UAE

Economic activity is expected to improve as non-oil growth could reach 1.7% in 2020-22 from an estimated 1% in 2019, while inflation would have a soft rebound in 2020 before rising to 2.4% in 2020-22. Accommodative monetary policy, fiscal stimulus, and pro-investment reforms and good business environment will help support non-oil activity. Oil revenues will remain subdued in the medium term, leading to narrower current account surpluses. The resilience of the UAE economy should help weather downside risks represented by prevailing geopolitical tensions, lower oil revenues, and weakened external demand.

Economic growth supported by the oil sector

Economic activity in the UAE will remain resilient over the forecast period, despite the expected continuation of crude production caps related to the OPEC+ agreement and lower energy demand, which may offset the impact of upstream investments. Growth in the oil sector is projected to reach, 2.2%, on average, during 2020-22. In contrast, the non-oil sector is expected to grow by a moderate 1% in 2019 before accelerating to around 1.8% in 2020-21 as EXPO 2020 boosts the tourism and retail sectors and as the effects of fiscal stimulus and reforms begin to be realized. Non-oil GDP growth is expected to slow down in 2022, declining to 1.5% in 2022 as the impact of Abu Dhabi's stimulus package and EXPO 2020 diminishes. (Chart 1)

Real Estate sector is still suffering

The UAE real estate market is still witnessing a correction as property prices are adjusting to the increased supply (Chart 2). The fall in property prices, which started in 2015, is expected to stabilize in the medium term with the establishment of a new committee to regulate the pace of real estate projects. Recent initiatives to cut transactions costs, and the expectations of interest rates remaining relatively low could provide some support and prevent further declines over the medium term.

Inflation is likely to have a soft rebound in 2020

The UAE has been in deflation territory in 2019. However, the expected pick-up in demand as EXPO 2020 draws nearer, and the impact of the new excise taxes, effective in December 2019, should help inflation gain more momentum. On the other hand, domestic fuel prices are expected to remain subdued in the medium term due to weak oil prices. Therefore, inflation is expected to average 2.4% in 2020-22. (Chart 3)

Looser monetary policy to support the private sector

The shift in the Federal Reserve's monetary stance during 2H19, which was followed by a reduction in the domestic interest rates since the UAE dirham is pegged to the US dollar, should reduce the private sector financing costs. The decline in interest rates should provide more support to public sector, personal and businesses' credit demand, and lower their debt service burdens. Despite the economic slowdown, credit conditions to remain supportive with some tightening related to collateral requirements on real estate loans and premiums charged on riskier loans. Domestic credit growth is expected to be average about 4% in 2020-22, supported by the demand of Government-Related Entities (GREs) and large firms. (Chart 4)

Solid fiscal position despite subdued revenues

Government revenues are expected to weaken from 29.2% of GDP in 2019 to 28.0% of GDP in 2020-22 due to softer oil prices and government measures that aimed at reducing doing business costs and improving the investment framework. On the other hand, total expenditures will rise in 2019-21 on government's plans to boost economic growth. Thus, the budget deficit is expected to widen to an average of 3.2% of GDP in 2019-22 (Chart 5). However, the fiscal position remains strong due to large buffers and sufficient fiscal space.

Slower global growth, subdued oil prices and regional geopolitical tensions will lead to a narrowing of the current account (CA) surplus in the medium term, from 8.8% of GDP in 2019 to about 6.5% of GDP in 2020-22. On the other hand, government reforms will improve the business environment in the medium term and increase FDI flows to the UAE.

Favorable outlook with some downside risks

UAE favorable business environment (ranked 16th in the World Bank's ease of doing business index), aided by recent pro-investment reforms, well-developed infrastructure, and strong banking sector make the UAE one of the most desirable destinations for FDI in the region.

However, downside risks— global growth uncertainties, regional geopolitical instability and weakened external demand—could limit non-oil economic growth. These risks have weighed on GREs—, which constitute a large share of the business sector—revenue streams. Lower interest rates may relieve some of GRE's debt-servicing pressures in the short-term, but the risk of overcapacity post Expo 2020 may strain their balance sheets.

In addition, the continued decline in real estate prices lowered banks' collateral quality and led to higher provisioning and lower net interest income. The establishment of a new committee to regulate the real estate sector as well as the central bank's recent efforts to limit bank exposures to real estate sector may help in managing these risks over the medium term.

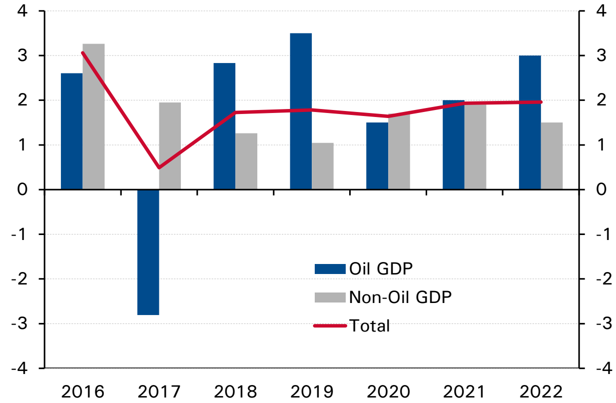
Table 1: Key economic indicators

		2018	2019e	2020f	2021f	2022f
Nominal GDP	% y/y	414	409	419	440	466
Real GDP	% y/y	1.7	1.8	1.6	1.9	2.0
- Oil sector	% y/y	2.8	3.5	1.5	2.0	3.0
- Non-oil sector	% y/y	1.3	1.0	1.7	1.9	1.5
Budget balance	% of GDP	-1.8	-2.5	-3.8	-4.1	-2.6
Current act. balance	% of GDP	9.1	8.8	6.4	6.1	7.0
Headline inflation	% y/y	3.1	-1.9	1.4	2.5	3.5

Source: Official sources, NBK estimates

Chart 1: Real GDP

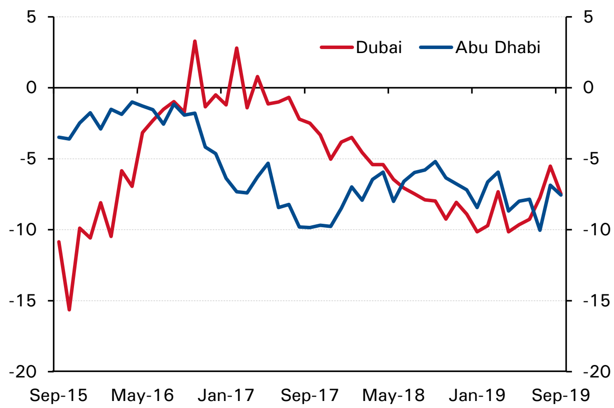
(% y/y)



Source: UAE Federal Competitiveness & Statistics Authority, NBK estimates

Chart 2: Abu Dhabi and Dubai residential property prices

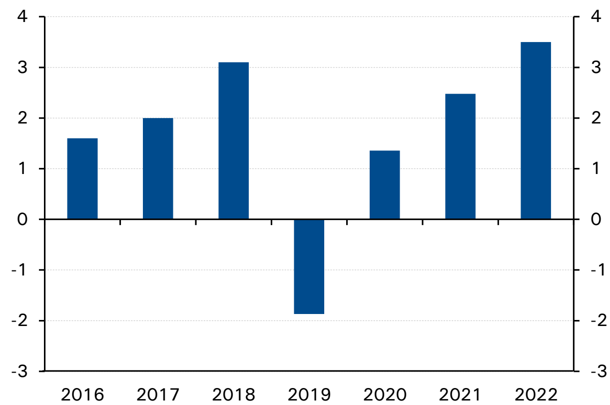
(% y/y)



Source: BIS

Chart 3: Headline Inflation

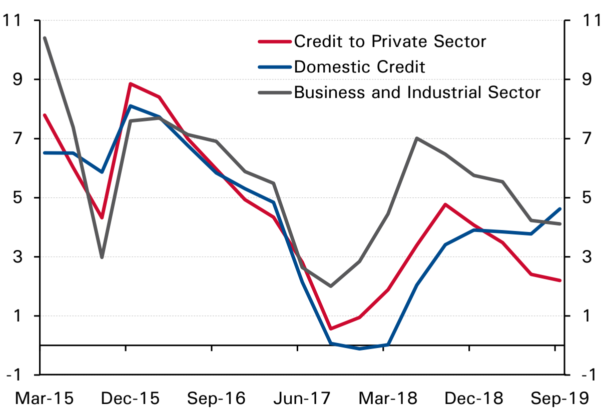
(% y/y)



Source: UAE Federal Competitiveness & Statistics Authority, NBK forecasts

Chart 4: Domestic and Private Sector Credit

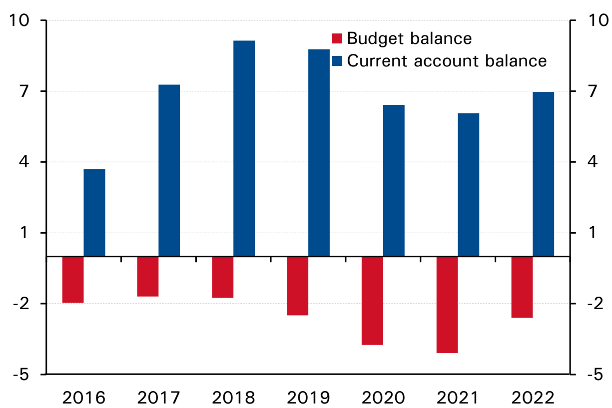
(%, y/y)



Source: Central Bank of the UAE

Chart 5: Current Account and Budget Balance

(% of GDP)



Source: Central Bank of the UAE, IMF, NBK forecasts