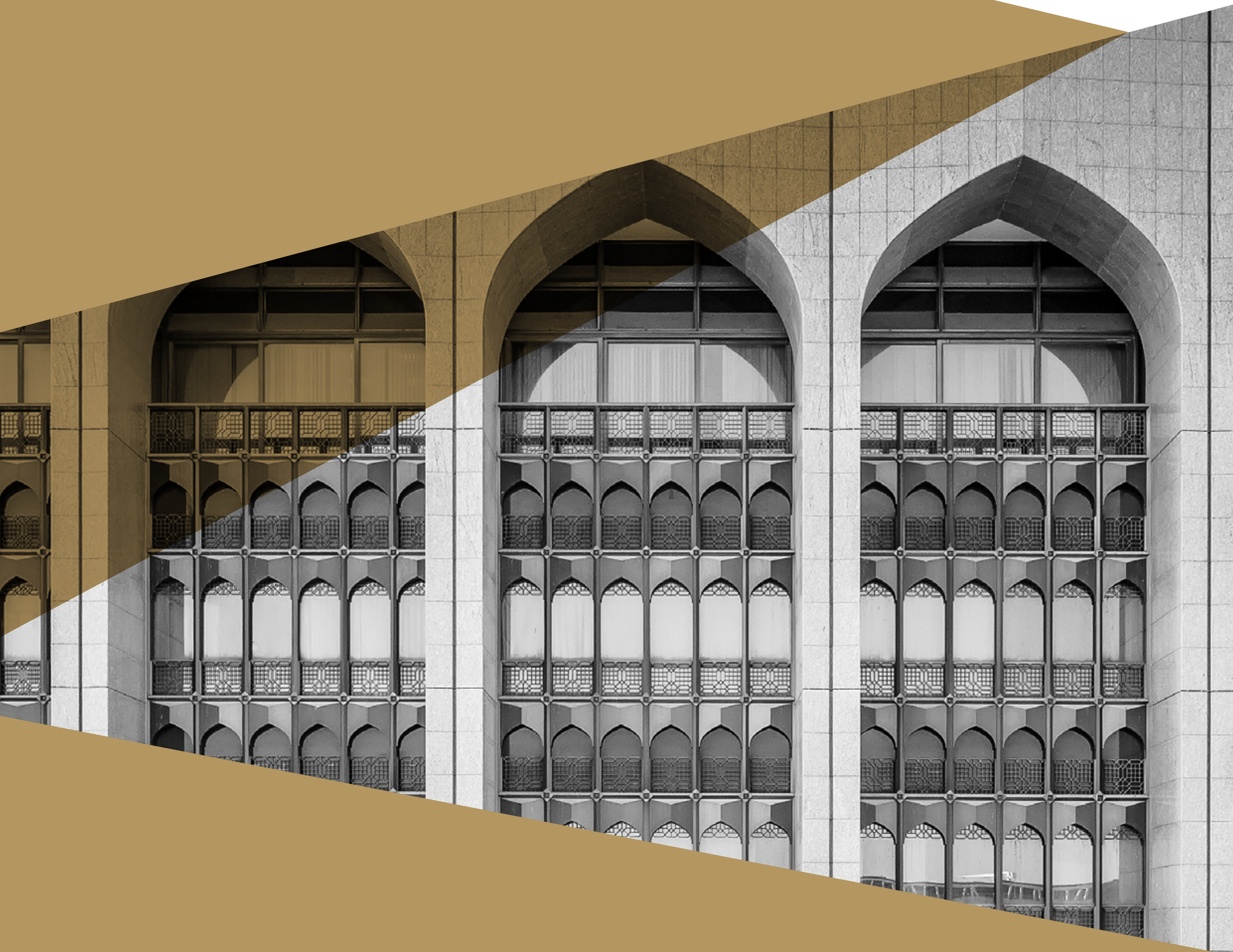
United Arab Emirates

مصرف الإمارات العربية المتحدة المركزي

CENTRAL BANK OF THE U.A.E.

ANNUAL REPORT
2018



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MESSAGE FROM THE CHAIRMAN OF THE BOARD OF DIRECTORS

In 2018, we marked the 47th anniversary of the UAE's union — a major milestone for our country — which coincided with the Year of Zayed. CBUAE celebrated this special occasion with the issuance of a commemorative silver one AED coin and an AED 100 denomination bank note with 'Year of Zayed' logo.

The year 2018 also marks an important milestone for the Central Bank of the UAE (CBUAE). It is the year that the Decretal Federal Law No. 14 was issued, which regulates CBUAE and stipulates the terms of the organisation of the financial institutions and their activities.

The law was issued in coordination with major stakeholders to accommodate continued developments of the financial system. More broadly, the new law reflects the evolving role of central banks in the post-global financial crisis era. It also aims to support UAE's strategic vision to reduce dependency on oil while propelling the country towards a well-diversified, competitive, and knowledge-based economy.

The new law introduces major changes related to enforcement, licensing, financial infrastructure, and consumer protection. Moreover, CBUAE is entrusted with the task of designating licensed financial institutions and financial infrastructure systems as systematically important and maintaining close oversight to ensure their soundness. The law broadens consumer protection of financial services and sets out comprehensive rules governing the confidentiality, protection and appropriate use of information, in order to maintain stability of the financial sector and strengthen financial inclusion in the UAE.

The Decretal Federal Law No. 14 of 2018 was issued in tandem with other laws and regulations with the aim to modernise the regulatory landscape in the UAE.

I would like to seize this opportunity to underline the importance of the newly-issued Federal Law No. 9 of 2018 (The Public Debt Law), which will allow the Ministry of Finance to issue public debt in Dirhams for the Federal Government for the first time. Article (3) of the said law states that the Public Debt Management Office at the Ministry of Finance will coordinate with CBUAE on matters relating to the administration of issuance of public debt as well as the sale of government bonds and treasuries.

With regard to the country's efforts to effectively counter money laundering and financing of terrorism, we welcome the issuance of Federal-Decree Law No. (20) of 2018 on Anti-Money Laundering and Combating the Financing of Terrorism and Financing of Illegal Organisations, which introduces important amendments to further strengthen the UAE's initiatives in tackling these crucial issues and addressing the requirements of the FATF recommendations. This was followed by the issuance of Cabinet resolution No. (10) of 2019 concerning the implementation of regulations of the above-mentioned Law, and issuance of cabinet resolution No. (20) of 2019 concerning terrorist lists and the implementation of Security Council resolutions on the prevention and suppression of terrorism and its financing, the cessation of arms proliferation and funding, and related resolutions.

With the rebound in oil prices in 2018, the outlook for bank credit as well as growth in non-hydrocarbon activities bodes well for sustained recovery. Nonetheless, in an environment characterised by regional risks and global headwinds, CBUAE needs to ensure the right balance between efficient financial intermediation and stability. To that end, CBUAE continues its close monitoring of the liquidity and capital situation of banks and other prudential financial ratios. Going forward, CBUAE will maintain this commitment while enhancing the capacity to forecast and manage liquidity in the system.

MESSAGE FROM THE GOVERNOR

CBUAE has made significant progress in several important areas, including the development of the regulatory framework, while the economy continued its recovery despite continued headwinds related to global uncertainties.

The improvement of oil prices in 2018 supported the recovery of the domestic economy, including non-oil activities, amid improved sentiment and growth-friendly fiscal policy. As a result, credit to the private corporate sector has recovered. In regard to inflation, following the one-off increase starting in January 2018, the rise in prices plateaued, as the impact of VAT faded along with the softening of fuel prices towards the end of the year.

Looking forward, the outlook of stronger economic recovery in 2019 seems positive for employment and financial conditions in the UAE. A well-capitalised, liquid and stable banking sector will continue to provide the platform to enhance financial stability and support economic growth.

Micro, small and medium enterprises (MSMEs) are at the fore of our drive for further economic diversification and sustainable and inclusive development. However, MSMEs still face multiple obstacles, which require a holistic approach for well-coordinated reforms targeting the development of the sector and ease in financing constraints. The UAE government and CBUAE accord high policy priority to this sector and are keen to boost its contribution to the national economy by 2021. In this mission, CBUAE has laid the foundation necessary to establish more efficient financial market infrastructure, which can help lower the cost of services and achieve higher penetration among SME customers, thereby expanding financial inclusion. We will continue to work jointly with key stakeholders to improve the ecosystem and ease financing constraints faced by MSMEs.

The international financial industry is undergoing rapid changes, driven by fintech advances in digital technology. Such advances are revolutionising the way financial services are provided and have the potential to enhance financial inclusion, efficiency, and access to financing. However, regulatory oversight is needed to manage the risks while we are leveraging these innovations. As exciting as these developments are, as a regulator we must always be mindful of our primary goal: to maintain both the safety and soundness of the banking system, along with adequate levels of consumer protection. In line with this, CBUAE is currently in the process of developing a fintech strategy that aims to capitalise on the UAE fintech eco-system and to cohesively deploy balanced regulatory and development initiatives.

The newly issued Federal Law No. 9 of 2018 (The Public Debt Law) will pave the way for stronger policy coordination between fiscal and monetary authorities. It will provide CBUAE an additional tool to enhance its capacity for conducting monetary operations within the country. Looking ahead, the Federal Law No. 14 of 2018 will enhance the capacity of CBUAE to support the country's overall strategy of further diversification of the economy and long-term inclusive growth.

Within the context of the fiscal and monetary policy coordination, CBUAE will continue to join efforts with the Ministry of Finance and other major stakeholders. A dedicated working group has been set up to coordinate the implementation of the planned initiatives.

OUR VISION

Promoting monetary and financial stability towards sustainable economic growth.

OUR MISSION

Enhancing monetary and financial stability through effective supervision, prudent reserve management, and robust financial infrastructure in line with international best practices and standards.

OUR VALUES

Proactive - Transparent - Talent-Centric.

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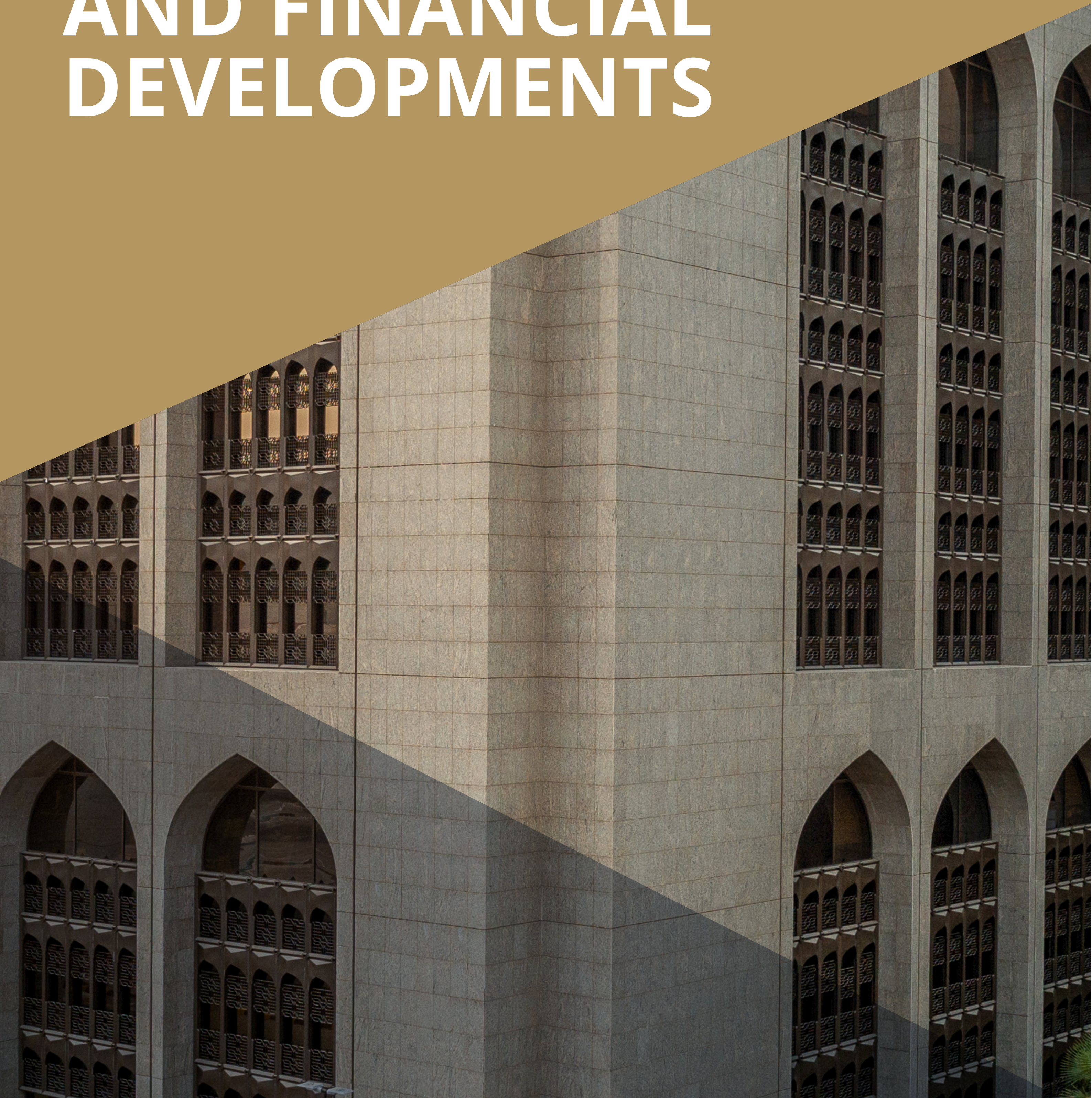
LIST OF ABBREVIATIONS

AAOIFI Accounting and Auditing Organization for Islamic Financial Institutions
ADNOC Abu Dhabi National Oil Company
ADSM Abu Dhabi Securities Market
ADX Abu Dhabi Securities Exchange
AED Arab Emirates Dirham
AML Anti-Money Laundering
AML/CFT Anti-Money Laundering/ Countering Financing of Terrorism
ASA Alternative; and Standardized Approach
AT1 Additional Tier 1
ATMs Automated Teller Machines
BCBS Basel Committee on Banking Supervision
BCM Business Continuity Management
BIA Basic Indicator Approach
BIA Business Impact Analysis
BOP Balance of Payments
CAGR Compounded Annual Growth Rate
CAR Capital Adequacy Ratio
CBUAE Central Bank of the UAE
CCB Capital Conservation Buffer
CCR Counterparty Credit Risk
CCyB Countercyclical Buffer
CDs Certificates of Deposit
CET Common Equity Tier 1 Capital
CIBAFI Council for Islamic Banks and Financial Institutions
CIF Cost of Insurance and Freight
CPD Consumer Protection Department
CPI Consumer Price Index
CRWA Credit Risk Weighted Assets
CVA Credit Valuation Adjustment
DET Dubai Economy Tracker
DFM Dubai Financial Market
DLD Dubai Land Department
DNFBPs Designated Non-Financial Businesses and Professions
D-SIB Domestic Systemically Important Bank Buffer
ECB European Central Bank
ECDD Enhanced Customer Due Diligence
ECQ Effective Compliance Questionnaire
EIA Emirates Investment Authority
EIBOR Emirates Inter-Bank Offer Rate
EIF Equity in Investment Funds
ELAR Eligible Liquid Asset Ratio
ELAR Eligible Liquid Assets Ratio
EMDE Emerging Markets and Developing Economies
FATF Financial Action Task Force
FCSA Federal Competiveness and Statistics Authority
FDI Foreign Direct Investment
Fed Federal Reserve
FI Financial Institutions
FIU Financial Intelligence Unit
FMI Financial Market Infrastructure
FOB Free on Board
FOMC Federal Open Market Committee
FSAP Financial Sector Assessment Program
G-20 Group of Twenty
GCC Gulf Cooperation Council
GCC-RTGS Gulf Cooperation Council Real Time Gross Settlement
GDP Gross Domestic Products
GREs Government Related Entities
HQLA High Quality Liquid Assets
ICAAP Internal Capital Adequacy Assessment Process
ICCS Image Cheque Clearing System
ICV In-Country Value
IFIs International Financial Institutions
IFSB Islamic Financial Services Board
IMF International Monetary Fund
IOSCO International Organization of the Securities Commissions
ISM Institute for Supply Management
L/D Loan-to-Deposit
LCR Liquidity Coverage Ratio
LIBOR London Inter-Bank Offer Rate
LSRR Lending to Stable Resources Ratio
M1 Money Aggregate 1
M2 Money Aggregate 2
M3 Money Aggregate 3
Mb/d. Million Barrels per Day
MENA Middle East and North Africa
MENAFATF Middle East and North Africa Financial Action Task Force
MENAP Middle East, North Africa, Afghanistan and Pakistan
MoF Ministry of Finance
MOU Memorandum of Understanding
MSMEs Micro, Small and Medium Enterprises
NAMLCFTIOC National Anti-Money Laundering & Combating Financing of Terrorism and Illegal Organization Committee
NEER Nominal Effective Exchange Rate
NPSS National Payment Systems Strategy
NSFR Net Stable Funding Ratio
OPEC Organization of Petroleum Exporting Countries
OTC Over-the-counter
PCE Private Consumption Expenditure
PFMIs Principles on Financial Market Infrastructures
PMI Purchasing Managers Index
PMO Project Management Office
RBI Reserve Bank of India
RBS Risk Based Supervision
RWA Risk Weighted Assets
SA Standardized Approach
SA-CCR Standardized Approach for Counterparty Credit Risk
SCA Securities and Commodities Authority
SDR Special Drawing Right
SIA Signals Intelligence Agency
SME Small and Medium Enterprises
STRs Suspicious Transaction Report
TCQ Technical Compliance Questionnaire
UAE Switch UAE Electronic Switch
UAE United Arab Emirates
UAEDDS UAE Direct Debit System
UAEFTS UAE Funds Transfer System
UAEPGS UAE Payment Gateway System
UK United Kingdom
UK-FIU UK Financial Intelligence Unit
US United States
USD United States Dollar
VaR Value at Risk
VAT Value Added Tax
WEO World Economic Outlook
WPS Wages Protection System
Y-o-Y Year-on-Year

PART ONE

ECONOMIC, MONETARY AND FINANCIAL DEVELOPMENTS



CHAPTER 1. INTERNATIONAL ECONOMIC DEVELOPMENTS

Global growth for both 2018 and 2019 was revised downward owing to uncertainties related to trade tensions and slowdown in the Eurozone and in China, in addition to risks threatening some emerging economies. Meanwhile, inflation remained below target in the Eurozone and in Japan; and commodity prices recovered, albeit at a slower pace compared to 2017. Besides, bond yields in major economies ended the year on a downward trajectory.

ECONOMIC GROWTH

The recovery in global economic growth is moderating as growth projections in major economies were revised down in the beginning of 2019. As reported in the April 2019 World Economic Outlook (WEO) report, the IMF reduced the global growth to 3.6% for 2018—following a 0.1% downward revision from October. For the years 2019 and 2020 global activity is projected to grow at 3.3% and 3.6%, respectively—0.4 and 0.1 percentage points below October's projection for 2019 and 20120, respectively. According to the report, the downward revision is partly because of the negative effects of the tariff increases implemented in the United States and China, a softer momentum in major EU economies, and macroeconomic stress in some emerging market economies.

The major advanced economies witnessed mixed economic performances. The United States' economic activity remained solid throughout the year, although showing subdued momentum in the fourth quarter. In contrast, growth in the Eurozone has been weaker than expected owing to low domestic demand, lower industrial production, weakening financial market sentiment, and the impact of trade tensions on global demand.

Growth in **Emerging Markets and Developing Economies (EMDE)** slowed down to an estimated 4.5% in 2018—i.e., 0.3 percentage point slower than in October—mainly due to financial market pressures in a context of high trade tensions. Growth among commodity exporters lost momentum significantly, despite some improvement in export prices, owing to country-specific challenges.

Meanwhile, commodity importers' growth remained robust despite a mild moderation due to capacity constraints and slowing export activities. Nonetheless, slower global trade and tighter financing conditions will adversely affect the growth of EMDE further in 2019, which is estimated at 4.4%.

ECONOMIC OUTLOOK FOR SELECTED ECONOMIES

UNITED STATES

The US economic outlook was healthy according to key indicators. Growth in the US economy for 2018 amounted to 2.9% reflecting stronger-than-expected domestic demand and investment. Consumer spending showed an upward trajectory (2.6%) supporting growth in 2018. The upward trend in consumer spending is mainly driven by rising wages and marked labor market gains. Although growth remains robust in the US, some signs indicate loss of momentum at the end of the year 2018. In particular, the ISM manufacturing index, posted at the end of the year, indicated a sharp drop in domestic new orders. Furthermore, the government's 35-day shutdown negatively impacted consumer confidence.

EUROZONE

The Eurozone annual growth is estimated at 1.8% in 2018. Economic activities had a strong start in the first half of 2018, followed by a loss of momentum in the second half due to the slowdown in exports, driven by the appreciation of the euro and weaker external demand. Hence, growth was marked down for Germany due to an underperforming exporting sector and for France following protests.

Growth in the Eurozone is projected to decelerate further to 1.3% in 2019—IMF's latest projections—especially under the withdrawal of the monetary stimulus and a softening of the global trade growth.

UNITED KINGDOM

In the UK, the economy continued to settle into a slower growth momentum throughout the year. In the second half of 2018, however, some positive data of the macroeconomic performance was released; namely, low inflation, higher employment, and firm wage growth. The economy was estimated to grow at 1.4% in 2018 and projected to expand at a slower rate of 1.2% in 2019, assuming a Brexit deal is reached in 2019.

CHINA

Concerns over China's economic outlook continue to linger. The economy grew by 6.6% in 2018, the slowest pace in 28 years, matching market expectations and slightly higher than the official 6.5% target. The decelerating growth pattern in China is projected to be gradual due to the trade dispute as industrial activities and new export orders are expected to put a downward pressure on the aggregate output amid rising concerns about China's debt. Real growth rates for 2019 and 2020 are forecasted at 6.3 and 6.1%, respectively.

TABLE. 1.1 REAL GDP GROWTH IN SELECTED ADVANCED COUNTRIES

	2017	2018*	2019*	2020**
World Output	3.8	3.6	3.3	3.6
USA	2.2	2.9	2.3	1.9
Eurozone	2.4	1.8	1.3	1.5
- France	2.2	1.5	1.5	1.3
- Germany	2.5	1.5	0.8	1.4
United Kingdom	1.8	1.4	1.2	1.4
Japan	1.9	0.8	1.0	0.5
EMDE 1/	4.8	4.5	4.4	4.8
- China	6.8	6.6	6.3	6.1
- India	7.2	7.1	7.3	7.5
MENAP 2/	2.2	1.8	1.5	3.2

Source: IMF, World Economic Outlook, April 2019

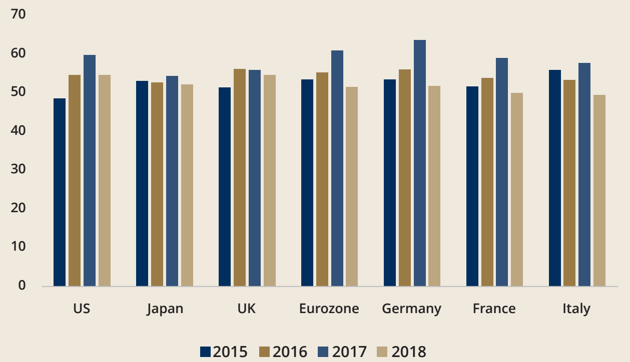
*Estimated
**Projected

1. Emerging Market and Developing Economies
2. Middle East, North Africa, Afghanistan, and Pakistan

JAPAN

Japan's real GDP was estimated to grow at 0.8% in 2018 and is projected to reach 1.0% in 2019 reflecting additional fiscal support. The slackening growth in the third-biggest economy was driven by a series of natural disasters that forced factories to cut production as well as low global demand.

FIGURE 1.1. PMI LEVELS FOR SELECTED DEVELOPED COUNTRIES



Source: Bloomberg

INDIA

Growth was estimated to remain solid at 7.1% in 2018 compared to 7.2% in 2017 and is projected to progress at a 7.3% rate in 2019 benefiting from lower oil prices and slower pace of monetary tightening, as inflation pressures eased.

MENAP

Growth in the Middle East, North Africa, Afghanistan, and Pakistan (MENAP) was estimated at 1.8% in 2018 and is projected to remain subdued at 1.5% in 2019 owing to a softer international oil market and geopolitical tensions. It is then projected to recover starting from 2020 with a rate of 3.2%.

ECONOMIC GROWTH IN THE GCC

Structural fiscal reforms allowed the Gulf economies to achieve stable growth footing in 2018. Real GDP growth mostly improved in 2018 and is projected to improve in 2019 on the back of more gradual fiscal consolidation enhanced by higher oil prices and the reform strategy. In Saudi Arabia, as an example, real GDP growth improved from negative 0.7% in 2017 to 2.2% in 2018, owing to more supportive government spending, despite the cap on oil production and mounting geopolitical risks.

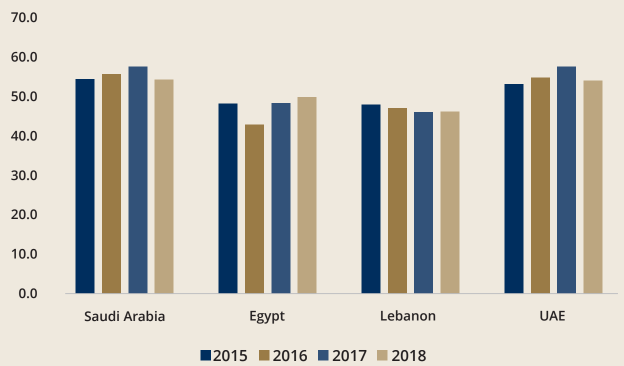
TABLE 1.3. GCC REAL GDP GROWTH

	2017	2018*	2019**
Bahrain	3.8	1.8	1.8
Kuwait	-3.5	1.7	2.5
Oman	-0.9	2.1	1.1
Qatar	1.6	2.2	2.6
Saudi Arabia	-0.7	2.2	1.8

Source: IMF, World Economic Outlook, April 2019.

*Estimated. **Projected

FIGURE 1.2. PMI LEVELS FOR SELECTED MENA COUNTRIES



Source: Bloomberg

INFLATION

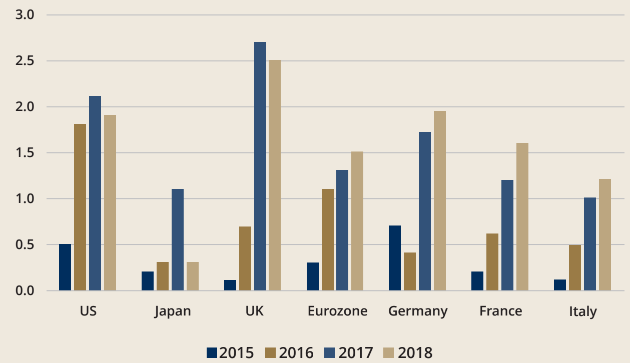
Global inflation rate exhibited an increase to 3.6% in 2018, compared to 3.2% in 2017. Consumer price inflation generally remained moderate in advanced economies during the second half of the year. In the US, however, Y-o-Y CPI increased by 2.4% at the end of 2018 compared to 2.1% increase during the previous year. The Federal Reserve target of Core Personal Consumer Expenditure Price Index (excluding volatile food and energy prices) increased by an average of 1.8% in 2018 compared to 1.7% in 2017.

In the Eurozone, Y-o-Y CPI inflation increased to an average of 1.8% in 2018 compared to 1.5% in 2017. In Germany, CPI inflation increased to 1.9% compared to 1.7% in 2017, while France's CPI inflation was recorded at 2.1% for the year 2018. Meanwhile, the end of period inflation for the euro zone was confirmed at a lower level of 1.5% increase.

In the United Kingdom, the increase in the Consumer Price Index slowed down from 2.7% in 2017 to 2.5% in 2018. The pressure came mainly from food, ferry prices, clothing, recreation, and culture. These influences, however, were partly offset by energy prices, with tariff hikes lifting the cost of electricity in the country.

In Japan, average inflation remained the lowest among advanced economies, evaluated at 1.0% in 2018 compared to 0.5% in 2017—i.e. well below the 2% target—amid further decreases in prices of food, transport and housing. One of the reasons that inflation remained stubbornly below target is that wages remained low despite tightened labor market.

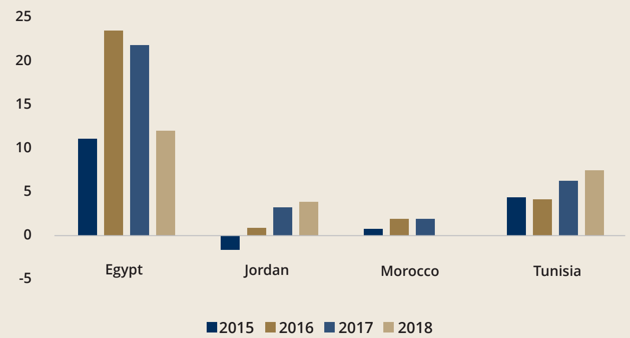
FIGURE 1.3. YEAR-ON-YEAR CONSUMER PRICE CHANGE FOR SELECTED DEVELOPED ECONOMIES (%)



Source: Bloomberg

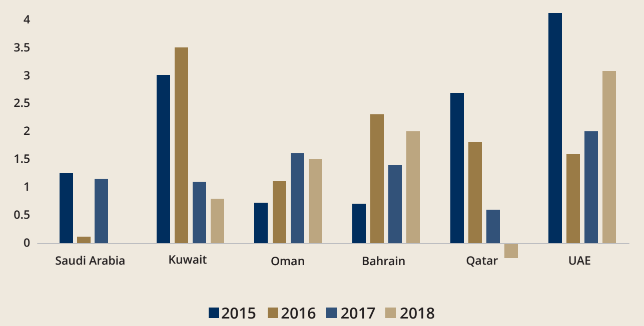
In emerging market and developing economies, inflationary pressures continued to ease as oil prices fluctuated on a declining trajectory during the second half of the year. Average inflation in China was estimated at 2.1% in 2018, compared to 1.6% in 2017, driven by higher food and energy prices. India's inflation is estimated to be 3.6% during the fiscal year 2017/18, while average inflation in Turkey registered a level of 16.3% in 2018.

FIGURE 1.4.A. YEAR-ON-YEAR CONSUMER PRICE CHANGE IN ARAB NON-OIL PRODUCING COUNTRIES (%)



Source: Bloomberg

FIGURE 1.4.B. YEAR-ON-YEAR CONSUMER PRICE CHANGE IN THE GCC (%)



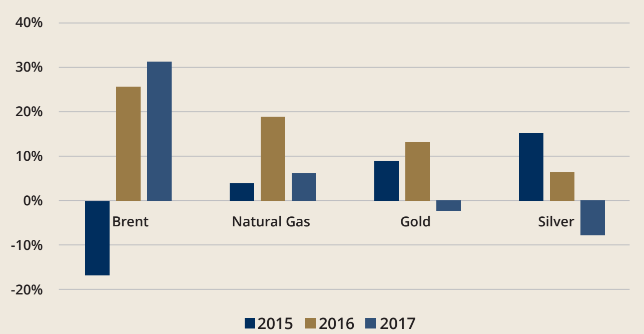
Source: Bloomberg

COMMODITY PRICES

Commodity prices fluctuated noticeably during the second half of 2018, with sharp falls toward the end of the year. The average price of Brent crude oil increased by 31% Y-o-Y in 2018, compared to the previous year, reaching USD 71 per barrel.

Brent crude oil prices surged in the first half of the year hitting over USD 75 per barrel in May 2018, almost 53% increase Y-o-Y, due to OPEC agreement to extend the accord. In addition, some oil supply disturbances affected international prices. In particular, Libya experienced supply outages affecting the supply of oil by almost 850,000 barrels per day. Further, Iran's oil exports were affected during the second half of the year due to renewed US sanctions. According to OPEC's monthly report, projected non-OPEC oil supply for 2018 was estimated to reach an average of 62.2 mb/d. Meanwhile, other commodities' prices witnessed mixed movements throughout the year. Natural gas, for instance, increased by 6% in 2018, compared to 19% increase in the previous year. While gold and silver prices decreased on an annual basis by 2% and 8%, respectively.

FIGURE 1.5. SELECTED COMMODITY PRICE LEVELS (Y-O-Y, % CHANGE)



Source: Bloomberg

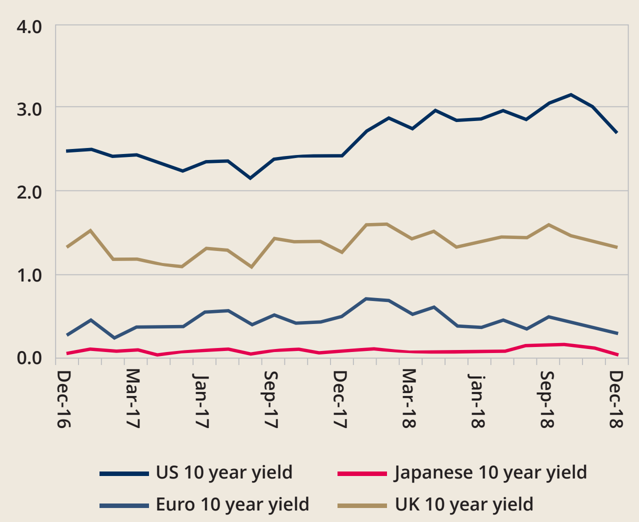
GOVERNMENT BOND YIELDS

During the first half of the year, the benchmark 10-year US treasury yield was relatively stable with an average of about 2.9% followed by an upward trajectory toward the end of the third quarter, reaching a monthly average peak of 3.15% in October, before falling to 2.83% at the end of the year.

The Japanese 10-year government bond fluctuated marginally above zero throughout the year reaching a monthly average peak of 0.13% in October, before falling in December below the zero threshold. Meanwhile, the UK 10-year bond yield reached its monthly average peak of 1.6% in February; followed by a decline up to the end of the year with a short-lived blip in October before closing the year at 1.32% (December average).

In the Eurozone, government bond yields reflected a moderate upward trend since the beginning of the year amid positive economic performance and the prospect of less accommodating monetary policy—average monthly 10-year yields increased from 0.88% in December 2017 to 1.56% in October 2018. However, the trend was reversed in the third quarter when markets were dominated by doubts about economic growth, a friction between Brussels and Rome over Italy's budget, a tumultuous Brexit process, and fall in stock prices. The end-of year economic data appeared to add new obstacles to the European Central Bank's (ECB) plans to normalise monetary policy.

FIGURE 1.6. THE 10-YEAR GOVERNMENT BOND YIELDS FOR SELECTED COUNTRIES (%)



Source: Bloomberg

BOX 1: POLICY INTEREST RATE IN SELECTED ECONOMIES

Monetary authorities determine the policy rate, i.e., the short-term interest rate they target based on domestic economic conditions. The expectation is that the change in the policy rate will affect short- and longer-term interest rates, with an impact on demand for credit, investment and economic growth.

The Federal Reserve Board targets the federal funds rate, which is the overnight interbank rate. This rate was reduced to the target range of 0-0.25% at the outbreak of the global financial crisis, then witnessed an increase since December 2015 as growth and employment in the US improved, albeit inflation remained below but close to the 2% target.

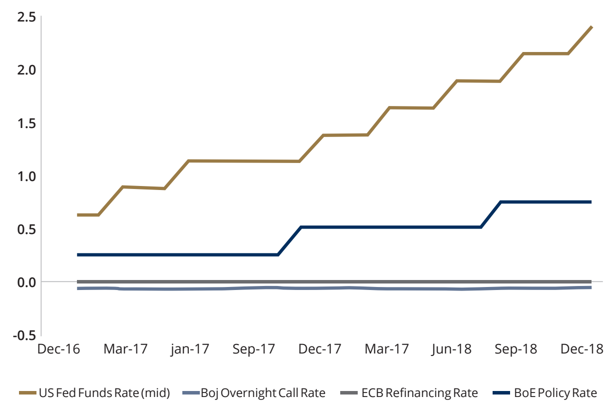
In 2018, the Federal Open Market Committee (FOMC) took decisions to increase the federal funds rate target four times, in March, June, September, and December by 25 basis points each to the target range of 2.25%-2.50%. The rationale for such increase is that the job market was tightening, inflation was nearing target, and there was a need to normalise interest rates in order to make room for a downward adjustment at the next downturn. Nevertheless, the market expects a slower pace of hikes in 2019 due to tightening of financial conditions, softening of the economic outlook and rising global uncertainties.

In the UK, the Bank of England raised the base rate (the official borrowing rate) from 0.5% to 0.75% last August despite mounting fears about a “no–deal” Brexit. Economic growth is expected to recover in the second half of the year and maintain the pace going forward.

Meanwhile, the ECB’s Governing Council decided to keep the interest rate of its main refinancing operations at zero; the marginal lending facility at 0.25%, and the interest rate on the deposit facility negative at -0.4%. Monetary policy normalisation was therefore put on hold as risks surrounding the Eurozone’s growth outlook have moved to the downside.

During the September’s policy meeting, ECB decided to reduce the monthly pace of the net asset purchase, from EUR 30 billion to EUR 15 billion a month, from October to December 2018. The outstanding volumes are expected to remain at the end-2018 level.

FIGURE 1.7. POLICY RATES FOR SELECTED DEVELOPED COUNTRIES (%)



Source: Bloomberg

In a widely expected move, the Bank of Japan left its key short-term interest rate unchanged at a negative -0.1%, mainly due to the disappointing inflation rate. The bank cut its price forecasts, reinforcing market expectations that subdued inflation will force it to maintain its massive stimulus programme for the time being.

BOX 2: TRADE DISPUTES BETWEEN US, CHINA, AND THEIR IMPACT ON THE UAE

During the past two years, protectionism has been viewed as a major downside risk on the global economy. Its intensification was triggered by the drive of the US administration to correct its trade imbalances with the rest of the world, in general, and China in particular through imposing tariffs on several durable and basic materials, which invoked US trading partners to adopt retaliatory measures.

In the past few months, retaliatory measures between China and the US have intensified, especially concerning intellectual property rights violations. The US imposed tariffs on washing machines and solar panels at the beginning of 2018 equal to 20%. China produces around 65% of the world's solar modules.

The series of tariff increases did not stop there as the US administration increased import taxes on steel and aluminum by 25% and 10%, respectively, noting that only 6% of imports come from China. As a retaliation measure, China issued tariffs on USD2.4 billion worth of US exports, covering a list of 128 goods.
The US administration quickly unveiled a list of 1,300 Chinese goods that could be impacted by 25% tariffs. The list—about USD50 billion of Chinese exports—includes goods such as semiconductors, medical devices and flat-screen televisions. Most of the targeted products are included in the "Made in China 2025" plan, which aims to break China's reliance on foreign technology while boosting its hi-tech industries.

TABLE 1. MAIN US IMPOSED TARIFFS ON CHINESE IMPORTS

Date	Affected trade value (USD billion)	Effective average tariff rate
6 July 2018	34.0	25%
23 August 2018	16.0	25%
24 September 2018	200.0	10%

Source: Peterson Institute for International Economics, US Census Bureau

The US plan was to gradually extend the list of products to cover around half of the Chinese imports, which would imply an effective rate of 25% on total imports. The announced tariffs were implemented by invoking Section 232 of the Trade Expansion Act of 1962. These tariffs targeted intermediate inputs and capital equipment that US companies import to remain competitive in the global marketplace.

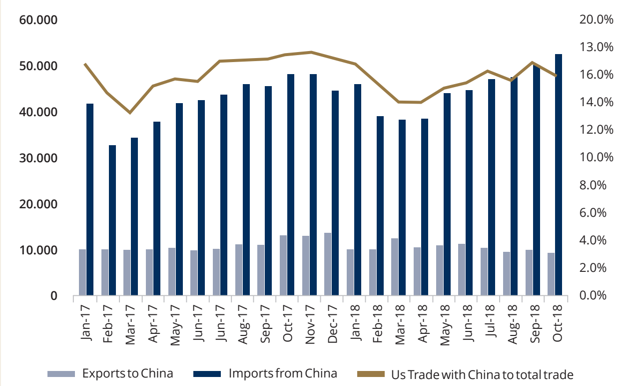
TABLE 2. MAIN CHINESE RETALIATORY MEASURES

Date	Affected trade value (USD billion)	Effective average tariff rate
6 July 2018	34.0	25%
23 August 2018	16.0	25%
24 September 2018	60.0	6.9%

Source: Peterson Institute for International Economics, US Census Bureau

The Chinese government started to take retaliatory measures at first by issuing its own list of tariffs on US exports at 25%. The list covered USD44.9 billion of US exports to China in 2017. Roughly, USD29.6 billion were targeted for an additional 25% tariff on July 6, and the remaining USD15.4 billion would be subject to 25% tariffs at a later time (table 2).

FIGURE 1. US-CHINA TRADE DEVELOPMENTS IN 2018



Source: US Census Bureau

However, the Chinese government moved away from this approach as US and Chinese officials are still trying to work out a trade deal.

BOX 2: TRADE DISPUTES BETWEEN US, CHINA, AND THEIR IMPACT ON THE UAE (CONTINUED)

TRADE DISPUTES' IMPACT ON THE US ECONOMY

Shedding protectionism policies towards a rule-based open trade system have led to widespread benefits, including higher income levels, lower prices, and greater consumer choice. It is commonly believed that openness to trade and investment has substantially contributed to US growth. Therefore, trade barriers should systematically raise prices and reduce available quantities of goods and services for US businesses and consumers, which would result in lower income, reduced employment, and slower economic growth.

According to the Peterson Institute for International Economics, the US tariffs are targeting multinational supply chains, which would drive up costs for domestic manufacturers and affect their competitiveness in the global markets as a considerable share of US tradable goods originates in foreign-invested enterprises—the Chinese-based affiliates of multinational firms. Furthermore, products impacted by tariffs are mainly capital and intermediate goods that are used for domestic production, which may affect the high value-added innovative and profitable services and inputs. In addition, tariffs on a large share of trade between the US and China may hinder American firms operations in China.

Many economists estimate that trade disputes will negatively influence global trade, reducing it by (1%-2%) and global GDP will decline by around 0.4% in the long term[1]. In addition, GDP in both countries will be affected negatively by (0.5%-1%) depending on whether the disputes will escalate further to engulf all of the bilateral trade. Also, the level of investment is estimated to drop by 1% in the United States in the short-term (2018-2019).

The tariffs would raise inflation indirectly, due to firms passing higher production costs into final prices. From the Chinese side, the new tariffs on U.S. imports would affect a diverse set of industries such as soybeans, vehicles, chemicals and aircraft. Moreover, the Bilateral trade dispute could radiate to impact other countries positively through rising demand on their goods owing to their relatively improved price competitiveness, or negatively through the reduction of US and China output. In addition, the dampening impact of higher inflation rates and interest rates could spillover from the US and China to other countries through the exchange rate channel and costly external borrowing.

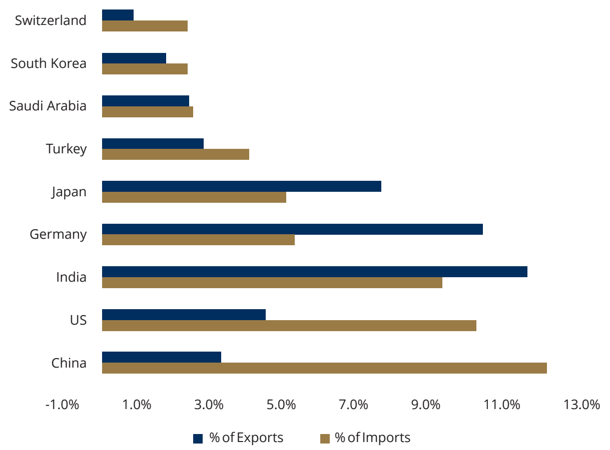
1 IMF (World Economic Outlook, October 2018) and Bundesbank estimates (Monthly Report, November 2018)

BOX 2: TRADE DISPUTES BETWEEN US, CHINA, AND THEIR IMPACT ON THE UAE (CONTINUED)

THE IMPACT OF US CHINA TRADE DISPUTES ON THE UAE

The US and China are considered to be two major UAE trading partners as the combined bilateral trade in 2017 amounted to a share of 19.3% of total UAE trade (see Figure 2). As an indirect effect, the UAE would be impacted negatively by the lower global commodity demand and softer oil prices in the medium term.

FIGURE 2. MAIN UAE TRADING PARTNERS



Source: The United Nation's trade statistics

The direct effect of US protectionism policies would impact the GCC aluminum and steel industry as the GCC exported around USD9.8 billion of aluminum; of which the UAE accounts for USD 6 billion—around 10.7% of total world export of aluminum.

Exports of UAE steel to the US, one of the biggest UAE sectors in the non-oil economy, would be impacted adversely by the 25% tariff on steel. Iron and steel exports constituted around 2.2% of total non-oil exports of the UAE in 2017. However, the impact will be limited due to the diversified exports' markets and the small share of UAE exports of iron and steel to the US.

On the other hand, aluminum exports constituted around 13.9% of total non-oil exports in 2017. The UAE is considered as one of the main suppliers of aluminum as it accounted for around 6.5% (around USD1.5 billion) of total US imports of aluminum in 2017.[2] The exemption from the imposed 10% tariff was granted only to Canada and Mexico as they account for 40.6% of total US imports of aluminum.

Moreover, the impact through indirect channels may include lower oil prices due to lower demand and higher uncertainties. The OPEC+ agreement at the end of 2018 is intended to support oil prices and stem further decline, but the decline in output will narrow the surpluses of the UAE. However, the strong economic base in the UAE as well as the planned federal and local government measures to stimulate investment and growth will help the UAE to mitigate the impact of trade disputes between the US and China.

2. Source: The United Nation's trade statistics.

CHAPTER 2. DOMESTIC ECONOMIC DEVELOPMENTS

Higher oil production, as well as growth in non-oil economic activity, supported the pace of economic growth in 2018, as approximated by the Augmented Economic Composite Indicator (AECI). Meanwhile, firming tradable prices and the implementation of VAT at the beginning of 2018 pushed inflation higher.

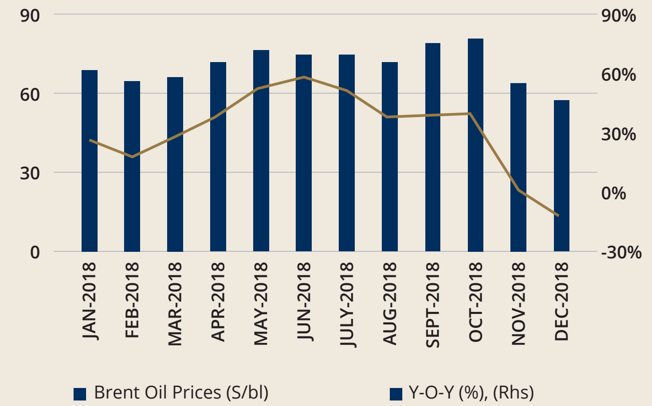
ECONOMIC ACTIVITY AND GROWTH

The continuous rise in oil prices in 2018 has bolstered the pace of economic growth in the UAE. Oil prices rose by 30.9% in 2018 compared to an increase of 24.6% in the previous year, averaging USD 71 per barrel, compared to USD 54 in 2017 (see Figure 2.1.a).

The volatility of oil prices increased in 2018, owing to fears of tighter oil supplies and expected higher demand that dominated the first half of the year. Moreover, the commitments of OPEC members to coordinated oil production cuts in January 2017 and the prospective sanctions to be imposed by the US on Iranian oil exports solidified oil prices in the first half of 2018.

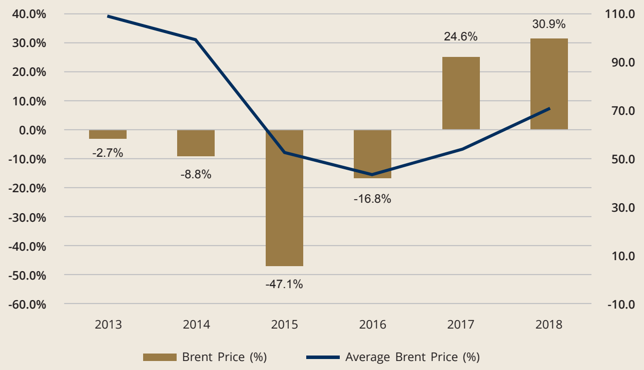
Signs of weaker economic growth in advanced economies as well as in some emerging markets have emerged towards the end of 2018. Trade disputes, and normalising US interest rates spurred the fears of weakening demand while the waivers on oil exports from Iran, coupled with weaker demand for oil, pushed oil prices downward to USD57 per barrel in December.

FIGURE 2.1.A. OIL PRICE DEVELOPMENTS IN 2018 (IN USD PER BARREL)



SOURCE: EIA

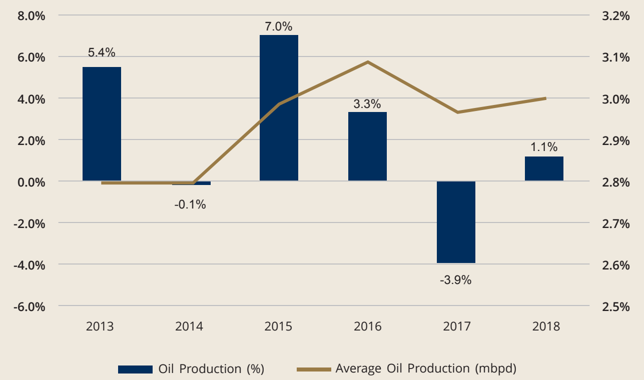
FIGURE 2.1.B. ANNUAL OIL PRICE DEVELOPMENT, BRENT PRICE



Source: EIA

From the supply side of the global oil markets, OPEC and non-OPEC members proceeded with a decision for further reduction of their oil production. The agreement aimed at correcting the growing imbalances between global oil supply and demand in 2019 through a reduction of the overall production by OPEC and Russia of 1.2 mb/d, effective January 2019 for an initial period of six months.

FIGURE 2.1.C. UAE OIL PRODUCTION

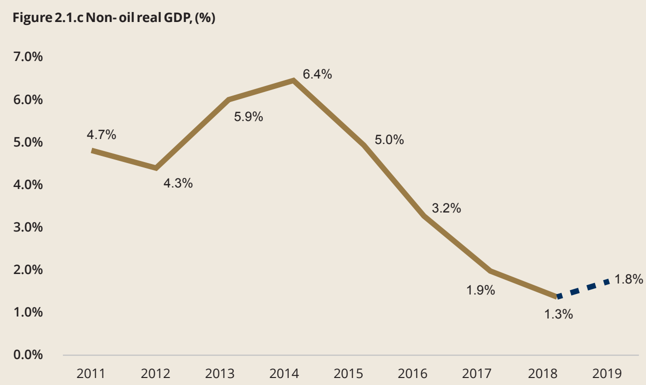


Source: OPEC

During 2018, oil production in the UAE averaged 3.0 mb/d; increasing mildly by 1% compared to a decline of 3.9% in 2017. However, production fluctuated throughout the year.

Domestic production has started to rise significantly since the second half of 2018 by 13.1% Y-o-Y averaging at 3.3 mb/d as US prospective sanctions on oil exports from Iran spurred the fears of declining oil supply. This increase was in line with OPEC's decision to increase production to ease concerns about increasing oil prices in the aftermath of the re-imposed sanctions on Iran by the US as well as falling production by Venezuela (see Figure 2.1.b.).

FIGURE 2.1.D. NON-OIL REAL GDP, (%)



Source: FCSA and CBUAE

The rise in crude oil production along with the higher oil prices resulted in an increase in growth estimates in the UAE. Compared to previous estimates, growth in the oil GDP sector significantly increased to 2.8% in 2018.

On the other hand, the non-oil sectors advanced at a softer pace; growing by 1.3% in 2018 compared to a growth of 1.9% in the previous year. Softer pace of growth was a reflection of the slowdown in some of the economic non-oil sectors (table 2.1)

TABLE 2.1 ECONOMIC GROWTH BY SECTOR(%)

Sector	Weights %	% Change	
		2017	2018
Agriculture	1.0%	3.3%	7.1%
Manufacturing	12.1%	5.0%	1.9%
Electricity, gas & water supply	4.0%	-2.9%	-2.3%
Construction	12.1%	0.1%	0.5%
Wholesale & retail trade	16.5%	0.1%	0.5%
Transportation & storage	7.8%	4.3%	1.4%
Accommodation & food service activities	3.2%	9.4%	4.1%
Information and communication	4.3%	6.5%	2.6%
Financial and insurance activities	12.2%	1.4%	0.8%
Real estate activities	8.4%	3.8%	3.6%
Professional, scientific and technical activities	3.6%	-1.8%	1.4%
Administrative and support service activities	2.5%	-0.8%	1.3%
Public administration and defense;	7.7%	0.4%	0.3%
Education	1.4%	4.6%	1.6%
Human health and social work activities	1.7%	0.0%	1.7%
Arts, recreation and other service activities	0.7%	5.1%	-0.1%
Activities of households as employers	0.8%	5.7%	3.5%
Non-oil GDP (Constant 2010 prices)	100%	1.9%	1.3%

Source: FCSA

In response, the federal and local governments took initiatives to stimulate the growth in the UAE as shown in the sections below.

FEDERAL AND LOCAL GOVERNMENT INITIATIVES TO BOOST GROWTH

To boost economic growth in the non-oil sector during 2018 and 2019, the government launched additional stimulus packages to target growth in the last quarter of 2018, in 2019 and beyond. The initiatives of both the Federal and Local governments as well as several GREs are aligned with the targeted non-energy growth in line with the UAE Vision 2021.

The federal government announced new measures to relax foreign ownership requirements and also introduced ten-year visas to stimulate the private sector and promote tourism. The new regulation also included job seekers who can now obtain a six -month visa, which will support companies and organisations in attracting and retaining talent. In addition, the government announced a landmark law allowing foreign investors to own 100% of companies in selected sectors in the UAE, resulting in an increase in foreign direct investment (FDI) and a boost in financing of the non-oil sector.

ABU DHABI AED 50 BILLION STIMULUS PACKAGE

His Highness Sheikh Mohammed bin Zayed, Crown Prince of Abu Dhabi, and Deputy Supreme Commander of the UAE Armed Forces, approved an AED 50 billion (USD13.6 billion) economic stimulus package, with a fund of AED 20 billion (USD5.4 billion) allocated to the 2019 development package. These packages aim to further reduce the UAE's economy's dependency on oil revenues, by encouraging the creation of new industries and attracting foreign investment. According to a report published by the Abu Dhabi Government, the package includes 10 economic initiatives that will support the generation of more business activities and enhance the economic environment in support of higher share of private sector economic activity, as well as address the structural bottlenecks.

The initiatives aim to:

- Implement an instant licensing system for most commercial license types and all services provided by the Abu Dhabi Government;
- Accelerate the settlement of payments due on contracts for the private sector;
- Establish the Abu Dhabi Accelerators and Advanced Industries Council to attract and support value added investments and technologies;
- Provide at least 10,000 jobs for Emiratis in the private and public sectors over the next five years.

Moreover, the initiatives focus on boosting, empowering and supporting small and medium-sized enterprises (SMEs), and supporting private companies operating in tourism and industrial sectors.

To facilitate the implementation and coordination of the stimulus package, the government ordered the establishment of the Abu Dhabi Accelerators and Advanced Industries Council, "Ghadan". Their primary focus is to attract and support value-added investment and technologies that would predict and lead the development of Abu Dhabi's economy on a local and regional scale

DUBAI FISCAL STIMULUS INITIATIVES

The government of Dubai announced several initiatives to stimulate growth that focus on cost reduction of key industries in Dubai including aviation, real estate and education. To help foster additional spending by investors and promote private sector growth, the government reduced the cost of doing business and lowered taxes. The initiatives also include reduced service fees for commercial entities by 50% through cancelling 19 fees related to the aviation industry and aircraft landing permits, in addition to, waiving 4% late property registration fees imposed by the Dubai Land Department to stimulate economic activity.

ADNOC IN-COUNTRY VALUE INITIATIVE

The Abu Dhabi National Oil Company (ADNOC) introduced an In-Country Value (ICV) programme for its suppliers. This procurement-led initiative aims to boost ADNOC's ICV contribution by focusing on local supplier selection, development of UAE Nationals, and the localisation of critical functionalities in the oil and gas industry.

The ICV programme will support the economy through diversification, building additional industrial clusters, Emiratisation, and strategic localisation of its supply chain. ADNOC five-year plan is expected to localise around 40% of the total awarded contracts, which are estimated to be around USD131 billion. It aims to create opportunities for both international and local businesses to further participate in ADNOC's projects and revitalise the domestic non-oil sector. It is also an extension of ADNOC 2030 smart growth strategy that aims at increasing its operational efficiency, profitability and sustainability.

NEW INVESTMENT LAW

The UAE President, and Ruler of Abu Dhabi His Highness Sheikh Khalifa bin Zayed Al Nahyan, mandated the issuance of Decree law No. 19 on Foreign Direct Investment, for the year 2018. The law which has been in effect since the beginning of 2019, focuses on attracting foreign direct investments to the UAE.

The new law recoganised the importance of FDI as one of the key factors influencing the non-oil activity. It also reaffirms the UAE's position as a major hub for FDI inflows at the regional and global levels, which aim to expand the country's production base through the transfer of technology, knowledge, and training, thereby creating job opportunities in various sectors. The rationale is to deviate away from the restrictions on foreign investment imposed in the commercial companies' law No. (2) of 2015, which stated that foreign investors should have a UAE national partner holding 51% ownership. The new Decree provides an exemption to this general rule granting certain foreign investors a 100% ownership in a range of sectors.

The Decree defines foreign capital that foreign investors will have to bring to the UAE in the form of fixed assets and intangible rights, such as patents, concession rights, trademarks and trade names owned or registered in accordance with the laws and regulations in force in the UAE.

GROWTH PROJECTIONS FOR 2019

CBUAE projectes that the non-oil GDP economic growth in 2019 would reach 1.8%, and continue its upward trajectory in the subsequent years, compared to a growth of 1.3% in 2018. The announced fiscal stimulus packages and the new investment law will encourage economic growth, increase consumption, reinvigorate the property market, and improve the labor markets as the investors and consumer sentiments continue to solidify.

Even though the non-oil growth is expected to reach 1.8% in 2019, supported by stronger fundamentals of the economy, CBUAE estimates that there would be deceleration in oil production consistent with the recent OPEC+ agreement. As a result, the overall production in 2019 is projected to be an average of 3.1million barrels per day, down from an average of 3.285million barrels per day in Q4 of 2018, resulting in a growth of 2.7% in 2019 in the hydrocarbon GDP. Therefore, real GDP growth rate is projected to reach 2.0% in 2019.

TABLE 2.1.3.1 ECONOMIC GROWTH IN THE UAE (%)

Period	2015	2016	2017	2018(E)	2019(P)
Real GDP, o/w:	5.1	3.0	0.5	1.7	2.0
Oil GDP	5.2	2.6	-2.8	2.8	2.7
Non-Oil GDP	5.0	3.2	1.9	1.3	1.8

Source: FCSA & CBUAE

CONSUMER PRICE INDEX AND INFLATION

Annual inflation in the UAE rose to 3.1% in 2018 compared to 2% in the previous year, which is higher than its five-year compounded annual growth rate (CAGR)1 at 2.5%. The rise in inflation occurred despite the continued decline in housing prices—around 34% of the consumption basket—due to the implementation of VAT at the beginning of 2018. Moreover, CPI inflation was influenced by the increase in oil prices in 2018, which was transmitted to the domestic fuel prices through the transportation prices, split equally between the tradable and non-tradable prices (table 2.2.1). Therefore, inflation in tradable prices rose from 3% in the previous year to 6.9% in 2018, higher than its five-year CAGR of 0.6%. In contrast, non-tradable price inflation decreased to 1.2% in 2018 compared to 1.8% in 2017, lower than its five-year CAGR of 2.3%.[1]

TABLE 2.2.1 UAE CPI INFLATION, (%)

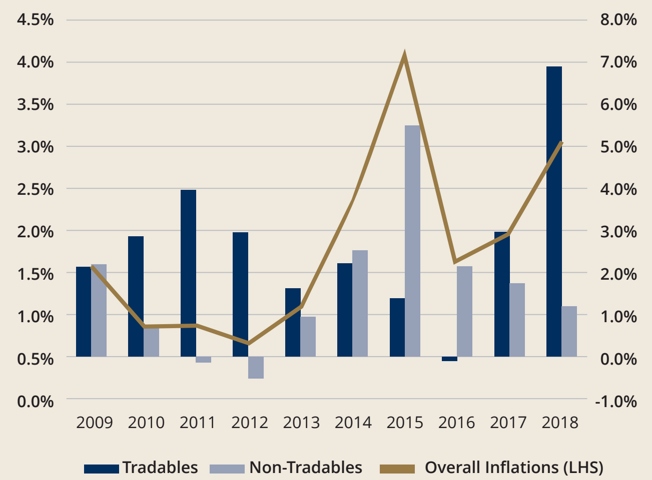
Items	Weight %	2015	2016	2017	2018
Inflation (period average)	100.0	4.1	1.6	2.0	3.1
Tradable inflation	34.0	1.4	0.0	3.0	6.9
Food and soft drinks	14.3	1.2	1.0	1.2	3.5
Beverages and tobacco	0.3	1.2	1.1	18.3	57.0
Textiles, clothing and footwear	3.2	-1.6	3.2	0.2	15.1
Furniture and household goods	5.6	2.2	0.3	1.1	4.6
Transportation	7.3	2.0	-4.1	5.4	11.0
Miscellaneous goods and services	3.2	2.2	0.8	10.4	3.5
Non-Tradables	66.0	5.5	2.1	1.8	1.2
Housing	34.1	8.8	3.6	0.9	-3.1
Medical care	1.4	0.3	1.7	3.9	0.0
Transportation	7.3	2.0	-4.1	5.4	11.0
Communications	5.4	0.1	-0.8	-1.6	3.6
Recreation and culture	3.2	0.1	0.3	-4.7	8.6
Education	7.7	3.8	4.2	4.1	4.1
Restaurants and hotels	4.0	2.7	2.1	1.0	7.5
Miscellaneous goods and services	3.2	2.2	0.8	10.4	3.5

Source: FCSA & CBUAE

The rise in the tradable prices in 2018, which accounts for 34% of the standard consumption basket in the UAE, was mainly due to the base year effect of the implementation of the VAT, as well as the excise tax in October 2017. For instance, the prices of beverages and tobacco rose by 57% in 2018 compared to the 18.3% increase in the previous year. In addition, prices of food and soft drinks rose at a higher pace than in 2017 due to the implementation of the VAT as well as the increase in prices of agricultural commodities in international markets. In particular, the prices of cereals, such as barley, maize and wheat rose in 2018 by 29%, 6.4% and 14.4% respectively in the international markets.2 Moreover, prices of poultry and lamb meat continued to increase in 2018 by 5.7% and 10.1% compared to a similar rise of 14.6% and 15.6% in the previous year.

Moreover, textiles, clothing and footwear increased at a faster pace in 2018 compared to the previous due to a noticeable increase in raw materials in international markets—cotton prices (USD/kg) rose in 2018 by 9.2% due to lower output in Bangladesh, Pakistan, Indonesia, Vietnam and China.[2]

FIGURE 2.2.A. TRADABLE AND NON-TRADABLE INFLATION (%, Y-O-Y)



Source: Federal Competitiveness and Statistics Authority (FCSA).

Domestic fuel prices were lifted largely by the rise in oil prices in 2018 registering a 30.9% hike. Prices of unleaded gasoline 98, 95, 91 and diesel increased by 23.5%, 24.7%, 25.1% and 30.0% in 2018 compared to a rise of 14.6%, 15.6%, 16.3%, and 18.8%, respectively in the previous year.

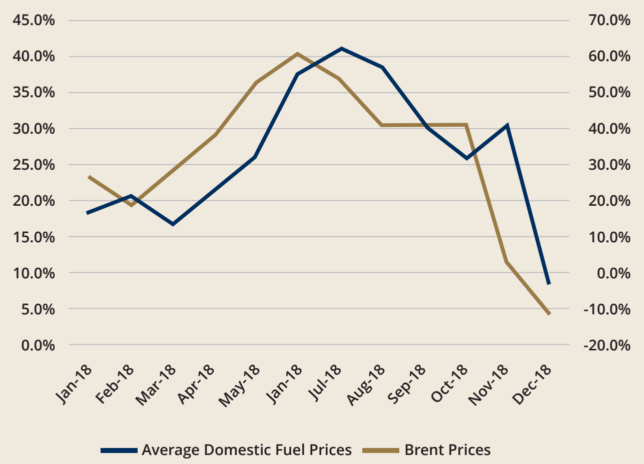
1 The CAGR is the mean annual growth rate (geometric mean) over a 5-year horizon.

2 Source: World Bank commodities price data. The percentage change in prices is calculated based on the annual average measured in US dollar per metric ton for cereals and US dollar per Kilogram for the prices of poultry and meat.

Domestic fuel price changes impacted the year average of the transportation price, which increased by 11% compared to 5.4% in the previous year. It is worth mentioning that the impact of oil price movements is reflected on the domestic fuel prices with a lag of one month (see Figure 2.2.b).

Domestic fuel prices changes impacted the year average of the transportation price, which increased by 11% compared to 5.4% in the previous year. It is worth mentioning that the impact of oil price movements is reflected on the domestic fuel prices with a lag of one month (see Figure 2.2.b).

FIGURE 2.2.B. DOMESTIC FUEL PRICES AND BRENT OIL PRICE, (Y-O-Y)



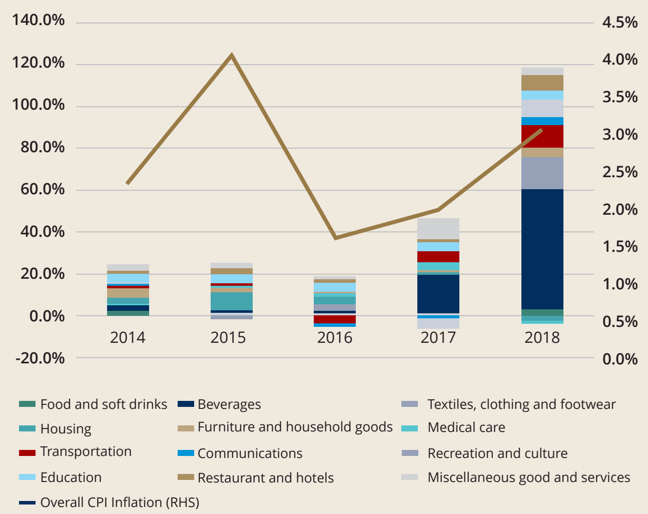
Source: EIA and MOEI

Nonetheless, non-tradable prices continued easing in 2018, similar to its 2017 trend, owing to the decline in housing cost by 3.1% as rents continued their downward trajectory throughout 2018. The housing group accounts for 34% of the UAE standard consumption basket, of which around 26% represents the actual rents paid by tenants. Therefore, the price moderation can be attributed to the continued decrease of rent on residential units, on average, in Abu Dhabi and Dubai by 10.7% and 8.9% in 2018 compared to a decline of 10.2% and 5.2% in the previous year.

Furthermore, the Medical Care group remained virtually stable and consistent with its 2017 levels as most of its sub-components such as medical services and pharmaceutical products' prices remained unchanged. In contrast, recreation, culture and restaurants as well as hotels groups, rose markedly in 2018 influenced by the increase in the number of tourists in Abu Dhabi and Dubai as well as the indirect effect of the rising cost of food and soft drinks.

The 6.9% rise in tradable prices in the UAE was a consequence of their increase in the Emirates of Abu Dhabi and Dubai by 7.7% and 5.1% in 2018 compared to a softer increase of 2% and 2.9% in the previous year, respectively. In parallel, non-tradable prices softened in Abu Dhabi and Dubai, increasing by 1% and 0.2% compared to 1.3% and 1.8% respectively.

FIGURE 2.2.C. CONTRIBUTION OF DIFFERENT SUB-COMPONENTS TO THE TOTAL CPI INFLATION (%, Y-O-Y)



Source: FCSA

Inflation excluding housing and transportation increased by 5.3% in 2018 compared to 2.2% in the previous year in tandem with the upward trajectory in the prices of oil, food, textiles, and recreation and culture.

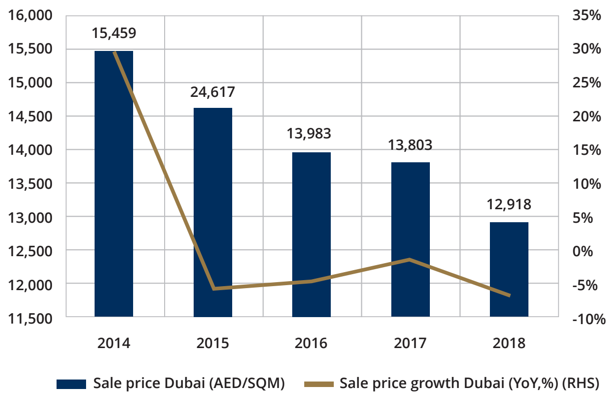
BOX 3: ANNUAL DEVELOPMENTS IN REAL ESTATE

According to REIDIN Price Index[1], the Real estate market in the UAE has seen similar patterns of change for the residential segment. In particular, the property prices in Dubai and Abu Dhabi decreased on average by 6.4% and 6.8% on an annual basis, respectively, during 2018. Therefore, the rental yield has contracted on average in both Emirates —6.85% for Abu Dhabi and 6.86% for Dubai—due to the continued fall in rents since mid-2014; although, both markets remained attractive for investors.

DUBAI RESIDENTIAL MARKET

Recent 2018 data show a fall in residential property price of 6.4%, on average, compared to a decrease of 1.3% in 2017 (Figure 1). The average price in the property market reached AED 12,918 per square meter (AED/m^2), compared to 13,803 AED/m^2 in 2017.

FIGURE 1. DUBAI RESIDENTIAL SALE PRICES



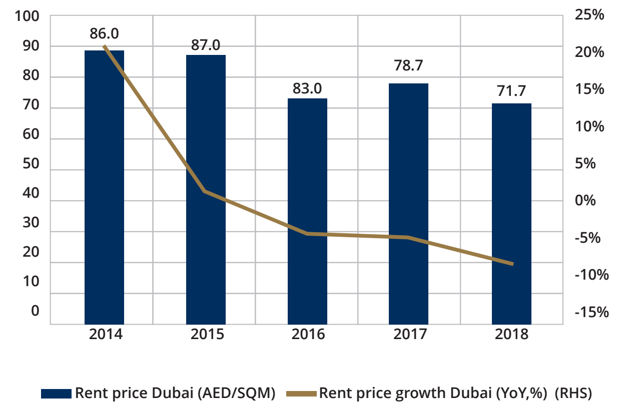
Source: REIDIN

Since the downward cycle in mid-2014, the fall in prices has led to the fall in rents in Dubai (Figure 2), which declined by 8.9% in 2018, on average, compared to a fall of 5.2% during the previous year.

Concerning the rental yield, Dubai registered a decelerating yield during 2018 over the previous year owing to a faster pace of decline in rent relative to property values. This trend reflected a decline of demand, in line with developments in the job market, compared to existing supply, during this period.

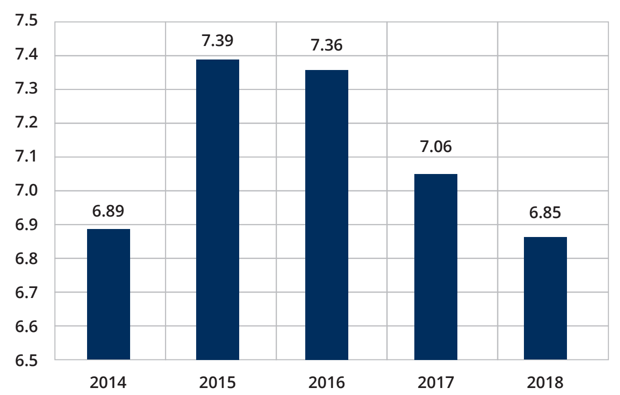
1. REIDIN Residential Sales Price Index series are calculated on a monthly basis and cover 21 areas and 6 districts in Dubai. For Abu Dhabi, the indices cover 7 areas and 5 districts.

FIGURE 2. AVERAGE MONTHLY DUBAI RESIDENTIAL RENT PRICES



Source: REIDIN

FIGURE 3. DUBAI RENTAL YIELD (%)



Source: REIDIN

As per the Dubai Land Department (DLD), in 2018 investment in real estate with a value of deals of less than AED 10 million in the Emirate of Dubai stood at AED 45.6 billion, of which AED 38.5billion or 84.4% were paid cash and AED 7.1billion or 15.6% made through mortgage. Compared to 2017, cash purchases declined by 36.6%, from AED

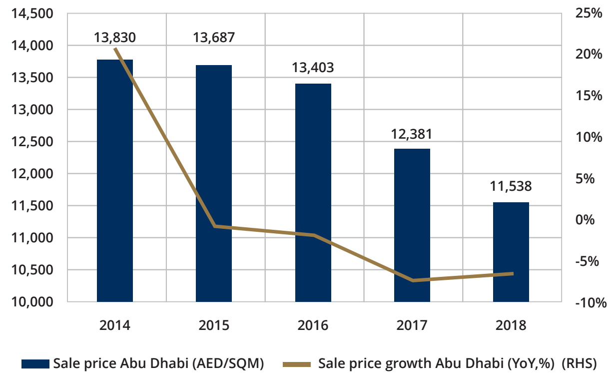
BOX 3: ANNUAL DEVELOPMENTS IN REAL ESTATE

60.7billion, while mortgage purchases dropped by 17.6% from AED 8.7billion. The fall in the amount of all investment transactions was at 34.2% in 2018.

ABU DHABI RESIDENTIAL MARKET

In 2018, the average price in the housing market in Abu Dhabi declined compared to the previous year, reaching 12,538 AED/m2. Thus, the downward trend observed illustrates a further deterioration in the property prices of the residential market during 2018 by 6.8% on average (Figure 4).

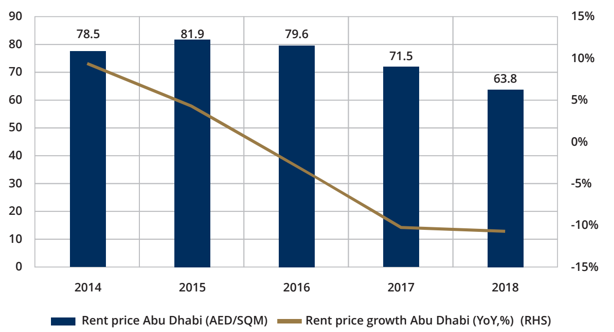
FIGURE 4. ABU DHABI RESIDENTIAL PRICES



Source: REIDIN

With regards to the rental market in Abu Dhabi, rent values declined by 10.7% in 2018, on average, slightly more than the previous year (Figure 5).

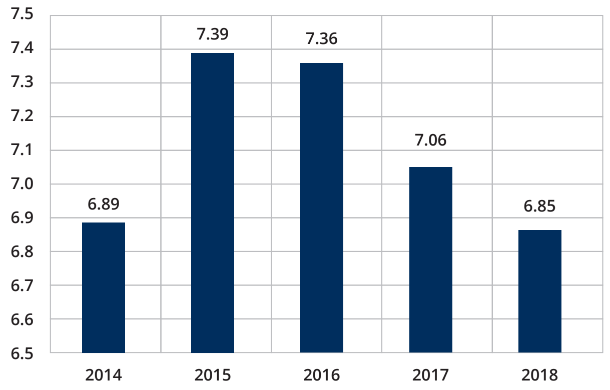
FIGURE 5. AVERAGE MONTHLY ABU DHABI RESIDENTIAL RENT PRICES



Source: REIDIN

In addition, the continued decline in rents relative to prices has pushed the rental yield to its lowest level in the last five years. The yield declined below the average of the four previous years while remaining close to 7% (Figure 6).

FIGURE 6. ABU DHABI RENTAL YIELD (%)



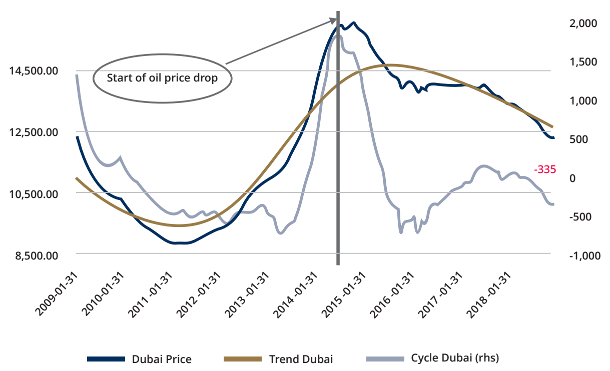
Source: REIDIN

CBUAE did an assessment of the deviation of the real estate prices relative to their long-term trend[1], on the Dubai property sale prices (Figure 7). From 2010 until late 2013, the gap was negligible oscillating around zero. From end of 2013 until mid-2014, the gap moved into a positive territory, signaling overheating of the real estate market. Since mid-2014, marking the beginning of decline of oil price, the gap started declining, moving to a negative territory by the end of 2015. Since then it started recovering with the downturn gap being negligible, but still negative as of July 2018. However, as of December 2018 the gap widened again to AED -335 (-2.6% of the long-term trend) which measures the difference between the observed price and the long-term trend (12,297 AED/m2 and 12,632 AED/m2, respectively), indicating that the real estate market in Dubai is underperforming compared to the varying long-term trend.

1. The analysis estimates the size of the gap (cyclical component in Figures 7 and 8) using a two-sided Hodrick-Prescott (HP) filter with a smoothing parameter of $\lambda = 14{,}400$ for the monthly series.

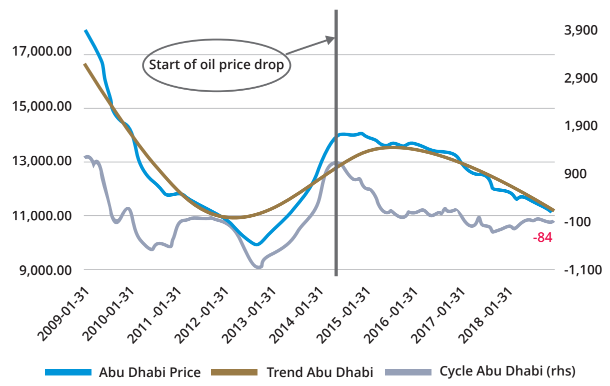
BOX 3: ANNUAL DEVELOPMENTS IN REAL ESTATE

FIGURE 7. DUBAI SALES PRICE, TREND AND GAP



Source: REIDIN

FIGURE 8. ABU DHABI SALES PRICE, TREND AND GAP



Source: REIDIN

As for Abu Dhabi, the real estate market (Figure 8) the gap of the actual price and its long term trend declined gradually starting in 2009. The gap moved to a negative territory in the middle of the year (during the Global Financial Crisis), with a slight recovery during 2011-12, and back to a new low in 2013. Subsequently, the positive gap, which indicates overheating reached a peak compared to the long term trend in mid-2014.

Since then, with the oil price decline, the gap became negative, reaching recently -84 AED/m2 (-0.7% of the long-term trend), registering a difference between the observed price and the long term trend (11,116 AED/m2 and 11,200 AED/m2, respectively). The market is underperforming relative to the varying long-term trend.

EXCHANGE RATE DEVELOPMENTS

In 2018, the Dirham appreciated overall, driven by the developments in the foreign currency movements.

On a yearly average basis, the Dirham has been appreciating for a relatively long period since 2014 against its top non-dollarized imports and exports partners.

TABLE 2.3.1 DIRHAM APPRECIATION AGAINST TOP NON-DOLLARIZED IMPORT PARTNERS (%)

Country	Weights %, 2017	2015	2016	2017	2018
China	18.7	2.0	5.7	1.6	-2.0
India	7.9	5.1	4.8	-3.1	5.0
Japan	5.4	14.3	-10.1	3.1	-1.5
Germany	4.6	19.6	0.3	-1.9	-4.5
South Korea	3.1	7.4	2.6	-2.6	-2.7
Turkey	3.0	24.5	11.0	20.6	32.7
Italy	2.6	19.6	0.3	-1.9	-4.5
UK	2.6	7.7	13.2	4.8	-3.4
France	2.4	19.6	0.3	-1.9	-4.5
Switzerland	2.0	5.2	2.4	-0.1	-0.6
Weighted Average	52.3	4.7	1.7	0.7	0.3

Source: Data on Import shares (weights) are provided by the Federal Competitiveness and Statistics Authority (FCSA) for 2017. Data for the bilateral exchange rates are the annual average observations as reported by Bloomberg.

Using the imports share as a metric for measuring weights on bilateral exchange rates, the Dirham has mildly appreciated by 0.3% in 2018 against its top 10 non-dollarized import partners, which account for 52.3% of the total imports, compared to 0.7% in the previous year. The appreciation occurred subsequent to the depreciation of the Turkish Lira by 32.7% in 2018 compared to 20.6% in 2017 owing to the challenges the Turkish economy was facing. This included a high current account deficit, combined with high levels of debt in the private sector and significant levels of foreign funding in the banking system.

The appreciation of the Dirham against the Turkish Lira was partially offset by the appreciation of other currencies such as the Chinese Yuan (2.0%), the Japanese Yen (1.5%), the Euro (4.5%), the Sterling Pound (3.4%), and the Swiss Franc (0.7%).

TABLE 2.3.1 DIRHAM APPRECIATION AGAINST TOP NON-DOLLARIZED NON-OIL EXPORT PARTNERS (%)

Country	Weights %, 2017	2015	2016	2017	2018
India	10.6	5.1	4.8	-3.1	5.1
Turkey	9.1	24.5	11.0	20.6	32.7
Iraq	4.7	2.6	-0.7	-0.8	0.4
China	3.1	2.0	5.7	1.6	-2.0
Singapore	3.0	8.5	0.5	0.0	-2.3
South Korea	2.5	7.4	2.6	-2.6	-2.7
Switzerland	2.0	5.2	2.4	-0.1	-0.6
Pakistan	1.7	1.7	1.9	0.6	15.3
Netherlands	1.7	19.6	0.3	-1.9	-4.5
Japan	1.6	14.3	-10.1	3.1	-1.5
Weighted Average	40.2	4.1	1.7	1.5	3.5

Source: Data on exports shares (weights) are provided by the Federal Competitiveness and Statistics Authority (FCSA) for 2017. Data for the bilateral exchange rates are the annual average observations, recorded and reported by Bloomberg.

Using the exports share as a metric for measuring weights on bilateral exchange rates, the Dirham displayed a higher appreciation against its top 10 non-dollarized export partners, which account for 40.2% of the total non-oil exports. The NEER appreciated by 3.5% in 2018 compared to 1.5% in the previous year. The difference in the weight of Turkey in the basket of non-energy exports versus imports exacerbated the impact of the depreciation of the Turkish Lira with respect to export partners—Turkey accounts for 3.0% (9.1%) of UAE imports (exports) in 2017.

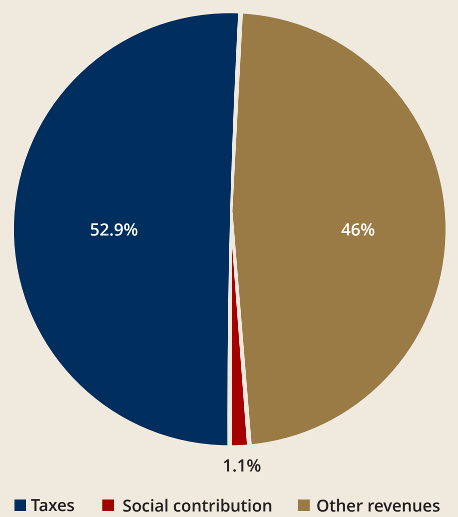
Moreover, the depreciation in the Indian Rupee in 2018—the largest export partner for the UAE—reinforced the appreciation of the Dirham. This came as a result of the monetary policy normalisation in the US, relative to an easing policy stance by the Reserve Bank of India (RBI). In addition, the Indian economy suffered from a worsening current account balance likely due to higher oil prices, which dampened the private sector external borrowing. Additionally, the trade tensions between the US and China took its toll on emerging economies' currencies in Asia, including India.

CONSOLIDATED FISCAL STANCE

The rise in oil prices in 2018 by 30.9% compared to 24.6% in the previous year has resulted in an increase in the net operational surplus by AED 41.6 billion; reaching AED 76.4 billion in 2018 compared to a surplus of AED 34.7 billion in the previous year. The increase in the surplus was a result of the rise in the revenues by 17.4% to reach AED 465.7 billion due to the rise in the tax revenues by 32.3% in 2018 to reach AED 214.3 billion. Moreover, expenditures rose at a softer pace by 4.8% to AED 423.1 billion, as a result of the increase in other expenses by 9.8% to reach AED 108.4 billion.

REVENUES

FIGURE 2.4.1.A. REVENUES COMPOSITION IN 2018 (%)



Source: Ministry of Finance (MoF)

As for 2018, revenues rose by AED 69.1 billion to reach 465.7 billion compared to AED 396.6 billion in the previous year. The increase in revenues was a direct result of tax and other revenues, which rose by 32.3% and 7.1% in 2018 to reach AED 214.3 billion and AED 246.4 billion, respectively. Social contributions, which represent a small part of budgetary revenues (around 1% of total revenues) increased by 7.1% in 2018 compared to the previous year.

It is worth noting that the adopted fiscal reforms by the federal government in 2018 have helped achieve the key objectives of diversifying the sources of government revenues while adhering to transparent tax procedures and promoting a more efficient allocation of resources.

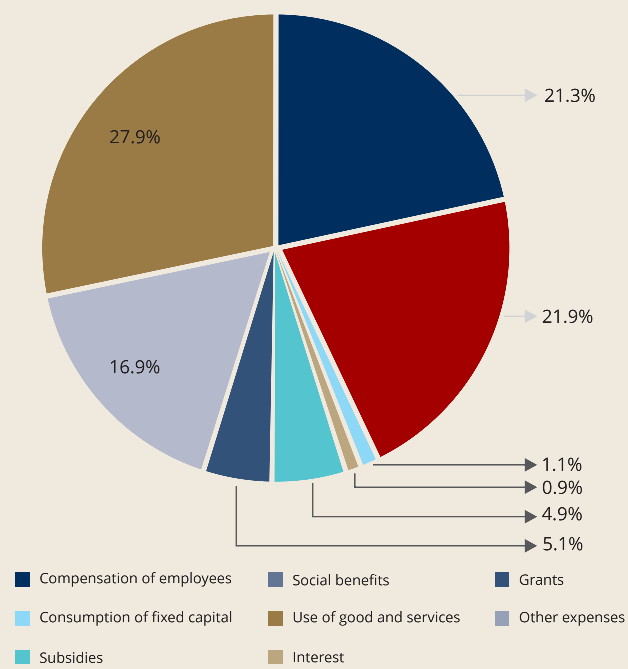
EXPENDITURES

On the expenditures side, total expenses rose Y-o-Y by 5.4% during the fourth quarter of 2018. This was compared to a higher increase of 6.3% in the previous quarter. The increase in government spending came as result of the drive to mitigate the recent growth moderation, while adopting a growth-friendly fiscal policy based on a medium- and long-term sustainable budget.

Compensation of employees, which accounts for 19.6% of total expenses in the fourth quarter of 2018, eased Y-o-Y by 4.1%% to AED 21.2 billion, compared to an increase of 12.3% in the previous quarter. Moreover, social benefits rose significantly by 68.2% compared to an increase of 43.6% in the previous quarter. Other expenses, which account for 27.4% of total expenses declined by 2.8% compared to a rise of 23.7% in the previous quarter. On the other hand, the use of goods and services continued to decline at a softer pace in the fourth quarter at 2.0% compared to a decline of 31.4% in Q3 2018. Further, capital spending, measured by the net acquisition of non-financial assets, increased in the fourth quarter Y-o-Y by 14.3% compared to a decline of 7.8% in the previous quarter.

As for 2018, total expenses rose by 7.6% to reach AED 389.3 billion compared to AED 361.9 billion in the previous year. The increase in expenses was a result of the rise in compensation of employees, grants, social benefits, and other expenses by 10.4%, 14.6%, 60.3%, and 9.8%, respectively. Collectively, these revenues constitute around 71.1% of total expenses.

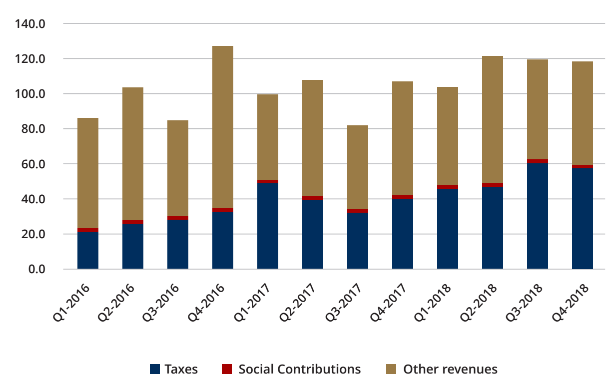
FIGURE 2.4.2.A. EXPENSES COMPOSITION IN 2018 (%)



Source: Ministry of Finance (MoF)

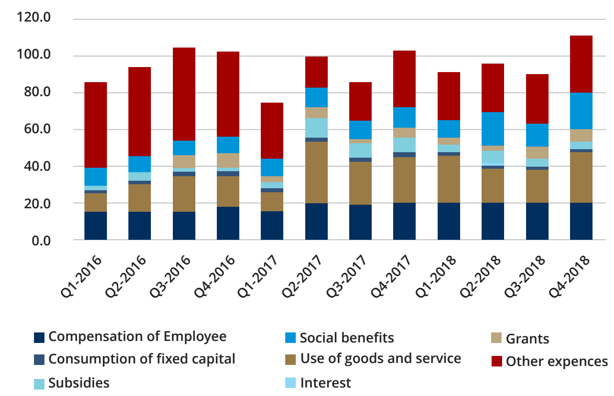
GOVERNMENT FINANCES

2.4.A. GENERAL GOVERNMENT REVENUES (BILLIONS OF DIRHAMS)



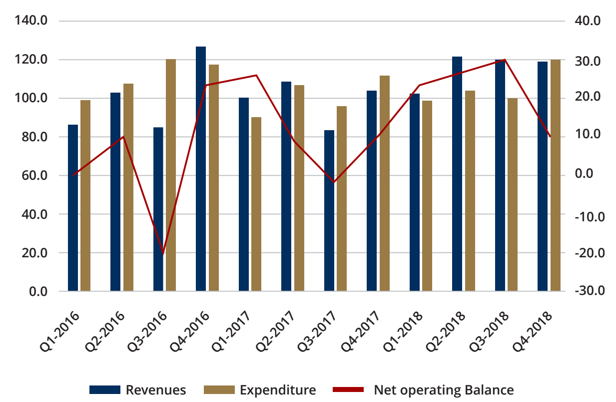
Source: Ministry of Finance (MoF)

2.4.B. GENERAL GOVERNMENT EXPENDITURES (BILLIONS OF DIRHAMS



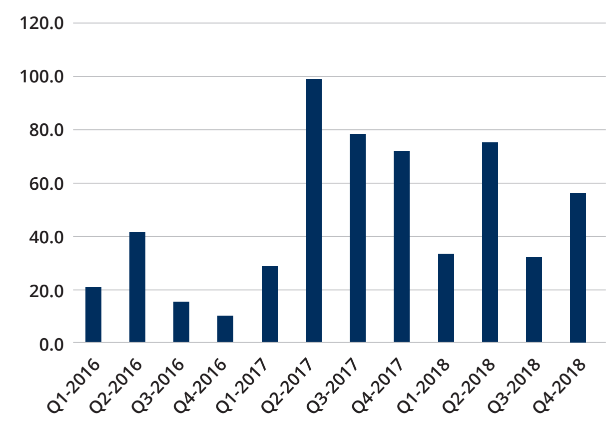
Source: Ministry of Finance (MoF)

2.4.C. FISCAL STANCE (BILLIONS OF DIRHAMS)



Source: Ministry of Finance (MoF)

2.4.D. SUBSIDIES AND TRANSFERS TO GRES (BILLIONS OF DIRHAMS)



Source: Ministry of Finance (MoF)

TABLE 2.4 CONSOLIDATED GOVERNMENT FINANCES (BILLION AED)

Consolidated	2017				2018				2017 (% Y-o-Y)				2018 (% Y-o-Y)			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Net Operating Balance	25.4	8.6	-3.0	3.7	12.7	23.9	29.5	10.4	-----	-----	-----	-----	-----	-----	-----	-----
Revenues (a)	99.6	107.9	82.8	106.3	103.8	122.7	120.6	118.5	16.2%	5.1%	-2.5%	-15.9%	4.2%	13.7%	45.7%	11.5%
Taxes	49.2	40.0	32.4	40.3	46.7	49.5	60.6	57.5	133.1%	53.7%	12.0%	23.3%	-5.1%	23.7%	86.9%	42.6%
Social contributions	1.2	1.1	1.3	1.1	1.3	1.3	1.3	1.2	-18.0%	-9.4%	8.3%	27.7%	3.9%	24.3%	0.8%	1.5%
Other revenues	49.2	66.8	49.1	64.9	55.9	71.9	58.8	59.9	-22.1%	-11.4%	-10.5%	-30.1%	13.6%	7.5%	19.7%	-7.7%
Expenditure (b)	89.5	106.4	95.2	112.5	97.9	105.9	99.9	119.4	-9.0%	-0.6%	-20.4%	-3.9%	9.4%	-0.5%	4.9%	6.2%
Expense	74.2	99.3	85.8	102.6	91.1	98.8	91.2	108.1	-13.3%	6.3%	-17.7%	-0.4%	22.8%	-0.5%	6.3%	5.4%
Compensation of employees	15.9	20.1	18.8	20.4	19.5	21.2	21.1	21.2	2.1%	27.6%	19.4%	12.1%	22.8%	5.1%	12.3%	4.1%
Use of goods and services	10.5	33.7	24.9	25.7	27.0	16.0	17.1	25.2	1.0%	127.2%	25.0%	50.4%	157.0%	-52.4%	-31.4%	-2.0%
Consumption of fixed capital	1.3	1.4	1.0	1.4	1.1	1.0	1.0	1.0	11.7%	-6.1%	-13.9%	-35.2%	-13.1%	-27.3%	3.4%	-29.2%
Interest	0.5	0.6	0.3	0.5	0.5	1.1	0.6	1.4	103.8%	42.6%	-4.6%	-48.0%	-2.4%	85.1%	111.0%	168.4%
Subsidies	2.9	9.9	7.9	7.2	3.2	7.5	3.1	5.3	38.4%	139.3%	406.3%	605.6%	12.7%	-23.9%	-60.5%	-26.1%
Grants	3.3	6.7	1.2	6.1	4.1	2.6	7.0	6.1	625.6%	1169.8%	-82.9%	-23.9%	22.6%	-60.5%	487.7%	0.7%
Social benefits	9.8	10.1	10.3	10.9	10.5	22.2	14.8	18.3	4.6%	19.4%	21.8%	20.4%	7.8%	120.0%	43.6%	68.2%
Other expenses	30.1	16.8	21.4	30.5	25.2	27.1	26.5	29.6	-35.1%	-64.9%	-57.2%	-34.6%	-16.2%	61.7%	23.7%	-2.8%
Net acquisition of non-financial assets	15.3	7.1	9.5	9.9	6.7	7.0	8.7	11.3	19.5%	-48.1%	-38.6%	-29.9%	-56.0%	-0.5%	-7.8%	14.3%

Source: Federal Competitiveness and Statistics Authority (FCSA).

- UAE Ministry of Finance, revenues do not include ADNOC transfers and government investment income.
- Other revenues covers: Property income (interest, dividends, rent), Sales of goods and services (including administrative fees), Fines and penalties and other revenues not elsewhere classified. Effective 2016Q1, the Emirate of Abu Dhabi has added some transfers of important investment authorities from financing accounts to revenues, included in the distributed profit computation.
- Subsidies include social and price subsidies as well as transfers to GREs.
- Other expenses include the payments of Abu Dhabi made on behalf of the Federal Government.
- Grants include current or capital transfers from the Government to other Government units, international organizations or foreign Governments, excluding transfers between Federal and Local Government

BALANCE OF PAYMENTS DEVELOPMENTS

The current account surplus increased from AED101 billion (7.3% of GDP) in 2017 to AED139 billion in 2018 (9.1% of GDP). The increase in the current account surplus in 2018 was attributed to the increase in the trade balance (increase of AED52.5 billion) associated mainly with the oil price evolution, which increased from an average of USD54 in 2017 to an average of USD71 in 2018. The increase in the trade balance surplus was complemented with narrower deficit in the services balance, however the surplus of the investment income decreased and the deficit in the transfers balance widened.

In 2018, the hydrocarbon exports increased by 13.9% or AED29.6 billion compared to 2017, due to the increase in the price of crude oil and other products. This increase was accompanied by a rise in non-hydrocarbon exports by 2.1% or AED8 billion. Meanwhile, re-exports of imported goods decreased by 4.6% (AED25.3 billion). As a result, total exports and re-exports (FOB, in free-on-board prices) increased by AED12.3 billion or 1.1%.

Meanwhile, total imports (CIF), i.e., including the cost of insurance and freight for the transport of the goods from the importing partners, decreased by AED44.7 billion or 4.4% in 2018, contributing to the substantial increase in the trade balance, reaching 19.7% of GDP in FOB prices.

As regards to the services balance, the marginal increase in the travel and transport accounts led to a narrower increase in both the credit and debit sides of the services balance, where the sub-accounts of travel and transport items represent 69.2% of credits and 45.5% of debits. Net travel recorded an inflow of AED12.4 billion, slightly decreased compared to AED12.5 billion in 2017.

Even though inbound tourism in the UAE continued to increase in 2018, however, the travel account grew at a much slower pace (1.5% in 2018 compared to 8% in 2017) due to a decrease in estimated spending per traveler.

Net investment income recorded inflow of AED7.3 billion in 2018, compared to AED10.2 in 2017, mainly due to higher interest rates and higher oil price. Transfers, however, recorded net outflow of AED166 billion (increased by AED14.7 billion), where private transfers increased by AED11.4 billion and public transfers marginally increased by AED3.3 billion.

The deficit of the financial account in 2018 widened noticeably by AED60.4 billion compared to 2017, reaching AED123 billion or 8.1% of GDP. The change in 2018 was mainly due to the increase in banks' investments abroad by AED46.9 billion. In addition, the financial outward flows by the public sector entities and private non-banks increased by AED7 billion and AED2.2 billion, respectively. A marginal increase was recorded in the inward foreign direct investment by AED0.1 billion in 2018 that was dominated by an increase in outward foreign direct investment by AED3.7 billion, reaching AED55.3 billion.

The combined effects of expansion in the current account surplus and a wider deficit in the financial account (almost doubled), resulted in smaller surplus in the overall balance of payments that was recorded at AED13 billion in 2018 (0.9% of estimated GDP). The net foreign assets of the CBUAE, including the reserve position with the IMF, increased during the same period by AED13.3 billion reaching AED 358.5 billion.

TABLE 2.5 UAE BALANCE OF PAYMENTS STATISTICS (BILLION AED)

	2017*	% change	% GDP	2018*	% change	% GDP
Current Account Balance	**101.0**	**108.3**	**7.3**	**139.0**	**37.6**	**9.1**
Trade Balance (FOB)	**246.9**	**22.0**	**17.8**	**299.4**	**21.3**	**19.7**
Trade Balance (CIF)	**146.3**	**40.1**	**10.5**	**203.3**	**38.9**	**13.4**
Total Exports of Hydrocarbon	**213.5**	**25.1**	**15.4**	**243.1**	**13.9**	**16.0**
Crude Oil Exports	115.0	24.5	8.3	132.4	15.1	8.7
Petroleum Products Exports	71.0	26.6	5.1	81.5	14.8	5.4
Gas Exports	27.5	24.4	2.0	29.2	6.1	1.9
Total Exports of Non-Hydrocarbon	**391.5**	**3.0**	**28.2**	**399.5**	**2.1**	**26.3**
Free Zone Exports	225.5	6.7	16.3	255.3	13.2	16.8
Other Exports[1]	166.0	(1.5)	12.0	144.3	-13.1	9.5
Re Exports[2]	**546.5**	**2.6**	**39.4**	**521.2**	**(4.6)**	**34.3**
Total Exports & Re Exports (FOB)	**1151.5**	**6.3**	**83.0**	**1163.8**	**1.1**	**76.5**
Total Imports (FOB)[3]	**(904.7)**	**2.7**	**(65.2)**	**(864.4)**	**(4.4)**	**(56.8)**
Total Imports (CIF)	**(1005.2)**	**2.7**	**(72.5)**	**(960.5)**	**(4.4)**	**(63.1)**
Other Imports[4]	(691.6)	(0.5)	(49.9)	(600.6)	(13.2)	(39.5)
Free Zone Imports	(302.1)	10.3	(21.8)	(347.0)	14.9	(22.8)
Imports (gas)	(11.5)	13.7	(0.8)	(12.8)	11.7	(0.8)
Services (NET)	**(4.8)**	**(73.5)**	**(0.3)**	**(1.7)**	**(64.0)**	**(0.1)**
Credits	**258.9**	**7.5**	**18.7**	**263.8**	**1.9**	**17.3**
Travel	77.3	8.0	5.6	78.5	1.5	5.2
Transport	102.5	9.5	7.4	104.0	1.5	6.8
Air	101.8	9.5	7.3	103.4	1.5	6.8
Postal	0.6	5.0	0.0	0.7	2.5	0.0
Government Services	3.4	2.8	0.2	3.5	2.9	0.2
Other services	75.7	4.6	5.5	77.8	2.7	5.1
Construction	9.6	4.0	0.7	9.8	2.4	0.6
Intellectual property	13.3	4.0	1.0	13.6	2.5	0.9
Information & Computer & Telecommunication	23.7	6.0	1.7	24.7	4.2	1.6
Computer	17.4	4.0	1.3	18.0	3.9	1.2
Information & Telecommunication	6.4	11.7	0.5	6.7	5.0	0.4
Other[5]	29.1	4.0	2.1	29.6	1.8	1.9

TABLE 2.5 UAE BALANCE OF PAYMENTS ESTIMATES (CONTINUED)

	2017*	% change	% GDP	2018*	% change	% GDP
Services (NET)	**(4.8)**	**(73.5)**	**(0.3)**	**(1.7)**	**(64.0)**	**(0.1)**
Debits	**(263.7)**	**1.8**	**(19.0)**	**(265.5)**	**0.7**	**(17.5)**
Travel	(64.8)	3.0	(4.7)	(66.1)	2.0	(4.3)
Transport	(52.9)	2.0	(3.8)	(54.9)	3.7	(3.6)
Air	(52.5)	2.0	(3.8)	(54.4)	3.7	(3.6)
Postal	(0.4)	3.0	(0.0)	(0.4)	4.0	(0.0)
Government Services	(4.5)	4.7	(0.3)	(4.8)	5.6	(0.3)
Freight & Insurance [3]	(100.5)	2.7	(7.2)	(96.0)	(4.4)	(6.3)
Other services	(41.0)	(2.3)	(3.0)	(43.8)	6.9	(2.9)
Construction	(9.0)	(21.3)	(0.6)	(9.6)	6.5	(0.6)
Intellectual property	(9.5)	4.8	(0.7)	(10.2)	7.3	(0.7)
Information & Computer & Telecommunication	(11.9)	4.8	(0.9)	(12.7)	6.6	(0.8)
Computer	(2.4)	4.8	(0.2)	(2.6)	6.3	(0.2)
Information & Telecommunication	(9.5)	4.8	(0.7)	(10.2)	6.6	(0.7)
Other [5]	(10.5)	4.8	(0.8)	(11.2)	7.3	(0.7)
Investment Income (NET)	**10.2**	**32.5**	**0.7**	**7.3**	**(28.6)**	**0.5**
Banking System [6]	(7.1)	4.0	(0.5)	(6.9)	(2.5)	(0.5)
Private non-banks	(5.0)	2.5	(0.4)	(4.8)	(3.5)	(0.3)
Enterprises of Public Sector	34.5	10.2	2.5	35.3	2.2	2.3
Official Debt Services (Interest)	(5.4)	1.9	(0.4)	(6.5)	20.4	(0.4)
Foreign Hydrocarbon Companies in UAE	(6.8)	3.0	(0.5)	(9.8)	43.4	(0.6)
Transfers (NET)	**(151.3)**	**5.4**	**(10.9)**	**(166.0)**	**9.7**	**(10.9)**
Public	(22.0)	(0.9)	(1.6)	(25.3)	14.8	(1.7)
Inflows	0.0	0.0	0.0	0.0	0.0	0.0
Outflows	(22.0)	(0.9)	(1.6)	(25.3)	14.8	(1.7)
Private	(129.3)	6.5	(9.3)	(140.7)	8.8	(9.3)
Inflows	35.1	(10.9)	2.5	28.5	(18.7)	1.9
Outflows	(164.4)	2.2	(11.9)	(169.2)	2.9	(11.1)

TABLE 2.5 UAE BALANCE OF PAYMENTS ESTIMATES (CONTINUED)

	2017*	% change	% GDP	2018*	% change	% GDP
Financial Account	**(62.6)**	**(11.9)**	**(4.5)**	**(123.0)**	**96.5**	**(8.1)**
Capital Account	0.0	0.0		0.0	0.0	
Financial Account	(62.6)	(11.9)	(4.5)	(123.0)	96.5	(8.1)
a. Private capital	(59.6)	(12.4)	(4.3)	(113.0)	89.7	(7.4)
a-1 Direct Investment	(13.6)	(7.5)	(1.0)	(17.2)	26.7	(1.1)
a-1-1 Outward	(51.6)	3.2	(3.7)	(55.3)	7.3	(3.6)
a-1-2 Inward	38.0	7.6	2.7	38.1	0.3	2.5
a-2 Portfolio Investment	4.7	7.5	0.3	4.0	(15.4)	0.3
a-3 Banks	(33.2)	(16.3)	(2.4)	(80.1)	141.2	(5.3)
a-3-1 Securities	(12.3)	5.1	(0.9)	(20.2)	64.3	(1.3)
a-3-1 Other Investment (loans, deposits)	(20.9)	(25.3)	(1.5)	(59.9)	186.4	(3.9)
a-4 Private Non-Banks	(17.5)	(2.8)	(1.3)	(19.7)	12.5	(1.3)
b. Enterprises of Public Sector	(3.0)	0.0	(0.2)	(10.0)	233.3	(0.7)
Errors and Omissions	(2.0)	(43.3)	(0.1)	(3.0)	53.3	(0.2)
Overall balance	**36.4**	**(240.2)**	**2.6**	**13.0**	**(64.4)**	**0.9**
Change in Reserves at the Central Bank **	(36.4)	(240.2)	(2.6)	(13.0)	(64.4)	(0.9)
Change in Reserve Position with IMF & SDR**	0.1	(88.7)	0.0	(0.3)	(286.9)	(0.0)
Total change in International Reserves **	**(36.3)**		**(2.6)**	**(13.3)**		**(0.9)**
CBUAE						
Foreign Assets (including the IMF)	350.3	11.7	25.3	365.4	4.3	24.0
Foreign Assets of the Central Bank	347.7	11.8	25.1	362.6	4.3	23.8
Reserve Position with IMF & SDR	2.6	(5.4)	0.2	2.9	10.6	0.2
Reserve Position with IMF	2.0	(2.3)	0.1	2.1	4.9	0.1
SDR	0.6	(14.3)	0.0	0.8	29.4	0.1
Foreign Liabilities	5.1	8.3	0.4	7.0	36.9	0.5
Net Foreign Assets (including the IMF)	345.2	11.8	24.9	358.5	3.8	23.6
Net Foreign Assets at CBUAE	342.6	11.9	24.7	355.6	3.8	23.4

SOURCE: CBUAE

Footnotes to the BOP table:

1. Including Estimates of other exports from all Emirates.
2. Including re-exports of non-monetary gold and the published re-export number in CBUAE's publications for the balance of payments, estimated by CBUAE staff and reflects estimated re-export value from the UAE to other destinations at the rate of 55% of the total imports.
3. The revision in the import (FOB) and freight & insurance (debit side of the service account) was due to changes in the ratio to compute FOB values of imports based on CIF values of imports. The ratio changed from 15% to 10% based on the survey conducted by a consultancy firm, which better reflects all-UAE trade aggregation using UAE 2017 import structure.
4. Including estimates of imports from all Emirates and imports of non-monetary gold.
5. Includes estimation for financial services, research and development services, professional and management consulting services, technical, trade-related and other business services and the rest of insurance services apart from cargo.
6. Central Bank and all banks.

Notes:

- The data for services account and outward FDI have been revised following the results of surveys conducted with consultancy firms and the data for services account have been updated again due to new survey results.
- The average price of oil of 2017 was $54.25per barrel and the price in 2018 rebounded to $71 per barrel.
- The trends in the evolution of growth of the economic activity of the UAE as well as the main trading partners are used from the World Economic Outlook to estimate subcomponents where survey results are not currently available.
- Final inputs were reported from the Ministry of Foreign Affairs on public transfers and from the Central Bank on workers' remittances and international reserves.
- * Preliminary estimates subject to revision.
- ** Negative indicates an increase, positive indicates a decrease

BOX 4: TOURISM ACTIVITY IN THE UAE

This box focuses on the development in tourism activity in the Emirates of Dubai and Abu Dhabi, the two major tourist destinations in the UAE during January-December 2018. For the Dubai Emirate, the Dubai Corporation of Tourism and Commerce Marketing publishes data on international guests covering international tourists arrivals to Dubai regardless whether they stay at hotels in Dubai or not. On the other hand, Abu Dhabi Tourism and Culture Authority publishes data on international guests covering only tourists that stay at Abu Dhabi hotels (hotel guests).

Total number of international tourist arrivals to the Emirate of Dubai during the period of January-December 2018 registered increase of 130 thousands (0.8%), while the international hotel guests in the Emirate of Abu Dhabi registered increase of 168 thousands (3.4%), compared to the same period in 2017 (Figure 1).

FIGURE 1. INTERNATIONAL TOURIST ARRIVALS TO DUBAI AND INTERNATIONAL HOTEL GUESTS IN ABU DHABI 2016-2018 (IN MILLIONS)

Source: Dubai Corporation of Tourism and Commerce Marketing, Abu Dhabi Tourism & Culture Authority

Source: Dubai Corporation of Tourism and Commerce Marketing, Abu Dhabi Tourism & Culture Authority

In both Emirates, the average daily rate and the revenue per available room in 2018 continued to decline, which has contributed to attracting additional customers and improved the growth rate in occupied room nights (Figure 2a. and 2b.).

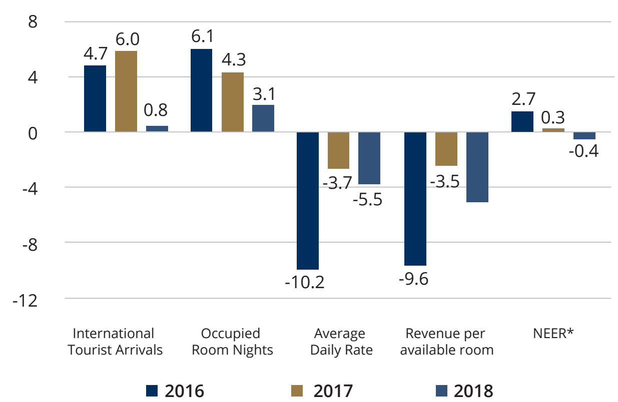
The data for the Dubai Emirate indicate that the number of international tourist arrivals moderately increased during January-December 2018 compared to the same period of 2017. However, the average daily rate and the revenue per available room substantially decreased. Despite continued discounts in the sector, occupied room nights increased at slower pace in 2018 compared to the previous years, which slightly compensated for the declining average revenue per room.

Meanwhile, international hotel guests in Abu Dhabi increased at a slower pace during January-December of 2018 compared to the same period of 2017.

Nevertheless, the reduction in the average daily rate contributed to the decrease in revenues per available room. The increase in the international hotel guests in Abu Dhabi compensated for the decline in the average revenue per room, which attests to a well performing strategy based on discounts.

FIGURE 2. ANNUAL PERCENTAGE CHANGE IN MAJOR INDICATORS OF DUBAI & ABU DHABI INBOUND TOURISM 2016-2018 (%)

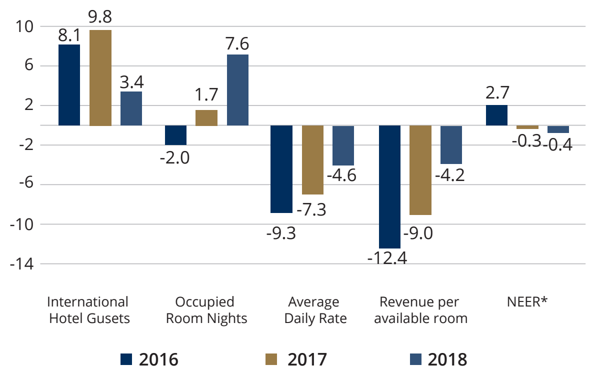
A: DUBAI



Source: Abu Dhabi Tourism & Culture Authority
* NEER is the Nominal Effective Exchange Rate (Source: Bank of International Settlement)

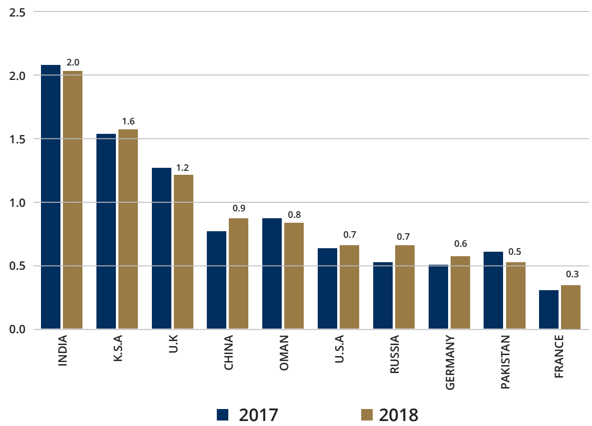
BOX 4: TOURISM ACTIVITY IN THE UAE

B: ABU DHABI



Source: Abu Dhabi Tourism & Culture Authority
* NEER is the Nominal Effective Exchange Rate (Source: Bank of International Settlement)

A: DUBAI



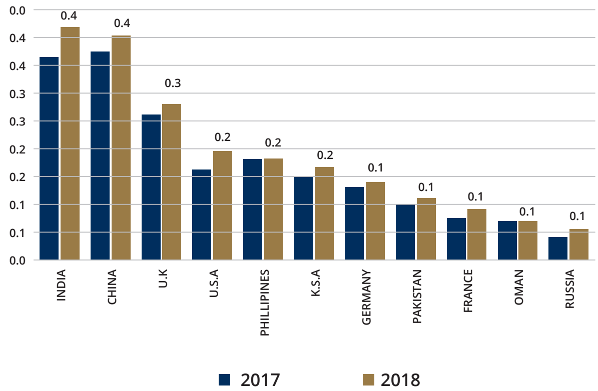
Source: Dubai Corporation of Tourism and Commerce Marketing

Countries that are the major markets for inbound tourism to Dubai show increase in the arrival of international tourists with the highest increase recorded for Russia, followed by China, Germany, USA, and Saudi Arabia.

The vast majority of tourists to Dubai originate from GCC countries and the MENA region (34% combined, 23% and 11%, respectively), while Western Europe and North America cover 21% and 6% of inbound tourism. Finally, 18% of inbound tourism comes from the region of South Asia.

For the Abu Dhabi Emirate, all of the countries that are major markets of inbound tourism recorded increase in international hotel guests during 2018.

A: ABU DHABI

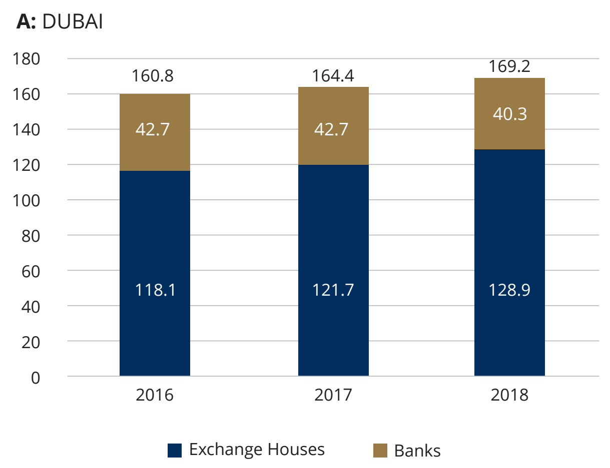


Source: Abu Dhabi Tourism & Culture Authority

BOX 5: OUTWARD PERSONAL REMITTANCES FROM THE UAE

The outward personal remittances[1] for 2018 registered AED 169.2 billion, an increase of 3% or AED 4.8 billion compared to the same period of 2017 (AED 164.4 billion) (Figure 1). During the year 2018, the outward personal remittances that were settled through the banks decreased from AED 42.7 billion in 2017 to AED 40.3 billion in 2018 (declining by 5.6% or AED 2.4 billion). Meanwhile, the outward personal remittances that were settled through the exchange houses registered AED 128.9 billion (an increase by 6% or AED 7.3 billion compared to 2017).

FIGURE 1. EVOLUTION OF OUTWARD PERSONAL REMITTANCES SETTLED THROUGH BANKS AND EXCHANGE HOUSES, 2016-2018 (AED BILLIONS)

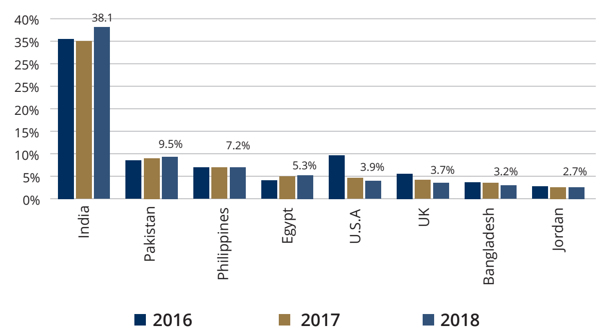


Source: CBUAE

The most important destination country for outward personal remittances during the year 2018 was India, accounting for 38.1% of the total outflows (Figure 2). This high share is in accordance with the significant share of expats from India working in the UAE and the depreciation of the Indian Rupee against the Dirham. According to the latest (2018) UAE population statistics published by the Global Media Insight, 59.5% of the expat population in the UAE originate from South Asian countries, and expats from India account for 27.5% of the total expat population in the UAE. The next five most important countries in the share of outflows of personal remittances were Pakistan (9.5%), Philippines (7.2%), Egypt (5.3%), and the United States of America (3.9%) (Figure 2).

1. The data capture the outward personal remittances reported from the exchange houses and the banks to the CBUAE, which capture expats remittances as well as personal transfers by UAE nationals.

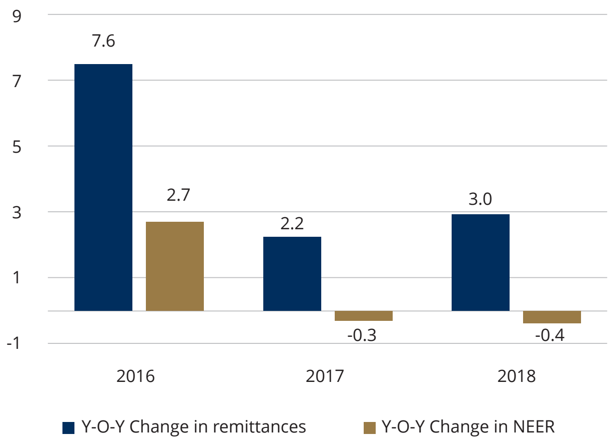
FIGURE 2. SHARE OF THE MAJOR COUNTRIES FOR OUTWARD PERSONAL REMITTANCES DURING 2016-2018 (PERCENTAGE OF TOTAL, EXCHANGE HOUSES AND BANKS)



Source: CBUAE, Bank of International Settlements

The annual growth rate of outward personal remittances during the year of 2018 is 3% (Figure 3) slightly higher compared to the growth for the year 2017 (2.2%). Even though the dirham only slightly depreciated in 2018 (0.4%) and 2017 (0.3%), there has been slowdown in outward personal remittances in 2017 and 2018 compared to 2016, in line with employment slowdown.

FIGURE 3. ANNUAL PERCENTAGE CHANGE OF TOTAL OUTWARD PERSONAL REMITTANCES VERSUS THE PERCENTAGE CHANGE OF NOMINAL EFFECTIVE EXCHANGE RATE, 2016-2018



Source: CBUAE

CHAPTER 3. BANKING AND FINANCIAL DEVELOPMENTS

Government deposits increased in 2018 with the recovery of oil prices and continued fiscal reforms. Credit growth picked up, in support of growth in the non-energy sectors of the economy. Overall, the banking sector in the UAE remains well capitalised, highly liquid, sound and stable, solidifying foundations for financial stability in the country.

BANKING LANDSCAPE

The number of locally-incorporated licensed banks is unchanged at 22 in 2018. The number of foreign banks declined to 38 in 2018.[1] The number of bank employees has increased for national banks from 29,056 in 2017 to 30,966 employees at the end of 2018. For the foreign banks, it declined from 7,311 in 2017 to 5,633 employees at the end of 2018, mainly due to consolidation in banking activity and increased efficiency, (See Table 3.1).

TABLE 3.1 BANKS IN THE UAE AND THEIR LOCAL BRANCHES

Type		Dec-15	Dec-16	Dec-17	Dec-18
National	# Banks	23	23	22	22
	# Branches	874	846	771	743
	# Employees	32,352	29,532	29,056	30,966
Foreign	# Banks	34	37	39	38
	# Branches	86	85	82	80
	# Employees	7,807	7,439	7,311	5,663

Source: CBUAE

BANKS' DEPOSITS

Total customer deposits at banks increased in 2018, due to the rise in both, resident and non-resident deposits. The two segments registered an increase higher than that witnessed in 2017 and above the CAGR[2] (5% and 8.5%, respectively) for the last four years.

This level of growth in deposits contributes to a strong liquidity in the banking system, (Table 3.2.a and Table 3.2.b).

TABLE 3.2.A DEPOSITS AT UAE BANKS

	2016	2017	2018
	Dec	Dec	Dec
Bank Deposits	1,563	1,627	1,756
(Y-o-Y change %)	6.2	4.1	7.9
Resident Deposits	1,364	1,436	1,542
(Y-o-Y change %)	4.9	5.3	7.4
Government Sector	187	212	290
(Y-o-Y change %)	18.7	13.5	36.9
GREs[3]	168	192	207
(Y-o-Y change %)	-11.7	13.7	8.1
Private Sector	981	1,001	1,009
(Y-o-Y change %)	6.1	2.1	0.8
NBFIs[4]	28	31	36
(Y-o-Y change %)	0.4	10.3	14.1
Non-Resident Deposits	199	192	213
(Y-o-Y change %)	16.0	-3.7	11.3

Source: CBUAE

Note: All data indicate the end-of-year values in billions of AED if not indicated otherwise.

1. Of which 27 full-fledged commercial banks and 11 wholesale banks.
2. The Compound Annual Growth Rate (CAGR) is the mean annual growth rate (geometric mean) over a specified period of time longer than one year. It is a more precise measure for average growth than the arithmetic mean. In this chapter, when referring to CAGR, it would be for the period 2014-2018, if not specified otherwise.

3. Government Related Entities
4. Non-Banking Financial Institutions

TABLE 3.2.B CAGR OF DEPOSITS AT UAE BANKS

Total	Resident	Gov.	GREs	Private Sector	NBFIs	Non-Resident
5.4%	5.0%	11.4%	4.6%	3.8%	-0.6%	8.5%

Source: CBUAE

The increase in private sector deposits in 2018 was at a slower rate in comparison to 2017 and CAGR (3.8%). The non-resident deposits marked a steady growth after a decline in 2017, performing better than the CAGR (8.5%).

Looking at the split between Conventional and Islamic Banks, while Islamic banks initially reported a better growth rate in 2017, Conventional Banks' deposits growth was stronger than that of the Islamic banks' in 2018.[5] Islamic banks' deposits in 2018 grew below the CAGR (9%), while the Conventional banks' deposits reported a higher growth in 2018 than their CAGR (4.5%) (Tables 3.2.c and 3.2.d, and Figures 3.1.a, 3.1.b, 3.1.c and 3.1.d).

The private sector deposits' growth is higher for Conventional Banks in 2018 although for the past few years, it was faster in Islamic banks. Nevertheless, non-resident deposits in Islamic banks increased at a higher rate in 2018 by 76.6%. The Non-resident deposits for the Conventional Banks increased in 2018 after a decline in 2017.

TABLE 3.2.C DEPOSITS AT CONVENTIONAL/ISLAMIC BANKS

	Conventional		Islamic	
	2017	2018	2017	2018
	Dec	Dec*	Dec	Dec*
Bank Deposits	**1,244**	**1354**	**384**	**402**
(Y-o-Y change %)	2.4	8.9	10.1	4.6
Share of Total, %	76.4	77.1	23.6	22.9
Resident Deposits	**1,065**	**1163**	**371**	**379**
(Y-o-Y change %)	3.9	9.3	9.4	2.2
Share of Total, %	74.2	75.4	25.8	24.6
Government Sector	**159**	**227**	**53**	**64**
(Y-o-Y change %)	11.1	42.5	21.3	20.2
Share of Total, %	75.0	78.1	25.0	21.9
GREs	**133**	**154**	**59**	**54**
(Y-o-Y change %)	10.7	15.7	21.3	-8.7
Share of Total, %	69.4	74.1	30.6	25.9
Private Sector	**750**	**759**	**252**	**250**
(Y-o-Y change %)	1.6	1.2	3.5	-0.4
Share of Total, %	74.9	75.2	25.1	24.8
NBFIs	**23**	**24**	**8**	**11**
(Y-o-Y change %)	-2.9	3.9	85.7	44.9
Share of Total, %	74.9	68.2	25.1	31.8
Non-Resident Deposits	**179**	**191**	**13**	**23**
(Y-o-Y change %)	-5.6	6.7	36.2	76.6
Share of Total, %	93.3	89.4	6.7	10.6

Source: CBUAE

TABLE 3.2.D CAGR OF DEPOSITS AT CONVENTIONAL/ISLAMIC BANKS

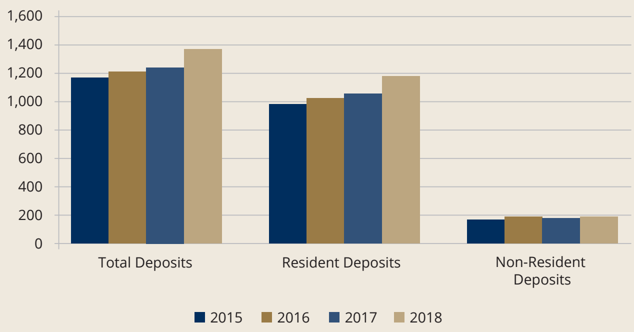
Type	Total	Resident	Gov.	GREs	Private Sector	NBFIs	Non-Resident
Conventional	4.5%	4.1%	11.0%	3.4%	2.9%	-5.2%	6.7%
Islamic	9%	8.1%	12.5%	8.6%	6.7%	14.8%	34.5%

Source: CBUAE.

Note: All data indicate the end-of-quarter values in billions of AED if not indicated otherwise.

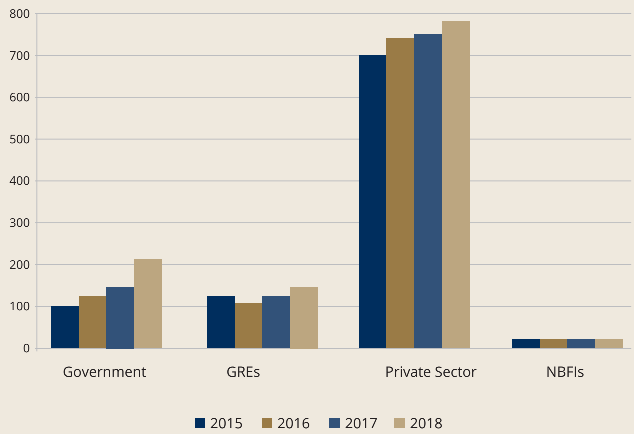
5. If Government deposits were not considered, the growth of deposits in the two types of banks would have been similar.

FIGURE 3.1.A. DEPOSITS AT CONVENTIONAL BANKS BY RESIDENT STATUS IN AED BILLIONS



Source: CBUAE

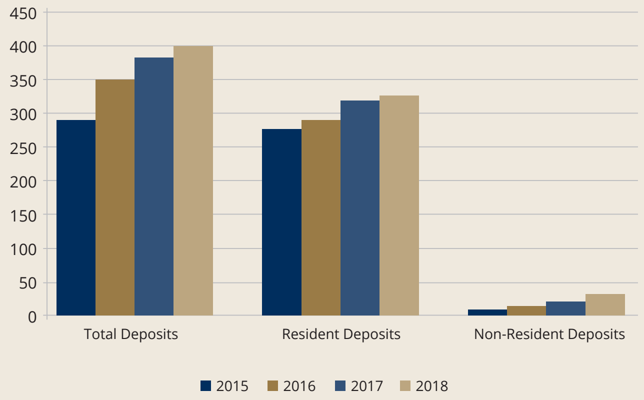
FIGURE 3.1.B. RESIDENT DEPOSITS AT CONVENTIONAL BANKS BY TYPE OF DEPOSITORS IN AED BILLIONS



Source: CBUAE

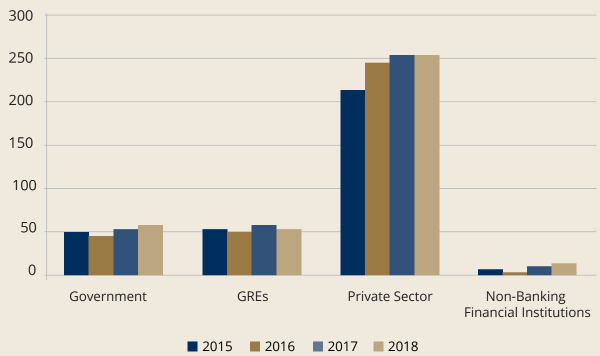
The breakdown of national and foreign banks in Figures 3.2.a, 3.2.b, 3.2.c and 3.2.d provides a clear trend that deposits in national banks grew in the last four years up to 2018, while deposits in foreign banks declined on a CAGR basis (-4.3%) . National banks' deposits grew at a higher rate on both Y-o-Y and CAGR (9.8% and 7.1%, respectively), at the end of 2018, compared to foreign banks which declined Y-o-Y and at a higher rate compared to the negative CAGR (-5.1% and -4.3%, respectively) (Tables 3.2.e and 3.2.f).

FIGURE 3.1.C. DEPOSITS AT ISLAMIC BANKS BY RESIDENT STATUS



Source: CBUAE

FIGURE 3.1.D. RESIDENT DEPOSITS AT ISLAMIC BANKS BY TYPE OF DEPOSITORS



Source: CBUAE

The sectors growing the most for the national banks in 2018 were the NBFIs, the government and GREs sectors, while in terms of CAGR non-resident deposits grew the fastest (13.5%).

For foreign banks, there was a general decline across all sectors in 2018, except for the NBFIs. The CAGRs of all sectors had also negative values.

TABLE 3.2.E DEPOSITS AT UAE NATIONAL/FOREIGN BANKS

	National		Foreign	
	2017	2018	2017	2018
	Dec	Dec	Dec	Dec
Bank Deposits	**1,420**	**1559**	**207**	**197**
(Y-o-Y change %)	5.0	9.8	-1.8	-5.1
Share of Total, %	87.3	88.8	12.7	11.2
Resident Deposits	**1,261**	**1,378**	**174**	**164**
(Y-o-Y change %)	5.9	9.3	1.1	-5.9
Share of Total, %	87.9	89.4	12.1	10.6
Government Sector	**210**	**289**	**2**	**2**
(Y-o-Y change %)	13.3	37.5	46.2	-21.1
Share of Total, %	99.1	99.5	0.9	0.5
GREs	**182**	**199**	**9**	**8**
(Y-o-Y change %)	13.3	9.3	23.0	-14.3
Share of Total, %	95.2	96.2	4.8	3.8
Private Sector	**843**	**860**	**158**	**150**
(Y-o-Y change %)	2.4	2.0	0.3	-5.4
Share of Total, %	84.2	85.2	15.8	14.8
NBFIs	**26**	**30**	**5**	**5**
(Y-o-Y change %)	16.6	16.9	-13.6	0.0
Share of Total, %	83.6	85.6	16.4	14.4
Non-Resident Deposits	**159**	**180**	**33**	**33**
(Y-o-Y change %)	-1.0	13.8	-14.7	-0.6
Share of Total, %	82.7	84.6	17.3	15.4

Source: CBUAE

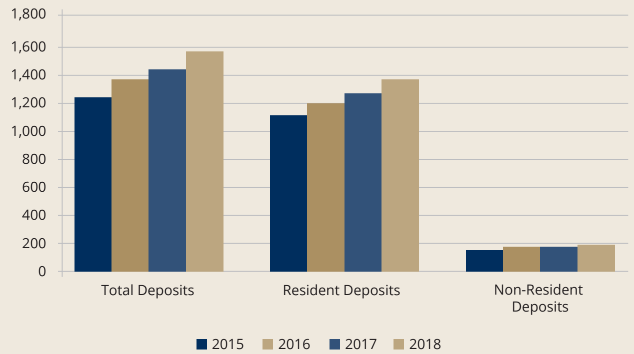
Note: All data indicate the end-of-quarter values in billions of AED if not indicated otherwise.

TABLE 3.2.F CAGR OF DEPOSITS AT NATIONAL/FOREIGN BANKS

	Deposits CAGR 2014-2018						
	Total	Resident	Gov.	GREs	Private Sector	NBFIs	Non-Resident
National	7.1%	6.3%	11.4%	5.3%	5.3%	0.2%	13.5%
Foreign	-4.3%	-3.6%	-4.5%	-8.2%	-3.2%	-5.1%	-7.7%

Source: CBUAE

FIGURE 3.2.A. DEPOSITS AT NATIONAL BANKS BY RESIDENT STATUS IN AED BILLIONS



Source: CBUAE

FIGURE 3.2.B. RESIDENT DEPOSITS AT NATIONAL BANKS BY TYPE OF DEPOSITORS IN AED BILLIONS

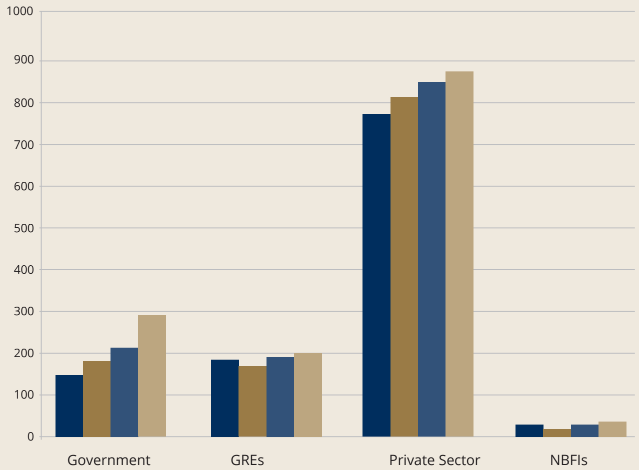
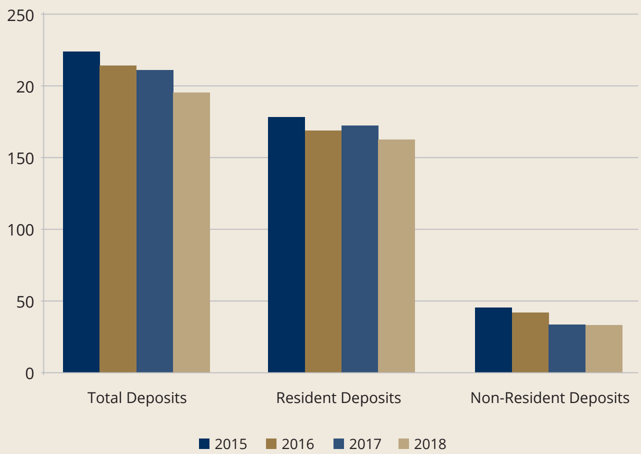
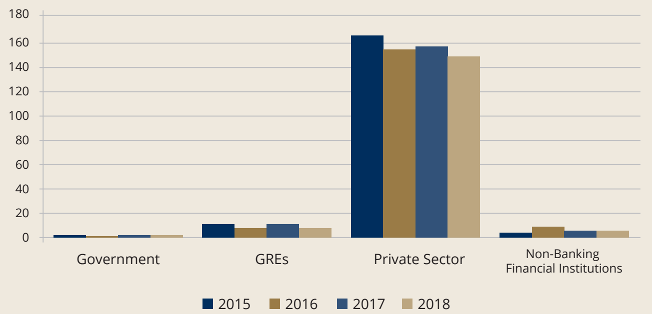


FIGURE 3.2.C. DEPOSITS AT FOREIGN BANKS BY RESIDENT STATUS



Source: CBUAE

FIGURE 3.2.D. RESIDENT DEPOSITS AT FOREIGN BANKS BY TYPE OF DEPOSITORS



Source: CBUAE

BANKS' CREDIT

Domestic credit increased in 2018 by AED 56 billion, registering a growth rate of 3.9% (CAGR 4.6%). Underlying the increase in domestic credit is credit to the government, private sector, NBFIs as well as foreign credit, both during the year and on a CAGR basis (Tables 3.3.a and 3.3.b). However, the credit to GREs is still declining over the same period. Meanwhile credit to government grew higher in 2018 than the CAGR (5.8%). Credit to non-residents also grew noticeably Y-o-Y and on a CAGR basis (10.1%) (Tables 3.3.a and 3.3.b).

TABLE 3.3.A ASSETS AND CREDIT AT UAE BANKS

	2016 Dec	2017 Dec	2018 Dec*
Total Assets	**2,593**	**2,694**	**2,869**
(Y-o-Y change %)	5.4	3.9	6.5
Gross Credit	**1,554**	**1,580**	**1,656**
(Y-o-Y change %)	6.0	1.7	4.8
Domestic Credit	**1,433**	**1,453**	**1,509**
(Y-o-Y change %)	5.2	1.4	3.9
Government	**172**	**175**	**192**
(Y-o-Y change %)	3.5	1.7	9.2
Public Sector (GREs)	**187**	**172**	**168**
(Y-o-Y change %)	9.3	-8.1	-2.7
Private Sector	**1,055**	**1,086**	**1,130**
(Y-o-Y change %)	5.5	3.0	4.0
Business & Industrial Sector Credit	**728**	**749**	**793**
(Y-o-Y change %)	5.9	2.8	5.8
Individual	**326**	**338**	**337**
(Y-o-Y change %)	4.7	3.5	0.0
NBFIs	**19**	**19**	**20**
(Y-o-Y change %)	-23.1	-2.1	7.5
Foreign Credit	**120**	**128**	**147**
(Y-o-Y change %)	15.9	6.8	15.5

Source: CBUAE

Note: All data indicate the end-of-quarter values in billions of AED if not indicated otherwise.

TABLE 3.3.B CAGR OF ASSETS AND CREDIT AT UAE BANKS

Assets	Gross Credit	Domestic Credit	Gov.	GREs	Private Sector	NBFIs	Foreign Credit
5.9%	5.0%	4.6%	5.8%	0.2%	5.2%	0.8%	10.1%

Source: CBUAE

The split between Conventional and Islamic Banks is presented in Figures 3.3.a and 3.3.b. The data in tables 3.3.c and 3.3.d indicate that the growth in Islamic banks' credit was steeper than in conventional loans in 2018 Y-o-Y. Similarly, on a CAGR basis, Islamic banks grew faster, due to the double-digit growth in the previous years. Overall lending growth in 2018 remains below CAGR (9%) for Islamic banks and above the CAGR (4%) for the conventional lenders.

The main drivers for Conventional banks' loan growth in 2018 are credit to the government, private corporates, NBFIs and non-residents sectors, as the increase Y-o-Y was higher than their CAGRs. Growth of the Shari' a compliant lenders was also mainly driven by the same sectors similar to growth in Conventional banks, except for the NBFIs sector. However, only the Y-o-Y growth in the government sector, among the three asset classes, outperformed its CAGR (10.2%).

TABLE 3.3.C ASSETS AND CREDIT AT UAE CONVENTIONAL/ISLAMIC BANKS

	Conventional		Islamic	
	2017	2018	2017	2018
	Dec	Dec*	Dec	Dec*
Total Assets	**2,144**	**2,295**	**550**	**583**
(Y-o-Y change %)	2.7	7.1	8.8	6.0
Gross Credit	**1,226**	**1,283**	**354**	**374**
(Y-o-Y change %)	0.6	4.6	5.6	5.6
Domestic Credit	**1,123**	**1,165**	**330**	**345**
(Y-o-Y change %)	0.7	3.7	3.6	4.6
Government	**164**	**177**	**12**	**14**
(Y-o-Y change %)	0.2	8.4	28.0	20.2
Public Sector (GREs)	**139**	**137**	**33**	**31**
(Y-o-Y change %)	-9.3	-1.9	-2.7	-6.1
Private Sector	**806**	**834**	**281**	**296**
(Y-o-Y change %)	2.9	3.5	3.3	5.4
Business & Industrial Sector Credit	**597**	**628**	**152**	**165**
(Y-o-Y change %)	2.8	5.2	2.9	8.5
Individual	**209**	**206**	**129**	**131**
(Y-o-Y change %)	3.4	-1.1	3.7	1.8
NBFIs	**15**	**17**	**4**	**3**
(Y-o-Y change %)	-7.5	13.6	25.8	-15.4
Foreign Credit *	**103**	**118**	**24**	**29**
(Y-o-Y change %)	-0.2	14.7	43.5	18.9

Source: CBUAE

Note: All data indicate the end-of-quarter values in billions of AED if not indicated otherwise.

* Foreign Credit does not include lending by foreign subsidiaries.

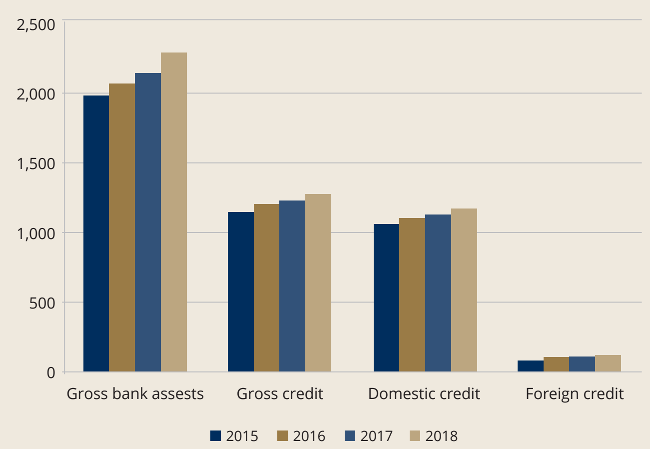
TABLE 3.3.D CAGR OF ASSETS AND CREDIT AT UAE

	Assets	Gross Credit	Domestic Credit	Gov.	GREs	Private Sector	NBFIs	Foreign Credit
Conventional	5.1%	4.0%	3.7%	5.4%	-0.8%	4.1%	6.7%	7.4%
Islamic	9.6%	9.0%	8.0%	10.2%	5.1%	8.8%	-15.6%	26%

Source: CBUAE

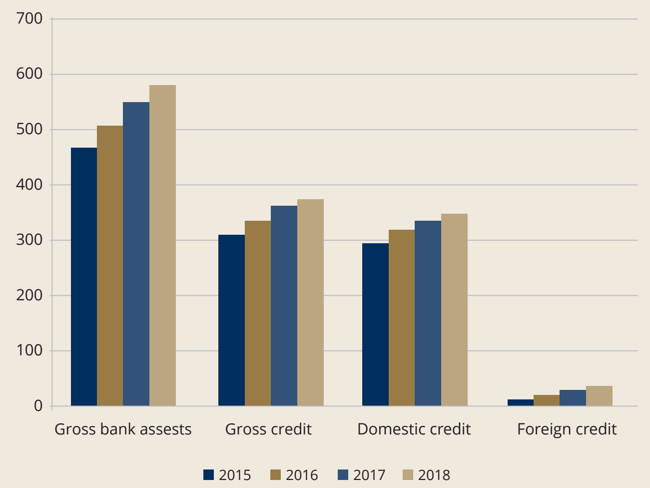
CONVENTIONAL/ISLAMIC BANKS

FIGURE 3.3.A. ASSETS AND CREDIT AT CONVENTIONAL BANKS



SOURCE: CBUAE

FIGURE 3.3.B.



Source: CBUAE

The breakdown of the assets and credit by national and foreign banks in Figures 3.4.a and 3.4.b, and Tables 3.3.e and 3.3.f shows that national banks were growing, Y-o-Y and by CAGR (CAGR of 7.6% for the assets and CAGR of 6.4% for the gross credit), with the assets' growth exceeding the average growth over the last four years. For the foreign banks, the levels of growth were declining for the assets, on a Y-o-Y and on CAGR basis (-1.7% and -3.8%, respectively). In terms of gross lending, however, the CAGR was negative (-3.1%), while it increased in 2018 Y-o-Y after a decline in 2017.

TABLE 3.3.E ASSETS AND CREDIT AT UAE NATIONAL/FOREIGN BANKS

	National		Foreign	
	2017	2018	2017	2018
	Dec	Dec	Dec	Dec
Total Assets	**2,333**	**2,514**	**360**	**354**
(Y-o-Y change %)	5.2	7.8	-4.0	-1.7
Gross Credit	1,391	1,466	189	190
(Y-o-Y change %)	**2.5**	**5.4**	**-3.7**	**0.7**
Domestic Credit	1,290	1,351	163	158
(Y-o-Y change %)	2.3	4.7	-5.8	-2.9
Government	**170**	**185**	**5**	**7**
(Y-o-Y change %)	2.2	8.6	-11.7	26.4
Public Sector (GREs)	**153**	**152**	**20**	**16**
(Y-o-Y change %)	-4.4	-0.3	-28.8	-21.2
Private Sector	**949**	**995**	**137**	**136**
(Y-o-Y change %)	3.5	4.8	-0.1	-1.4
Business & Industrial Sector Credit	**644**	**688**	**105**	**105**
(Y-o-Y change %)	3.2	6.8	0.3	-0.1
Individual	**305**	**307**	**33**	**31**
(Y-o-Y change %)	4.0	0.6	-1.2	-5.5
NBFIs	**18**	**19**	**1**	**1**
(Y-o-Y change %)	5.3	7.8	-68.4	0.0
Foreign Credit	**102**	**115**	**26**	**32**
(Y-o-Y change %)	4.4	13.5	12.6	23.6

Source: CBUAE

Note: All data indicate the end-of-quarter values in billions of AED if not indicated otherwise.

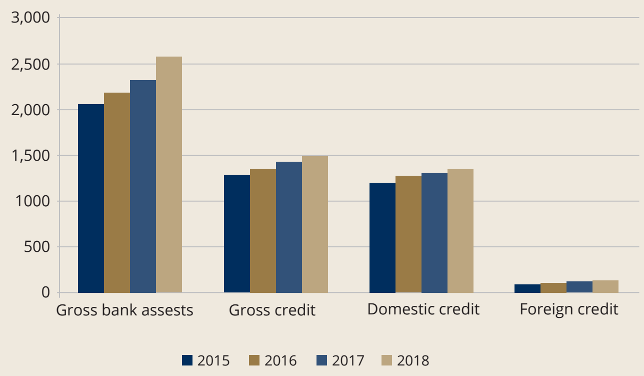
TABLE 3.3.F CAGR OF ASSETS AND CREDIT AT UAE NATIONAL/FOREIGN BANKS

	Assets and Loans 2014-2018							
	Assets	**Gross Credit**	**Domestic**	**Gov.**	**GREs**	**Private Sector**	**NBFIs**	**Foreign Credit**
National	7.6%	6.4%	6.0%	6.1%	3.6%	6.4%	2.0%	11.4%
Foreign	-3.8%	-3.1%	-4.5%	-2.5%	-18%	-2%	-20.5%	5.8%

Source: CBUAE

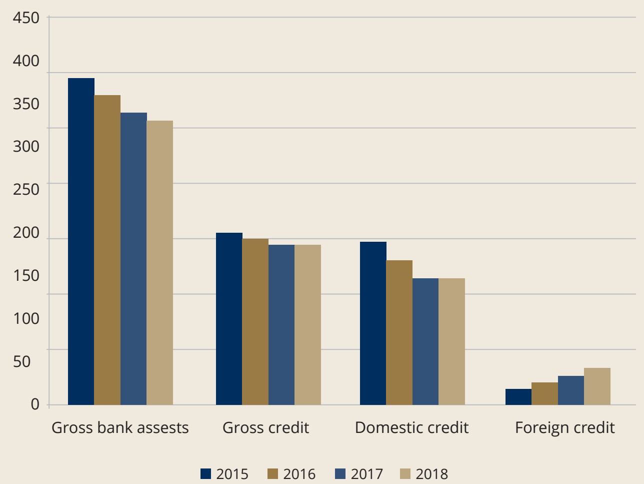
The share of national banks' credit has been also growing in 2018 compared to 2017 and the main drivers of growth for the national banks in 2018 were all the sectors except for GREs, which marked a slight decrease. While the highest growth rate observed for the foreign banks is marked by government and foreign credit.

FIGURE 3.4.A. ASSETS AND CREDIT EXTENDED BY NATIONAL BANKS



Source: CBUAE

FIGURE 3.4.B. ASSETS AND CREDIT EXTENDED BY FOREIGN BANKS



Source: CBUAE

Banks' lending by economic activity (Tables 3.3.g and 3.3.h) shows an increase in 2018 Y-o-Y in mining and quarrying, manufacturing, electricity, gas and water, construction and real estate, trade, financial institutions (excluding banks). On the other hand, agriculture, transport, storage and communication show a decline in their exposure in 2018.

On a CAGR basis, construction and real estate as well as mining and quarrying showed the fastest growth, while for agriculture, electricity, gas, water, transport, storage and communication credit decreased.

The sectors with higher Y-o-Y growth in 2018 than their CAGR were mining and quarrying; electricity, gas and water; and trade and financial institutions (excluding banks).

TABLE 3.3.G BANKS' CREDIT TO RESIDENTS BY ECONOMIC ACTIVITY

	2016	2017	2018
Economic Activity	**Dec**	**Dec**	**Dec**
Agriculture	**1.4**	**2.1**	**2.0**
(Y-o-Y change %)	-11.9	54.8	-6.7
Mining and Quarrying	**13.6**	**12.1**	**14.7**
(Y-o-Y change %)	13.7	-10.7	21.8
Manufacturing	**69.3**	**75.2**	**77.0**
(Y-o-Y change %)	0.3	8.6	2.3
Electricity, Gas and Water	**18.5**	**16.7**	**17.0**
(Y-o-Y change %)	-9.9	-9.3	1.6
Construction and Real Estate	**264.8**	**298.1**	**315.5**
(Y-o-Y change %)	12.7	12.6	5.8
Trade	**155.8**	**152.8**	**154.0**
(Y-o-Y change %)	-3.6	-2.0	0.8
Transport, Storage and Communication	**63.5**	**54.9**	**51.5**
(Y-o-Y change %)	7.4	-13.5	-6.3
Financial Institutions (Excluding Banks)	**145.6**	**127.5**	**130.1**
(Y-o-Y change %)	7.3	-12.4	2.0
All Others	**125.3**	**138.4**	**148.8**
(Y-o-Y change %)	11.3	10.3	7.6

Source: CBUAE

Note: All data indicate the end-of-quarter values in billions of AED if not indicated otherwise.

TABLE 3.3.H CAGR OF BANKS' CREDIT TO RESIDENTS BY ECONOMIC ACTIVITY

Credit by Economic Activity 2014-2018	
Agriculture	-7.2%
Mining and Quarrying	12%
Manufacturing	4.3%
Electricity, Gas and Water	-2.6%
Construction and Real Estate	10.4%
Trade	-0.3%
Transport, Storage and Communication	-2.4%
Financial Institutions (Excluding Banks)	-0.3%
All Others	11.5%

Source: CBUAE

FINANCIAL SOUNDNESS INDICATORS

The overall soundness of the banking sector remained positive during 2018.

Banks operating in the UAE remain well capitalised, on aggregate with the capital adequacy ratio (CAR) 17.5%, while CAR for Tier1 capital at 16.2% and Common Equity Tier 1 (CET1) at 14.3% at the end of 2018, which is well above the regulatory requirements set by CBUAE and Basel III. Conventional banks have higher CAR compared to the Islamic ones and foreign banks' CAR is higher than that for national banks.

To capture the composite effects of changes in loans and deposits, two key ratios related to the funding of banks are considered: Loan-to-Deposit (L/D) ratio, which measures developments in lending relative to deposits, and Lending to the Stable Resources Ratio (LSRR[6]), which measures lending relative to a broader base of liabilities.

L/D ratio for the overall banking system has moved from 97.1% at the end of 2017 to 94.3% at the end of 2018. This is mainly due to the stronger growth in deposits compared to loans, with government contributing to the decline in loan to deposits ratio by lower lending growth compared to the parallel higher deposit growth, reflecting higher oil prices and fiscal reforms.

Looking at the breakdown between conventional and Islamic banks, the L/D ratio is respectively 94.7% and 93% at the end of 2018, marking a decrease from December 2017 for the Conventional banks, while slight increase for the Islamic ones. National banks had L/D ratio of 94% at the end of 2018 (down from 98% a year ago), while the ratio for foreign banks was 96.6% which increased from 91.1% in 2017.

Loan to Stable Resources Ratio (LSRR) also declined from 84.5% in December 2017 to 82.3% a year later, reflecting higher increase in stable resources compared to the slower credit growth at banks. In the segmentation, Islamic, conventional, national and foreign banks the LSRR was declining for all types of banks in 2018.

6. Net Lending + Net Financial Guarantees+ Stand-by Letters of Credit+ Interbank Placements (3 months and more)/ (Net Free Capital Funds+ interbank deposits received of more than 6 months+ Stable customer deposits, including all refinancing obtained in the UAE and abroad, all deposits of more than 6 months and 85% of all other deposits). It is also known as Funding to Stable Resources Ratio (FSRR).

Meanwhile, the Eligible Liquid Assets Ratio (ELAR[7]) moved from 18.3% at the end of 2017 to 17.5% at the end of 2018. The level of total liquid assets at banks at the end of 2018 is at AED 407.6 billion, AED 9.7 billion higher compared to the end of 2017, registering an increase of 2.4% Y-o-Y. However, the total assets rose at a much higher rate, which is one of the reasons for the ELAR to decline, however remaining significantly above the regulatory threshold of 10%.

TABLE 3.4.A FINANCIAL SOUNDNESS INDICATORS IN THE UAE (IN %, UNLESS OTHERWISE INDICATED)

Total system	December			
	2015	2016	2017	2018
Lending to Stable Resources Ratio	87.1	86.2	84.5	82.3
The Eligible Liquid Assets Ratio (ELAR)	17.4	16.2	18.3	17.5
Capital Adequacy Ratio (CAR)	18.3	18.9	18.1	17.5
Tier 1 Capital	16.6	17.3	16.6	16.2
CET 1			14.6	14.3

Source: CBUAE.

Note: All data indicate the end-of-quarter values

TABLE 3.4.B FINANCIAL SOUNDNESS INDICATORS IN THE UAE FOR CONVENTIONAL BANKS (IN %, UNLESS OTHERWISE INDICATED)

Conventional	December			
	2015	2016	2017	2018
Lending to Stable Resources Ratio	87.4	86.1	84.9	82.5
The Eligible Liquid Assets Ratio (ELAR)	17.5	16.0	17.7	16.6
Capital Adequacy Ratio (CAR)	18.9	19.3	18.5	17.6
Tier 1 Capital	16.9	17.4	16.9	16.2
CET 1			15.4	14.7

Source: CBUAE.

Note: All data indicate the end-of-quarter values

7. The ratio of liquid assets, which include reserve requirements, mandated by the Central Bank, certificates of deposits held by banks at the Central Bank, excess reserves at the Central Bank, in addition to zero-risk weighted government bonds and public sector debt and cash at banks, as a share of the total assets.

TABLE 3.4.C FINANCIAL SOUNDNESS INDICATORS IN THE UAE FOR ISLAMIC BANKS (IN %, UNLESS OTHERWISE INDICATED)

Islamic	December			
	2015	2016	2017	2018
Lending to Stable Resources Ratio	86.1	86.7	83.1	81.6
The Eligible Liquid Assets Ratio (ELAR)	17.0	16.8	20.0	19.6
Capital Adequacy Ratio (CAR)	15.6	17.1	16.4	17.3
Tier 1 Capital	14.9	16.5	15.3	16.2
CET 1			11.4	12.7

Source: CBUAE.

Note: All data indicate the end-of-quarter values.

TABLE 3.4.D FINANCIAL SOUNDNESS INDICATORS IN THE UAE FOR NATIONAL BANKS (IN %, UNLESS OTHERWISE INDICATED)

National	December			
	2015	2016	2017	2018
Lending to Stable Resources Ratio	88.6	88.1	86.1	83.4
The Eligible Liquid Assets Ratio (ELAR)	16.5	14.9	17.1	16.6
Capital Adequacy Ratio (CAR)	18.0	18.5	17.7	17.2
Tier 1 Capital	16.5	17.1	16.3	16.0
CET 1			14.0	13.7

Source: CBUAE.

Note: All data indicate the end-of-quarter values.

TABLE 3.4.E FINANCIAL SOUNDNESS INDICATORS (FSIS) IN THE UAE FOR FOREIGN BANKS (IN %, UNLESS OTHERWISE INDICATED)

Foreign	December			
	2015	2016	2017	2018
Lending to Stable Resources Ratio	78.6	74.8	74.6	74.0
The Eligible Liquid Assets Ratio (ELAR)	22.2	24.3	26.3	24.4
Capital Adequacy Ratio (CAR)	20.2	21.4	21.3	20.3
Tier 1 Capital	17.1	18.6	18.9	18.4
CET 1			18.9	18.4

Source: CBUAE.

Note: All data indicate the end-of-quarter values.

FINANCIAL DEVELOPMENTS

SHARE PRICE MOVEMENT

In general, mixed trends were observed in the UAE financial markets during 2018 as evident by the increase of the share price index on the Abu Dhabi Bourse and the drop of the index in the Dubai securities markets. Market Capitalization on the Dubai Financial Market (DFM) and Abu Dhabi Securities Exchange (ADX) followed the same trend, similar to the change in their share price indices (see Table 3.5.a.).

On ADX, the average Share Price Index and Market Capitalisation rose in 2018, mainly driven by higher oil prices, the fiscal reforms and stimulus packages put forward by the Abu Dhabi Government.

In Dubai, the average Share Price Index and Market Capitalisation declined in 2018, mainly due to the real estate sub index on DFM.

TABLE 3.5.A UAE – SECURITIES MARKETS

			2015	2016	2017	2018
Abu Dhabi	**Change of Share Price Index Y-o-Y (%)**	**Period Average**	-7.6	-2.7	1	6.9
		End of Period	-4.9	5.6	-3.3	11.7
	Market Capitalization	**Period Average AED Billion**	422.2	429.9	432.4	483.3
		End of Period AED Billion	411	444.2	457.3	505.4
	Change of Market Capitalization Y-o-Y (%)	**Period Average**	-7.9	4.6	3.7	9.5
		End of Period	-1.6	15.1	2	7
	Turnover (Traded Value)	**AED Billion**	60.3	48.9	48.1	39.6
		Y-o-Y (%)	-58.6	-18.7	-1.8	-17.7
Dubai	**Change of Share Price Index Y-o-Y (%)**	**Period Average**	-17.6	-9.3	4.3	-16.5
		End of Period	-16.5	12.1	-4.6	-24.9
	Market Capitalization	**Period Average AED Billion**	340.9	319.6	376.6	375.5
		End of Period AED Billion	300.7	337.7	394	343.3
	Change of Market Capitalization Y-o-Y (%)	**Period Average**	2.8	-5.4	15.3	-0.3
		End of Period	-4.5	9.6	16.7	-12.9
	Turnover (Traded Value)	**End of Period AED Billion**	151.4	133.2	114.7	59.2
		Y-o-Y (%)	-60.3	-12	-13.9	-48.4

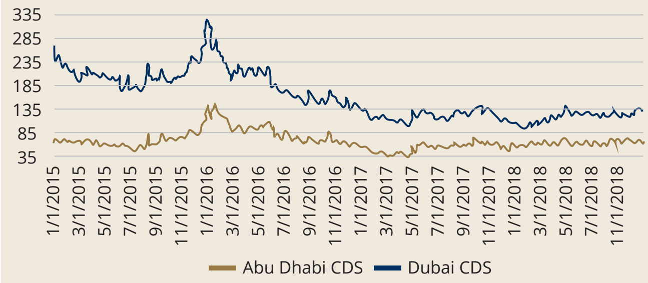
Source: Securities and Commodities Authority (SCA)

CREDIT DEFAULT SWAPS PREMIUMS

In 2018, on average, the default risk premium for the Emirate of Abu Dhabi slightly increased, while in the Emirate of Dubai it continued dropping (see Table 3.5.b). Both are low in historical terms.

TABLE 3.5.B UAE - CREDIT DEFAULT SWAPS (CDS)

	Year Average			
	2015	2016	2017	2018
Abu Dhabi	67.0	88.5	53.8	62.6
Dubai	205.8	193.8	123.7	118.2



Source: CBUAE

Source: Bloomberg.

Note: All data are at the observed end-of-period values. Premiums are expressed in basis points..

This is a reflection of the investors continued confidence based on, but not limited to, strong economic fundamentals, successful fiscal reforms and improved oil prices.

CHAPTER 4.
MONETARY DEVELOPMENTS AND THE CBUAE'S FINANCIAL POSITION

The CBUAE balance sheet exhibited an increase in 2018, reflecting an increase in foreign exchange inflows, which led to an increase in liquidity in the banking system, including commercial banks' holdings at the CBUAE. The increase in total assets at CBUAE was mainly allocated into Cash and Bank Balances and Deposits at banks abroad, while on the liabilities side the increase was evident in the Current Account and Required Reserves as well as in Certificates of Deposit (CDs). Meanwhile, interest rates in the UAE continued their upward trend in line with the Fed's decisions to increase the target Federal Funds policy rate. The spread of the EIBOR vs. the USD LIBOR remained positive during most of the year, while the spread of the swap rate of the Dirham relative to the US dollar has been mostly increasing during the year.

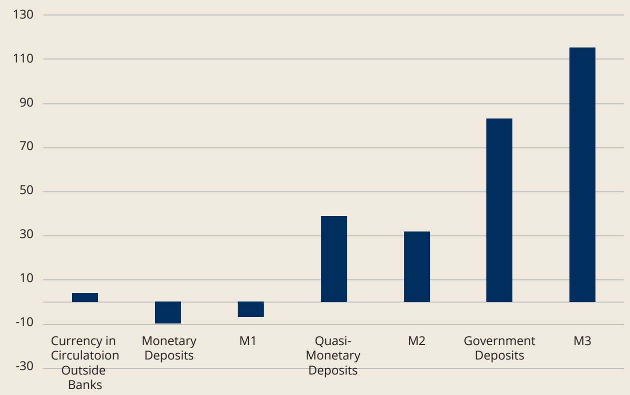
MONETARY AGGREGATES

In 2018, M1 decreased by 1.4% to reach AED 485.6 billion, due mainly to a decrease in Monetary Deposits by 2.3% to reach 415.1 billion.

Meanwhile, Money Supply M2 increased by 2.5% to reach AED 1,308.4 billion due to 5% increase in Quasi- Monetary Deposits, which reached AED 822.8 billion.

Money Supply M3 increased by 7.7% to reach AED 1,602.3 billion, owing to an increase in government deposits by 39.3% to reach AED 293.9 billion. The latter signals a reversal of the previous downward trend, and it was instrumental in supporting bank liquidity (see boxes 9 and 10).

FIGURE 4. 1 CHANGE IN MONETARY AGGREGATES IN 2018
IN BILLIONS OF DIRHAMS



Source: CBUAE

CBUAE BALANCE SHEET

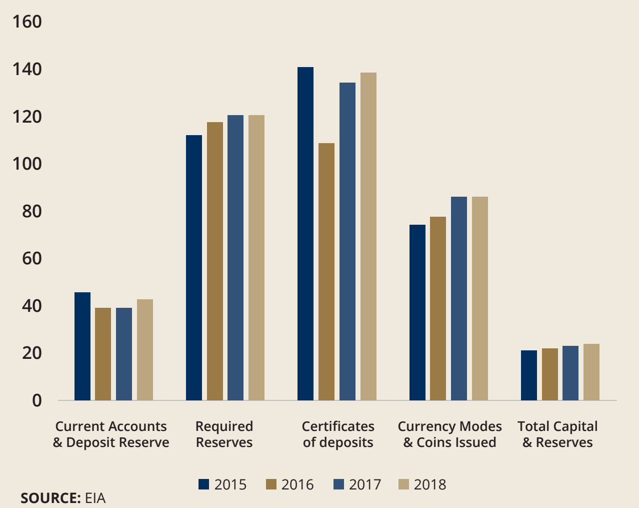
The year 2018 witnessed growing inflows of foreign exchange partly reflecting inflows in the financial account, as well as a rise in the current account surplus, which reached AED 139 billion owing to an increase in both the hydrocarbon and non-hydrocarbon exports (see Chapter 2).

The inflow of foreign exchange to the economy led to an increase in banks' foreign receipts, among which is borrowing in US dollars, including Money at Call and Short – Notice, Nostro Balances, Bills and Lending under Repurchase Agreement, and Term Placements and Loans, increasing by AED 6 billion. Capital Market Funding, which is medium term funding overseas increased by AED 4.2 billion.

Against this backdrop, the balance sheet of the CBUAE has expanded in 2018 by 3% (AED 11.3 billion) to reach AED 417.7 billion. Assets were mainly allocated as follows: AED 200.9 billion Cash and Bank Balances, AED 106.8 billion Deposits and other Advances Abroad, and AED 104.2 billion investments in government and debt securities. Cash and bank balances show a marked increase by AED 46.7 billion, driven mainly by foreign securities investments having matured and being reinvested.

On the liabilities' side, current accounts and certificates of deposits showed an increase of AED 3.6 billion and AED 3.1 billion, respectively. The latter reached AED 138.2 billion indicating sufficient liquidity in the banking system in the face of limited lending opportunities. Meanwhile, required reserves remained unchanged.

FIGURE 4.2. CBUAE LIABILITIES
IN BILLIONS OF DIRHAMS



SOURCE: EIA

TABLE 4.1 CBUAE BALANCE SHEET

In Billions of Dirhams

	2015	2016	2017	2018
Total Assets	393.7	364.5	406.4	417.7
Of which:				
Cash and Bank Balances	78.6	90.1	154.2	200.9
Deposits	96.4	61.7	111.3	106.8
Foreign Securities	164.5	149.3	84.5	55.2
Securities-Dubai Government/MoF	49.2	49.2	49.2	49
Gold Bullion	0.9	1	1.2	1.1
Total Liabilities	393.7	364.5	406.4	417.7
Of which:				
Required Reserves	111.9	116.9	121.2	120.6
Current Accounts & Deposits Reserve	45.1	37.8	38.6	42.2
CDs	139.8	108.2	135.1	138.2
Currency Notes & Coins issued	73.5	77.6	85.4	85.8
Total Capital & Reserves	20.2	21	22.1	23.3

Source: CBUAE

CBUAE FOREIGN ASSETS

The balance of foreign assets held at the CBUAE increased from AED 347.7 billion at end of 2017 to AED 362.6 billion at end of 2018 (see Table 4.2).

The credibility of the fixed peg arrangement requires the CBUAE to hold sufficient foreign currency reserves. To this end, Article 63 of Decretal Federal Law No. 14 of 2018 regarding the CBUAE and Organization of Financial Institutions and Activities, states that the market value of the balance of foreign reserves “shall not, at any time, be less than seventy percent (70%) of the value of the monetary base.” Article 62 of the said Law defines Reserves of Foreign Assets as follows:

1. Gold bullion and other precious metals.
2. Cash, deposits and other monetary and payment instruments denominated in foreign currencies, freely convertible in global markets.
3. Securities denominated in foreign currencies and issued or guaranteed by foreign governments and their related companies, entities, institutions, and agencies, by international monetary and financial institutions, or by multinational corporations, and are tradable in global markets.

TABLE 4.2 CBUAE’S FOREIGN ASSETS

In Billions of Dirhams

	2015	2016	2017	2018
Total Foreign Assets	341.2	311.0	347.7	362.6
Of which:				
Foreign Securities	164.7	149.5	84.6	55.3
Current Account Balances & Deposit with banks Abroad	171.8	147.9	256.6	294.1
- Current & Call Accounts	75.4	86.2	145.3	187.2
- Deposits	96.4	61.2	98.8	93.3
- Tri-Party Deposits	--	0.6	12.5	13.6

Source: CBUAE

Table 4.3 reports the international reserve position at the CBUAE, which increased from AED 350.3 billion at end of 2017 to AED 365.4 billion at the end of 2018. As a ratio of the monetary base, the International Reserve Position increased from 92.8% to 96.2%, i.e., well above the minimum cover ratio.

TABLE 4.3 INTERNATIONAL RESERVE POSITION

In Billions of Dirhams

	2015	2016	2017	2018
1. International Reserve Position	345.2	313.6	350.3	365.4
Of which:				
Current Account Balances & Deposits with Banks Abroad	171.79	147.85	256.6	294.1
Foreign Securities	164.5	149.34	84.5	55.2
IMF Reserves Postion+SDR Holdings	4.05	2.7	2.6	2.9
2.Monetary Base	365.2	338.1	377.4	379.7
Of which:				
- Currency Issued	73.5	77.6	85.4	85.8
- Reserve Requirements	111.9	116.9	121.4	120.6
- Banks & OFCs Current Account at CBUAE	40	35.4	35.5	35.1
- Ratio (1/2)	94.52%	92.75%	92.80%	96.20%

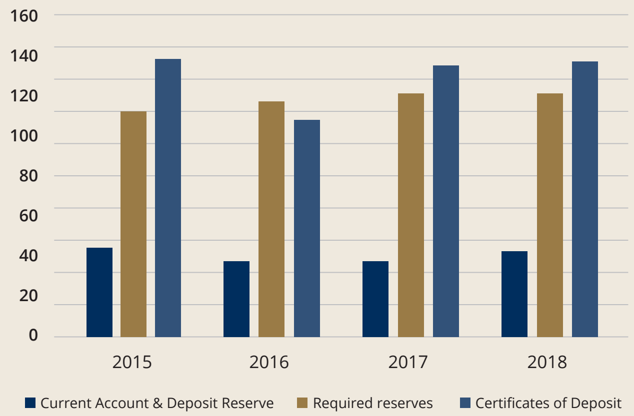
Source: CBUAE, end of year data

*Gross International Reserves including IMF Reserve Position and SDR Holdings

DEVELOPMENTS IN BANKS’ LIQUIDITY AT THE CBUAE

Banks’ liquid assets at the CBUAE are composed mainly of reserve requirements, current accounts, and CDs, which increased from AED 294.9 billion at the end of 2017 to AED 301 billion at the end of 2018 (see Table 4.1).

FIGURE 4.2. CBUAE LIABILITIES
IN BILLIONS OF DIRHAMS



SOURCE: CBUAE

INTEREST RATES

The fixed peg of the exchange rate of the Dirham to the US dollar means that the CBUAE has to adjust its policy rate to changes in the interest rate policy in the U.S. Therefore, the CBUAE announced an increase in interest rates applied to its CDs, in line with the Fed's decision to increase its target Federal Funds rate, which took place four times in 2018, in the months of March, June, September and December, reaching 2.25–2.50% range. Similarly, the Repo Rate, applicable to banks' borrowing of short-term liquidity from the CBUAE against their holding of CDs, has increased in line with the Fed hikes.

SHORT-TERM INTEREST RATES

The Emirates Interbank Offer Rate (EIBOR) is the daily reference rate at which the panel banks are able and willing to access Dirham funding, in reasonable market size for a given tenor from the UAE money market just prior to 11:00 hours local time. New "Regulations on Interbank Rate Submissions by EIBOR Panel Banks" were issued on 25 March 2018, in line with the recommendations of the International Organization of the Securities Commissions (IOSCO), with the aim to enhance governance, standardization and transparency in the rate-setting process at Panel Banks.

The main requirements of the new regulations are: (i) EIBOR Panel Banks are to rely, as much as possible, on the use of available transaction data from the day before. In the absence of actual data on transactions within the interbank Dirham market, panel banks are to follow a waterfall strategy based on the following guiding principles for rate validation: (A) Unsecured interbank transactions amounting to AED 20 million or greater; (B) Unsecured Wholesale Deposits from GREs, Corporate and NBFI, amounting to AED 20 million or greater; (C) Panel Bank's Internally developed expert judgment; and (ii) Panel Banks are required to appoint an independent auditor from a panel of audit firms nominated by the CBUAE.

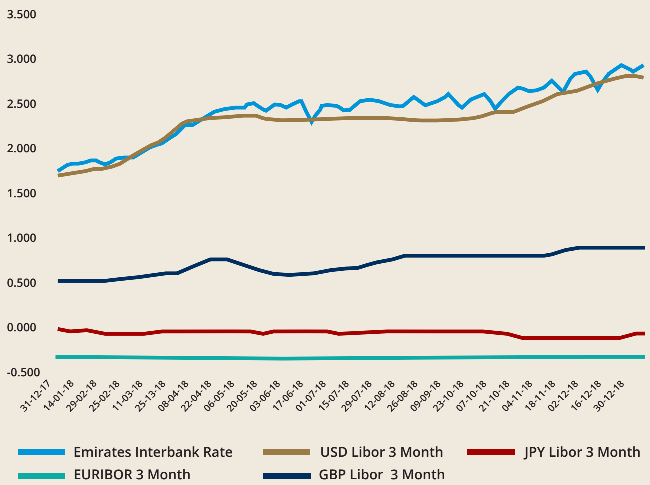
In tandem with the increase in the Fed's policy rate by 100 basis points during 2018, the 3-month EIBOR increased from 1.77% in January to 2.93% at the end of the year, tracking the increase in the LIBOR on the US dollar, which increased from 2.34% to 2.80% (Figure 4.4.a). The latter continued to rise in expectation of: (1) the Fed's decisions to increase its policy rate, (2) higher US government borrowing, and (3) the reduction in the Fed's Balance Sheet, targeted at $50 billion a month.

By mid-December however, Libor on USD started to decrease, reflecting the market perception that the Fed may not increase its policy rate as previously expected.

The 3-month LIBOR on the British Pound increased by about 38 basis points in 2018 reflecting the bank of England's decision to increase its policy rate despite Brexit uncertainties (see chapter 1).

The Libor rates for the Euro and Japanese Yen remained in negative territory, however, in line with the directions of monetary policy undertaken by the respective central banks.

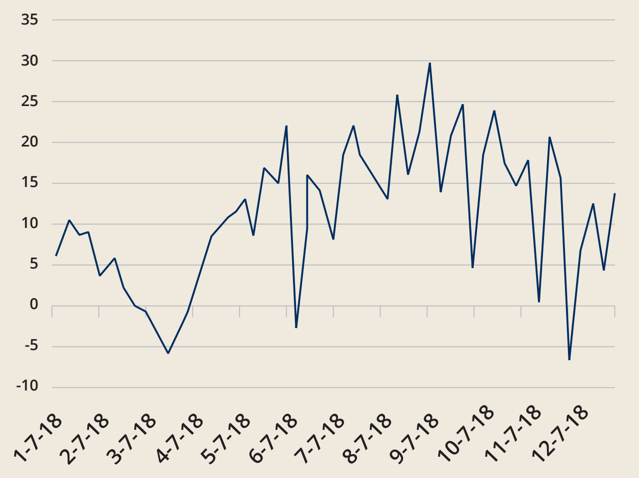
FIGURE 4.4.A. LIBOR RATES (3-MONTH)
FOR THE DIRHAM AND KEY OTHER CURRENCIES (%)



Source: CBUAE

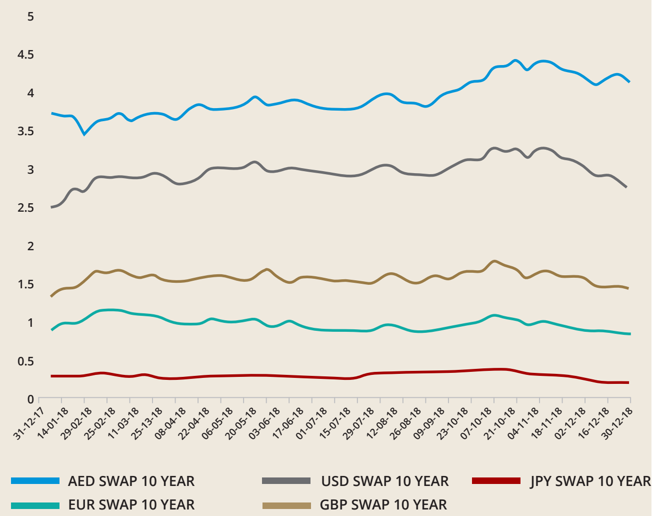
The spread between 3–month Eibor vs the USD LIBOR of similar maturity is positive in general, i.e., EIBOR is higher than LIBOR (Figure 4.4.b). Nonetheless, in 2018, EIBOR was below LIBOR on USD in the 3rd week of February to the end of March. The Spread returned positive for the rest of the year, increasing to a peak of 30 basis points in early September. Subsequently, the spread eased to about 14 basis points by the end of the year, owing to higher liquidity within banks operating in the UAE during the recent period. The average spread in 2018 was 11.2 basis points compared to 25.0 basis points in 2017.

FIGURE 4.4.B. DIRHAM SPREAD WITH USD LIBOR (3 MONTH, bps)



Source: CBUAE

FIGURE 4.5.A. 10-YEAR SWAP RATES (%)



SOURCE: CBUAE

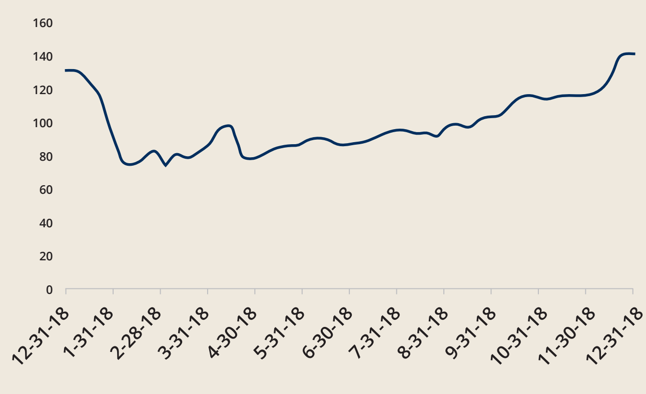
LONG-TERM SWAP RATES

By definition, interest rate swaps correspond to an exchange of a fixed rate for a floating payment that is linked to an interest rate, most often the London Interbank Offer Rate (LIBOR).

As shown in Figure 4.5.a, the 10-year swap rate on the Dirham has been mostly on a rising trend in 2018, from 3.7% in early January to a peak of 4.39% by mid-November, before decreasing to 4.15% by the end of the year.

As regards the Spread of the 10-year Dirham swap rate vs. USD (Figure 4.5.b), it was positive during 2018, albeit showing fluctuations. At the beginning of the year, the spread was at 130 basis points, decreasing to a trough in February before increasing to reach 140 basis points at the end of the year.

FIGURE 4.5.B. SPREAD 10-YEAR SWAP DIRHAM/USD (bps)



Source: CBUAE

BOX 6: FISCAL AND MONETARY POLICY COORDINATION IN THE UAE

The coordination between fiscal and monetary authorities aims at supporting sustainable and balanced growth. Such coordination is especially important in the UAE where the fixed peg of the Dirham to the US dollar means that policy interest rates set by CBUAE are pegged as well. The direction of the US monetary policy may not be compatible with the requirements of the domestic economic cycle. More recently, increasing interest rates in the US has not been compatible with the slowdown in non-oil activities. Hence, fiscal and monetary policies should capitalize on available tools to mitigate the adverse impacts of oil volatility and spillovers from the global economy on non-energy growth.

The CBUAE in coordination with the Ministry of Finance and the local finance departments have agreed on an initiative to foster strong fiscal and monetary policy coordination. The objective is to ensure that both the fiscal and monetary authorities' actions are consistent with further diversification of the economy to attain the target for non-oil GDP growth in a sustainable manner, as per UAE Vision 2021. Therefore, sources of potential risks need to be identified and contingency plans should be prepared and activated as needed in a well - coordinated manner between the concerned stakeholders in order to counter unforeseen disturbances and foster confidence in policy commitments to safeguard the course of sustainable non-energy growth and further diversification of the economy.

SOURCES OF POTENTIAL RISKS FOR THE UAE

Despite the successful diversification drive over the last four decades, the UAE economy remains to some extent oil-dependent as oil revenues remain the main source of financing the budget and determining the fiscal stance. Moreover, the openness to trade and free movement of capital across borders makes the economy vulnerable to several external shocks. The main potential risks could be summarized as follows:

1. Continued volatility of the oil price.
2. Increasing the cost of funding and lending by banks due to policy normalization in the US and liquidity tightening in international capital markets.
3. Dirham appreciation vs. currencies of non-oil export partners due to the continued appreciation of the US dollar. Such an appreciation reduces the competitiveness of the export-oriented activities, thereby weakening the non-energy growth outlook.
4. Spillovers from the global economic slowdown, as growth prospects are revised downward for most regions of the world.
5. Fallback from regional instability and increased geopolitical tension.

To achieve further diversification and sustainable growth in the "After Oil" era, some structural reforms have been introduced, namely the Value Added Tax at the federal level, in January 2018, as well as a host of business enhancing laws, like the SME Law, the corporate Bankruptcy Law, the Public Debt Law and the Decretal Federal Law Regarding the Central Bank and Organization of Financial Institutions and Activities (see Box 10). Nonetheless, the vulnerability of the economy to the above-indicated potential shocks requires further initiatives, including better coordination between the fiscal and monetary authorities, which requires monitoring of the non-oil growth, spillovers from the global economy, contingency planning in case of divergence from the target, and the role of stakeholders in this regard.

To implement the initiative, stakeholders have agreed to adopt the following action plan:

1. Generate forward-looking projections over the medium term and compare observed real non-oil GDP growth with the target on a regular basis.
2. Identify policy intervention tools, design and mobilise intervention measures as needed.
3. On the fiscal side, review revenues and expenditures of the Emirates compared with levels required to achieve the non-oil growth target, along with their contingency plans, in case of deviation due to unexpected fall in revenues, to safeguard priority spending.
4. Prepare the consolidated UAE budget (of local governments as well as the federal government) and assess the consistency of the fiscal stance with the growth target.

BOX 6: FISCAL AND MONETARY POLICY COORDINATION IN THE UAE (CONTINUED)

5. Monitor cyclicality of the economy and the scope for countercyclical measures to stay on the course of non-energy growth and avert pro-cyclicality with the oil price cycle and continued spillovers from the global economy.
6. Review debt financing needs and local credit in the banking sector granted to the public and private sectors to assess that adequate funding is available to meet the financing needs of the private sector.
7. Develop medium term liquidity forecasting and identify necessary tools for liquidity management in line with the objectives for financial stability and non-energy growth.

PRO-ACTIVE MEASURES TO MITIGATE THE RISKS

In case of unexpected shocks, there is a need to identify their lasting impact on the economy and the way a coordinated approach between the stakeholders needs to be implemented. Interventions should be based on contingency plans of the local authorities, fiscal support by the federal authorities, and Central Bank's activation of the available tools to provide banks with the needed liquidity. The coordination should focus on what follows:

1. Maintain and prioritize public spending at levels consistent with the objective of non-oil GDP growth, with reference to UAE Vision 2021, as an example, and determine the role of the local as well as the federal authorities in this regard.
2. Align deficit financing and debt issuance, including issuance of federal public debt made possible with the recent issuance of the Public Debt Law, with the need for financing from the banking sector.
3. Manage deposits and credit by the public sector to prevent crowding out of the private sector and abrupt liquidity shortfalls.
4. Enhance liquidity forecasting and management capabilities at the Central Bank and at commercial banks, and avail flexible instruments to inject liquidity or absorb it to ensure the availability of lending required for the private sector in support of non-energy growth.
5. Enhance capacity to adopt macro-prudential policies to safeguard financial stability.
6. Communicate effectively to foster confidence in the capacity of the fiscal and monetary authorities to stem the risk and proactively intervene as necessary to signal continued commitments to non-energy growth objectives and further diversification of the economy.

BOX 7: DECRETAL FEDERAL LAW NO. (14) OF 2018 REGARDING THE CENTRAL BANK & ORGANIZATION OF FINANCIAL INSTITUTIONS AND ACTIVITIES

The Law was issued in September 2018, replacing Union Law No. (10) Of 1980, and taking into account financial regulation developments, both at international as well as at domestic levels. The Law aims at strengthening Central Bank independence and executive powers, thereby allowing for an effective regulation and supervision, with a focus on compliance, licensing, financial stability and prudent management of foreign reserves, in addition to ensuring well-functioning financial infrastructure systems, and consumer protection.

The main chapters of the Law could be summarized as follows:

MAIN OBJECTIVES:

These objectives are: (1) Maintaining the stability of the national currency, (2) Safeguarding the stability of the financial system, and (3) Prudent management of Foreign Reserves.

To attain these objectives, the Central Bank was tasked with the functions of: (1) Currency issuance and conduct of monetary policy, (2) Organization and licensing of financial institutions, (3) Monitoring credit conditions

BOX 7: DECRETAL FEDERAL LAW NO. (14) OF 2018 REGARDING THE CENTRAL BANK & ORGANIZATION OF FINANCIAL INSTITUTIONS AND ACTIVITIES

to achieve balanced growth, (4) Constantly maintaining a minimum Cover Ratio of foreign currency assets to safeguard the credibility of the fixed peg arrangement, and (5) regulating and maintaining the soundness of the Systematically Important Financial Infrastructure Systems.

The Central Bank and the Ministry of Finance, in coordination with local finance departments, are also requested to establish a mechanism for coordination and data sharing to ensure a consistent fiscal stance to counter unexpected external shocks in order to achieve the target for real annual non-oil GDP growth (Article (34)).

The Law also specifies the instruments in which foreign reserves shall be invested so that sufficient foreign currency assets are maintained to cover a minimum of 70% of the Monetary Base.

CENTRAL BANK'S ROLE AS ADVISOR TO THE GOVERNMENT

The Central Bank shall provide its opinion on monetary, banking and financial affairs, contribute to international monetary and financial agreements and their implementation (Article (39)), and it may be requested to sell and manage securities issued or secured by the federal or local governments (Article (38)).

ORGANIZATION OF LICENSED FINANCIAL INSTITUTIONS AND ACTIVITIES

Fines and/or other restrictive measures are provided by the Law against the violating financial institutions. Article (71) gives the Central Bank the authority of "Suspension, Withdrawal, or Revocation of License." And CBUAE's designated Staff shall have the capacity of judicial officers, i.e., the authority to verify and penalize any violation of laws and regulations.

A Committee will be established to regulate financial activities other than those mentioned in the laws of the various regulatory authorities. Similarly, the Law calls also for the establishment of the Higher Shari'ah Authority to set up the rules and standards applicable to Shari'ah-compliant businesses and Licensed Financial Activities, and their supervision and oversight (Article (79)).

The Central Bank shall, at its own discretion, decide on measures and actions for the protection of financial institutions and their depositors in order to minimise the effect that a deficiency in their financial position may have on the financial system as a whole, as per Article (116); a "Grievances and Appeals Committee" shall be established under the chairmanship of a Court of Appeal's judge to decide on grievances and appeals against any decisions undertaken by the Central Bank.

Oversight of Systematically Important Financial Infrastructure Systems

The Central Bank shall assume the oversight over the operations of these systems, including Electronic Payment Systems, Digital Currency, and Stored Value Facilities. The provisions of the Law provide precedence of implementation of these financial infrastructure systems' rules and procedures over the general insolvency and bankruptcy rules and procedures.

CONSUMER PROTECTION

The Law provides the authority for the CBUAE to strengthen consumer protection measures, more specifically the Central Bank is mandated to:

- Establish the appropriate regulations and standards for the protection of customers (Article (4)).
- Governing the confidentiality, protection and appropriate use of customer banking and credit information (Article (120)).
- Requiring financial institutions to raise public awareness of the types of banking services and financial products, and their inherent risks (Article 121 (2)).
- Preventing financial institutions from charging interest on accrued interest charged on any credit or funding facilities granted to customers (Article 121 (3)).
- Ensuring that every natural person shall have the right to access to all or part of the banking and financial services and products (Article 123).
- Defining and expanding the regulatory standards that are necessary to provide a stronger consumer protection framework, while promoting financial consumer educational and awareness among the public.

PART TWO

CENTRAL BANK ACTIVITY

CHAPTER 5.
STRATEGY AND SHAPING THE FUTURE

CBUAE 2017-2021 strategy includes key objectives that focus on CBUAE's role in enhancing financial stability in the UAE, strengthening the monetary and reserves management functions, and enhancing the regulatory and supervisory framework. The 2018 Operational Plan was revised and approved by the Board of Directors in 2017 that concentrated on 22 focus areas.

CBUAE maintains its continued commitment toward supporting the "UAE Vision 2021" and all strategic decisions taken by the federal government. This journey started with formulating an ambitious strategy for 2017-2021 that meets the expectations of all relevant stakeholders.

The vision of CBUAE is "promoting monetary and financial stability towards sustainable economic growth", which will be achieved by enhancing monetary and financial stability through effective supervision, prudent reserve management, and robust financial infrastructure.

The strategy and its detailed operational plans are revised on yearly basis through an extensive consultation and analysis process to build on the foundations that were completed and introduce new future-oriented initiatives.

In 2018, CBUAE continued to adopt the Government Excellence Model to transform CBUAE into a leading, innovative and smart organization. These efforts have been acknowledged by being shortlisted as one of the top three Leading Federal Entity Award.

Moreover, CBUAE concentrated on 22 different focus areas as part of the 2018 operational plan. From there, CBUAE has successfully completed key deliverables and made significant progress in enhancing the regulatory and supervisory framework for licensed Financial Institution such as developing a new licensing policy, approving risk based supervision strategy to ensure: compliance with best supervision practices, implementing new automated tool for examination process, implementing Basel III, issuing critical regulations related to the Financial Sector Assessment Programme (FSAP), drafting the new corporate governance framework for banks operating in the UAE, issuing new regulation regarding Interbank Rate Submissions (EIBOR Regulation) and establishing discussion forums with the banking sector (e.g. Banks CEOs, Banks CROs, Exchange House CEOs, External Audit Firms).

In addition, CBUAE enhanced and introduced comprehensive frameworks to ensure the effective contribution to the protection of the stability of the financial system in the UAE, developed new framework to ensure crisis readiness within CBUAE and the UAE banking system, enhanced the financial system surveillance framework, developed comprehensive regulatory stress testing framework and enhanced capabilities of UAE banks to perform the stress test according to CBUAE's modelling standard. 2018 was also marked by the approval of a comprehensive national strategy for payments in the UAE to ensure safe, innovative and convenient electronic payments to become a leading cashless economy. CBUAE also organised a Happython composed of six innovation labs that involved all stakeholders to facilitate ideation using many tools of design thinking.

SHAPING THE FUTURE

During 2018, CBUAE continued its efforts to finalize and syndicate the Financial Sector Master Plan with all relevant stakeholders. The Master plan supports the UAE's global competitiveness and its role in shaping the future and expected to be endorsed by the UAE Cabinet of ministers during the upcoming years.

Moreover, in November 2018, CBUAE conducted its 2019 Strategy Retreat, which concluded by identifying 14 new focus areas including:

- Implementing the framework for Financial Crisis Management
- Developing CBUAE's fintech strategy in coordination with national stakeholders, with significant focus on developing the appropriate fintech regulatory environment.
- Developing Islamic Finance Regulatory Framework for financial institutions operating in the UAE.
- Assuring the CBUAE readiness for FATF/ MENAFATF mutual evaluation.
- Assuring compliance with the Financial Sector Assessment Programme (FSAP) requirements including the deployment of risk-based supervision approach, issuing and implementing the regulations critical to FSAP such as the development of the resolution and recovery framework and supporting the implementation of the new Corporate Governance Framework for banks, enhancing CBUAE enforcement capabilities and ensuring compliance with the Principles on Financial Market Infrastructures (PFMIs).
- Implementing the National Payments Strategy to ensure safe, innovative and convenient electronic payments to become a leading cashless economy.
- Strengthening the Consumer Protection Framework.

The above focus areas will be achieved through the implementation of the following business enablers:

- Improving effective training and capability building based on the organisation's priorities.
- Implementing the Business Continuity Management System
- Complying with Signals Intelligence Agency (SIA) requirements related to information security.
- Design data strategy to improve CBUAE's methods related to acquiring, storing, managing, sharing and usage of data
- Enhancing the work environment in line with the National Programme for Happiness and Positivity
- Establishing a Quality Management System according to ISO 9001 and other standards
- Setting-up and managing a contact centre to address external enquires related to CBUAE services.

CHAPTER 6. REGULATORY DEVELOPMENT AND BANKING SUPERVISION

CBUAE made significant progress in developing its new regulatory framework in 2018. The reform agenda is built around five pillars: (i) Risk Management, (ii) Basel III Framework, (iii) Controls/Compliance, (iv) Resolution Framework and (v) Market Development, along with an overarching Corporate Governance framework.

CBUAE's objective is to maintain the safety and soundness of the licensed financial institutions. It has been given five main tasks:

- **Regulatory Development**: Develops the regulatory strategy and regulations for supervising licensed financial institutions and activities
- **Licensing**: Grants licenses needed for financial activities as per CBUAE's law
- **Supervision and Examination**: Conducts examination of licensed financial institutions
- **Payment Systems Oversight**: Undertakes oversight over the operations of licensed payment systems;
- **Enforcement**: Exercises disciplinary powers for non-compliance with regulatory and licensing standards as per CBUAE's law.

REGULATORY DEVELOPMENT

REGULATORY DEVELOPMENTS IN 2018

CBUAE made significant progress in developing its new regulatory framework in 2018. The reform agenda is built around five pillars, as follows:

1. **Risk Management Framework;**
2. **Basel III Framework;**
3. **Controls/Compliance Framework;**
4. **Resolution Framework;**
5. **Market Development Framework.**

These five pillars are bolstered by an overarching Corporate Governance framework.

1. The pillar on risk management was fully completed in 2018 with the issuance of a new risk management framework for banks. It comprises five regulations covering overall risk management, operational risk, market risk, interest rate risk, and country and transfer risk.
2. New regulatory standards supporting the Basel Capital Regulation (Leverage Ratio, Counterparty Credit Risk, Credit Value Adjustment, Equity Investments in Funds, Securitisation) were drafted in 2018 and will be published in 2019.
3. The pillar on controls and compliance was largely completed in 2018. Regulations on internal controls, compliance and internal audit were completed, giving significant responsibility to the heads of compliance and internal audit regulation on financial reporting and external auditor were also issued. This required transparent financial reporting and high-quality external audits in banks, including mandatory auditor rotation. CBUAE further issued a new regulation on dormant accounts in banks and the protection of customers' rights in this area. The Controls/Compliance pillar will be fully completed in 2019 with the issuance of two additional regulations for banks on major acquisitions and significant ownership transfer.
4. In 2019, CBUAE plans to commence its work on the resolution framework pillar of the regulatory framework, which covers recovery and resolution planning.

ANNUAL REPORT 2018

5. Under the market development pillar, CBUAE issued a regulation for non-bank financial institutions in 2018, which sets out the new regulatory framework for finance companies operating in the UAE. The regulation includes requirements for a specific business model, governance model, risk management and appropriate controls/compliance functions. A regulation on crowd-funding as well as a strategy and regulations aimed to support the financing of the UAE's micro, small and medium enterprises (MSME) in coordination with the wider UAE authorities were under development in 2018. Under this pillar, CBUAE plans to commence in 2019 further work on other regulations relating to payments and fintech.

The new corporate governance framework for banks operating in the UAE largely progressed in 2018 and is planned for issuance in 2019.

ISLAMIC FINANCE

In 2018, CBUAE initiated work on its Islamic Finance Development Framework. The objective is to help accelerate the growth of the sector in a progressive and competitive manner and promote the UAE to be a leading Islamic financial services hub. Important focus areas include the legal and regulatory framework for Islamic banks, liquidity support mechanisms and the wider UAE Islamic finance knowledge economy.

CBUAE continued to play an active role in contributing to the work of the Islamic Financial Services Board (IFSB) as Chair of its Technical Committee and full council member in 2018. CBUAE's staff were nominated to support the IFSB working groups that develop the IFSB-15 Capital Adequacy Standard update and the technical note on financial inclusion. In 2018, CBUAE also provided feedback and regulatory insights to IFSB as part of its strategy to assist in promoting implementation of their standards across member jurisdictions.

CAPITAL

Capital adequacy is a key pillar for ensuring the safety and soundness of banks. CBUAE requires all banks operating in the UAE to comply with the Basel III standardised approach when assessing their regulatory capital adequacy. CBUAE is currently conducting a thorough review of its approach to Pillar 2 concerning the Internal Capital Adequacy Assessment Process (ICAAP) and Supervisory Review and Evaluation Process (SREP). Basel III minimum capital requirements, including a framework for Domestic Systemically Important Banks, are currently in place.

Traditionally, banks in the UAE have had significant exposure to credit risk, and limited exposure to market risk due to the lack of large proprietary books and a policy of customer driven matched deals or fully hedged positions.

Although losses attributable to operational risks have decreased over recent years through the application of new technologies and improved processes, those technologies and processes have created potential for even more complex types of operational risk. Under CBUAE's regulatory framework, banks implement the following approaches to calculate the equivalent risk weighted assets relating to operational risk: Basic Indicator Approach; Standardised Approach and Alternative Standardised Approach.

LIQUIDITY

Regulatory minimum liquidity requirements are an essential part of the Basel III framework. They provide resistance against short-term and longer-term liquidity imbalance. In the UAE, banks manage their liquidity based on the CBUAE's Regulation No. 33/2015 issued in 2015. The regulation implements the Liquidity Coverage Ratio (LCR) covering short-term imbalances and the Net Stable Funding Ratio (NSFR) covering longer-term structural funding imbalances. Both ratios are applicable to large international active banks for all other banks, the UAE adopted alternative, less complex, balance sheet based, ratios: the short-term Eligible Liquid Asset Ratio (ELAR) and the longer-term funding Lending to Stable Resources Ratio (LSRR). The qualitative liquidity management requirements are applicable to all banks in the UAE. In 2018, four banks were under Basel III liquidity regime with LCR and NSFR. The minimum requirements for banks are in line with the phased-in Basel requirements of LCR minimum requirement of 90% and NSFR of 100% as of 31 December 2018. The ELAR requirement is set at 10% and the LSRR requirement at 100%.

THE HIGHER SHARI'AH AUTHORITY

The Higher Shari'ah Authority (HSA) was established pursuant to the UAE Cabinet resolutions, commencing in February 2018. The HSA aims to harmonise and standardise the practices of Islamic Financial Institutions, aligning them to international Shari'ah standards and widely recognised practices through collaboration with the relevant stakeholders. HSA's goal is to support creation of a robust infrastructure that enables further development of the Islamic financial sector in the country and advances the UAE's vision in becoming an internationally recognised hub for Islamic finance.

HSA was established and its members appointed as per the UAE Cabinet's resolutions (No. 1 102//5و of the year 2016) and (No. 31م/6و of the year 2017) respectively. Decretal Federal Law No. (14) of 2018, regarding CBUAE and the organisation of financial institutions and activities, reaffirmed the establishment of HSA and provided further details related to its mandate.

HSA MEETINGS AND COLLABORATION

In 2018, HSA held six meetings, during which it discussed various matters related to the Islamic Banking industry and issued 40 resolutions and guidance notes. The HSA's meetings covered the four focus areas:

1. Ascertainment of Shari'ah Compliance: One of the key outcomes of HSA's work is the adoption of Shari'ah standards issued by Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI) as the minimum requirement for Shari'ah compliance.
2. Strengthening Shari'ah Governance: HSA worked on the development of several documents related to Shari'ah governance. The governance standards will be shared with the relevant stakeholders for consultation and feedback before their issuance.
3. Research and Development: HSA conducted studies to identify the best practices and made adequate recommendations related to the UAE market.
4. Strengthening Harmonisation: HSA is working closely with the UAE Islamic financial institutions to smooth the implementation of Shari'ah standards. Collaborative activities are taking place between market players to harmonise practices and to work out solutions to any potential challenge that may occur during implementation.

To strengthen collaboration with relevant local and international entities, HSA engaged with various Islamic finance institutions/bodies. In the international domain, HSA participated in a number of events including:

1. Inaugural roundtable meeting of Centralised Shari'ah in Islamic finance
2. AAOIFI Annual Shari'ah Conferences
3. Islamic Financial Services Board (IFSB) meetings
4. Global Islamic Economic Summit
5. General Council for Islamic Banks and Financial Institutions (CIBAFI) and World Bank Conference on Governance for Islamic Financial Institutions
6. Joint meeting between HSA and the Shari'ah Advisory Council of the Bank Negara Malaysia and its Secretariat

LICENSING

CBUAE processes requests received from new applicants and existing licensees. The existing licensees are classified according to their license type to banks, representative offices, finance companies, exchange house and payment service providers.

In 2018, CBUAE processed applications for the following services:

- New license
- License modification
- License renewal
- Branches licenses and approvals (Opening/ relocation/ closure)
- Electronic Banking Service Units licenses and approvals (Opening/ relocation/ closure)
- Pay Offices licenses and approvals (Opening/ relocation/ closure)
- ATMs installation
- Capital/shareholding structure amendments
- Receipt of resolutions issued from courts and forwarding to banks and other financial institutions for their action.

As of year-end 2018, a total of 38 licensed foreign banks and 97 Representative Offices from 23 countries operated in the UAE. In addition, 22 local banks operated in the UAE with a total of 756 branches, Electronic Banking Units and Pay Offices.

SUPERVISION AND EXAMINATION

Within the framework of its 2017-2021 strategic plan, CBUAE continued its work to enhance the Regulatory and Supervision Framework for licensed financial institutions. During 2018, CBUAE significantly advanced its agenda to move towards a forward looking and proportionate implementation of Risk Based Supervision (RBS) approach that comprises of full-scope, limited and thematic reviews.

The pillars for the new Banking Supervision Framework will compromise of:

Enhanced regulatory framework, to support the development of a long-term supervisory roadmap;

Improved efficiency and effectiveness of the overall supervisory framework using the new supervisory handbook in accordance with international standards and best practices, which includes new supervisory methodologies for the assessment of risks;

Full compliance with BCBS's core principles.

THE SUPERVISORY METHODOLOGY

During 2018, CBUAE made significant advance in the implementation of the new RBS methodology. Its implementation will further enhance supervision by introducing additional regulatory returns that capture the existing and emerging risks, enabling the development of risk tools for enhancement of off-site monitoring, and hiring specialised teams for targeted examinations. Furthermore, CBUAE implemented a tool for automation of the examination process and operationalisation of the electronic document management system.

PAYMENT SYSTEMS OVERSIGHT

CBUAE's main function is to supervise and conduct oversight assessments of all financial market infrastructures payment system falling under the regulatory regime of CBUAE as well as to ensure their safety, efficiency and compliance with the Principles for Financial Market Infrastructures (PFMI).

CBUAE conducts periodic assessment of the following CBUAE operated payment systems: UAE Funds Transfer System (UAEFTS), Image Cheque Clearing System (ICCS), UAE Direct Debit System (UAEDDS), Wages Protection System (WPS), UAE Electronic Switch for card transactions (UAE Switch) and UAE Payment Gateway System (UAEPGS).

ENFORCEMENT

CBUAE Enforcement's role is to support the strategic objectives in an efficient and flexible manner by maintaining a disciplined approach towards enforcement. This includes deterring violations of and enhancing compliance with the applicable laws of the UAE.

CHAPTER 7.
RESERVE MANAGEMENT, MONETARY MANAGEMENT AND FINANCIAL STABILITY

CBUAE managed its foreign exchange reserves efficiently with emphasis on safety, liquidity and return, and produced a satisfactory return. The framework for monetary operations was developed in consultation with local market participants and the CBUAE put in place a new framework for setting the interbank rates (EIBOR). The key focus areas of financial stability during 2018 comprised financial stability surveillance and analysis, assessment of domestic systemically important banks, crisis preparedness and management framework and the 2018 regulatory stress test, which demonstrated resilience of the banking system to potential shocks considered under adverse scenarios.

RESERVE MANAGEMENT

CBUAE is responsible for the management of the foreign exchange reserves of the UAE. The primary objective for holding the foreign exchange reserves is to:

- Support the confidence in the pegged exchange rate policy
- Mitigate disturbances arising from the balance of payments and/or domestic banking system
- Facilitate transactions in foreign currency with government departments and the local banking system; and
- Maximize the return at an acceptable level of risk.

The Reserve Management Framework aligns with *the IMF Guidelines for Foreign Exchange Reserve Management* that sets best international practice in this area. In 2018, CBUAE put in place a new front-office asset management system and developed its work on strategic asset allocation, liquidity management, investment policy and external manager arrangements. These building blocks create a strong foundation for prudent reserve management with emphasis on a strong governance structure, clear separation of duties and asset and risk management practices in line with the best international practice.

In 2018, CBUAE managed its foreign exchange reserves efficiently, as in the past, with the key focus on safety, liquidity and return. The assets were managed in full observance of the agreed investment guidelines and produced a satisfactory return.

MONETARY MANAGEMENT

CBUAE is responsible for the implementation of monetary policy that aimed at maintaining soundness and stability of the monetary system in the state. For the purpose of achieving its mandate, it focuses primarily on undertaking the following functions:

- Design and develop the Monetary Management Framework for the domestic market and related operational tools and other practical means, including policies related to the management of the national currency exchange rate and domestic money markets;
- Define parameters and conduct the day-to-day use of monetary management tools related to the drainage/injection of liquidity in the domestic market.

As part of its efforts to strengthen its monetary management framework and to foster money market development in the UAE, CBUAE's initiated in 2018 work on reorganising its operations in the Dirham money markets – referred as the "Dirham Monetary Framework" – while taking into consideration the policy primary objective of maintaining the peg of the Dirham to the US Dollar. In this regard, a comprehensive consultation paper was released during Q4 2018 to banks operating in the UAE, where it showcased the main pillars of the newly proposed framework and related operational set-up.

Moreover, 2018 was also marked by the issuance of the new regulations regarding Interbank Rate Submissions (EIBOR Regulation). This regulation, which is in line with the recommendations of the International Organisation of Securities Commissions (IOSCO), is aimed at enhancing governance, standardisation, and transparency in rate setting process at EIBOR Panel banks.

FINANCIAL STABILITY

CBUAE contributes to the promotion and protection of the stability of the financial system by identifying, analysing, and mitigating current and future financial system risks. Financial stability activities during 2018 covered the implementation, execution and enhancement of the following key areas:

- Comprehensive financial system surveillance framework covering banking system, financial markets, and central bank indicators and analysis. The financial system surveillance comprised regular assessments of key developments in the financial system and implementation of financial system soundness measures. In addition, the Financial Stability Report published during the year provided an annual CBUAE assessment on the stability of the financial system and related developments.
- Further, macroprudential surveillance assessed relations between the macroeconomy and the financial system, macro-financial cycles, early warning indicators to detect build-up of potential systemic risks and conducted an annual review of domestic systemically important financial institutions. During 2018, one additional bank was designated as systemically important, bringing the total number of domestic systemically important banks to four.
- Comprehensive financial crisis preparedness and management framework, with the objective to ensure high-level crisis readiness within CBUAE and the UAE banking system. The CBAUE internal crisis preparedness and management framework enhances quick and effective response to potential shock in the financial and banking system. This is achieved through immediate action and coordination across CBUAE departments in order to contain situations that could threaten UAE financial stability.
- Comprehensive regulatory stress testing framework with the purpose to evaluate the resilience of individual banks and the banking sector as a whole to severe adverse scenarios and to support the development of internal stress testing capabilities of banks across the UAE. Overall, the 2018 regulatory stress test demonstrated resilience of the banking system to potential shocks considered under the adverse scenarios. Stress testing results are designed to contribute to the CBUAE risk-based banking supervision.

CHAPTER 8. FINANCIAL MARKET INFRASTRUCTURE AND PAYMENT SERVICES

Financial Market Infrastructure (FMI) is the backbone of the financial market as it enables a safe flow and efficient clearing and settlement of funds and financial assets in the economy. Its smooth operation and safety and soundness is crucial to maintaining confidence in the currency and banking system, in addition to supporting the monetary policy operations and the stability of the financial system as a whole.

The FMI and payment services in the UAE continued to evolve in accordance with CBUAE strategic plan during 2018. Under the CBUAE's, major reforms took place to gradually bring the FMI and payment services in line with the international standards and best practices adopted in many developed economies.

In addition, CBUAE continued to contribute to the UAE's strategies in the field of financial sector, through on-going enhancements of FMI and related payment services and regulations.

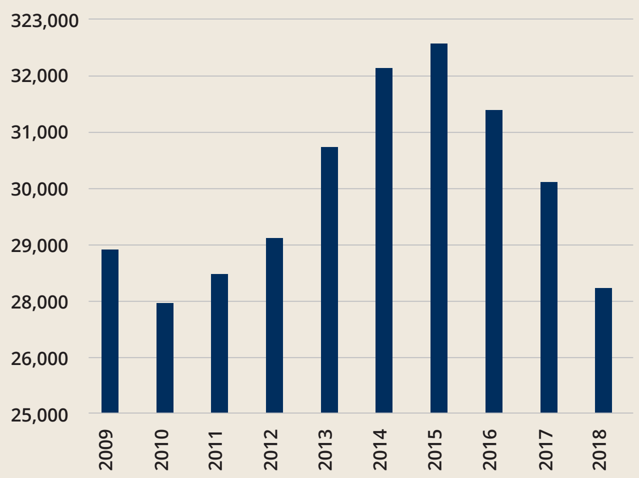
The major focus areas of CBUAE in this field include the following:

- Provide regulatory clarity and a level playing field for payment services providers
- Strengthen the UAE's leading position through the development of the regional and cross-border payment systems
- Ensure that CBUAE's business contingency plan is properly tested and updated
- Implement the projects depicted in the National Payment Systems Strategy (NPSS), based on the roadmap defined by CBUAE
- Continue the development of the Renminbi Clearing Center established in the UAE on May 2017

MAIN ACHIEVEMENTS IN 2018

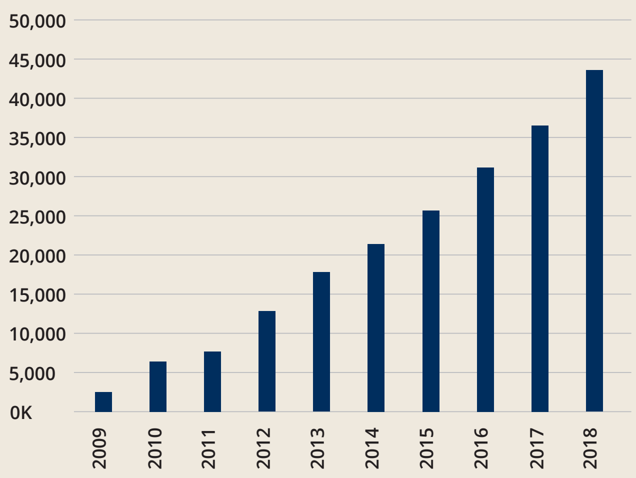
1. Completion of the document of NPSS
2. Commencement of the Joint Central Bank Digital Currency (CBDC) and Distributed Ledger Technology Proof Project (Aabir) with another central bank
3. Improving renminbi clearing arrangements in the UAE
4. Revamping the UAE Switch
5. Launching the Court Cases Management System (CCMS)

ICCS PRESENTED CHEQUES
COUNT (IN THOUSANDS)



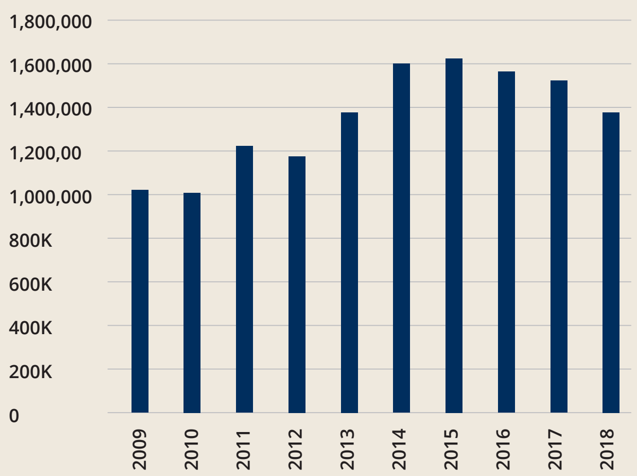
SOURCE: CBUAE

FTS CUSTOMER TO CUSTOMER TRANSFERS
COUNT (IN THOUSANDS)



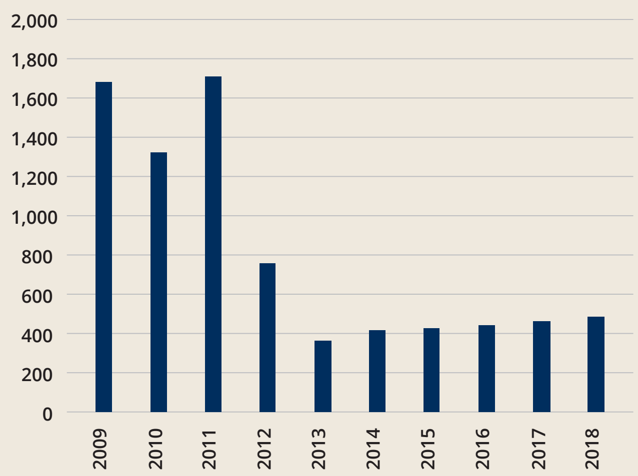
SOURCE: CBUAE

ICCS PRESENTED CHEQUES
VALUE (AED IN MILLIONS)



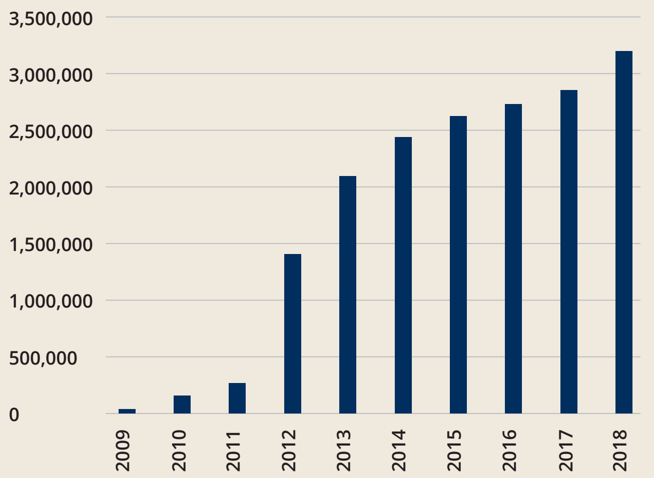
SOURCE: CBUAE

FTS BANK TO BANK TRANSFER
COUNT (IN THOUSANDS)

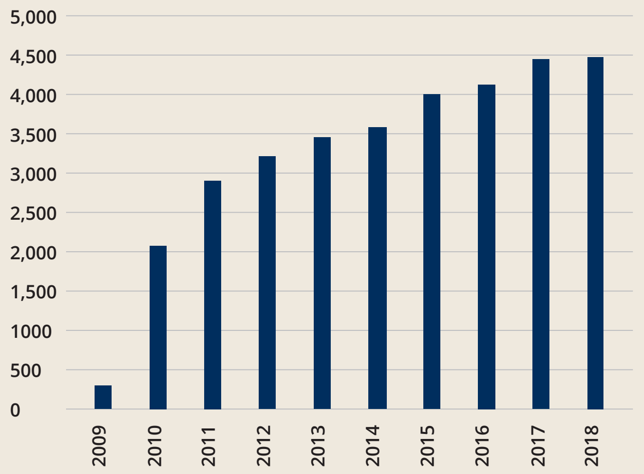


SOURCE: CBUAE

FTS CUSTOMER TO CUSTOMER TRANSFERS VALUE (AED IN MILLIONS)

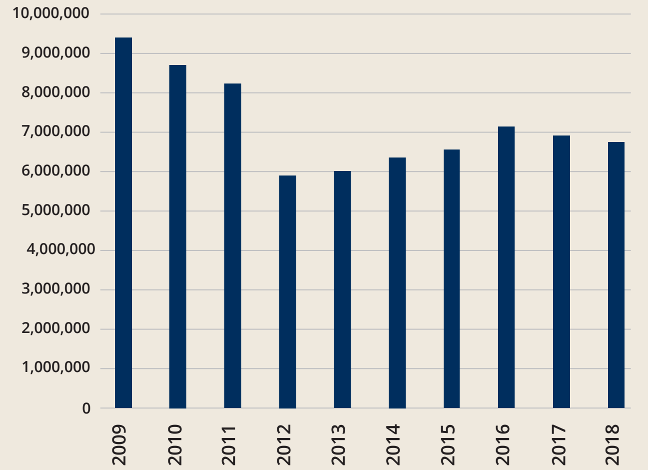


WPS REGISTERED NUMBER OF EMPLOYEES AVERAGE (IN THOUSANDS)

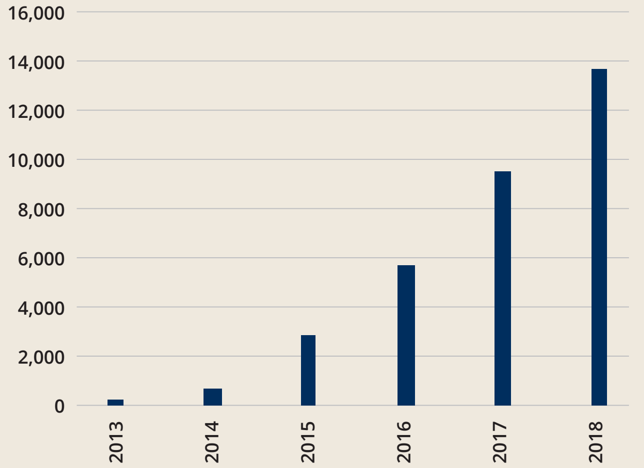


SOURCE: CBUAE

FTS BANK TO BANK TRANSFER VALUE (AED IN MILLIONS)

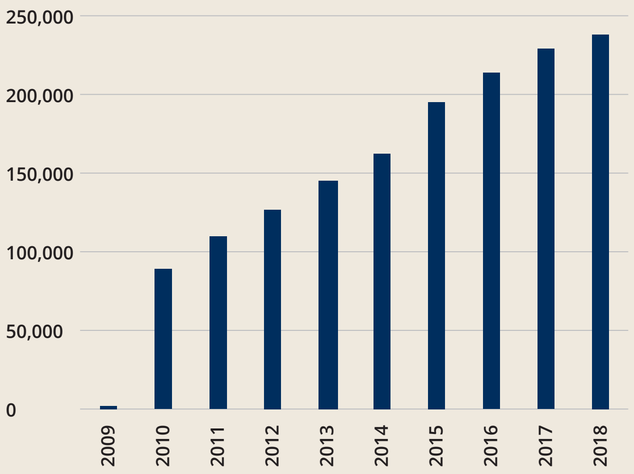


DDS PRESENTED CLAIMS COUNT (IN THOUSANDS)



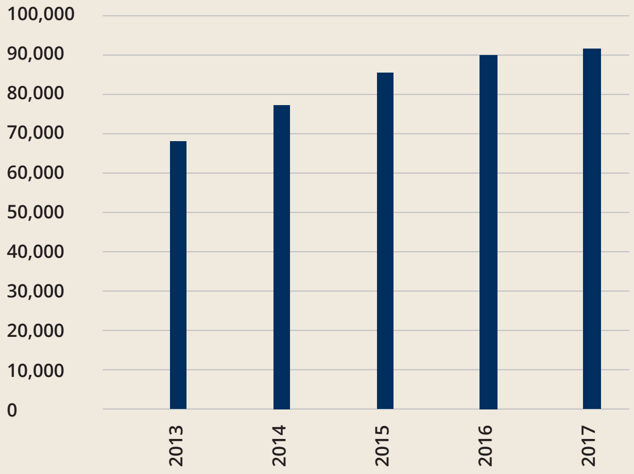
SOURCE: CBUAE

WPS SALARIES PROCCESSED
VALUE (AED IN MILLIONS)



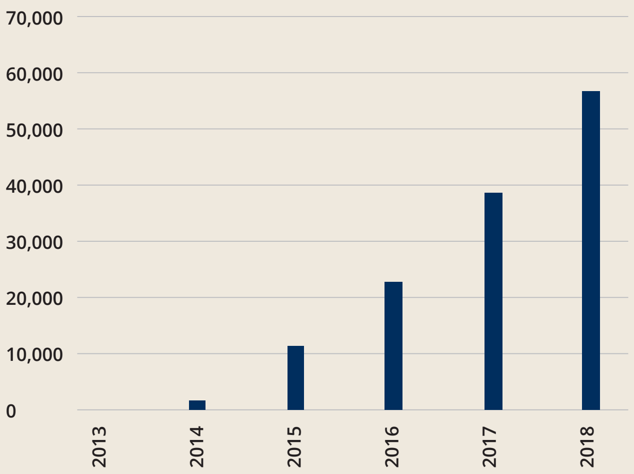
SOURCE: CBUAE

UAESWITCH CASH WITHDRAWAL (DOMESTIC)
COUNT (IN THOUSANDS)



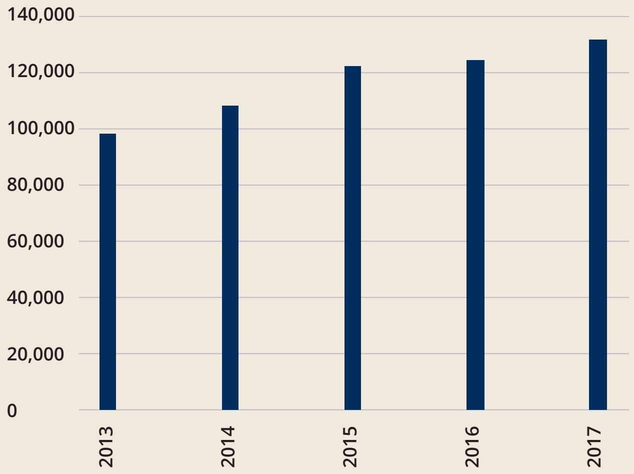
SOURCE: CBUAE

DDS PRESENTED CLAIMS
VALUE (AED IN MILLIONS)



SOURCE: CBUAE

UAESWITCH CASH WITHDRAWAL (DOMESTIC)
VALUE (AED IN MILLIONS)



SOURCE: CBUAE

CHAPTER 9. CONSUMER PROTECTION

CBUAE Board of Directors had issued a decision in 2017 that provided authority to create a new Consumer Protection Department (CPD), contributing to the stability of a highly competitive financial market through the strengthening of consumer confidence.

CBUAE Consumer Protection provides a Consumer Contact Center that responds to consumers with information on questions they have as well as provides financial product information. The Center will register complaints against licensed financial institutions and will work with the institutions and their customers in an effort to encourage resolution of customer complaints. The Department's mandate is expanding to include consumer education and awareness and strengthen regulatory oversight of market conduct.

NEW LAW

The UAE Government passed the new Decretal Federal Law No. (14) 2018, regarding the Central Bank & Organisation of Financial Institutions and Activities. The new law has provided CBUAE with a clear mandate to regulate and supervise market conduct and implement new consumer protection measures. CBUAE will contribute to the stability of a competitive financial sector by strengthening consumer confidence in the integrity of the market place through effective oversight.

NEW DEPARTMENT

The Consumer Protection Department (CPD) is developing a new technology to enhance its services regarding customers' inquiries and complaints. CPD will develop new consumer protection measures to protect consumers against market place mis-conduct by financial institutions. Furthermore, a key focus includes the development and expansion of consumer education, outreach and awareness programmes in addition to, initiatives to support the development and coordination of the national financial literacy strategy.

NEW STANDARDS:

During 2018, CBUAE moved forward with its agenda to strengthen its consumer protection framework with the addition of three new initiatives including dealing with issues of managing dormant accounts, improving complaint management and increasing disclosure in lending products. These include:

- A new regulation that provides oversight of dormant accounts.
- Another regulation was issued establishing standards in the licensing and monitoring of the Exchange Business Department
- A new regulation for finance companies which aims to improve disclose of procedures to consumers related to the costs of borrowing risks.

CONSUMER ISSUES:

In relation to CBUAE's Customer Contact Centre, this year thousands of consumer visits and calls have been processed. In addition to providing information to consumers, the center works with the banks and their customers in an effort to encourage resolution of customer complaints. Reviewing the volume of complaints and enquiries, the five top issues raised by consumers are:

- Debt level management;
- The refusal or delays by banks in issuing necessary documentation; Bank delays/rejections related to issuing necessary documentation;
- Aggressive selling of credit cards and lack of disclosures;
- Issues related to opening, operating and closing of bank accounts;
- Issues regarding the remittance of funds.

CPD is addressing these issues with the financial institutions and where necessary will take enforcement measures.

CONSUMER EDUCATION AND AWARENESS

To promote consumer education and awareness, CBUAE presented and spoke on financial topics in several workshop sessions that were open to the public. The events were partnered through the *Family Development Foundation* during 2018. Each session focused on a different topic and was open for discussion, including:

- The benefits of saving;
- How to make a budget for family (income and expenses);
- Personal loans: Reasons for obtaining credit and the risks;
- Credit cards - benefits and risks.
- Understanding bank products - mortgages and overdrafts.

CPD is currently working on enhancing its awareness activities as it completes the staffing of new positions in the Consumer Education and Outreach Unit.

CHAPTER 10.
RISK MANAGEMENT, BUSINESS CONTINUITY AND INFORMATION SECURITY

CBUAE faces a number of financial and non-financial risks during its day-to-day operations. The Risk Management and Compliance Department manages these risks across all functions and business areas. In addition, a Board Risk Committee and an Executive Level Risk Committee, which is chaired by H.E. the Governor, support the Board of Directors in effectively overseeing risk management across all areas.

FINANCIAL RISK

The financial risks that CBUAE faces in the management of its foreign reserves include currency, interest rate, credit, counterparty and liquidity risks. Multiple tools are used to measure and control these risks, including traditional sensitivity measures and limits to various potential exposures, as well as Value at Risk (VaR) and stress testing. Furthermore, CBUAE uses established credit loss metrics that measure potential credit loss under simulated credit events. Stress tests are used to ensure that CBUAE maintains an adequate share of its reserves portfolio in liquid assets. It also collateralises all liquidity-providing operations with domestic banks and ensures regular revisions of the eligibility criteria and the risk control measures that are applied to the assets accepted as collateral.

OPERATIONAL RISK

CBUAE is also exposed to operational risks, which are defined as the risks of loss resulting from inadequate or failed internal processes, people and systems, or from external factors. These risks are identified and measured by both the risk team and risk coordinators within each department. In 2018, several tools were introduced to track, monitor and report emerging risks. The level of the risks, their mitigation plans and risk acceptance requests are reported and presented to the Risk Committee and the Board Risk Committee for approval.

BUSINESS CONTINUITY

In 2018, the Board Risk Committee approved CBUAE's new Business Continuity Policy. As part of the new policy, a new in-depth Business Impact Analysis exercise was conducted within all departments to identify critical processes and recovery requirements, in case of a disruption of these processes. Furthermore, the team conducted a Threat Risk Assessment, in which medium and high residual risks that could lead to business disruption were highlighted

COMPLIANCE

The compliance function assists the organisation's leadership in managing the risk of adverse consequences that could affect CBUAE or the UAE, as a result of the bank's failure to comply with laws, regulations, rules, applicable international conventions, adopted internal organisational standards, or the bank's code of conduct.
During 2018, the Board of Directors approved a Whistleblowing Policy that allows stakeholders to directly report perceived or alleged misconduct and corruption to the compliance unit. Furthermore, the compliance function initiated a review of the existing employee code of conduct, including a detailed policy on conflict of interest and anti-corruption.

INFORMATION SECURITY

Against the background of increasingly digitalised financial services, the CBUAE continued its close collaboration with numerous organisations within the banking sector and government entities to promote cyber resilience. Furthermore, in order to enhance its internal processes and capabilities in tackling cyber security risks, CBUAE recruited top talent and adopted best practices in information security. It also strengthened its information and cyber risk management processes by implementing a dynamic risk-analysis methodology, identifying and protecting high-value information assets, assessing third parties and enhancing reporting at the executive level.

CHAPTER 11.
FINANCIAL INTELLIGENCE

The Financial Intelligence Unit (FIU) is empowered to exchange information on suspicious transactions and any other information that has direct or indirect access to, with its counterpart FIUs and local stakeholders for AML/CFT purposes.

Article 9 of decree federal law no (20) of 2018 on Anti-Money laundering and Combating Financing of Terrorism and Illegal Organisations establishes an independent Financial Intelligence Unit (FIU) in the Central Bank as the sole national center for receiving, analysing and disseminating suspicious transaction reports filed by banks, financial institutions and Designated Non-Financial Businesses and Professions (DNFBPs) to law enforcement authorities.

It has access to all relevant authorities in the UAE under the aegis of the National Anti-Money Laundering and Combating Financing of Terrorism and Illegal Organisation Committee (NAMLCFTIOC). The appropriate mechanisms are in place to ensure adequate cooperation and information sharing among different government agencies involved in combating ML/TF and related crimes. It links the private and the public sectors in combating money laundering, terrorist financing and proliferation.

MAIN ACHIEVEMENTS IN 2018:

- 7,404 STRs received from banks and other financial, commercial and economic entities, in addition to 1,516 reports on suspected fraud, an increase of 18.2% from last year. 7,451 STRs were reviewed and analysed during the year, on a risk-based basis.
- 79% of all received STRs were filed by banks, similar to 2017.
- 1,922 STRs were referred to law enforcement authorities in the UAE, for further investigation.
- 270 search and/or freeze requests received from law enforcement, public prosecution and other domestic authorities were executed.
- Financial institutions were instructed to repatriate unauthorised transfers related to 26 cases.
- 990 Enhanced Customer Due Diligence (ECDD) and fraud alerts were initiated to relevant financial institutions based on STRs.
- 539 requests for information and 115 spontaneous disclosures were received relating to 3102 natural and juridical persons.
- Dissemination of 78 spontaneous information STRs to counterpart FIUs.
- FIU responded to five questionnaires from counterpart FIUs and Egmont secretariat in addition to two reports for special requests received from Egmont Secretariat and Regional Representatives. Also, worked on 19 ADHOC requests from counterpart FIUs.
- FIU conducted meetings and AML/CFT outreach programmes which benefited representatives of public and private sector entities in the UAE, including foreign stakeholders.
- FIU participated in various international (Egmont, FATF, MENAFATF, etc.), regional and domestic training programmes and other events to build capacity.
- National Anti-Money Laundering and Combatting Financing of Terrorism Committee approved FIU's initiative of opening dialogue with universities/ colleges on the importance of developing AML/ CFT curriculum.

APPENDIX

CBUAE: SELECTED MACROECONOMIC INDICATORS 2011-2020 - 5 MAY 2019 EDITION

	2011	2012	2013	2014	2015	2016	2017	2018 (E)	2019 (P)	2020 (P)
World GDP (%)	4.2	3.5	3.4	3.5	3.4	3.2	3.8	3.6	3.3	3.6
US GDP (%)	1.6	2.2	1.7	2.4	2.6	1.6	2.2	2.9	2.3	1.9
Oil Price (S/BI)[1]	110.9	112.0	108.9	98.9	52.4	44.0	54.2	71.1	63.0	66.0
Oil production UAE (Million Barrels / day)[2]	2.5	2.7	2.8	2.8	3.0	3.1	3.0	3.0	3.1	3.1
In Billions of AED										
Real GDP (2010 prices)	1,138	1,189	1,249	1,304	1,370	1,411	1,418	1,442	1,471	1,510
Real Non Oil GDP	768	801	849	903	949	979	1,003	1,010	1,029	1,059
Real Oil GDP	370	388	400	401	421	432	420	432	444	450
Nominal GDP	1,288	1,376	1,433	1,481	1,315	1.311	1,387	1,521	1,527	1,597
Nominal Non Oil GDP	786	838	904	975	1,028	1,058	1,096	1,128	1,172	1,231
Nominal Oil GDP	501	537	529	505	287	253	291	393	354	366
Annual percent change (%)										
Real GDP	6.9	4.5	5.1	4.4	5.1	3.0	0.5	1.7	2.0	2.6
Real Non Oil GDP	4.7	4.3	5.9	6.4	5.0	3.2	1.9	1.3	1.8	3.0
Real Oil GDP	11.8	4.8	3.2	0.1	5.2	2.6	-2.8	2.8	2.7	1.3
Nominal GDP	21.0	6.8	4.1	3.3	-11.2	-0.3	5.8	9.7	0.4	4.6
Nominal Non Oil GDP	7.3	6.6	7.8	7.9	5.4	2.9	3.6	2.9	3.9	5.0
Nominal Oil GDP	51.5	7.2	-1.6	-4.5	-43.2	-11.8	15.0	35.1	-9.9	3.3
CPI (2014 base year)	96	97	98	100	104	106	107.8	111.1	109.8	112.0
CPI Inflation (%)	0.9	0.7	1.1	2.3	4.1	1.6	2.0	3.1	-1.2	2.0

Source: FCSA, OPEC, IMF & Central Bank of UAE

1 For Oil pirce projections, we assumed the annual average prices of oil futures on March 6th, 2019

2 As reported by OPEC

ABU DHABI

King Abdullah Bin Abdulaziz
Al Saud Street
P.O Box 854
Abu Dhabi
United Arab Emirates

DUBAI

26th Street
Bur Dubai
P.O. Box 448
Dubai
United Arab Emirates

SHARJAH

King Abdul Aziz Street
Sharjah Industrial Area
P.O. Box 645
Sharjah
United Arab Emirates

AL AIN

Ali Bin Abi Talib Street
P.O. Box 1414
Al Ain
United Arab Emirates

RAS AL KHAIMAH

Al Muntasir Road
P.O. Box 5000
Ras Al Khaimah
United Arab Emirates

FUJAIRAH

Hamid Bin Abdullah Road
P.O. Box 768
Fujairah
United Arab Emirates

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