UAE

A strong rebound in tourism, buoyant real estate demand, high oil prices and rising oil output have helped deliver strong economic growth this year and although an easing is seen in 2023, our base case is for a further solid expansion of 3%. The positive medium-term outlook is reinforced by plans by ADNOC to ramp-up oil production capacity to 5 mb/d potentially to an accelerated time schedule. Downside risks include exposure to slowing global growth, tightening financial conditions, and a loss in competitiveness due to the strong dirham. The main upside risk would be higher oil prices lifting regional growth, optimism and liquidity.

Slower but still solid growth expected for 2023

GDP growth this year is expected to reach its strongest since 2016 at 5.3%, and although a slowdown is projected for 2023 underlying economic performance should remain solid, building on the UAE's position as a leading hub for regional business activity and investment, strong infrastructure, the government's pro-growth reform initiatives and plans to ramp up capacity in the hydrocarbon sector. Oil GDP is forecast up 8.7% this year reflecting OPEC+ production policy and a more modest 1.7% in 2023, which would leave oil output at 3.1 mb/d by next year-end. (Chart 1.) State oil firm ADNOC has reportedly brought forward plans to expand capacity to 5 mb/d (from 4 mb/d currently) to 2025 versus 2030 before, reflecting a desire to monetize oil and gas reserves more quickly ahead of the global energy transition. This goal looks ambitious, but the potential acceleration of its five-year $127 billion investment program (which covers both upstream and downstream sectors) provides a significant upside risk to the medium-term growth outlook.

Meanwhile, non-oil GDP enjoyed a post-Covid bounce to 8.8% y/y in 1Q22, taking output back above pre-pandemic levels. While this strength will not be sustained, the PMI activity gauge has drifted higher this year, reaching a three-year best of 56.7 in August signaling robust expansion despite sluggishness in export conditions. Supportive factors include a strong rebound in tourism, spillovers from the upcoming World Cup in Qatar, rising real estate demand, and high oil prices. We see non-oil growth at 4% overall this year. Slowing global growth, lower (though still high) oil prices and rising interest rates point to a softer performance in 2023, though our base case is still for a decent 3.4% expansion. Key strategic policy initiatives driving the medium-term outlook include the 'Circular Economy Policy' 2021-31 to encourage sustainable use of natural resources, the 'Digital Economy Strategy' aimed at doubling the sector's GDP contribution to 19.4% in 10 years, and 'Operation 300bn', which looks to double the industrial sector's GDP to AED 300 billion by 2031 especially via SMEs.

CPI inflation and house price rises to ease next year

Strong demand, supply chain disruptions, rising food and oil prices and a recovery in housing rents pushed inflation in Dubai to 6% y/y in August and 4.5% in the first 8M22 (up to date nationwide figures were not available). However, given the softer growth outlook, declining input costs, strong dirham and rising interest rates (the central bank has matched aggressive Fed policy tightening so far this year), we expect inflation to ease going forward and average 3.8% in 2022 and 3.6% in 2023 for the UAE overall. (Chart 2.) Residential real estate demand remains strong for prime properties with the large influx of investors, especially from Eastern Europe, helping push prices up 1.8% and 10.8% y/y in 1H22 in Abu Dhabi and Dubai, respectively. (Chart 3.) Demand next year could soften as this influx fades, interest rates rise and growth slows, and together with rising supply (a yearly average of 40,000 units, or 4.3%, in 2022 and 2023) will take some heat out of the Dubai market, leading to smaller price rises. Meanwhile, private sector credit growth has recovered to pre-pandemic levels this year, and the central bank's survey shows firms' lending demand at strong levels in Q2, with property and construction firms doing well though showing signs of softening looking forward. (Chart 4.)

Fiscal surpluses provide room for increased spending

The overall fiscal position remains solid, with the government recording only one relatively modest annual deficit (2.5% of GDP in 2020) through the pandemic period and now set to post large surpluses in 2022 (8.9%) and 2023 (6.4%). (Chart 5.) Key to this has been spending control, with cuts in both (non-wage) current and capital spending seen during the pandemic, the recovery in oil prices but also revenue diversification, which has limited the downside from volatile oil receipts. We project spending increases averaging 5% in 2022-23, covering wages and social welfare but also capital spending to support government-led initiatives. Aside from still-high oil prices, revenues will be boosted by the 9% tax on corporate earnings set for introduction in June 2023, yielding estimated annual receipts of 1.5-2% of GDP. The external accounts meanwhile are very strong, with the current account in persistent large surplus and the huge combined SWF assets of ADIA and Mubadala (estimated at around $1 trillion) providing a buffer against external shocks.

Outlook and risks

Despite this broadly positive base case picture, risks are skewed to the downside including the UAE's relatively high exposure to a potentially sharp slowdown in global growth, tighter financial conditions, the impact of dirham strength on competitiveness and inward investment, debt rollover at GREs and a flare up in regional geopolitical tensions. The main upside risk would be higher oil prices lifting regional growth, optimism and liquidity.

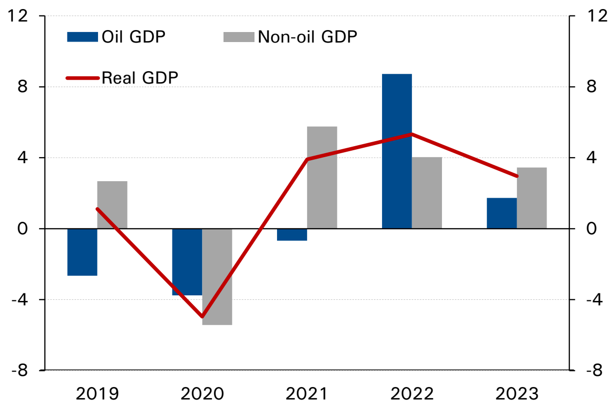
Table 1: Key economic indicators

		2019	2020	2021e	2022f	2023f
Nominal GDP	$ billion	418	349	415	487	482
Real GDP	% y/y	1.1	-5.0	3.9	5.3	3.0
- Oil sector	% y/y	-2.6	-3.8	-0.7	8.7	1.7
- Non-oil sector	% y/y	2.7	-5.4	5.8	4.0	3.4
Headline inflation	% y/y	-1.9	-2.1	0.2	3.8	3.6
Budget Balance	% of GDP	2.6	-2.5	4.1	8.9	6.4
Current act. balance	% of GDP	8.9	6.0	11.6	21.0	14.2

Source: Official sources, NBK estimates.

Chart 1: Real GDP

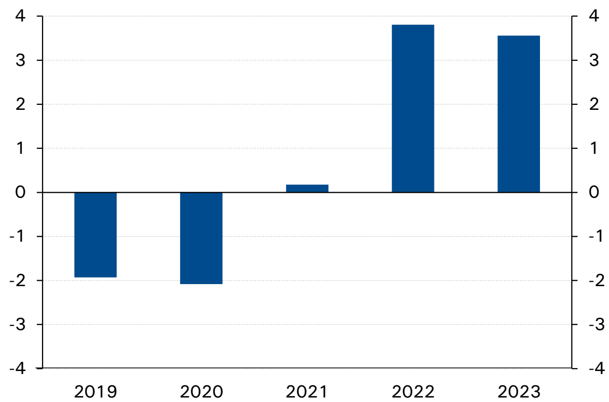
(%, y/y)



Source: Federal Competitiveness & Statistics Centre (FCSC), NBK estimates

Chart 2: Headline inflation

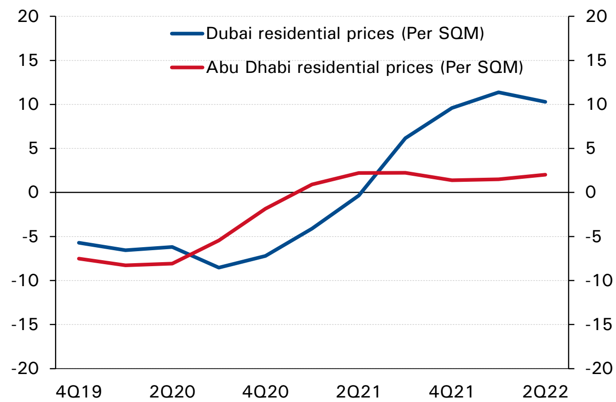
(%, y/y)



Source: FCSC, NBK estimates

Chart 3: Abu Dhabi and Dubai residential prices

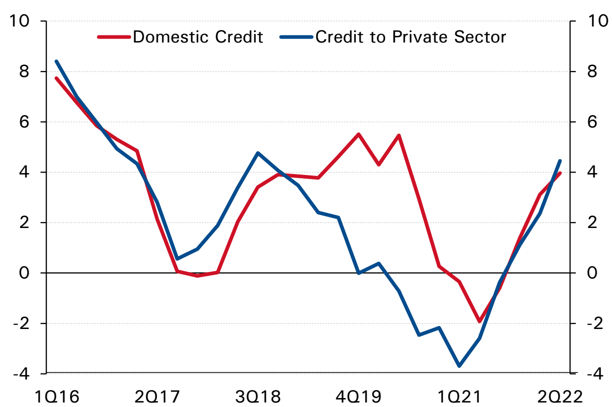
(%, y/y)



Source: Bank of International Settlements

Chart 4: Credit growth

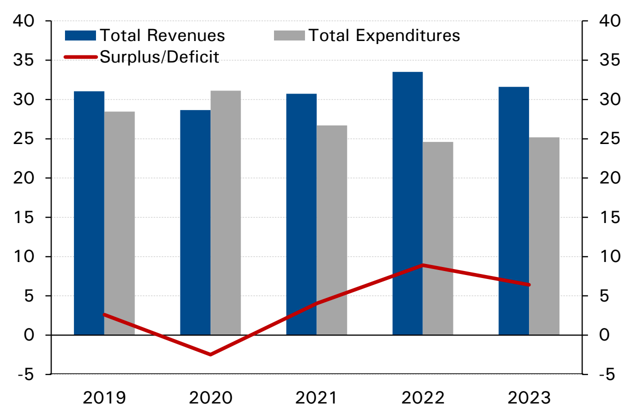
(%, y/y)



Source: Central Bank of UAE

Chart 5: Fiscal balance

(% of GDP)



Source: Ministry of finance, NBK forecasts