, improved labour productivity through education, a business-friendly environment, and a push for industrial diversification. With a native population of less than one million citizens, large numbers of migrant workers and highly skilled “expats” have been recruited to help achieve these goals.

Education

The UAE maintains a dual system of education. Public education is free for Emirati citizens, including higher education at public universities. Importantly, there is also a large private education sector, [both in K-12](#), with English language education and pricier schools offering Western curricula, and higher education. In fact, the UAE has the highest concentration of international branch campuses, including New York University, the Sorbonne, and the University of Birmingham.

While the Ministry of Education is the umbrella body that oversees education – both public and private – some emirates have their own governing bodies that provide licensing and accreditation for private education, such as the Abu Dhabi Education Council and the Knowledge and Human Development Authority in Dubai.

Economic Freezones

These private universities operate in economic freezones. Specialised freezones exist for multiple sectors, including trade, IT, higher education, scientific research, and ecommerce. They offer foreign companies and investors a business-friendly environment with 100% foreign ownership, streamlined administrative procedures, tax exemption, low regulation and legal independence from the host country. The freezone strategy is partly responsible for the UAE's regional leadership in attracting foreign direct investments, with an FDI net inflow of 5.5 percent of GDP in [2020](#).

Foreign Labour

Freezones are the main drivers of private-sector activity, which rests in large part on foreign labour. Emiratis only make up about 10-12 percent of the country's population (the lowest percentage globally) and are mostly employed in the public sector, where many jobs are reserved for Emirati citizens. The majority of the workforce are migrant labourers, mostly from South Asia, working in low-skill jobs including construction, logistics, gastronomy, household help, and agriculture. Global talent is recruited to fill high-skilled jobs in sectors such as law, consulting, finance, IT, higher education and higher management. Until recently, the stated intention was to upskill Emirati citizens to gradually replace skilled expatriate workers, a process called "Emiratisation" (similar policies exist in all GCC countries). However, the UAE has since adopted a new outlook of [naturalising](#) global talents instead of emiratising positions as a means to address the presumed deficit.

Economic Diversification

The end goal of all these policies is to modernise the economy and untether it from natural resources. The government's industrial policy has been targeting several key sectors: construction, logistics and trade, tourism and meetings-incentives-conferences-exhibitions (MICE), and finance.

Megaprojects

Megaprojects and a vast array of suburban and exurban neighbourhoods are the most visible signs of the construction boom in the UAE. Construction is thus a means to attract tourists, expatriates, and foreign companies to the country, a [strategy](#) dubbed "build it and they will come".

Tourism

The most prominent use of these construction projects is tourism, as exemplified with the Instagram icon Burj Khalifa, sports venues like the Yas Marina Formula One circuit, cultural venues like the Louvre Abu Dhabi, the Museum of the Future, mega indoor theme parks, and the Expo 2020, which will soon be [repurposed](#) to host the COP28 in 2023. As a result, Dubai International has been one of the busiest airports for international flights, and tourist spending has been steadily increasing, at least until the Covid-19 pandemic. Luxury residential megaprojects like Palm Jumeirah and The World and high-end shopping malls cater to global high net worth individuals (HNWIs) as part-time residents.

Trade and Logistics

The UAE are a natural transportation hub due to both the trade in oil and gas and the tourism industry. Besides aviation, the country also has some of the world's largest ports and serves as an entrepot for international logistics. This sector also has some of the most internationally active companies, such as DP World and Dnata.

Finance

As a regionally leading business hub, the UAE has also emphasised growth in the finance sector, with a large number of banks and several stock exchanges in Dubai and Abu Dhabi.

Technology

Many recent projects have tried to shift towards high-productivity industries, including IT, media, and technology. These projects include freezones such as Silicon Oasis and Media City, as well as the Arabian Peninsula's only nuclear powerplant and one of the world's largest solar parks. The UAE has recently launched a space programme that has sent an astronaut to the International Space Station (ISS), as well as a space probe to Mars.

Sovereign Wealth Funds

A significant part of oil income goes to the UAE's Sovereign Wealth Funds (SWFs), most notably the Abu Dhabi Investment Authority. These, in turn, serve multiple functions, such as state finance, financing domestic investment projects, and managing a large portfolio of international asset holdings. As such, returns from their endowment are [another important factor to gain independence from oil income](#).

Challenges and Threats

The Stickiness of Oil

While all these attempts at diversification have seen notable successes, oil still looms large over the economy. Oil rents as a percentage of GDP have fluctuated over the decades but are not appreciably lower today than in 2000. In fact, the absolute amount of oil produced is still increasing, and the government recently [announced](#) a \$5 billion investment into additional drilling infrastructure.

This has important consequences for the economy: economic growth is still tightly correlated with the highly volatile price of oil, and large public sector companies still dominate the business landscape.

Unemployment

The public sector is currently proving essential as the country is currently experiencing an [unemployment](#) crisis among young Emiratis. Youth unemployment is a pervasive problem in the region, not least because of the “youth bulge” as the country is going through a demographic transition and because of increased female labour-market participation.

Emiratisation is also proving difficult. As with previous such efforts, Emiratis are finding that they have difficulty accessing the private sector, as private businesses are reluctant to pay a premium for nationals. In addition, both regional K-12 and higher education institutions, particularly public ones, still [lag](#) in international rankings, which makes their degrees less marketable. As a result, the government periodically issues compulsory quotas for citizens, but these often lead only to “phantom employment”. The repeated invitations for foreign talent to make the UAE home has further exacerbated the unemployment situation for Emirati youth, many of whom are not equipped for an increasingly competitive job market.

Earlier this year, the UAE introduced a [new visa](#) for job seekers and graduates of top international universities to explore opportunities in the UAE. This promises to make the UAE a destination for global talent, potentially becoming a hub for investors and start-ups who will be reliant on such talent.

Public Finance Transition

The post-oil transition is also proving difficult because it entails a shift from resource-rent-based public finance to a tax-based one. We are already seeing the beginnings of this transition with the introduction of value-added tax and corporate tax (from June 2023), as well as debt: Dubai has a [150 percent debt-to-GDP ratio](#) (including state-owned enterprises). We also see the beginnings of austerity measures.

The introduction of taxes and the reduction of the welfare state are never well-received by citizens. The lack of taxes has also been one of the major attractions for both businesses and wealthy individuals. The introduction of a corporate tax (depending on how much it will be enforced) may reduce the attractiveness of the country as a business hub, and the potential introduction of income tax, albeit necessary, may potentially do the same for HNWIs.

Sluggish Productivity

A third reason why oil is still such a large economic factor is the lack of highly productive sectors to replace it. Most labour in the country is low-skilled and many of the alternative industries such as tourism, construction and household services all have low to middling value added. As a consequence, [real GDP per capita has fallen by 35 percent since 2000](#).

Although there have been efforts to increase labour productivity, notably through higher education and attracting global talent, challenges remain, one being the overbearing public sector. While there have been many IPOs of state-owned companies in the region (most spectacularly Saudi Arabia's Aramco), these offerings are always partial and never give up state control.

The Gulf region lags both in public and private R&D, as [evidenced](#) in the low output in intellectual property. Most universities in the UAE are teaching-oriented and lack the staffing (research assistants, PhDs, postdocs) and infrastructure for research. Without an ecosystem of research facilities, it is difficult

to attract top global researchers. Additionally, there is no national science foundation like the American NSF that could coordinate and promote research on a national scale. Without this public research ecosystem, it is proving difficult to attract corporate R&D to the region. But scarcity is always an opportunity, which may become another selling point for the UAE.

Regional Imbalances

The UAE is a federation of seven emirates that differ wildly in area, population, urbanisation, and economy. Abu Dhabi is the largest emirate, with 87 percent of the country's surface area, and 86 percent of its oil reserves. The city of Abu Dhabi is also the country's political capital and the emirate's ruler, Sheikh Mohammed bin Zayed Al Nahyan, is also the president of the country.

Dubai is the second-largest emirate but has the largest population. Due to its relative lack of oil reserves, the emirate was also instrumental in the economic transition towards non-oil industries. Dubai and Abu Dhabi also host most of the country's foreign residents.

The remaining five emirates collectively make up 8 percent of the area and 32 percent of the population. The northern emirates are largely rural, less cosmopolitan and less economically developed.

The country's politics and economy thus revolve around the two poles of oil-rich, politically dominant Abu Dhabi and the cosmopolitan business hub Dubai, with the remaining emirates largely dependent on federally allocated budgets.

Competition

Another quickly developing challenge is competition between different Gulf states, all of which are trying to move into similar industries. Most notably, the UAE's [larger neighbour Saudi Arabia](#) has launched a grand strategy to boost their tourism sector, promoting their flag carrier airline as a rival to Dubai's Emirates. They are also expanding their stock exchange, Tadawul, and are planning their own mega-project, NEOM. Even more directly, the Saudi government is trying to [push](#) foreign companies to relocate their regional headquarters to Saudi Arabia, a move directly aimed at Dubai.

Another regional rival is Qatar, which is flush with funds from natural gas (which it also exports to the UAE through the Dolphin pipeline), and is a serious contender in terms of prestigious international branch campuses with Carnegie Mellon, Georgetown, Northwestern University and HEC Paris, as well as a rival in international mega-events with the 2022 World Cup.

Globally, there is intense competition from successful countries like Singapore and South Korea, which have developed similar industries and outperform the UAE in terms of productivity, R&D and foreign direct investment.

Sector-Specific Issues

Some of the sectors championed in the UAE offer opportunities for improvement. For example, both the finance and the construction industry have profited from the UAE's status as an offshore finance hub and a tax haven.

High-networth and ultra-high-networth individuals from countries like Russia and China are seeking stability in the UAE, which they cannot find in their home countries. For the moment, they confine their activities mostly in buying real estate, but, in the medium term, their capital and business acumen could flow into future-oriented investment projects.

The UAE's stock exchanges have also seen growth challenges due to a lack of private companies. Partial IPOs of state-owned companies have so far proven insufficient to push ahead of regional and global competitors, and there were even several prominent de-listings.

Other sectors seem to have hit limits to their growth, too. In tourism, visitor numbers have stagnated since 2017; new infrastructure is sitting idle, including mega-projects like Palm Jebel Ali and Deira Islands.

Ways Forward

The UAE is part of the six-country Gulf Cooperation Council (GCC). The GCC was conceived to stimulate the regional economy through integration. Unfortunately, not much has come to fruition; a common currency was shelved, a common patent office was closed, and [construction for a regional highspeed train network](#) is not getting ahead. Moreover, as mentioned above, the constituent members, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates, are locked in an internecine economic rivalry. But the GCC could be revived as a venue to stop this race to the bottom and instead foster cooperation in domains such as research, education and green growth.

As stated in the UAE's Vision 2021, a "first-rate education system" and a "competitive knowledge economy" are crucial. To achieve this, the UAE needs a nationally coordinated R&D strategy, with a national science foundation and an ecosystem of research universities and research-focused private companies. This would also include a fundamental overhaul of the education system, from kindergarten to higher education, to provide the locally-grown knowledge workers necessary to move past oil. This presents an opportunity to global partners to tap into a niche market, and foster collaboration in research of common and global interest.

Finally, the UAE could stay ahead of its neighbour's vision. Saudi Arabia's "Vision 2030" aims at "building an effective, transparent, accountable, enabling and high-performing government." Administrative and overall reforms to ensure transparent and efficient governance, rule of law and low institutional uncertainty are key drivers of growth and prosperity.

Opportunities for Cooperation

The new [agreement](#) between the UAE and Germany on the fossil energy market could become the catalyst for developing the many opportunities for mutual benefit between the two countries. For example, Germans are a still relatively untapped market for the tourism hubs of Dubai and Abu Dhabi compared to other Western countries. And while the UAE hosts branch campuses from the United States, the UK, France and Australia, there are to date none from Germany.

In 2008, the Mohammed bin Rashid Al Maktoum Foundation [hosted](#) the Arab-German Cultural Dialogue, cultivating an appetite for common understanding and cultural exchange. This momentum was, however, interrupted by a global recession that shifted focus from public diplomacy initiatives. The new agreement between the UAE and Germany could hold potential for other forms of partnerships, particularly pertaining to education, culture and research.

Many of Germany's research-focused universities and STEM-heavy institutions may be excellent candidates for boosting the UAE's R&D ecosystem. Germany's private sector, with many technology and manufacturing SMEs (the famous "Mittelstand"), could find regional growth markets, an attractive base for their MEA business, and even open local production and development sites.

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