



UNITED ARAB EMIRATES

2012 ARTICLE IV CONSULTATION

May 2012

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2012 Article IV consultation with United Arab Emirates, the following documents have been released and are included in this package:

- **Staff Report** for the 2012 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on March 14, 2012, with the officials of United Arab Emirates on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on April 27, 2012. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- **Public Information Notice (PIN)** summarizing the views of the Executive Board as expressed during its May 14, 2012 discussion of the staff report that concluded the Article IV consultation.
- **Statement by the Executive Director** for the United Arab Emirates.

The document listed below has been or will be separately released.

Selected Issues Paper and Statistical Appendix

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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UNITED ARAB EMIRATES

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION

April 27, 2012

KEY ISSUES

Context. The UAE economy is gradually recovering from the 2009 crisis. The banking sector was strengthened through significant capital injections, and some progress has been made in restructuring the debt of government-related entities (GRE). The ailing real estate sector is beginning to find bottom but, given the ongoing oversupply, an early and broad-based recovery of the sector remains unlikely.

Outlook and risks. The recovery of the nonhydrocarbon economy, however, looks set to continue this year, backed by strong trade, tourism, logistics, and manufacturing, and helped by high oil prices. With limited near-term potential for further increases in real oil production, overall GDP growth is expected to moderate to 2.3 percent. Downside risks relate to a possible increase in regional geopolitical tensions, a potential decline in oil prices, a renewed worsening of global financial conditions, or a marked slowdown in Asia.

Macroeconomic policy mix. The UAE plans a gradual fiscal consolidation this year which will help unwind the fiscal stimulus of recent years and lower the currently high fiscal breakeven oil price without undermining the economic recovery. The planned fiscal consolidation will also increase the room for maneuver in case the downside risks materialize. Monetary policy will stay appropriately accommodative under the U.S. dollar peg.

Government-related entities. The GREs continue to face financial challenges in light of their high debt and rollover needs. Further deleveraging and strengthening of impaired GRE balance sheets is needed. Improving GRE corporate governance and increasing transparency about their financing strategies, financial conditions, and debt profile would be important to strengthen market confidence. Channeling bank funding to non-viable GREs should be avoided.

Financial stability. The banking system maintains significant buffers to withstand a further deterioration in asset quality and external liquidity conditions. The central bank should nonetheless continue to closely monitor banks' liquidity and capital buffers as individual banks could be affected if downside risks materialize.

Statistics. Effective policymaking is contingent on timely and accurate data, rendering further improvements in the statistical framework important.

Approved By
Alfred Kammer;
David Marston

Discussions were held in Abu Dhabi during February 28–March 14, 2012. The staff team comprised Harald Finger (head), Ananthakrishnan Prasad, Zsofia Arvai, Gohar Minasyan (all MCD) and Jiri Jonas (FAD). The team met with H.E. Minister of State for Financial Affairs Obaid Humaid Al Tayer, H.E. Minister of Economy Sultan Bin Saeed Al Mansoori, H.E. Governor of the Central Bank of United Arab Emirates Sultan Bin Nasser Al Suwaidi, and other senior officials and representatives from the business and financial community. Taline Koranchelian (SPR) and Alfred Kammer (MCD) joined for parts of the mission.

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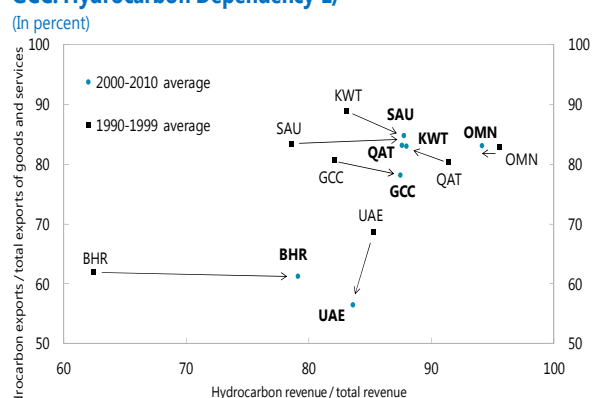
BACKGROUND

1. **Following the 2009 crisis, the economy has been slowly recovering and repairing its balance sheets.** The Dubai World debt restructuring was completed, but several other troubled government-related entities (GRE) are still in the process of restructuring. The authorities strengthened the banking sector through liquidity support, recapitalization, and deposit guarantees, and the emirate of Abu Dhabi provided financial support to the emirate of Dubai. The Dubai Financial Support Fund (DFSF) was called to support troubled entities in the emirate and has now almost exhausted its funding of \$20 billion.¹

2. **The UAE has been reaping the benefits of its early efforts to diversify the economy.** As the UAE developed into a major services hub in the Middle East, its dependency on oil exports declined markedly. Based on its well-developed hospitality and services sectors, tourism, transportation and

logistics have been major drivers of the post-2009 recovery. The UAE has also been benefiting from high oil prices and strong growth in Asia. As a result of its perceived safe haven status and developed services sector, the country benefited from an increase in demand for property by expatriates and a surge in tourism in the wake of the turmoil in the MENA region that began last year.

GCC: Hydrocarbon Dependency 1/



Sources: Country authorities; and IMF staff estimates.

1/Total government revenue includes investment income, which is included in hydrocarbon income. Total exports exclude re-exports.

RECENT DEVELOPMENTS

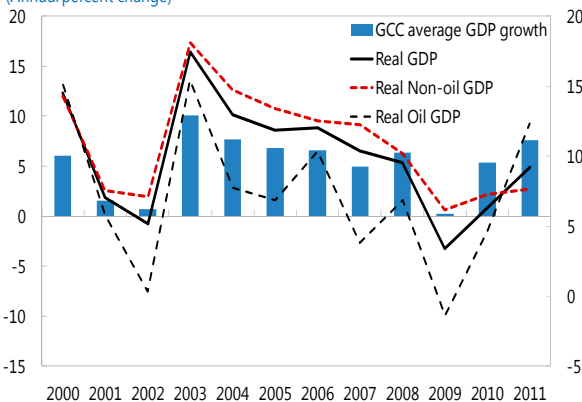
3. **The economic recovery continued and the external position strengthened significantly in 2011.** Real GDP growth reached an estimated 4.9 percent, supported by high oil prices and production in response to disruptions in Libya. Nonhydrocarbon growth also strengthened, to around

2.7 percent, backed by strong trade, logistics and a surging tourism sector, despite the continued weakness of the construction and real estate sectors in the aftermath of the 2009 crisis. Backed by high oil prices and buoyant nonhydrocarbon exports, the external current account surplus increased markedly, to around 9 percent of GDP. Inflation remained subdued at an average of 0.9 percent in 2011, mainly due to a continuing decline in housing rents and limited pass-through of international food prices.

¹ The Dubai Financial Support Fund, financed in equal parts by the central bank and Abu Dhabi, was established in 2009 to provide financial support and liquidity to government and government-related entities undertaking projects of strategic importance in Dubai.

Real GDP Growth, 2000–11

(Annual percent change)



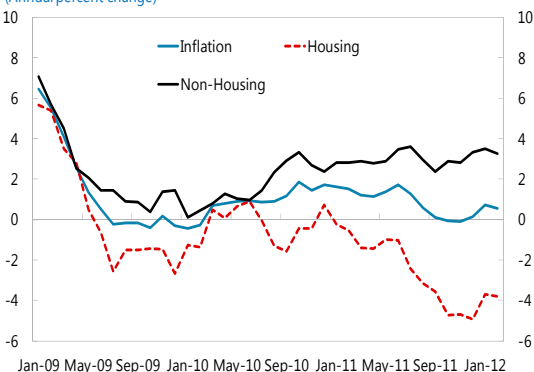
Sources: Country authorities; and IMF staff estimates.

4. The large property overhang continues to be a drag on the economy.

Since mid-2008, real estate prices have fallen by more than 60 percent in Dubai, and to a lesser extent in Abu Dhabi. The large supply overhang and the completion of additional projects in the coming years render an early and broad-based recovery of the sector unlikely (Box 1).

CPI Inflation, 2009–12

(Annual percent change)



Sources: Haver; and IMF staff estimates.

5. **The recovery was supported by an expansionary fiscal policy.** The consolidated government nonhydrocarbon primary deficit (including loans and equity) rose to nearly 42 percent of nonhydrocarbon GDP in 2011 (from 36 percent in 2010), as Abu Dhabi

increased its current and development expenditures, and extended substantial financial support to Aldar, its flagship real estate developer.² Following a contraction in 2010, Dubai's deficit increased slightly in 2011, mostly on account of further spending from the DFSF. Nonetheless, high oil prices led to an improvement in the consolidated overall balance from a deficit of 2.1 percent of GDP in 2010 to an estimated surplus of 2.9 percent of GDP in 2011.

6. **Supported by accommodative monetary policy, banks remained amply liquid but private sector credit growth did not pick up.** In light of low U.S. interest rates, monetary policy stayed accommodative under the fixed exchange rate regime. Lending to the private sector has nonetheless remained sluggish and lagged behind the recovery in credit growth in neighboring GCC countries, as excess capacity in the real estate sector and the debt overhang still limit lending opportunities. Despite a continued rise in nonperforming loans (second highest level among GCC countries), the banking sector has remained well-capitalized and profitable, as the net interest margin has remained comfortable. In October 2011, the authorities quickly resolved Dubai Bank through a takeover by Emirates NBD bank.³

² The consolidated government comprises the federal, Abu Dhabi, Dubai, and Sharjah governments accounting for over 99 percent of total UAE fiscal expenditures.

³ In connection with this transaction, Emirates NBD received a Dh2.8 billion deposit from the ministry of finance. The government of Dubai has provided a guarantee—with a fair value of Dh768 million—for any losses relating to existing assets for seven years.

Box 1. Real Estate Market Developments

Following the large decline in real estate prices since 2008, some segments of the real estate market have begun showing signs of stabilization. By the end of 2011, in Dubai the hotel and retail segments and some parts of the residential market started to pick up, whereas office rents have continued to decline. In Abu Dhabi, where the initial real estate drop was less pronounced, both commercial and residential rents have continued to decline.

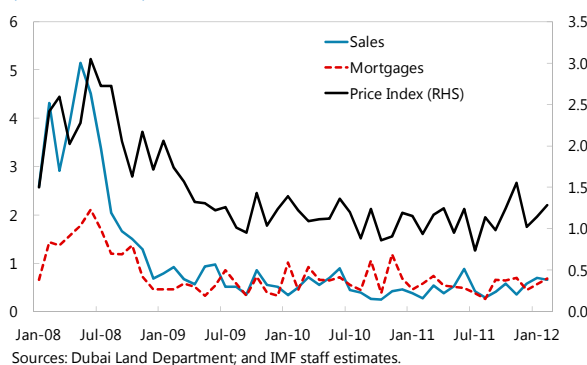
The ongoing large oversupply and upcoming project completions continue to weigh on the sector.

- In Dubai, the office vacancy rate (30 percent at end-2011) is expected to increase further as large additional supply will come on stream this year. Retail and hotel vacancy rates (20 and 25 percent at end-2011, respectively) could stabilize as fewer new projects are in the pipeline and demand continues to be substantial.
- In Abu Dhabi, the real estate supply and demand gap continues to widen. The office market vacancy rate (23 percent at end 2011) is expected to grow in light of the expected large new supply. Many projects in the residential market are also expected to come on stream. In the hotel segment, vacancies remain high at 35 percent.

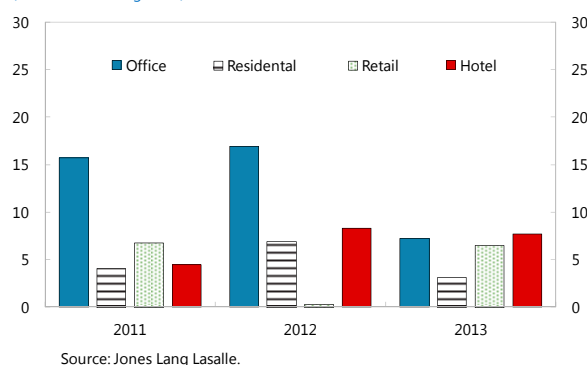
The authorities have taken steps to help the real estate sector. In Dubai, 220 projects in early stages have been canceled, and the Dubai Land Department has introduced initiatives to support projects that are close to completion, by certifying viable projects to facilitate financing. The Abu Dhabi government has reviewed the project pipeline of Abu Dhabi GREs, which are now proceeding at a reduced pace. In addition, Aldar,

one of the largest developers, has received support from the Abu Dhabi government and has progressed with its restructuring plans to adjust to market conditions. On the federal level, legal amendments are under discussion that would relax foreign ownership restrictions, which could help boost demand.

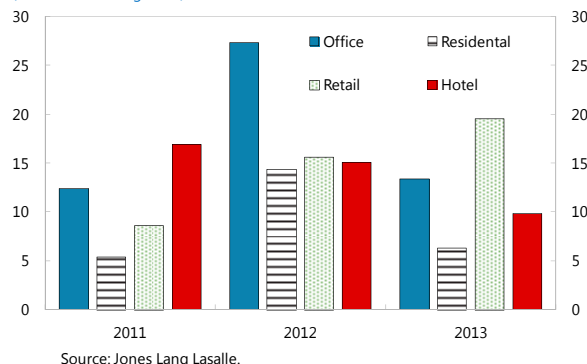
Value of Dubai Real Estate Transactions, 2008–11
(Billions of Dirhams)



Dubai: Estimated New Real Estate Supply
(Percent of existing stock)

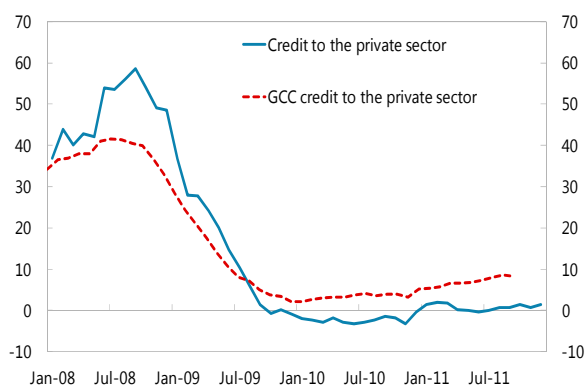


Abu Dhabi: Estimated New Real Estate Supply
(Percent of existing stock)



Banking System Credit Growth, 2008–11

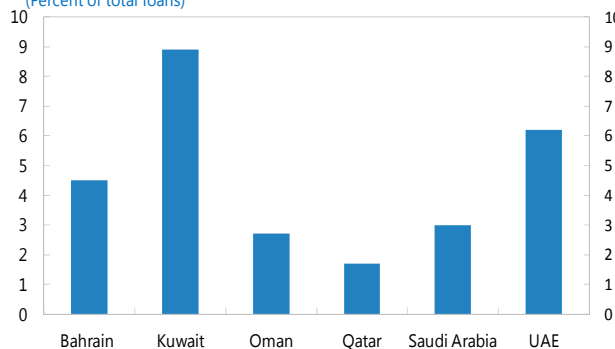
(Annual percent change)



Source: Haver.

Nonperforming Loans

(Percent of total loans)



Source: Country authorities.

Note: Data for Kuwait and Saudi Arabia for December 2010, for Bahrain and Oman for September 2011, for Qatar and the United Arab Emirates for December 2011. Data for the UAE for national banks only.

Bank Financial Soundness Indicators 1/
(In percent)

	2008	2009	2010	2011
Capital adequacy ratio	13.2	19.9	20.7	21.2
Return on assets	1.4	1.4	1.3	1.5
Return on equity	13.0	10.9	10.4	11.4
Nonperforming loans to total loans	2.3	4.3	5.6	6.2
Provisions to nonperforming loans	92.7	63.9	65.2	67.1

Source: National authorities

1/ National banks

7. Spillovers from deleveraging in Europe have so far been manageable.

European banks, traditionally major providers of funding for GCC borrowers, have started to retrench from non-core markets, including the UAE, in an effort to deleverage. While conditions for external borrowing have deteriorated, there are signs that Asian and local GCC banks have increasingly stepped in to provide funding.

OUTLOOK AND RISKS

8. The recovery in nonhydrocarbon growth looks set to continue in 2012. Despite the continued domestic deleveraging and the ongoing oversupply in the real estate market, real nonhydrocarbon GDP growth is projected to further strengthen to 3.5 percent, supported by strong trade, tourism, logistics, and manufacturing. With limited potential for further increases in oil production in light of production levels already close to capacity, overall GDP growth is expected to moderate to 2.3 percent. Inflation is likely to remain subdued at around 1½ percent. Supported by high oil prices, the external current account surplus is projected to further increase to 10.3 percent of GDP.

9. Downside risks to this outlook reflect the UAE’s reliance on hydrocarbon exports and its close links with international markets:

- **A more pronounced impact of the international sanctions on Iran** could affect the UAE through a reduction in bilateral trade, real estate demand, tourism, and financial services to Iran-based customers (Box 2).
- **A renewed worsening of global financial conditions** could make it more difficult to roll over GREs’ debt and banks’ wholesale funding.

- **A decline in oil prices** in light of weak growth prospects in the advanced economies would affect export earnings, fiscal revenues, and ultimately nonhydrocarbon GDP growth, with an adverse impact on asset prices (Figure 1).⁴
- **A marked economic slowdown in emerging Asia** would affect trade, tourism, and external financing conditions.

10. **A slowdown of the UAE economy would also exert spillovers on other countries.**

Given the UAE's large foreign labor force, remittances to countries in South Asia and the Mashreq could be significantly affected (Box 3).

11. **There are also a number of mitigating factors and upside risks to the outlook.**

Central bank and sovereign wealth fund foreign assets provide a comfortable buffer to the economy. Higher oil prices in the context of heightened regional geopolitical tensions would further support fiscal revenues and the external current account, as long as oil exports are not disrupted. Heightened regional tensions, while potentially affecting confidence, could also lead to renewed safe-haven capital inflows and increased real estate demand.

Box 2. The Economic Impact of Sanctions on Iran

Trade data available through Q3, 2011, suggest that international sanctions on Iran since June 2010 have so far not led to a lasting reduction in Dubai's bilateral trade with Iran.¹ Both exports to Iran and their share in Dubai's total exports increased in 2011, reflecting an increased importance of re-exports, which account for more than 90 percent of bilateral trade with Iran.

The trade impact on UAE growth of the more recent tightening of sanctions by the US and EU on Iran is expected to be moderate. Trade could be affected by reduced demand from Iran due to economic hardship, and by complications with trade finance and payments. As an illustrative scenario, a 30 percent reduction of exports to Iran would impact the UAE's GDP growth by 0.3 percentage point.²

¹Recent data for the UAE as a whole are not available.

²Calculations assume that the local value-added content of re-exports to Iran is 25 percent.

In addition to being an important trade partner, Iran has been a significant source of demand for real estate, tourism and financial services. The impact of sanctions on the real estate market is ambiguous, influenced on the one hand by capital flight from Iran, and on the other hand by the difficulty for Iranians to carry out large financial transactions in the UAE. Tourism is likely to be negatively affected as are financial services, including trade finance. However, the latter is unlikely to significantly affect the profitability of the UAE banking system.

Dubai - Exports to Iran, 2009–11



⁴ Two risk scenarios are generated by assuming (i) a temporary drop in oil prices to the 2009 level in 2012 (\$61.8 per barrel) and to the 2010 level in 2013 (\$79 per

(continued)

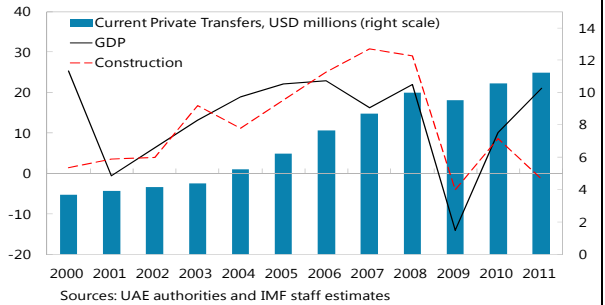
barrel), subsequently recovering to benchmark values; and (ii) a prolonged drop to \$61.8 per barrel in 2012–17.

Box 3. Outward Remittances

Outward remittances from the UAE are substantial, reflecting the large foreign workforce. Foreigners comprise more than 70 percent of UAE’s population and 96 percent of the workforce. While the largest foreign communities in the UAE are from South Asia, there is also a substantial presence from the MENA region. Most foreign workers maintain close ties to their home countries and send remittances, which are estimated at \$11 billion (2011).

An economic downturn could significantly affect remittances. Remittances tend to be strongly correlated with GDP, and the construction sector is particularly important since it employs 38 percent of foreign workers, many of whom from South Asia. The trade and services sectors are also important employing nearly one third of foreign workers from Lebanon, Syria, and Jordan.

Remittances and Economic Growth, 2000–11
(Percent change, unless otherwise indicated)

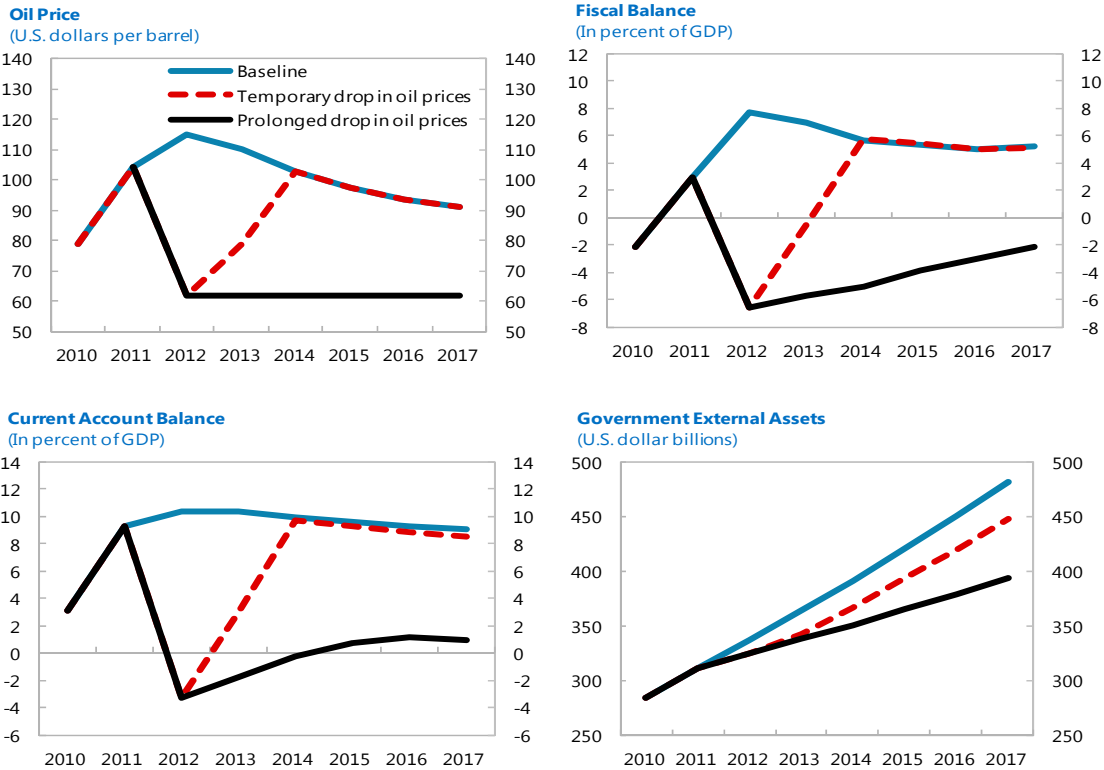


Foreign Workers in the UAE 1/
(In percent)

	Share in UAE foreign workforce	Share in home country population
India	38.36	0.13
Bangladesh	22.08	0.53
Pakistan	16.22	0.37
Philippines	5.56	0.23
Egypt	3.38	0.16
Syria	1.72	0.32
Sri Lanka	1.09	0.21
Jordan	0.86	0.56
Iran	0.62	0.03
Lebanon	0.55	0.50
Sudan	0.40	0.04
Yemen	0.31	0.05
Morocco	0.26	0.03
Tunisia	0.11	0.04

Sources: UAE authorities, and World Bank.
1/ Excludes household employees and public sector employees.

Figure 1. United Arab Emirates: Medium-term Risk Scenarios, 2010–17



Source: IMF staff calculations.

UAE: Risk Assessment Matrix		
Nature/Source of Main Threats	Likelihood of Realization in the Next Three Years	Expected Impact on Economy if Risk is Realized
A more pronounced impact of the international sanctions on Iran	Staff assessment: Medium to High Likelihood arises from the currently heightened geopolitical risks.	Staff assessment: Low to Medium Sanctions could exert a further adverse impact on the UAE economy through a reduction in bilateral trade, real estate demand, tourism, and financial services to Iran-based customers. The impact could be offset if oil prices increase, as long as exports are not disrupted.
A worsening of global financial conditions	Staff assessment: Medium Likelihood follows from continued stress in the Euro area and the deleveraging by international banks.	Staff assessment: Medium Would make it difficult to roll over some of the GREs' maturing debt, and would raise the overall cost of their borrowing from international markets, thus further straining their balance sheets. Individual banks, especially those that have relied on large wholesale funding, might face liquidity pressures.
A large and prolonged decline in the hydrocarbon prices	Staff assessment: Low The UAE remains heavily dependent on crude oil. A global recession followed by several years of slow growth would depress demand for energy and could lead to a sharp fall in oil and gas prices. By contrast, a further increase in geopolitical tensions could raise oil prices.	Staff assessment: High Would reduce export earnings and fiscal revenues. While the UAE maintains significant buffers in the form of international reserves and sovereign wealth fund assets, a prolonged fall in oil prices would ultimately imply reduced fiscal spending and nonhydrocarbon GDP growth, and an adverse impact on asset prices. This would also further expose vulnerabilities in GREs and private companies affected by the ailing real estate sector.
A marked economic slowdown in emerging Asia	Staff assessment: Low While a gradual reduction in emerging Asia GDP growth rates appears likely this year, there are currently few indications that would suggest a pronounced economic slowdown.	Staff assessment: Medium to High Would affect trade, tourism, and external financing conditions. Robust external demand from Asia has helped limit the impact on the UAE of the weakness of European economies and of the international sanctions on Iran. Moreover, increasing capital flows from Asia have dampened the effect of the European financial sector deleveraging on the UAE foreign funding situation.

POLICY DISCUSSIONS

A. Maintaining Macroeconomic Stability and Supporting the Economy

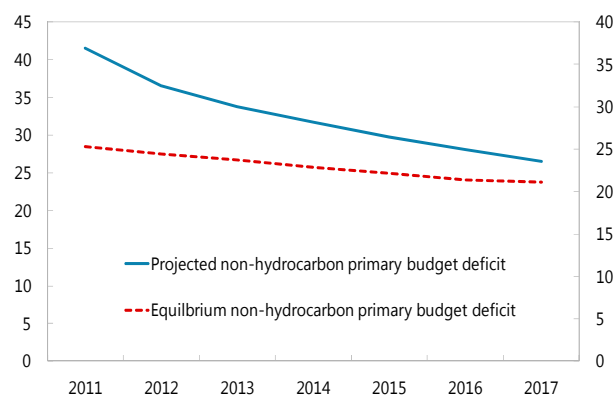
12. **Following last year's fiscal expansion, the UAE plans to start consolidating its fiscal accounts in 2012.** The federal and emirate budgets imply a modest consolidation of the fiscal stance by 0.5 percent of nonhydrocarbon GDP.⁵ A substantial salary increase for federal employees and a large increase in Abu Dhabi's planned development expenditures are more than offset by reductions in other expenditures (among others the assumption of no further bailouts) and increases in non-tax revenues.⁶

13. **Staff concurred with the pace of the planned fiscal correction.** Staff's fiscal sustainability analysis based on the permanent income hypothesis suggests that the UAE's fiscal stance has been too loose to ensure intergenerational equity.⁷ This is in line with the findings of the external sustainability analysis (Appendix I). Moreover, the fiscal break-even oil price (the theoretical oil price at which fiscal accounts would be in balance) has increased markedly in recent years, from \$23 in 2008 to \$92 in 2011, the second highest in the GCC,

exposing the UAE to the risk of falling oil prices. Prudent fiscal plans are also appropriate as they increase the scope for fiscal expansion in case downside risks to the economy materialize, including the risk that further funds may be needed to support ailing GREs. At the same time, the gradual pace of fiscal consolidation implies that the fiscal stance is unlikely to undermine the economic recovery.

Fiscal Sustainability Analysis, 2011–17

(In percent of Non-hydrocarbon GDP)



Source: IMF staff calculations.

14. **Staff advised to be vigilant regarding the expenditure composition.** The generous federal salary increase will add to expenditure rigidities while further raising reservation wages for nationals seeking private sector employment. Abu Dhabi's recently approved capital spending plan on education, healthcare, industry, tourism, infrastructure, and renewable energy projects will be an important contribution to supporting growth, but the magnitude of the increase in development spending suggests a need for careful project evaluation to ensure that spending is productive.

⁵ The fiscal stance is defined as the consolidated non-hydrocarbon primary balance for the federal, Abu Dhabi, Dubai, and Sharjah budgets including loans and equity but excluding (i) the operations of Dubai Financial Support Fund, (ii) Abu Dhabi government's support for the real estate company Aldar in 2011, and (iii) the investment income from the sovereign wealth funds. Abu Dhabi's 2012 budget is not yet available; numbers are staff estimates.

⁶ Effective January 2012, federal salaries were raised between 35 and 100 percent depending on grade and sector, adding Dh3.4 billion to the federal wage bill.

⁷ The equilibrium non-hydrocarbon primary deficit is calculated assuming constant real per capita government spending consistent with a constant per capita annuity after depletion of hydrocarbon resources.

15. **Both Abu Dhabi and Dubai intend to improve their fiscal positions in the medium term.** Abu Dhabi plans a continued fiscal consolidation through 2017. Dubai intends to bring its fiscal accounts close to balance by 2014, as major infrastructure projects will have been completed. Staff welcomed these plans, as continued fiscal consolidation will

improve the UAE's fiscal sustainability and will increase the available policy space in case downside risks, such as a sustained decline in oil prices, materialize. Moreover, debt sustainability analysis for Dubai indicates that the planned fiscal consolidation is key to reducing the emirate's fiscal vulnerability (Box 4).

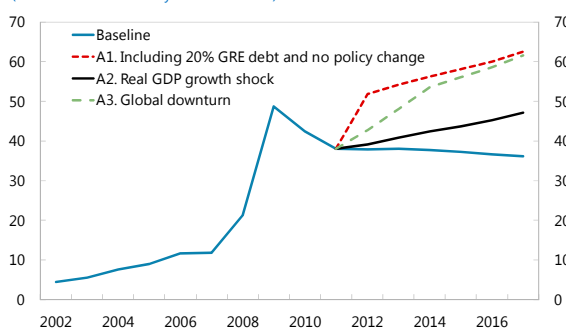
Box 4. Dubai's Debt Sustainability

With better growth prospects and plans to consolidate public finances, Dubai's government debt sustainability has improved. Dubai's government debt spiked in 2009 as a result of the crisis as the emirate provided support to its troubled GREs. The baseline scenario reflects a projected steady recovery of growth in the medium term and a gradual consolidation of Dubai government's fiscal accounts aiming to bring the fiscal accounts close to balance by 2014 in line with Dubai's plans. Under this scenario, the debt-to-GDP ratio is on a gradual declining path.

Fiscal consolidation is key to reducing fiscal vulnerability, especially as GREs continue to pose fiscal risk to the sovereign. An alternative scenario assuming a constant primary balance at 2011 levels (1.6 percent of GDP) and augmenting government debt by 20 percent of GRE debt would raise the debt-to-GDP ratio by about 26 percentage points by 2017 compared to the baseline.

Moreover, Dubai's debt could become unsustainable if the economy is hit by severe shocks. A decline in GDP growth to 1.3 percent (that is, by ½ standard deviation from the baseline), would add 9 percentage points to the debt-to-GDP ratio by 2017. A deterioration of the external environment would have an even more pronounced impact: a global downturn scenario in which growth, the real interest rate and the primary balance deteriorate significantly in 2012–14 and stay below baseline in 2015–17, would result in an increase in the debt-to-GDP ratio to 62 percent by 2017.

Dubai – Government Debt Sustainability Analysis
(Percent of Dubai nonhydrocarbon GDP)



Sources: Country authorities; and IMF staff projections.

Dubai Government Debt Sustainability, 2007–17
(In percent of GDP of Dubai and the Northern Emirates)

	Actual					Projections							Debt stabilizing primary balance
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017		
Government debt 1/	11.9	21.2	48.7	42.4	38.0	37.8	38.0	37.8	37.2	36.7	36.2		
Alternative scenarios													
A1. Including 20% of GRE debt as contingent liability and no policy change (constant primary balance in 2011–17)						51.7	54.1	56.2	58.0	60.0	62.5	0.6	
A2. Real GDP growth is at baseline minus one-half standard deviation						38.0	39.2	40.8	42.3	43.7	45.2	1.9	
A3. Global downturn scenario 2/						42.7	48.1	53.5	56.0	58.5	61.5	2.7	
Memorandum items													
Real GDP growth baseline						3.7	3.9	4.1	4.4	4.4	4.4		
Real GDP growth path in the global downturn scenario						0.6	0.8	1.0	2.8	2.8	2.8		

Sources: UAE authorities and Fund staff estimates and projections.

1/ Dubai government and government guaranteed debt.

2/ Combination of 1/2 standard deviation shocks in 2012–14 and 1/4 standard deviation shocks in 2015–17 to the baseline for real GDP growth, real interest rate and primary balance.

16. **The authorities noted that several initiatives are under consideration to diversify revenue sources and to improve budgetary practices.** The federal government is planning an overhaul of multiple fees collected by federal ministries. Technical preparations are under way for the eventual introduction of a value added tax, which is under discussion at the GCC level. The authorities are also conducting an economic impact study for the possible introduction of a corporate income tax. Passage of the draft organic budget law would help improve federal budgetary practices, as it mandates the preparation of a medium-term expenditure framework and requires the use of a treasury single account.

17. **Low global interest rates ensure appropriately accommodative monetary conditions under the U.S. dollar peg while inflation remains subdued.** Low interest rates

facilitate the economic recovery and the continued repair of balance sheets. At the same time, in light of continued slack in the economy and a high degree of flexibility and openness of the economy, there are few near-term inflationary risks.

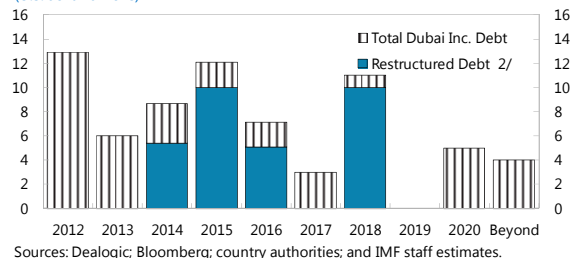
18. **There is little evidence for exchange rate misalignment.** Different methodologies yield mixed results for the exchange rate assessment (Appendix I). The macroeconomic balance approach shows little evidence for misalignment, whereas the equilibrium exchange rate approach points to moderate undervaluation. By contrast, the external sustainability approach indicates moderate overvaluation, underscoring the desirability of medium-term fiscal consolidation to support intergenerational equity, in line with the fiscal sustainability analysis above.

B. Managing Risks Stemming from GREs

19. **Despite recent progress in debt restructuring, GREs are still facing financial challenges.** While the debt of some GREs has been restructured (including Dubai World), the process has been more protracted in other cases, such as Dubai Holding.⁸ The estimated total GRE debt declined to 51 percent of 2011 GDP as of March 2012, from 61 percent of 2010 GDP, though Abu Dhabi's GRE debt still rose in nominal value (Appendix II). Rollover risks are still considerable, with \$30 billion falling due in 2012. Moreover, significant amounts of debt will mature in 2014–15.

⁸ Dubai International Capital recently reached agreement for a restructuring of \$2.5 billion in liabilities. Other restructurings under the Dubai Holding remain under discussion.

Maturity Profile of Dubai Inc. Debt, 2012–20 1/
(U.S. dollar billions)



1/ Not including GREs with government ownership below 50 percent.

2/ Preliminary estimates based on public information about Dubai Holding and other GRE ongoing debt restructurings, as well as Dubai World's completed restructuring; including debt guaranteed by the Dubai government.

20. **The Abu Dhabi and Dubai authorities noted that lessons have been learned from the crisis and that GREs have become more proactive in managing debt rollovers.** Staff welcomed this more proactive approach, and noted that the combination of large refinancing needs and reliance on

foreign funding continues to pose a challenge against the backdrop of the current uncertain global financial environment and the retrenchment of European banks. Some upcoming large rollovers later this year may yet test the market's appetite for GRE debt.

UAE Gross Public and Publicly Held Debt
(In billion of US\$)

Maturing in	2012	2013	Beyond	Total
Government of Abu Dhabi 1/	1.4	0.5	7.1	9.1
Abu Dhabi GREs	15.8	18.3	65.1	99.2
Total Abu Dhabi	17.2	18.8	72.2	108.3
<i>In percent of Abu Dhabi 2011 GDP</i>	7.8	8.5	32.8	49.1
Government of Dubai 1/	0.6	4.5	47.9	53.1
Dubai GREs	14.0	4.9	57.0	76.0
Total Dubai	14.6	9.4	104.9	129.0
<i>In percent of Dubai and Northern Emirates' 2011 GDP</i>	10.5	6.8	75.1	92.4
Other Emirate Sovereign	0	0	3.2	3.2
Other Emirate GREs	0.3	0.4	1.9	2.6
Total Other Emirates	0.3	0.4	5.1	5.8
Federal Government				9.8
<i>In percent of U.A.E. 2011 GDP</i>				2.7
Total U.A.E.	32.2	28.7	182.3	252.9
<i>In percent of UAE GDP</i>	8.9	8.0	50.6	70.2
Memorandum Items:				
Total GRE debt including government guarantees				184.8
<i>In percent of 2011 UAE GDP</i>				51.3

Sources: Dealogic, Zawya, Bloomberg, UAE authorities, and Fund staff estimates.

1/ Including GRE debt guaranteed by the Abu Dhabi and Dubai governments.

21. **Staff stressed the desirability of a comprehensive strategy aimed at bolstering market confidence in GREs, and transparent reporting of GRE-related fiscal risks.** Such a strategy should include:

- **Stronger GRE balance sheets.** Further deleveraging and strengthening of impaired GREs' balance sheets is required, including, where needed, through debt restructuring and asset sales.
- **Proper fiscal risk management and reporting framework.** While both Abu Dhabi and Dubai have made progress in

identifying and monitoring GRE liabilities, and new borrowing by GREs is subject to approval, contingent liabilities continue to be undisclosed.

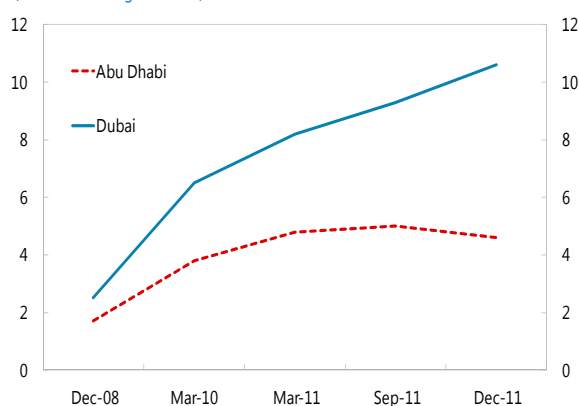
- **Better availability of information on GRE debt.** Disseminating information on GRE debt has improved, particularly by Abu Dhabi's debt management office. However, the availability of information on financial conditions, debt stock and the maturity profile of Dubai GREs needs further improvement. Passage of the draft Public Debt Law would help to further strengthen the monitoring of GRE debt. Moreover, increased communication about the GREs' financing strategies would be important to strengthen market confidence.
- **Improved GRE corporate governance and transparency** would also be essential, including by delineating clearly their commercial and noncommercial operations, and standardizing their accounting, auditing, and financial reporting practices.

22. **The authorities noted that data availability and risk management regarding GREs are gradually improving.** In particular, Abu Dhabi has made public the list of companies explicitly supported by the government. The Dubai government, in turn, emphasized that Dubai GREs are not backed by a sovereign guarantee, and that the Department of Finance and Supreme Fiscal Committee now play a major role in GREs debt monitoring and approval of new borrowing.

C. Financial Sector Soundness and Financial Spillovers

23. **The banking system maintains significant buffers to withstand a further deterioration in asset quality, though individual banks could be affected.** The NPL ratio of national banks has sharply increased from their 2008 pre-crisis levels to 6.2 percent in 2011. The NPL ratio in Dubai banks is higher at 10.6 percent. This ratio could further increase by about 5 percentage points this year as a result of the ongoing restructuring of Dubai Holding, the potential restructuring of other maturing GRE debt, repeated rescheduling of loans, and continued stress of real estate companies. Staff's stress tests show that the domestic banking system could absorb a significant increase in nonperforming loans.⁹ Nevertheless, for some banks with high loan concentration in the real estate sector, Tier 1 capital would fall below the regulatory minimum in a severe stress scenario. The authorities agreed with this assessment and will continue to closely monitor banks' capitalization.

Gross Nonperforming Loans, Dec. 2008–Dec. 2011
(Percent of total gross loans)



Source: Country authorities.

⁹ See accompanying Selected Issues Paper.

Nonperforming Loans Stress Testing for UAE Banks
(Percent unless otherwise specified)

	UAE Local Banks		Dubai Banks	
	Regulatory capital	Tier 1 capital	Regulatory capital	Tier 1 capital
CAR (2011)	20.0	15.3	19.7	13.4
NPL ratio (2011)	6.8	6.8	10.6	10.6
Baseline scenario				
NPL ratio ¹	10.0	10.0	15.0	15.0
CAR	19.1	13.8	17.1	10.6
Stress scenario (50 percent increase in NPLs from baseline)				
NPL ratio	15.0	15.0	22.0	22.0
CAR ²	15.9	10.5	14.1	7.4
Memorandum items				
Minimum regulatory capital	12.0	8.0	12.0	8.0

Source: IMF staff estimates and calculations.

¹ Takes into account potential NPLs pertaining to Dubai Holding, Dubai Drydocks, loans rescheduled twice, and other real estate companies in Abu Dhabi that are making losses or do not have debt servicing capacity.

² Assumes a provisioning rate of 90 percent on new NPLs.

24. **The Central Bank of the UAE (CBU) will continue to closely monitor the liquidity of individual banks and encourage them to proactively manage liquidity risks.** The funding structure of the banking system has substantially improved since the 2009 crisis. Nonetheless, since last summer, banks have increased their liabilities to foreign banks somewhat. Although the banking system remains comfortably liquid, staff's stress tests indicate that a foreign funding shock may generate some tightening of foreign currency liquidity, which would need to be managed, in particular, at the individual bank level. The central bank noted that it is closely monitoring the liquidity of banks.

Non-Resident Liquidity Withdrawal Scenario¹
(US\$ Billion)

	National Banks	Foreign Banks	All Banks
Total non-resident liabilities	53.1	16.5	69.6
Total liquid non-resident assets	17.5	6.0	23.5
Non-resident liquidity gap (liquid liabilities minus liquid assets) ²			
Scenario 1	-6.7	-3.3	-9.9
Scenario 2	-1.1	-2.6	-3.8
Scenario 3	6.7	-1.0	5.7
Memorandum items:			
Available domestic liquid assets ²	16.2	12.0	28.3
Central Bank foreign currency assets (Dec 2011)	---	---	36.4

Sources: Country authorities; and IMF staff calculations.

¹ Based on position at end-January 2012.

² Scenarios assume the withdrawal of all estimated speculative non-resident deposits plus the withdrawal of wholesale funding:

Scenario 1: demand deposits + 20% of time deposits.

Scenario 2: demand deposits + 33% of time deposits + 20% of capital funding.

Scenario 3: demand deposits + 67% of time deposits + 40% of capital funding.

25. **Looking ahead, liquidity management will be strengthened by a new liquidity facility and the development of domestic capital markets.** In June 2011, the CBU launched a repurchase facility for Islamic certificates of deposits (CD) in an effort to provide new liquidity tools for Islamic banks. The CBU mainly relies on CDs to manage banking system liquidity and has started work towards creating a marginal lending facility as a means of providing standing liquidity when needed. This facility, together with the development of domestic money and bond markets, will be key in preparing for the implementation of the Basel 3 liquidity norms (planned to be phased in between 2015 and 2018), both in terms of eligible liquid assets and stable sources of funding. Passage of the draft Public Debt Law would help accelerate the preparations.

26. **Shielding the banking system from further GRE risks is key.** In 2011, the net exposure of the banking system to government and public institutions increased by 3.5 percent of GDP (2.6 percent of banking system assets). Staff pointed out that some of these exposures are not consistently classified across banks' balance sheets and government fiscal accounts, leading to some non-transparency in bank regulatory compliance. The authorities agreed that there is a risk that GREs will increasingly turn to domestic banks for their funding needs in case they face difficulties in external financing, and agreed with staff that it will be important to avoid channeling bank funding to non-viable GREs. Effective implementation of the recently introduced aggregate limits on bank lending to GREs will help contain banks'

risks from GREs.¹⁰ In addition, there was agreement that imposing higher capital charges and introducing forward provisioning on exposures to risky GREs would further mitigate risks to the banking system.

Change in Net Exposure of Banks to Government and Public Institutions
(AED Billions)

	2008	2009	2010	2011
Loans to Government and Public Institutions (A)	150.1	189.2	205.6	230.0
Investment in Government and Official Entities Bonds (B)			41.0	53.9
Government Deposits (C)	206.8	202.0	187.4	180.6
Net Exposure (A + B - C)			59.2	103.3
Change in Net Exposure in 2011 over 2010				44.1

Source: Staff calculations based on official data

27. **Staff stressed that the CBU should build on recent progress in further strengthening bank regulation.** Staff welcomed the CBU's efforts to further increase general and specific provisioning requirements and to restrict dividend distribution in some cases. Staff stressed the importance of implementing regulations under consideration on liquidity and real estate lending. This will pave the way for a formal macroprudential framework, which, with the appropriate legal underpinning, will help calibrate regulation from a systemic perspective. In this context, tailoring the CBU's early warning system to system-wide risks (including related to GREs and real estate) would help the central bank identify risks at an early stage and enable appropriate action.

¹⁰ In April 2012, the central bank set new limits of 100 percent of the capital base for all lending by a bank to UAE emirate governments and their non-commercial entities, and 25 percent to individual borrowers. It also introduced an aggregate limit of 100 percent of capital of banks for lending to commercial entities of the federal government and local governments, and a cap of 15 percent for funded exposure to individual borrowers.

28. **Effective bank governance is fundamental to support financial sector soundness.** There was agreement that, in light of the government's control of banks and the banks' high exposure to GREs, a clear

governance framework is needed to safeguard the banks' financial integrity. Staff suggested that the CBU undertake a bank governance diagnostic in the context of the forthcoming Financial Sector Assessment Program.

D. Other Issues

Fiscal Policy Coordination

29. **Effective intergovernmental coordination of fiscal policy will buttress effective demand management and fiscal sustainability.** Given the federal structure, information sharing between the federal and emirate governments and the CBU is a key precondition for effective fiscal policy. Staff welcomes progress made in information sharing, facilitated by the Fiscal Coordination Council (FCC), and encouraged the authorities to include information sharing on GRE financial operations.

30. **The authorities plan to extend the FCC's work to the effective coordination of fiscal policy plans.** This would include the joint determination of aggregate revenue, expenditure, and financing plans in light of macroeconomic and other policy considerations, and the breakdown of these goals into plans for the federal and emirate level authorities. The authorities asked for Fund technical assistance in this area.

Statistics

31. **The authorities recognized the need to further strengthen statistics.** They have already made good progress in establishing databases and improving the quality of economic statistics. The establishment of the National Bureau of Statistics and Debt Management Offices were important steps to that end. Nevertheless, the authorities recognized that more progress is needed towards improving methodologies and timely compilation and dissemination of key statistics, including on balance of payments, national accounts, fiscal accounts and labor market statistics. Moreover, further progress is needed in the coordination among federal and emirate-level statistical agencies. The authorities requested follow-up technical assistance on national accounts statistics and the balance of payments. They also intend to upgrade the labor market statistics.

STAFF APPRAISAL

32. **The continued economic recovery is encouraging.** Growth has been supported by high oil prices and strong demand from the UAE's trading partners, notwithstanding the continued weakness of the domestic

construction and real estate sectors. The still uncertain global environment and regional geopolitical tensions could pose risks to the favorable outlook, but the sizeable buffers of the sovereign wealth funds and the central

bank strengthen the economy's resilience to external shocks.

33. **Fiscal policy is appropriately aimed at gradual consolidation.** The authorities' fiscal plans adequately imply a gradual unwinding of the past fiscal stimulus in response to the 2009 crisis. The consolidation is welcome as the expansionary stance led to a significant increase in the breakeven oil price and is no longer needed, and fiscal policy should now focus on fiscal sustainability. Prudent fiscal policy also increases the room for maneuver in case downside risks to the economy materialize. At the same time, the gradual pace of consolidation would not undermine the economic recovery. Dubai's plans for fiscal consolidation are especially welcome as they help improve the emirate's debt sustainability in the face of contingent liabilities related to GREs and the still weak real estate market.

34. **Care should be taken in managing the expenditure composition.** The generous federal salary increase adds to expenditure rigidities, while the planned increase in Abu Dhabi's development expenditures suggests a need for careful project evaluation.

35. **The policy mix will be balanced by an accommodative monetary stance under the peg to the U.S. dollar.** Continued low U.S. interest rates will imply appropriately accommodative monetary conditions in the near term accompanying the fiscal tightening in the face of the still fragile economic recovery. The exchange rate has remained broadly aligned with fundamentals, and the exchange rate peg continues to serve as an effective nominal anchor for the economy.

36. **Mitigating the continued risks posed by GREs should remain a priority.** Total GRE debt as percent of GDP declined last year and the GREs are now more proactive in managing debt rollovers. Nonetheless, they are still faced with high refinancing needs and reliance on foreign funding. Further deleveraging and strengthening of impaired GRE balance sheets is needed, together with increased transparency and communications about their financial strategies. Improvements in corporate governance would also be essential.

37. **The CBU should continue to closely monitor banks' liquidity and capital buffers.** While the aggregate banking system maintains significant buffers, individual banks could be affected if downside risks materialize. The CBU should continue to encourage banks to proactively manage their liquidity and capital positions in light of these potential risks.

38. **The banking system should be shielded from taking further GRE risks.** With reduced availability of foreign funding, GRE exposures are increasingly transferred to the domestic banking system. In this environment, it is important to avoid channeling bank funding to non-viable GREs. The recently introduced aggregate limits on lending to GREs will help contain this risk. Imposing higher capital charges and introducing forward provisioning on exposures to risky GREs would further alleviate risks to the banking system. Classification of GRE and sovereign exposures across banks' balance sheets and government fiscal accounts should be consistent to ensure proper accounting of fiscal and banking system risks.

39. **Developing the domestic fixed income market would support banks' liquidity management.** Passage of the Public Debt Law would help accelerate the process of preparing banks for the Basel 3 liquidity framework without constraining credit growth. In addition, well-developed domestic debt markets would also aid the diversification of funding sources for corporates.

40. **The recent progress in fiscal coordination among federal and emirate-level entities is encouraging.** Building on achievements in information-sharing, the next step will be to extend the FCC's work to the effective coordination of fiscal policy plans and to include information on GREs.

41. **Efforts to further improve the statistical capacity are welcome.** Priority areas are the balance of payments, national accounts, fiscal accounts and labor market statistics.

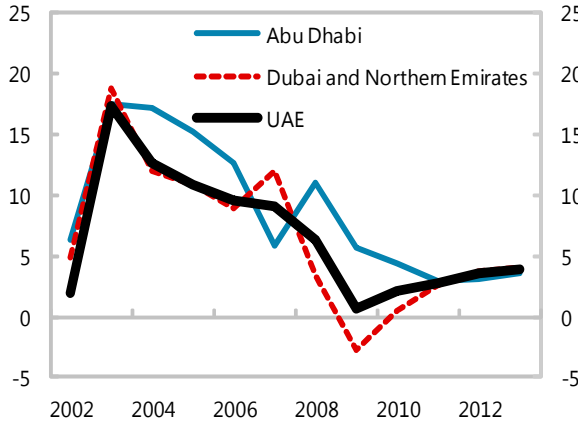
42. **It is recommended that the next Article IV consultation take place on the standard 12-month cycle.**

Figure 2. United Arab Emirates: The Nonhydrocarbon Economy

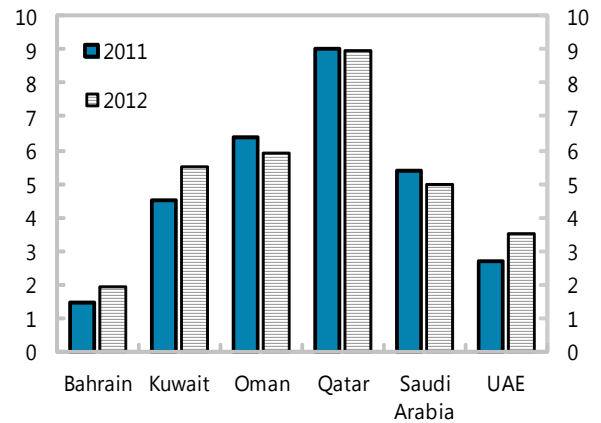
The recovery in nonhydrocarbon growth is gaining strength...

...but the UAE still lags behind most of its GCC peers.

Dubai and Abu Dhabi Non-hydrocarbon GDP Growth
(Annual percent change)



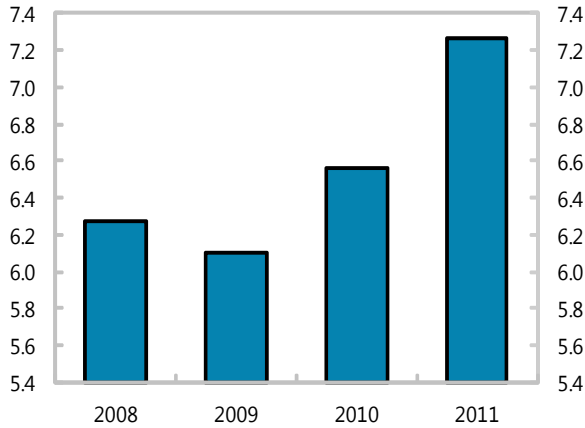
GCC Non-oil GDP Growth
(Percent change)



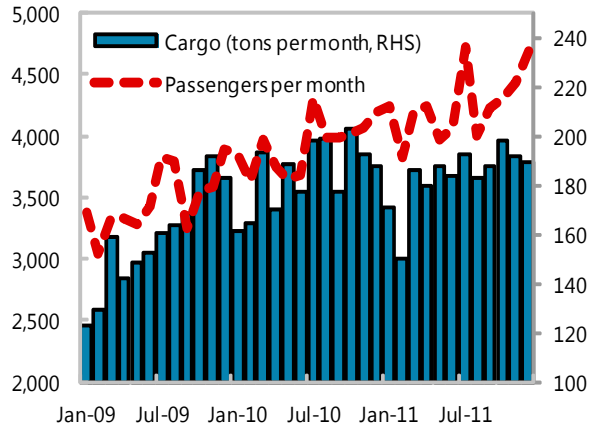
The hospitality sector is one of the major drivers of Dubai's growth...

...along with the transportation sector.

Dubai: Total Hotel Guests, 2008–2011
(Millions)



Traffic at Dubai International Airport
(Thousands)



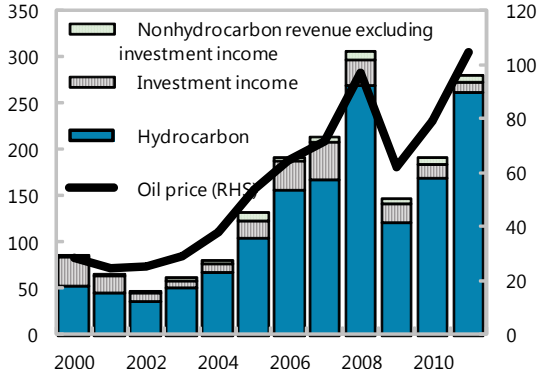
Sources: Dubai Statistics Center; Dubai Airport; country authorities; and IMF staff estimates.

Figure 3. United Arab Emirates: Fiscal Developments

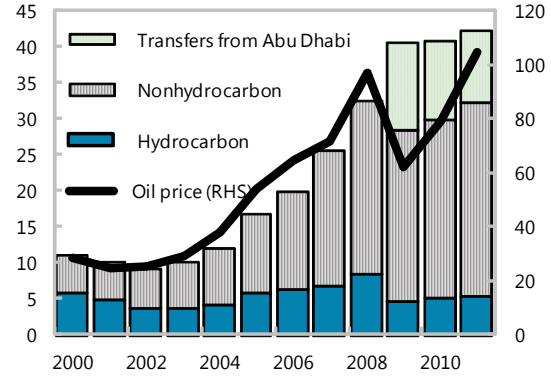
Abu Dhabi relies overwhelmingly on hydrocarbon revenues...

... while Dubai's revenues are mostly from nonhydrocarbon sources.

Abu Dhabi Revenues and the Oil Price
(Billions of Dirhams)



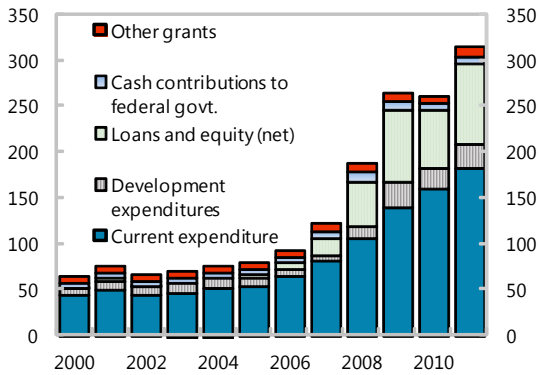
Dubai Revenues and the Oil Price
(Billions of Dirhams)



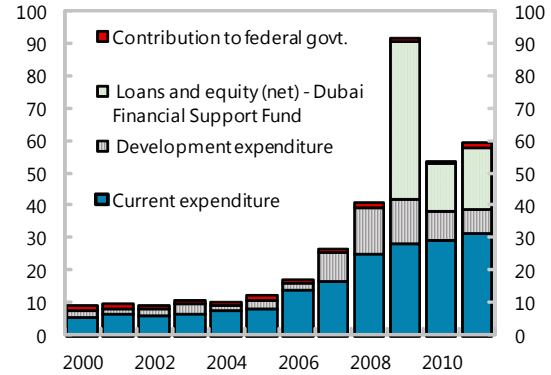
Government support to GREs ballooned in Abu Dhabi ...

... and Dubai.

Abu Dhabi Expenditures
(Billions of Dirhams)



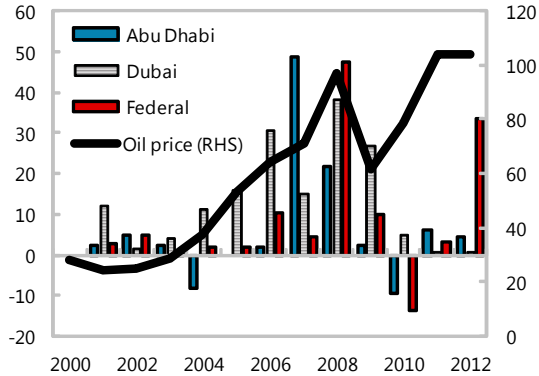
Dubai Expenditures
(Billions of Dirhams)



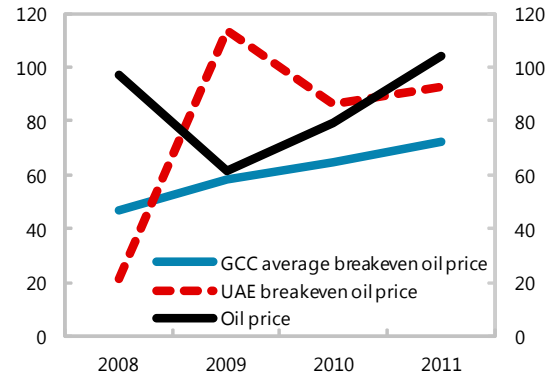
Wage bill growth moderated during the crisis, but it is picking up again this year.

The UAE's fiscal breakeven oil price has almost quadrupled since 2008.

Wage Bill Growth Rate and the Oil Price
(In percent)



Breakeven Oil Prices
(U.S. dollars per barrel)



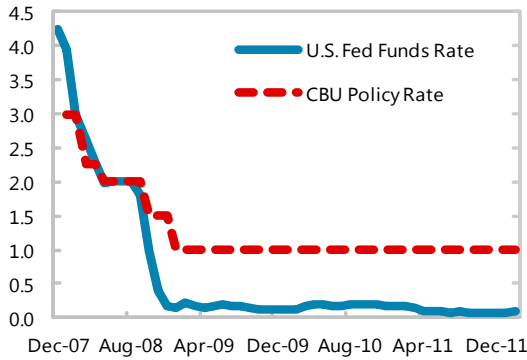
Sources: Country authorities and IMF staff calculations.

Figure 4. United Arab Emirates: Monetary and Financial Developments

Monetary conditions remain accommodative...

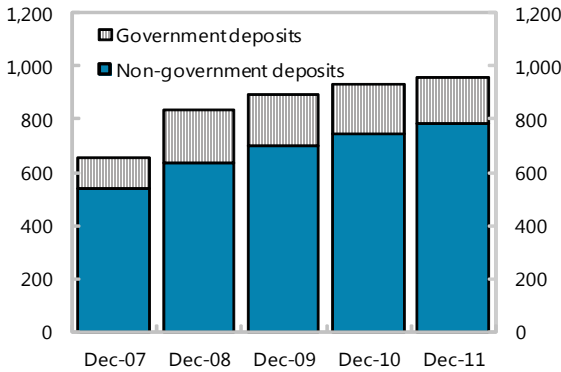
...with ample liquidity...

Policy Rates
(Percent)



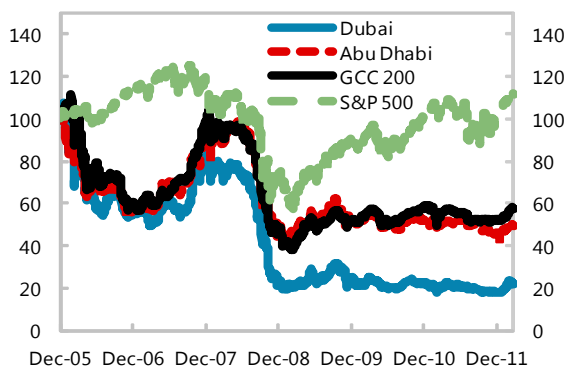
...despite slow deposit growth in 2011.

Bank Deposits
(Billions of Dirham)

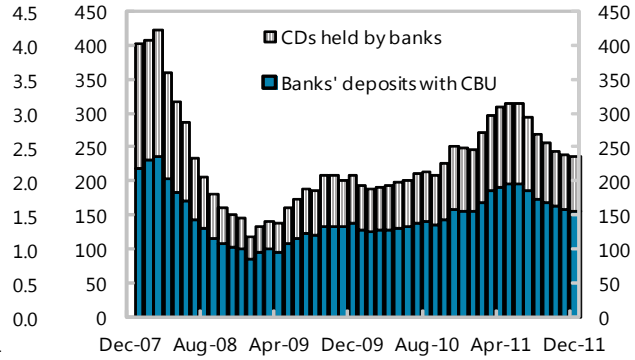


Equity markets remain subdued.

Stock Market Indices
(Index, Dec. 31, 2005=100)

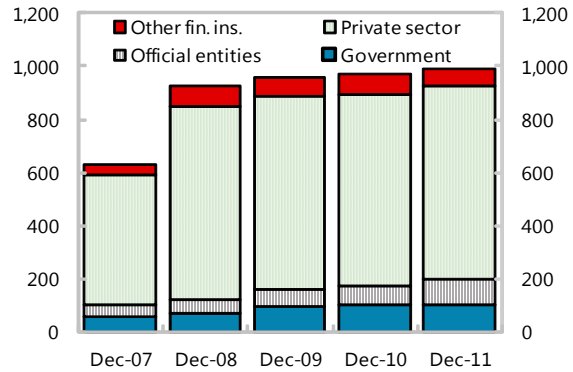


Bank Liquidity
(Billions of Dirham)



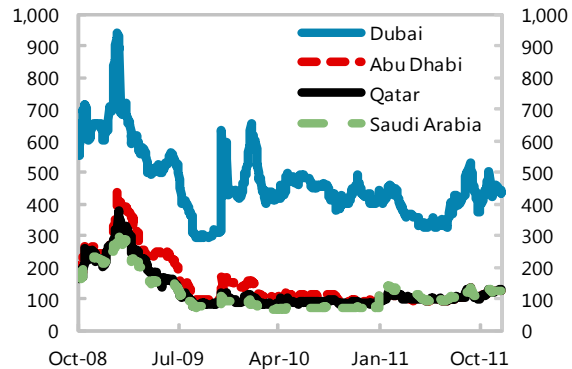
The increase in credit in 2011 was mainly to Government and official entities.

Bank Credit
(Billions of Dirham)



CDS spreads in Dubai are in a downward trend

GCC: CDS Spreads
(Basis points)



Sources: Haver; Markit; Bloomberg; and country authorities.

Table 1. United Arab Emirates: Selected Macroeconomic Indicators, 2008–17

(Quota: SDR 752.5 million)
 (Population: 5 million, nationals: 1 million)
 (Per capita GDP-2009: \$53,477; poverty rate: n.a.; unemployment rate: 4.2% (2009))

	2008	2009	2010	Est. 2011	Proj. 2012	Proj. 2013	Proj. 2014	Proj. 2015	Proj. 2016	Proj. 2017
Hydrocarbon sector										
Exports of oil, oil products, and gas (in billions of U.S. dollars)	103.0	68.1	74.6	111.6	122.1	118.4	112.9	108.7	106.2	105.3
Average crude oil export price (in U.S. dollar per barrel)	96.3	62.8	77.0	109.6	119.7	115.0	107.8	102.2	98.3	96.0
Crude oil production (in millions of barrels per day)	2.6	2.3	2.3	2.6	2.6	2.6	2.6	2.7	2.7	2.8
(Annual percent change, unless otherwise indicated)										
Output and prices										
Nominal GDP (in billions of UAE dirhams)	1,156	993	1,093	1,323	1,419	1,449	1,480	1,520	1,576	1,646
Nominal GDP (in billions of U.S. dollars)	315	270	298	360	386	394	403	414	429	448
Real GDP	5.3	-3.3	0.9	4.9	2.3	2.8	3.3	3.5	3.6	3.7
Real hydrocarbon GDP	1.6	-9.9	-1.5	9.2	0.0	1.0	2.0	1.9	1.8	1.9
Real nonhydrocarbon GDP	6.3	0.6	2.1	2.7	3.5	3.8	4.0	4.2	4.5	4.5
CPI inflation (average)	12.3	1.6	0.9	0.9	1.5	1.7	1.9	1.9	1.9	2.1
(Percent of GDP, unless otherwise indicated)										
Investment and saving										
Gross domestic investment	22.5	23.9	25.3	22.4	24.6	23.4	22.4	22.5	22.9	23.5
Change in stocks	1.3	1.6	1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total fixed capital formation	21.2	22.3	23.8	22.4	24.6	23.4	22.4	22.5	22.9	23.5
Public	7.4	9.1	8.6	7.5	10.6	9.3	8.3	7.5	6.8	6.2
Private	13.8	13.2	15.2	14.9	14.0	14.2	14.1	15.0	16.1	17.2
Gross national saving	30.1	27.1	28.5	31.7	34.9	33.8	32.3	32.0	32.2	32.6
Public	24.3	4.5	7.6	13.8	16.3	15.0	13.2	12.5	11.8	11.7
Private	5.8	22.7	20.9	17.8	18.6	18.8	19.1	19.6	20.4	20.9
Public finances										
Revenue	39.0	25.7	28.7	33.3	34.6	33.2	31.5	30.7	30.0	29.7
Hydrocarbon	31.2	17.5	21.4	27.4	28.5	26.9	25.1	23.6	22.2	21.2
Nonhydrocarbon	7.9	8.2	7.2	5.9	6.1	6.2	6.4	7.2	7.7	8.5
Expenditure and net lending	22.3	38.0	30.8	30.4	26.9	26.2	25.9	25.4	25.0	24.5
Current	14.8	21.2	21.0	19.4	18.3	18.2	18.3	18.3	18.2	18.0
Capital	7.2	16.5	9.5	10.5	8.2	7.5	7.1	6.7	6.3	6.0
Overall balance	16.8	-12.3	-2.1	2.9	7.7	7.0	5.7	5.3	5.0	5.2
Non-hydrocarbon primary balance (excluding investment income) 1/	-26.4	-44.3	-35.5	-41.5	-36.5	-33.8	-31.7	-29.8	-28.0	-26.5
Adjusted non-hydrocarbon primary balance 1/ 2/	-26.4	-37.4	-33.6	-37.0	-36.5	-33.8	-31.7	-29.8	-28.0	-26.5
Central government debt to banking system 3/	12.5	22.5	21.3	16.9	14.6	14.3	14.9	15.1	15.1	14.7
(Annual percent change, unless otherwise indicated)										
Monetary sector										
Net foreign assets	-79.4	42.0	67.7	17.9	18.9	8.4	7.6	6.8	7.0	5.7
Net domestic assets	58.2	8.2	2.0	3.6	5.8	9.2	10.3	10.5	11.7	12.4
Credit to private sector	49.3	0.7	1.2	2.3	3.1	5.7	6.5	6.3	7.3	7.6
Broad money	19.2	9.8	6.2	5.0	7.1	9.2	10.0	10.0	11.1	11.6
(Billions of U.S. dollars, unless otherwise indicated)										
External sector										
Exports and re-exports of goods, of which:	240	192	212	279	307	321	336	347	360	376
Hydrocarbon	103	68	75	112	122	118	113	109	106	105
Nonhydrocarbon, excluding re-exports	43	44	51	62	69	74	80	87	95	102
Imports of goods	176	150	161	198	217	228	242	254	266	282
Current account balance	24.8	9.1	9.1	33.3	40.0	40.9	40.1	39.6	39.8	40.8
Current account balance (in percent of GDP)	7.9	3.4	3.1	9.2	10.3	10.4	9.9	9.6	9.3	9.1
External debt (in percent of GDP) 4/	43.2	48.4	47.2	41.0	39.0	39.5	40.1	40.3	40.3	39.9
Gross official reserves 5/	30.9	25.5	32.8	36.4	40.8	44.4	48.2	51.4	55.1	58.6
In months of next year's imports of goods & services	2.0	1.5	1.6	1.6	1.7	1.8	1.8	1.9	1.9	1.9
Memorandum items:										
Local currency per U.S. dollar (period average)	3.67	3.67	3.67	3.67	..	..	..	..	..	..
Nominal effective exchange rate (2000 = 100)	84.2	88.3	87.5	84.9	..	..	..	..	..	..
Real effective exchange rate (2000 = 100)	102.9	107.2	102.7	95.3	..	..	..	..	..	..

Sources: UAE authorities; and IMF staff estimates.

1/ In percent of nonhydrocarbon GDP.

2/ Excludes DFSF related transactions for Dubai, and 2011 ALDAR support and investment income for Abu Dhabi

3/ Banking system claims only. Excludes debt raised by federal and emirati governments in the international markets.

4/ Foreign liabilities of banking system only due to incomplete coverage of debt raised by non-banks in the international markets.

5/ Excludes foreign assets of sovereign wealth funds.

Table 2. United Arab Emirates: Balance of Payments, 2008–17

(Billions of U.S. dollars)

	<u>Est.</u> 2008	<u>Est.</u> 2009	<u>Est.</u> 2010	<u>Est.</u> 2011	<u>Proj.</u> 2012	<u>Proj.</u> 2013	<u>Proj.</u> 2014	<u>Proj.</u> 2015	<u>Proj.</u> 2016	<u>Proj.</u> 2017
Current account balance	24.8	9.1	9.1	33.3	40.0	40.9	40.1	39.6	39.8	40.8
(in percent of GDP)	7.9	3.4	3.1	9.2	10.3	10.4	9.9	9.6	9.3	9.1
Trade balance	63.8	42.5	50.4	81.5	90.7	93.2	94.1	93.1	93.6	94.6
Exports	240.1	192.2	211.9	279.3	307.5	320.7	335.6	346.8	359.8	376.2
Hydrocarbon	91.4	59.6	66.8	99.6	108.8	105.5	100.9	97.5	95.6	95.2
Natural gas	11.5	8.6	7.9	12.0	13.3	12.9	12.0	11.2	10.6	10.2
Nonhydrocarbon	43.0	44.0	51.0	62.1	69.4	74.3	80.4	87.2	94.9	101.6
Re-exports 1/	94.2	80.1	86.2	105.6	116.1	128.0	142.3	150.9	158.7	169.3
Imports (f.o.b.)	-176.3	-149.7	-161.4	-197.8	-216.8	-227.5	-241.6	-253.7	-266.2	-281.6
Imports by emirates	-115.9	-101.4	-113.9	-141.5	-144.8	-148.2	-153.3	-160.2	-167.8	-176.6
Free zones	-60.4	-48.3	-47.5	-56.3	-72.0	-79.3	-88.2	-93.5	-98.4	-105.0
Income, net	5.4	4.2	-0.1	0.0	0.5	0.6	0.6	2.8	4.5	6.8
Banking system (net)	1.3	0.6	-1.3	-1.4	-1.4	-1.4	-1.4	-1.2	-0.9	-0.2
Private non-banks (net)	-0.7	-0.5	-1.6	-1.8	-2.0	-2.1	-2.1	-2.5	-3.2	-4.3
Government	9.8	6.0	6.0	6.8	8.2	8.2	8.2	10.7	12.9	16.1
Official debt service (interest)	0.0	0.0	-0.9	-1.1	-1.1	-1.1	-1.1	-1.3	-1.6	-2.1
Foreign partners - oil	-4.2	-1.5	-2.0	-2.2	-2.4	-2.3	-2.2	-2.2	-2.1	-2.1
Foreign partners - gas	-0.8	-0.3	-0.2	-0.4	-0.8	-0.7	-0.7	-0.7	-0.7	-0.6
Services, net	-33.8	-27.4	-29.9	-36.2	-38.4	-39.6	-41.2	-42.5	-43.9	-45.6
Credits	9.6	10.2	11.7	12.8	13.8	14.9	16.2	17.5	19.0	20.7
Debits	-43.4	-37.6	-41.7	-49.0	-52.2	-54.5	-57.3	-60.0	-62.9	-66.3
Transfers, net	-10.6	-10.2	-11.3	-12.0	-12.9	-13.2	-13.5	-13.8	-14.3	-15.0
Capital account balance	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial account balance	-19.9	8.4	5.8	-17.1	-35.5	-37.3	-36.2	-36.4	-36.1	-37.4
Private capital	9.6	-4.4	7.7	9.4	8.3	9.9	10.1	10.4	10.7	11.0
Direct investment, net	-2.1	1.3	3.5	5.5	5.7	5.8	6.0	6.1	6.2	6.4
Portfolio flows, net	2.2	2.5	1.0	0.7	1.0	1.0	1.0	1.1	1.1	1.2
Commercial banks	-12.2	-9.9	-1.3	0.7	-0.3	1.0	1.1	1.1	1.1	1.2
Private non-banks and other 2/	21.7	1.8	4.6	2.5	1.9	2.0	2.1	2.2	2.2	2.3
Official capital 3/	-29.5	12.8	-1.9	-26.5	-43.8	-47.2	-46.4	-46.9	-46.9	-48.4
Errors and omissions	-51.7	-23.5	-7.6	-11.7	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-46.8	-6.0	7.3	4.6	4.5	3.6	3.8	3.2	3.7	3.5
Change in central bank reserves	46.8	6.0	-7.3	-4.6	-4.5	-3.6	-3.8	-3.2	-3.7	-3.5
Memorandum items:										
GDP (billions of U.S. dollars)	314.8	270.3	297.6	360.1	386.4	394.5	402.9	414.0	429.1	448.3
Gross reserves of central bank (billions of U.S. dollars)	30.9	25.5	32.8	36.4	40.8	44.4	48.2	51.4	55.1	58.6
in months of next year's imports	2.0	1.5	1.6	1.6	1.7	1.8	1.8	1.9	1.9	1.9

Sources: UAE authorities; and IMF staff estimates.

1/ Not separately compiled; estimated at 40 to 70 percent of emirates imports.

2/ Estimate based on *UNCTAD World Investment Report*.

3/ Including estimated changes in SWF net external assets.

Table 3. United Arab Emirates: Consolidated Government Finances, 2008–12 1/

	2008	2009	2010	Est. 2011	Proj. 2012
	(Billions of UAE dirhams)				
Total revenue	449.6	255.0	313.2	439.6	490.4
Hydrocarbon 2/	360.5	174.1	234.0	362.6	404.3
Nonhydrocarbon	89.1	80.9	79.2	77.0	86.1
Expense	174.4	214.2	232.8	227.8	231.2
of which: foreign grants 3/	3.6	3.3	2.6	5.6	5.9
Gross operating balance	275.2	40.8	80.4	211.7	259.2
Net acquisition of nonfinancial assets	29.5	45.0	35.1	36.8	55.8
Net lending(+)/borrowing(-)	245.7	-4.2	45.3	175.0	203.3
Net acquisition of financial assets	255.6	169.3	135.5	186.1	171.7
of which: Dubai Financial Support Fund	...	48.9	14.7	19.2	...
Net incurrence of liabilities	10.0	173.4	90.2	11.2	-31.6
	(Percent of GDP)				
Total revenue	38.9	25.7	28.6	33.2	34.6
of which: hydrocarbon revenues	31.2	17.5	21.4	27.4	28.5
Expense	15.1	21.6	21.3	17.2	16.3
Gross operating balance	23.8	4.1	7.4	16.0	18.3
Net acquisition of nonfinancial assets	2.5	4.5	3.2	2.8	3.9
Net lending(+)/borrowing(-)	21.2	-0.4	4.1	13.2	14.3
	(Percent of nonhydrocarbon GDP)				
Total revenue	61.7	36.1	41.8	55.6	58.5
of which: nonhydrocarbon revenues	12.2	11.5	10.6	9.7	10.3
Expense	23.9	30.4	31.1	28.8	27.6
Net acquisition of nonfinancial assets	4.0	6.4	4.7	4.6	6.7
Memorandum items:	(Percent of nonhydrocarbon GDP, unless otherwise indicated)				
Nonhydrocarbon primary balance incl loans and equity; excl. investment income	-26.4	-44.3	-35.5	-41.5	-36.5
Nonhydrocarbon primary balance (net lending/borrowing) excl. investment income	-19.2	-27.6	-26.4	-24.3	-25.3
Adjusted non-hydrocarbon primary balance 4/	-26.4	-37.4	-33.6	-37.0	-36.5
Overall balance (in billions of UAE dirhams)	193.7	-122.4	-23.0	38.6	109.2
(In percent of GDP)	16.8	-12.3	-2.1	2.9	7.7
Net loans and equity (in billions of UAE dirhams)	51.8	117.9	68.2	101.6	60.0
(In percent of GDP)	4.5	11.9	6.2	7.7	4.2
Hydrocarbon share of revenue (in percent)	80.2	68.3	74.7	82.5	82.4
Nonhydrocarbon revenue, excl. investment income (in billions of UAE dirhams)	60.6	61.2	63.4	64.8	68.9
Sources: Federal government; Emirate finance departments; and IMF staff estimates.					
1/ Consolidated accounts of the federal government, Abu Dhabi, Dubai and Sharjah. GFSM 2001 classification.					
2/ Includes staff estimates of revenues from other government entities operating in the oil and gas sector.					
3/ Intragovernmental grants are netted out in the consolidated fiscal accounts.					
4/ Excludes DFSF related transactions for Dubai, and 2011 ALDAR support and investment income for Abu Dhabi.					

Table 3a. United Arab Emirates: Abu Dhabi Government Finances, 2008–12 1/

	2008	2009	2010	Est. 2011	Proj. 2012
(Billions of UAE dirhams)					
Total revenue	305.7	147.1	192.2	280.9	320.0
Hydrocarbon	269.6	121.8	169.1	261.5	295.2
Nonhydrocarbon	36.1	25.3	23.0	19.4	24.8
Expense	105.4	139.0	159.1	182.0	180.6
of which: grants	19.0	17.4	14.1	17.5	17.9
Gross operating balance	200.3	8.1	33.1	98.9	139.5
Net acquisition of nonfinancial assets	13.2	27.6	23.8	27.4	44.8
Net lending(+)/borrowing(-)	187.1	-19.5	9.4	71.5	94.7
(Percent of Abu Dhabi GDP)					
Total revenue	43.4	24.7	31.0	34.7	36.7
Hydrocarbon	38.2	20.4	27.3	32.3	33.9
Nonhydrocarbon	5.1	4.2	3.7	2.4	2.8
Expense	15.0	23.3	25.6	22.5	20.7
Grants	2.7	2.9	2.3	2.2	2.0
Gross operating balance	28.4	1.4	5.3	12.2	16.0
Net acquisition of nonfinancial assets	1.9	4.6	3.8	3.4	5.1
Net lending(+)/borrowing(-)	26.5	-3.3	1.5	8.8	10.9
Memorandum items:	(Percent of Abu Dhabi GDP, unless otherwise indicated)				
Nonhydrocarbon balance (net lending/borrowing)	-11.7	-23.7	-25.8	-23.5	-23.0
Loans and equity net (billions of UAE dirhams)	49.7	79.8	63.3	87.9	57.5
Loans and equity net	7.0	13.4	10.2	10.8	6.6

Sources: Abu Dhabi Department of Finance, and IMF staff estimates and projections.

1/ GFSM 2001 classification.

Table 3b. United Arab Emirates: Dubai Government Finances, 2008–12 1/

	2008	2009	2010	<u>Est.</u> 2011	<u>Proj.</u> 2012
	(Billions of UAE dirhams)				
Total revenue	32.6	28.4	29.9	32.3	30.4
Nontax revenue	25.0	21.3	22.8	24.3	23.8
Tax revenue	7.6	7.1	7.1	8.0	6.6
Expense	25.3	28.4	29.4	31.7	29.7
Gross operating balance	7.3	0.0	0.5	0.5	0.8
Net acquisition of nonfinancial assets	14.3	13.5	8.9	7.1	5.9
Net lending(+)/borrowing(-)	-7.0	-13.5	-8.4	-6.5	-5.1
	(Percent of Dubai and Northern Emirates GDP)				
Total revenue	7.2	7.2	6.3	6.3	5.6
Expense	5.6	7.2	6.2	6.2	5.4
Gross operating balance	1.6	0.0	0.1	0.1	0.1
Net acquisition of nonfinancial assets	3.2	3.4	1.9	1.4	1.1
Net lending(+)/borrowing(-)	-1.6	-3.4	-1.8	-1.3	-0.9
Memorandum items:	(Billions of UAE dirhams, unless otherwise indicated)				
Loans and equity net	0.0	48.9	14.7	19.2	0.0
of which Dubai Financial Support Fund	0.0	48.9	14.7	19.2	0.0
Loan from Abu Dhabi	0.0	12.1	11.0	9.9	0.0
Loans and equity net (in percent of GDP)	0.0	12.3	3.1	3.7	0.0
Loan from Abu Dhabi (in percent of GDP)	0.0	3.1	2.3	1.9	0.0

Sources: Dubai Department of Finance, and IMF staff estimates and projections.

1/ GFSM 2001 classification.

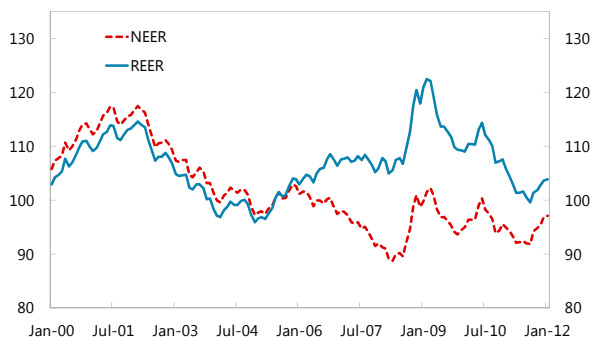
Table 4. United Arab Emirates: Monetary Survey, 2008–12

	2008	2009	2010	Est. 2011	Proj. 2012
	(Billions of UAE dirhams)				
Net foreign assets	33	47	78	93	110
Foreign assets	317	302	354	382	401
Central Bank	114	94	121	134	150
Commercial banks	203	208	234	249	251
Foreign liabilities	284	255	276	290	291
Central bank	1	4	4	0	0
Commercial banks	283	251	272	290	291
Net domestic assets	641	694	708	733	774
Claims on government (net)	-85	10	30	45	46
Claims	140	219	228	220	206
Deposits	225	208	198	175	160
Claims on public sector enterprises	56	77	88	120	134
Claims on private sector	875	881	892	912	940
Real estate mortgage loans					
Other items (net)	-205	-275	-301	-343	-346
Capital and reserves (-)	-167	-246	-275	-298	-311
Other assets (net)	-38	-29	-26	-45	-35
Central Bank	-108	-141	-167	-172	-178
Commercial banks	70	112	141	126	144
Of which: certificates of deposits	47	71	94	80	91
Broad money (M2)	674	741	786	826	884
Money	208	223	233	264	283
Currency outside banks	37	37	39	42	45
Dirham demand deposits	171	186	194	223	238
Quasi-money	466	517	553	562	602
Foreign currency deposits	119	122	129	144	154
Dirham time and savings deposits	348	396	425	418	447
<i>Memorandum items:</i>					
Dh-denominated liquidity	556	619	658	682	730
Reserve money	37	37	39	42	45
Foreign currency deposits / total deposits (in percent)	18.6	17.3	17.2	18.4	18.4
NFA/ M2 (in percent)	4.9	6.3	10.0	11.2	12.4
CBU foreign assets/reserve money (in percent)	93.3	82.3	107.2	97.0	103.4
NFA of Central Bank	112.2	89.7	116.7	133.4	149.9
NFA of commercial banks	-79.2	-42.9	-38.2	-40.9	-39.9
M2 velocity (nonhydrocarbon GDP)	1.1	1.0	1.0	1.0	0.9
	(Changes in percent; unless otherwise indicated)				
Claims on private sector	49.3	0.7	1.2	2.3	3.1
Broad money (M2)	19.2	9.8	6.2	5.0	7.1
Money	14.6	7.4	4.2	13.4	7.1
Quasi Money	21.4	10.9	7.0	1.5	7.1
Base money	32.2	-6.5	-1.3	22.5	5.3
Money multiplier (M2/base money)	5.5	6.5	7.0	6.0	6.1
Sources: Central Bank of the UAE, and IMF staff estimates and projections.					

Appendix I. Exchange Rate Assessment

1. **The real exchange rate has continued depreciating.** Following a period of appreciation between 2005 and 2008 in light of inflation developments, the real effective exchange rate (REER) has been depreciating since 2009. It depreciated by a further 4 percent in 2011.

Real and Nominal Effective Exchange Rates, 2000–12
(Index, 2005=100)



Source: Fund staff estimates.

2. **The standard methodologies for exchange rate assessment yield mixed results, suggesting that there is no strong evidence for exchange rate misalignment.**

- **The equilibrium exchange rate approach indicates undervaluation.** This approach estimates a cointegration relationship between the REER and the real oil price. As of end-2011, the REER was about 10 percent undervalued.¹

- **The macroeconomic balance approach indicates little evidence of exchange rate misalignment.** This approach (MB) employs a generalized method of moments (GMM) estimation in a dynamic panel setting, and explicitly adds underground hydrocarbon wealth and estimates of accumulated foreign assets.² It yields a current account norm surplus of 10.7 percent of GDP in 2017 (average of four specifications ranging from 1.8 to 18.7 percent of GDP), compared to a projected current account position of 9.1 percent, yielding little evidence of exchange rate misalignment.

Results of CGER-type Analysis
(Percent of GDP)

	MB ¹	ES ²	ERER ³
Current account balance (2017 proj.)	9.1	9.1	9.1
Current account norm	10.7	16.8	...
Deviation from norm	-1.6	-7.7	...
ER over/undervaluation (percent)	2.6	12.5	-10

Source: IMF staff estimates and projections.

¹ Average of all specifications in Beidas-Strom and Cashin (2011).

² Follows a constant real per capital allocation rule.

³ Equilibrium exchange rate approach.

¹ See: Cashin, P., S. Ouliaris, and T. Poghosyan (forthcoming), "Oil currencies." Working Paper, International Monetary Fund, Washington, D.C.

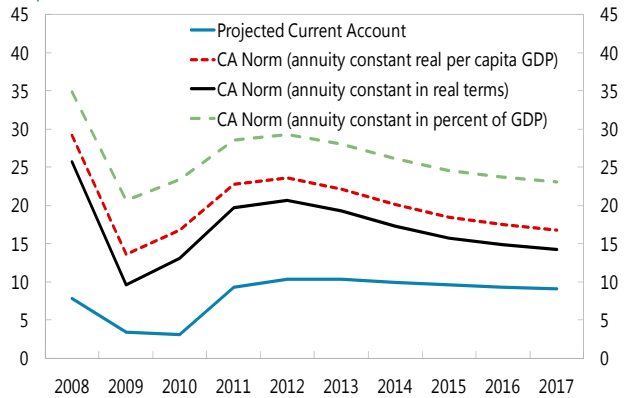
² See: Beidas-Strom, S. and P. Cashin (2011), "Are Middle-Eastern Current Account Imbalances Excessive." IMF Working Paper 11/195, Washington, D.C.

3. The external sustainability approach indicates an overvaluation of the dirham.

Based on the permanent income hypothesis, this approach estimates the current account norm such that future oil and financial income is sufficient to finance a steady stream of imports, even after the depletion of hydrocarbon resources, supporting intergenerational equity. Choosing a constant real per capita annuity as a benchmark indicates an overvaluation which implies a need to accumulate further savings of about 8 percent of GDP in 2017.

Current Account Norms vs. Projected Current Account

(In percent of GDP)



Source: IMF staff calculations and projections.

Appendix II. Government-Related Entities: Financial Risk and How to Manage It

1. GREs play an important role in the UAE economy but are also a source of risks.

While the GREs have been instrumental to the U.A.E. rapid economic development and diversification, large borrowing during the boom period led to a boom-bust cycle, reinforced by heightened vulnerabilities to the global financial crisis. The relatively large importance of GREs in the UAE, and the lack of timely and aggregate information about their performance and financial situation, creates potential risks.

2. Following the crisis, some progress was made in GRE debt restructuring.

The debt restructuring of Dubai World was completed with the involvement of the authorities, and more recently, Dubai International Capital announced an agreement to restructure about \$2.5 billion of its debt. However, restructuring of other GREs debt has been progressing more slowly. In particular, a restructuring of \$10 billion of Dubai Group debt (part of Dubai Holding) is under discussion.

3. GRE activities are increasingly coordinated within emirates.

The Dubai’s Supreme Fiscal Council is now monitoring the overall level of sovereign and GRE debt, which should allow for better risk management. Abu Dhabi’s debt management office is playing a similar role.

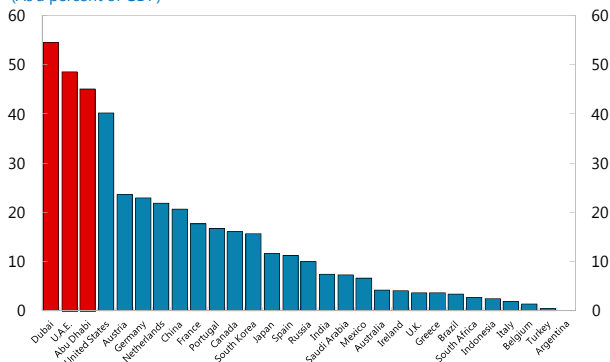
4. GRE indebtedness and rollover needs remain large.

Since 2010, GRE debt (including government-guaranteed debt) has remained broadly stable in nominal terms (\$185 billion), but the ratio of GRE debt to GDP has fallen significantly, to 51 percent. The UAE’s GRE debt remains high in international

comparison. Dubai GRE debt moderately decreased while Abu Dhabi’s GRE debt rose. Rollover needs remain significant, with \$30 billion in GRE debt maturing this year, a multiple of maturing government debt. Significant amounts of debt will mature in 2014–15, partly as result of earlier debt restructuring.

GRE Gross Debt, 2011

(As a percent of GDP)



Sources: Dealogic; and WEO.

United Arab Emirates GRE Debt

	End-2010		March 2012	
	US\$ billion	in % of 2010 GDP 1/	US\$ billion	in % of 2011 GDP 1/
Total GRE debt	182.3	61.2	184.8	51.3
Government guaranteed	13.0	4.4	9.7	2.7
Other	169.3	56.9	175.2	48.6
Abu Dhabi GRE debt	92.9	55.0	100.6	45.6
Government guaranteed	0.5	0.3	1.4	0.6
Other	92.4	54.7	99.2	45.0
Dubai GRE debt	89.4	69.4	84.3	60.4
Government guaranteed	12.5	9.7	8.3	5.9
Other	76.9	59.7	76.0	54.4

Sources: Dealogic, Zawya, Bloomberg, U.A.E. authorities, and Fund staff estimates.
1/ In percent of Abu Dhabi GDP and Dubai and Northern Emirates GDP; UAE GDP for total debt.

5. Refinancing this large amount of maturing debt remains a challenge.

The GREs’ high dependence on foreign funding increases the vulnerability to rollover and financing risk, especially in the current volatile external financial environment. This vulnerability is exacerbated by the deleveraging of European banks, which have been reducing their exposure to the region.

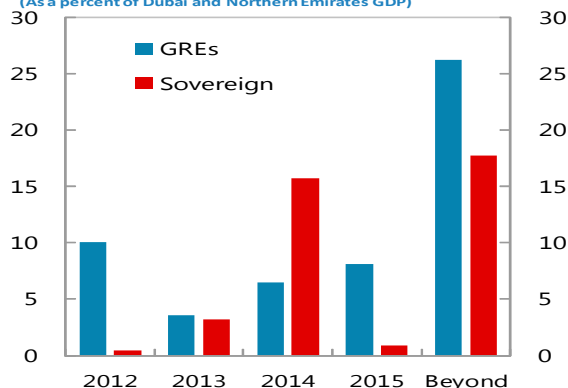
Credit rating agencies have pointed out risks related to two 2012 maturities: DIFC Investments' \$1.25 billion sukuk maturing in June, and Jebel Ali Free Zone's (JAFZA) \$2 billion sukuk maturing in November. JAFZA has announced preliminary plans for managing this maturity.

6. Improved economic prospects and a more proactive approach to managing rollovers mitigate the refinancing risks.

Nonhydrocarbon GDP growth is gradually picking up, supporting asset prices and improving GREs cash flows, and GREs are now focusing less on expansion and borrowing than on consolidation and deleveraging. A number of GREs are planning to use cash from asset sales and operational cash flow to repay part of the maturing debt.¹ In response to the prospects that some European banks may not renew their credit, GREs are actively looking for alternative investors, particularly in Asia and the Gulf region. At the same time, the authorities noted that lenders are becoming more diligent in evaluating borrowers' repayment capacity.

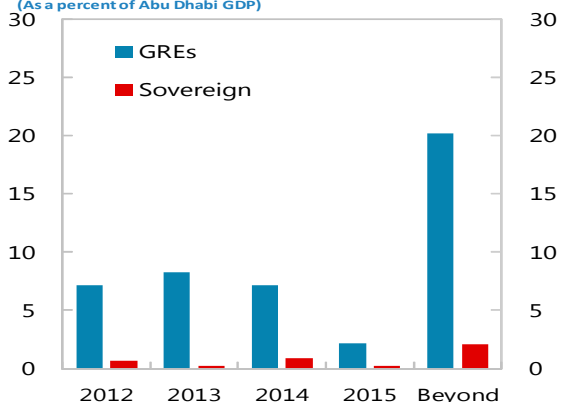
7. Financial market developments appear to be supporting this view of a cautious optimism. Following a moderate increase in late 2011, sovereign and GRE CDS spreads have been coming down in 2012.

Dubai Maturing GREs and Sovereign Debt
(As a percent of Dubai and Northern Emirates GDP)



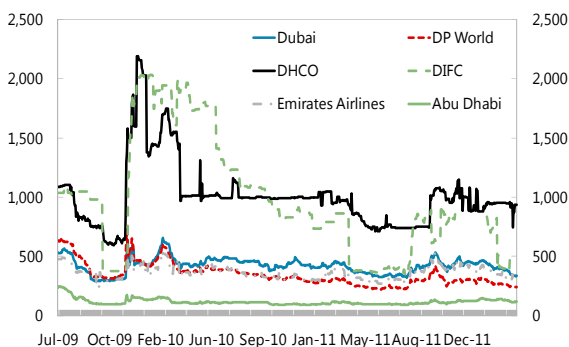
Sources: Bloomberg; Dealogic; country authorities; and IMF staff estimates.

Abu Dhabi Maturing GREs and Sovereign Debt
(As a percent of Abu Dhabi GDP)



Sources: Bloomberg; Dealogic; country authorities; and IMF staff estimates.

UAE – Government and Selected GRE CDS Spreads
(Basis points)



Source: Markit.

¹ Dubai Ports World has recently announced the intention to repay the \$3 billion loan maturing in October 2012 using the available cash.

Table A.1. Dubai: Maturing Bonds and Syndicated Loans 1/ 2/
(In millions of U.S. dollars)

Debt Type	2012	2013	2014	2015	Beyond	Total
Dubai World and subsidiaries						
Bonds	2,043	0	350	3,200	3,600	9,193
Loans	3,000	546	409	6,662	12,937	23,554
Total	5,043	546	759	9,862	16,537	32,747
Dubai Holding and subsidiaries						
Bonds	0	93	995	0	977	2,065
Loans	0	0	3,645	705	5,220	9,570
Total	0	93	4,640	705	6,197	11,635
Investment Corporation of Dubai and subsidiaries						
Bonds	1,678	1,288	67	0	4,374	7,407
Loans	2,282	2,080	93	510	6,473	11,438
Total	3,960	3,368	160	510	10,847	18,845
Other Dubai Inc. 3/						
Bonds	1,250	871	0	1,000	2,000 4/	5,121
Loans	2,639	1,100	3,090	0	2,289	9,118
Total	3,889	1,971	3,090	1,000	4,289	14,239
Total Dubai Inc.						
	12,891	5,978	8,649	12,077	37,871	77,466
Other Dubai Inc. 5/						
Bonds	750	599	0	0	520	1,869
Loans	1,000	1,100	1,149	0	1,676	4,925
Total	1,750	1,699	1,149	0	2,196	6,794
Government of Dubai						
Bonds	0	1,770	21,211	500	2,250 6/	25,731
Loans foreign	0	0	0	0	1,011	1,011
Loans domestic						18,026
Total	0	1,770	21,211	500	3,261	44,767
Total Dubai Debt						
	14,641	9,447	31,008	12,577	43,327	129,027
In percent of Dubai and NE 2011 GDP						
	10.5	6.8	22.2	9.0	31.0	92.4
Memorandum items:						
Restructured Debt	0	0	5,400	10,005	15,100	30,505
Government guaranteed 7/	648	2,734	748	748	3,414	8,292
Total GD including Guarantees	648	4,503	21,959	1,248	6,675	53,059

Sources: Dealogic, Zawya, Bloomberg, Dubai authorities, and Fund staff estimates.

1/ Excluding bilateral bank loans and accounts payable, except for bilateral domestic loan to GoD.

2/ Regardless of residency of debt holders.

3/ Includes DEWA, DIFC, DAE, Borse Dubai, and others.

4/ Assuming DEWA fully draws its receivables-securitization program under Thor Asset Purchase (Cayman) Ltd.

5/ Dubai GREs with government ownership below 50% (Emaar, DIB, CBD).

6/ Assuming Abu Dhabi direct and indirect support is fully drawn.

7/ Mainly ICD holding level and DEWA debt, in addition to the governments'.

Table A.2. Abu Dhabi: Maturing Bonds and Syndicated Loans

(In millions of U.S. dollars)

Debt Type	2012	2013	2014	2015	Beyond	Total
Abu Dhabi Investment Council 1/						
Bonds	903	365	1,933	1,345	3,138	7,684
Loans	980	1,218	750	0	881	3,829
Total	1,883	1,583	2,683	1,345	4,019	11,513
Abu Dhabi Water & Electricity Authority 2/						
Bonds	0	0	0	0	0	0
Loans	698	659	610	610	1,165	3,742
Total	698	659	610	610	1,165	3,742
Etihad						
Bonds	0	0	0	0	0	0
Loans	0	0	0	0	3,652	3,652
Total	0	0	0	0	3,652	3,652
International Petroleum Investment Company 3/						
Bonds	389	355	0	1,001	8,713	10,458
Loans	6,486	9,526	1,805	262	1,730	19,809
Total	6,875	9,881	1,805	1,263	10,443	30,267
Mubadala Development Company 4/						
Bonds	0	0	1,250	0	2,000	3,250
Loans	755	460	600	744	5,154	7,712
Total	755	460	1,850	744	7,154	10,962
Tourism and Development Investment Company						
Bonds	0	0	2,000	0	0	2,000
Loans	0	600	0	0	0	600
Total	0	600	2,000	0	0	2,600
Other Abu Dhabi Inc. 5/						
Bonds	0	0	0	0	0	0
Loans	1,446	749	491	390	740	3,816
Total	1,446	749	491	390	740	3,816
GREs & Banks with 50% or above owned by Abu Dhabi government: TAQA						
Bonds	1,500	2,088	1,200	0	3,413	8,201
Loans	0	850	9	0	1,126	1,985
IWPP Nonrecourse loan	363	411	438	455	8,072	9,738
Total	1,863	3,348	1,647	455	12,611	19,924
Other Abu Dhabi Inc. (less than 50% state-owned) 6/						
Bonds	470	1,021	1,250	0	2,063	4,804
Loans	1,806	0	3,394	0	2,708	7,907
Total	2,276	1,021	4,644	0	4,771	12,711
Total Abu Dhabi Inc.	15,796	18,302	15,729	4,806	44,555	99,188
Government of Abu Dhabi						
Bonds	1,000	0	1,500	0	1,500	4,000
Loans	331	396	383	384	2,206	3,700
Guarantees	75	150	150	150	875	1,400
Total	1,406	546	2,033	534	4,581	9,100
Total Abu Dhabi Debt	17,202	18,848	17,762	5,340	49,136	108,288
In percent of Abu Dhabi 2011 GDP	7.8	8.5	8.1	2.4	22.3	49.1

Source: Dealogic, Zawya, Bloomberg, U.A.E. authorities, and Fund staff estimates

1/ Includes ADCB, NBAD, UNB

2/ Excludes TAQA

3/ Includes US\$2.5 billion Nov issuance

4/ Includes Dolphin, EMAL

5/ DMO coverage (TDIC, Etihad, ADPC, ADNEC, GHC) less TDIC and Etihad that are recorded separately

6/ Below 50 percent Government owned entities; includes Aldar, FGB, NCCC, Sorouh, ADIB



UNITED ARAB EMIRATES

STAFF REPORT FOR THE 2012 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

April 27, 2012

Prepared By

Middle East and Central Asia Department

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ANNEX I. FUND RELATIONS

(As of April 2012)

I. **Membership Status:** Joined 9/22/72; accepted Article VIII status in February 1974

II. General Resources Account

	SDR Million	Percent Quota
Quota	752.5	100.00
Fund holdings of currency	514.46	68.37
Reserve position in Fund	238.62	31.71

III. SDR Department

	SDR Million	Percent Allocation
Net cumulative allocation	568.41	100.00
Holdings	541.89	95.33

IV. **Outstanding Purchases and Loans:** None

V. **Latest Financial Arrangements:** None

VI. Projected Payments to Fund

	Forthcoming				
	2012	2013	2014	2015	2016
Principal					
Charges/interest	0.04	0.05	0.05	0.05	0.05
Total	0.04	0.05	0.05	0.05	0.05

VII. Implementation of HIPC Initiative:

Not Applicable

VIII. Implementation of Multilateral

Debt Relief Initiative (MDRI): Not Applicable

IX. Implementation of Post-Catastrophe

Debt Relief (PCDR): Not Applicable

X. Exchange Arrangement

The UAE dirham was officially pegged to the SDR at the rate of AED 4.76190=SDR1 from

November 1980 to February 2002—albeit de facto it was pegged to the dollar at a fixed parity. Since then, the U.A.E. dirham has been de jure pegged to the U.S. dollar, with the mid-point between the official buying and selling rates fixed at AED 3.6725 = US\$1.

The U.A.E. has accepted the obligation of Article VIII, Sections 2, 3, and 4. There are no restrictions on the making of payments and transfer for current international transactions, except for those restrictions for security reasons that have been notified to the Fund, by the authorities, in accordance with Executive Board Decision No. 144 (52/51).

XI. Article IV Consultation

The U.A.E. is on the annual consultation cycle. The previous consultation discussions were held during February 27-March 7, 2011. The Article IV was concluded on a Lapse of Time basis on April 27, 2011. The staff report was published on May 23, 2011, and is available at <http://www.imf.org/external/pubs/cat/longres.aspx?sk=24865.0> (Country Report No. 11/111).

XII. FSAP Participation, ROSCs, and OFC Assessments

FSAP missions visited the UAE in 2003 and 2007.

XIII. **Technical Assistance:**

FAD	Public Expenditure Management Follow up	May 2003
STA	Multi-sector	December 2003
MFD	Anti-Money Laundering/Combating Terrorist Financing	March 2004
STA	Coordinated Portfolio Investment Survey	April 2004
FAD	Revenue Diversification and VAT Feasibility	November 2005
FAD	Public Financial Management	November 2005
FAD	Gulf Cooperation Council: Options for Indirect and Taxation	March 2006
FAD	UAE: Options for New Indirect Taxation and Intergovernmental Fiscal Relations	March 2006
STA	Compilation of a High-Frequency CPI Index	March 2007
STA	Multi-sector	April 2008
STA	Balance of Payments	March-April 2009
MCM	Macprudential Tools and Liquidity Management	January 2011
STA	National Accounts	September 2011
MCM	Payment Systems	November 2011

XIV. **Resident Representative:** None

ANNEX II. RELATIONS WITH THE WORLD BANK GROUP

(As of March 2012)

Technical cooperation between the United Arab Emirates (UAE) and the Bank started in 1980 on a case-by-case basis. By 1994, the relationship developed to the extent that a Framework Agreement for technical cooperation was signed to facilitate an ongoing program of advisory services.

At the federal level, the Bank provided assistance to the Ministry of Finance in the area of debt market development: a bond market development strategy was completed in May 2008, and the Bank later assisted with certain aspects of its implementation. In 2010, the Ministry of Labor requested technical assistance in labor market development, including Emiratization policies and Labor Market Information System development; the project was completed in 2011. Looking forward, the Bank has submitted a proposal for assistance in the health insurance domain, and there is ongoing dialogue for potential assistance in budget transparency and in enhancing the effectiveness and efficiency of public expenditures in specific sectors.

The Bank has also delivered technical assistance to individual Emirates. In Ras Al Khaimah (RAK), technical cooperation included assistance in promoting a better investment climate and in mobilizing private investment. Following such assistance, an investors' conference (May 2005) attracted major strategic, financial and individual investors from around the world. More recently, the Bank provided advice to the Government of RAK on a multi-jurisdictional student loan program design.

In Abu Dhabi, the Bank provided assistance to Abu Dhabi Food Control Authority on a food security program for the Emirate of Abu Dhabi; at present, the Bank is providing assistance to Abu Dhabi Judicial Department on a court reform process.

In Dubai, the Bank assisted in the analysis of retirement planning options for expatriate workers; follow-up technical assistance is under discussion.

ANNEX III. STATISTICAL ISSUES

(As of April 10, 2012)

I. Assessment of Data Adequacy for Surveillance	
<p>General: Data provision is broadly adequate for surveillance, but there are substantial shortcomings on the accounts of government-related corporations. In particular, there is limited data on GRE debt and contingent liabilities to the government. The federal and individual emirates' agencies have improved the availability and quality of the statistics, but more progress is needed. The adoption of the Federal Statistics Law on May 18, 2009, and the establishment of an independent National Bureau of Statistics (NBS) are important steps in establishing a statistical system at the federal level. While the Law expressly requires all agencies and local statistical centers to provide data as required by the NBS, its success will depend on implementing arrangements, staffing, funding and training.</p>	
<p>National Accounts: The methodology broadly conforms to the 1968 SNA. GDP is compiled annually with a lag of around 12 months. Some progress has been made in improving the source data but further work is needed to improve updating procedures, and quarterly indicators are not available.</p> <p>Price statistics: Following technical assistance from the IMF Statistics Department, the Ministry of Economy started publishing a monthly CPI since January 2008. However, price indexes and GDP deflators need further harmonization at the federal level.</p>	
<p>Government finance statistics: In 2008, six of the seven emirates and the federal government have received technical support in the compilation of fiscal data on a consolidated basis, using the GFSM 2001 format and 2008 as a base year. In 2011, GFSM 2001 was introduced by the federal and several emirate governments, and the institutional arrangement to ensure adequate data provision was established. This consolidation should complement initiatives to establish debt management units at both the emirate and federal levels.</p>	
<p>Monetary statistics: The central bank has recently shifted the responsibility for compiling and disseminating monetary data to the Banking Supervision and Examination Department, in order to improve the timeliness of data to monthly frequency with less than a month lag. Although some monthly aggregates and FSIs are already published on a monthly basis, the Banking Supervision and Examination Department has not been trained in MFSM 2000 and the published data do not follow the recommended methodology.</p>	
<p>Balance of Payments: The information needed to compile the balance of payments is insufficient, especially for the financial account. Many components of the IIP also are missing or incomplete, as the data on government foreign assets and private holdings of foreign assets and liabilities are not published or lack appropriate surveys. The development of a comprehensive Balance of Payments and IIP is however within the reach of the U.A.E. if the central bank, the NBS, and the Ministry of Economy strengthen their capacity and receive appropriate support at the high level. The authorities have indicated their interest in IMF technical assistance.</p>	
II. Data Standards and Quality	
Participant in the GDDS since July 31, 2008. The metadata were last updated in 2008 (Monetary and BOP), 2008 (National Accounts and Prices), and 2008 (Government Finance).	No Data ROSC is available.

UAE: Table of Common Indicators Required for Surveillance

(As of April 6, 2012)

	Date of latest observation	Date received	Frequency of Data ⁶	Frequency of Reporting ⁶	Frequency of publication ⁶
Exchange Rates	Real time	Real time	D	M	M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities ¹	12/11	2/12	M	M	M
Reserve/Base Money	12/11	2/12	M	M	M
Broad Money	12/11	2/12	M	M	M
Central Bank Balance Sheet	12/11	2/12	M	M	M
Consolidated Balance Sheet of the Banking System	12/11	2/12	M	M	M
Interest Rates ²	Real time	Real time	D	D	D
Consumer Price Index	02/12	3/12	M	M	M
Revenue, Expenditure, Balance and Composition of Financing ³ — Central Government	12/11	3/12	A	A	A
Stocks of Central Government and Central Government-Guaranteed Debt ⁴	12/11	03/12	A	A	A
External Current Account Balance	2011	3/12	A	A	A
Exports and Imports of Goods and Services	2011	3/12	A	A	A
GDP/GNP	2010	1/12	A	A	A
Gross External Debt	...	...	NA	NA	NA
International Investment Position ⁵	...	...	NA	NA	NA

¹ Any reserve assets that are pledge of otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by means as well as the national values of derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

² Both market-based and officially determined, including discount rates, money market rates, and rates on treasury bills, notes and bonds.

³ Foreign, domestic bank, and domestic nonbank financing.

⁴ Including currency and maturity composition.

⁵ Includes external gross financial asset and liability positions vis-à-vis nonresidents.

⁶ Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I): Not Available (NA).



INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 12/49
FOR IMMEDIATE RELEASE
May 16, 2012

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2012 Article IV Consultation with the United Arab Emirates

On May 14, 2012, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the United Arab Emirates.¹

Background

The recovery of the economy is continuing despite the uncertain global economic environment. High oil prices and increased production, strong growth in Asia, and the UAE's perceived safe haven status in the context of the regional turmoil contributed to an estimated real GDP growth of 4.9 percent in 2011. Despite the continued weakness of the construction and real estate sectors in the wake of the 2009 crisis, real nonhydrocarbon growth picked up to an estimated 2.7 percent last year, supported by trade, logistics, and tourism. For 2012, oil production is projected to be flat, whereas nonoil growth is expected to strengthen further to 3.5 percent. Inflation remained low at 0.9 percent in 2011, mainly due to a continuing decline in housing rents, and price pressures are expected to remain subdued this year.

The Dubai World debt restructuring was completed, but several other troubled government-related entities (GRE) are still in the process of restructuring. GRE indebtedness, refinancing needs and reliance on foreign funding remain high, with about \$30 billion GRE debt maturing this year and significant amount of debt falling due in 2014–15.

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

Despite the accommodative monetary stance under the peg to the U.S. dollar, lending to the private sector has remained sluggish as excess capacity in the real estate sector and the debt overhang still limit lending opportunities. The banking sector has remained well-capitalized and profitable, despite a continued rise in nonperforming loans and higher provisioning.

Executive Board Assessment

Executive Directors welcomed the continued economic recovery and favorable near-term outlook, but noted downside risks from the uncertain global environment and regional geopolitical tensions. Going forward, Directors encouraged the authorities to continue their efforts to sustain growth and diversify the economy, while maintaining macroeconomic and financial stability.

Directors regarded the fiscal stance as appropriately focused on a gradual consolidation to unwind the large fiscal stimulus undertaken in response to the 2009 crisis without undermining the economic recovery. They particularly welcomed the consolidation plans in Dubai, which will help improve the emirate's debt sustainability in the face of contingent liabilities related to government-related entities (GRE) and the still weak real estate market. Noting the recent federal salary hike and the planned increases in development spending in Abu Dhabi, Directors emphasized the importance of managing the composition of public expenditure carefully. They commended the authorities' efforts to strengthen coordination of fiscal policies between the federal and emirate governments.

Directors agreed that a continued accommodative monetary stance under the peg to the U.S. dollar would counteract fiscal tightening and support the economic recovery. They took note of the staff assessment that the exchange rate has remained broadly aligned with fundamentals, and agreed that the exchange rate peg continues to serve as an effective nominal anchor for the economy.

Directors noted the progress made in restructuring and managing the debt of GREs, but stressed the need for further efforts to mitigate the fiscal risks posed by these entities. They cautioned that GREs are still faced with high refinancing needs and are reliant on foreign funding. In this context, Directors encouraged further deleveraging and strengthening of impaired GRE balance sheets, increased transparency, and improvements in corporate governance at GREs.

Directors took note of the resilience of the banking sector grounded on ample liquidity and capital buffers. They nonetheless encouraged the authorities to continue monitoring closely the financial situation of individual banks and their ability to cope with adverse shocks. Directors emphasized the importance of shielding the banking system from taking further GRE-related risks, including by avoiding channeling bank funding to non-viable GREs. In this regard, they welcomed the recent introduction of aggregate lending limits to GREs. Directors also suggested further strengthening the governance framework for the financial sector. Looking forward, they encouraged the development of domestic debt markets, which would among other things support banks' liquidity management in preparation for the introduction of the Basel III liquidity framework.

Directors welcomed the authorities' efforts to strengthen the statistical base, including the plans for improving the national accounts, balance of payments, fiscal accounts, and labor market statistics.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

United Arab Emirates: Selected Macroeconomic Indicators, 2008–12 ¹

	2008	2009	2010	Est. 2011	Proj. 2012
(Annual percent change, unless otherwise indicated)					
Output and prices					
Nominal GDP (billions of UAE dirhams)	1,156	993	1,093	1,323	1,419
Nominal GDP (billions of U.S. dollars)	315	270	298	360	386
Real GDP (at factor cost)	5.3	-3.3	0.9	4.9	2.3
Real oil and gas GDP	1.6	-9.9	-1.5	9.2	0.0
Real non-oil GDP	6.3	0.6	2.1	2.7	3.5
CPI inflation (average)	12.3	1.6	0.9	0.9	1.5
(Percent of GDP, unless otherwise indicated)					
Public finances					
Revenue	39.0	25.7	28.7	33.3	34.6
Hydrocarbon	31.2	17.5	21.4	27.4	28.5
Non-hydrocarbon	7.9	8.2	7.2	5.9	6.1
Expenditure and net lending	22.3	38.0	30.8	30.4	26.9
Budget balance	16.8	-12.3	-2.1	2.9	7.7
Non-hydrocarbon balance ²	-22.9	-42.0	-34.3	-41.0	-35.2
(Annual percent change)					
Monetary sector					
Credit to private sector	49.3	0.7	1.2	2.3	3.1
Broad money	19.2	9.8	6.2	5.0	7.1
(Billions of U.S. dollars, unless otherwise indicated)					
External sector					
Exports of goods	240	192	212	279	307
Oil and gas	103	68	75	112	122
Imports of goods	-176	-150	-161	-198	-217
Current account balance	24.8	9.1	9.1	33.3	40.0
Current account balance (percent of GDP)	7.9	3.4	3.1	9.2	10.3
Gross official reserves	30.9	25.5	32.8	36.4	40.8
In months of next year imports of goods and services	2.0	1.5	1.6	1.6	1.7
Real effective exchange rate (2000=100)	102.9	107.2	102.7	95.3	..

Sources: UAE authorities; and IMF staff estimates.

¹ Projections are based on information received through November 2009.

² In percent of non-hydrocarbon GDP.

**Statement by Mr. Shaalan, Executive Director for the United Arab Emirates
May 14, 2012**

1. On behalf of the United Arab Emirates (UAE) authorities, I thank staff for their engagement and the constructive Article IV Consultation discussions. The authorities highly value the views of the Fund on the UAE's economic and financial policies.

Overview

2. The UAE has weathered the global economic and financial crisis well, on account of strong fundamentals as well as timely policy responses. The economy has benefited from an increase in hydrocarbon prices and production. Moreover, the economic recovery in non-oil sectors continues to gain momentum, especially in trade and tourism which offset the slowdown in construction and real estate. The authorities remain committed to policies aimed at sustaining growth and diversifying the economy, while maintaining macroeconomic and financial stability.

Fiscal Consolidation

3. Fiscal policy is shifting from an expansionary phase to a consolidation phase, which will be implemented at a gradual pace in order not to undermine the economic recovery. This consolidation will further widen the fiscal space to support the economy in the event that downside risks—such as a decline in oil prices—were to materialize. The government of Abu Dhabi will start implementing its fiscal consolidation plan as of this year, having already completed a review of its development strategy. Plans are for Dubai to further cut public spending and balance its fiscal accounts by 2014.

4. The authorities remain committed to reducing the dependence of fiscal revenues on the hydrocarbon sector. They are considering several initiatives in this regard, including the introduction of a value-added tax in the context of a GCC-wide initiative and a corporate income tax.

5. *Fiscal Policy Coordination* - The authorities consider intergovernmental coordination to be key for an effective fiscal policy. The Fiscal Coordination Council (FCC) has been facilitating the exchange of information between the federal and emirate governments. The authorities plan to further extend the FCC's role to coordinating fiscal policy among the different tiers of government and have requested Fund technical assistance in this regard.

6. *Government Related Entities* - The government is addressing the pending Government-Related Entities (GREs) issues. The Dubai World debt restructuring was completed and several other troubled GREs are in the process of restructuring. GRE risk management is being strengthened; data availability has improved with the Abu Dhabi authorities publishing the list of companies supported by it; and the government of Dubai has clarified that Dubai GREs are not backed by sovereign guarantees. The Department of Finance and the Supreme Fiscal Committee are playing a major role in Dubai GRE debt monitoring and in the approval of new borrowing.

Financial Sector Policies

7. The financial sector remains resilient to domestic and external shocks, thanks to the central bank's strong regulation and macroprudential policies. The banking sector is highly capitalized and profitable. However, credit growth to the private sector is still sluggish, mainly due to the performance of the real estate sector.

8. The Central Bank of the UAE has actively pursued policies aimed at preserving the soundness of the financial sector. It has taken timely measures to support financial stability by providing liquidity, guaranteeing deposits, and encouraging bank capitalization. It will continue to closely monitor the capital adequacy and liquidity of banks, especially those that were found to be most vulnerable under severe stress test scenarios. The central bank is striving to develop domestic capital markets, and it has launched a repurchase facility for Islamic certificates of deposit. Banking regulations have been strengthened by tightened limits on large exposures, and by introducing caps on loans to local governments and their related entities.

9. *Spillover effects* - The authorities appreciate staff's work on the global spillovers to the UAE's financial system. They share staff's view that financial vulnerabilities have decreased since the 2008 real estate problems. While stress tests show that the banking sector has adequate liquidity to withstand substantial shocks and is moderately exposed to Europe, staff points in their Selected Issues Paper to continued vulnerabilities to global financial conditions in a few banks, especially those with high exposure to the real estate sector. In this regard, it is worth mentioning that the central bank has been very active in this regard, and will continue to remain vigilant and monitor cross border and domestic interbank exposures. It stands ready to take additional remedial actions if needed to mitigate possible risks and strengthen the stability of the system. The authorities look forward to the forthcoming Financial Sector Stability Assessment which is expected to take place in the course of 2012.

Other Reforms

10. The federal government will further improve the business environment in order to keep attracting foreign investment. Tourism remains a priority as part of efforts to diversify the economy. Labor policy will continue to focus on increasing the employment of Emiratis in the private sector. Abu Dhabi's capital spending plan on tourism, health, infrastructure, and renewable energy projects will also help to support the economic recovery and create jobs for UAE citizens.

11. The authorities are committed to continue their progress in improving the quality and coverage of economic statistics. They have established the National Bureau of Statistics and Debt Management Offices, and will continue to improve the compilation and dissemination of national, fiscal, and external accounts.