

## **Diversification Resistance to Economic Resilience: UAE's Public Policy Shift**

**By Usman Khalid**

The United Arab Emirates (UAE) is a young nation that climbed the ranks of emerging economies and managed to translate considerable oil wealth into net economic development gains. Despite impressive achievements, oil price shocks continue to be a drag on non-oil activities to this day. The projected future declines in oil prices due to slower expected global demand growth would threaten not only the UAE's fiscal stance sustainability but also its diversification prospects and productivity growth.

The COVID-19 pandemic and global economic shock, exacerbated by declining oil prices from 2014 until recently, have been a natural experiment in economic resilience, bringing this goal to the policy forefront. In addition, the UAE's ratification of the 2016 Paris Climate Agreement and the recent integration of the Sustainable Development Goals (SDGs) into the national strategy mandated a shift to embrace significant climate change adaptation and mitigation policies. Against this backdrop, policymakers are reassessing decades of diversification experience to reposition the economy on a new sustainable path.

A recent paradigm shift in public policy has emerged to shift strategic goals from achieving "traditional diversification" that focused on expanding economic activities related to the hydrocarbon sector to the broader goals of "sustainable diversification" and "economic resilience". This shift signals the adoption of systematic policy priorities that integrate long-term environmentally sustainable growth goals into diversification policies; ones that can ensure actual structural, long-lasting changes away from oil dependency.

One example of such a policy is the shift towards innovation-centered sustainable development strategies that emphasize investments in science and technology. These strategies rest on expanding significant bilateral technological partnerships and corporations with innovative global leaders in Asia, namely South Korea, Hong Kong, China, and Japan. The main areas that witnessed extensive collaborations in the past decade are nuclear energy, aerospace, and artificial intelligence investments. In sum, after years of having its foreign policy eyes on the West, the UAE directs its new economic diplomacy and soft power toward the Far East to successfully implement its innovation-driven diversification strategies.

### ***UAE's Diversification Experience and a Move Towards Sustainable Development***

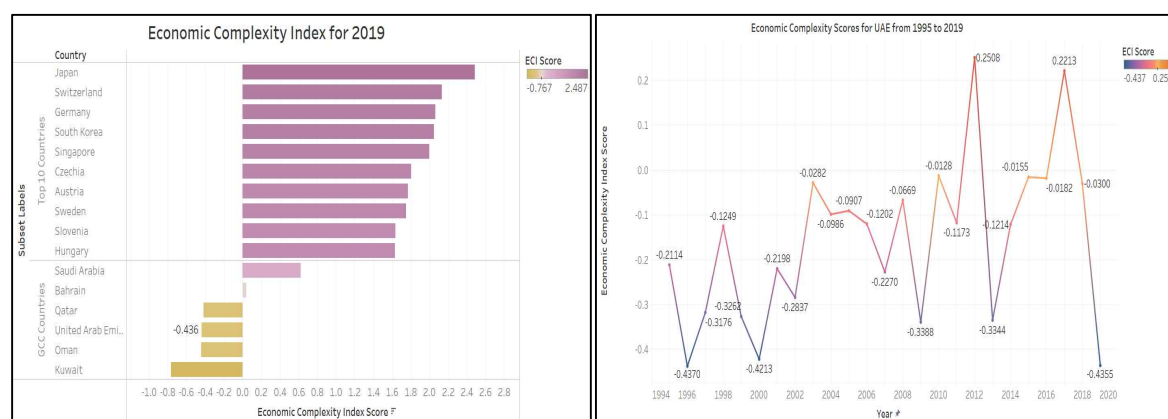
The diversification trajectories of the UAE's seven emirates have varied considerably due to the significant autonomy each enjoys. Dubai, facing declining oil and gas reserves, embarked on an ambitious diversification path in the 1980s, establishing itself as a hub for trade, real estate, logistics, tourism, and international finance, and more recently, expanding its vision to become a smart city and

a center for education (Gelb, 2010; Soto and Haouas, 2016). In contrast, Abu Dhabi's ample oil revenues delayed its diversification until the 1990s. Its diversification efforts have been largely driven by the oil sector itself, with subsequent emphasis on sectors such as information and communication technology, petrochemicals, and renewable energy. In addition, Abu Dhabi's economic model—characterized by low corporate taxes and liberal labor and trade policies—has focused on attracting foreign direct investment and multinational corporations, thereby improving governance indicators like corruption and government effectiveness and enhancing competitiveness.<sup>1</sup>

Overall, the UAE has successfully leveraged its oil wealth to enhance the quality of life for its residents, as evidenced by its high rankings in global competitiveness reports. These reforms have reduced the oil sector's share of GDP to around 30%, yet the country remains vulnerable to resource dependency. Despite decades of diversification, a significant portion of economic activity is still tied to hydrocarbons, suggesting that traditional strategies have yet to produce a fully sustainable economy in a world increasingly focused on decarbonization.

This dependency is further reflected in the nation's export complexity. The Atlas of Economic Complexity (2019) from Harvard University ranks the UAE 17th in per capita income but only 82nd in export complexity among 133 countries, indicating a less diversified export base than its peers and raising concerns about future growth prospects. Recent data even show a deterioration in both the export rank and complexity score, which may be attributed in part to increased crude oil production during periods of low oil prices, exacerbating volatility compared to more diversified economies.

**Figure 1: Economic Complexity Index**



Source: Atlas of Economic Complexity, 2019 (Harvard University's Growth Lab)

<sup>1</sup> See Abu Dhabi Economic vision 2030 for more details (<https://www.actvet.gov.ae/en/media/lists/elibraryld/economic-vision-2030-full-versionen.pdf>)

However, recent developments in the UAE have created a promising opportunity for a transformative shift toward sustainable development and a reduction in diversification resistance. According to El Anshasy and Khalid (2022) three key realities have emerged in recent years that set the stage for this change. First, increased oil price volatility has exposed the UAE's economy to frequent external shocks, disrupting ambitious development plans and compelling policymakers to reconsider long-term economic strategies.

Second, significant structural shifts in the global energy market—fueled by growing concerns over global warming and the commitments under the 2016 Paris Climate Agreement—have necessitated a move away from heavy reliance on oil. Furthermore, recent shale discoveries, evolving production trends in the United States, and a consistent drop in oil prices since 2014 have reshaped oil market fundamentals, applying downward pressure on medium-to-long-term oil revenue projections. Third, the UAE government has maintained high levels of political stability and strong public support, which have enabled the implementation of substantial institutional and policy reforms that further support economic diversification.

These dynamics have spurred a vigorous policy debate concerning the socio-economic benefits of diversification and the challenges posed by diversification resistance. A growing consensus now favors innovation-centered sustainable development strategies that emphasize robust investments in science and technology. Such strategies are built on forging significant bilateral technological partnerships and collaborations with innovative economies in Asia, including South Korea, Hong Kong, China, and Japan. Over the past decade, key areas of collaboration have emerged in nuclear energy, aerospace, and artificial intelligence investments. This realignment marks a notable departure from previous foreign policy orientations, as the UAE increasingly leverages its economic diplomacy and soft power toward the Far East to implement innovation-driven diversification strategies.

In 2016, the UAE further institutionalized its commitment to sustainable development by establishing the Climate Change and Environment Council. In the same year, the Ministry of Climate Change and Environment launched two platforms designed to foster collaboration among public, private, and academic sectors. These initiatives aim to align private sector activities with governmental environmental strategies and to accelerate research on climate change and sustainability. They are integral to achieving the strategic objectives of the UAE's National Climate Change Plan 2017-2050 and the Green Agenda 2015-2030, as well as advancing the Sustainable Development Goals (SDGs), particularly SDG 7, which seeks to ensure universal access to affordable, clean energy (National Committee on SDGs, 2017).

According to the latest Sustainable Development Report (2021), the UAE currently ranks 71st out of 165 nations, indicating progress but also highlighting substantial challenges in fully achieving the 17

SDGs. Notably, the UAE's SDG index score of 70.2 surpasses the regional average of 67.1, and while notable advances have been made in areas such as poverty eradication and quality education, several goals—particularly those related to environmental sustainability—continue to face significant hurdles.

In conclusion, these developments illustrate that while the UAE has made substantial strides in redirecting its economic focus, further efforts are required to build a fully sustainable and diversified economy that is resilient to global shocks.

### ***Building a Resilient Economy: Where to go next?***

Building a resilient economy goes far beyond merely pursuing diversification, sustainable development, or the achievement of Sustainable Development Goals (SDGs). While these elements are undoubtedly important, true resilience is a multidimensional concept that reflects a country's ability to manage risks, adapt quickly, and recover from disruptions—whether they be economic, financial, or natural in nature. Resilience embodies the capacity to adjust, respond, and evolve in the face of both major crises and routine challenges. Recent global health and economic crises have underscored the importance of resilience, revealing vulnerabilities even in well-diversified economies like that of the UAE. Despite decades of diversification efforts, the UAE's traditional reliance on oil has been repeatedly tested, yet the nation's effective crisis management and increasingly flexible labor market have helped maintain stability.

Beyond diversification, several factors play a critical role in building an economy's resilience. Technological readiness has emerged as a cornerstone, as rapid digital transformation during crises—through the adoption of new communication platforms and advanced information systems—has proven essential for maintaining continuity in business, education, and government services. Equally important is the agility of the labor market. In the UAE, where foreign labor forms a significant part of the workforce, the ability to quickly reabsorb laid-off workers and facilitate intersectoral mobility is vital for rapid recovery after shocks.

Entrepreneurship is another key driver of resilience. At the micro level, entrepreneurial firms—characterized by flexibility, perseverance, and innovation—tend to be better equipped to navigate crises. On the macro scale, a vibrant entrepreneurial ecosystem stimulates innovation and growth across regions and sectors, further enhancing overall economic resilience. However, many small and medium enterprises (SMEs) currently lack clear bailout strategies, highlighting the need for policies that facilitate financial easing and risk management for these crucial players.

## ***Policy Recommendations***

Recent policy debates in the UAE have also emphasized that not all diversification efforts lead to a sustainable or resilient economy. Evidence suggests that the diversification strategies employed over the past four decades have not fully decoupled the economy from the hydrocarbon value chain, limiting growth potential and long-term sustainability. In response, policymakers are now prioritizing initiatives such as accelerating climate change mitigation and adaptation, decoupling public finances from oil revenues, and supporting high-value chain services that promote green growth.

In summary, while diversification and sustainable development remain key pillars for building resilience, a truly resilient economy also depends on technological innovation, labor market flexibility, and a dynamic entrepreneurial ecosystem. The UAE's evolving policy landscape demonstrates a commitment to these areas, yet further coordinated efforts are essential to fully achieve resilience in a rapidly changing global environment.

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