

# **Contributions of, and Issues Faced by, Japanese Companies in UAE Economic Development: A Comparison with South Korea**

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## **1. Introduction**

South Korean companies have expanded their presence in the Gulf Arab states. South Korean cars account for a growing share of the long lines of cars backed up in evening rush-hour traffic in Kuwait, Dubai, and Manama. Space previously set aside for Japanese products in the mobile phone showcases of electronics shops throughout the cities is increasingly being allocated to South Korean products.

This paper will attempt to consider the types of markets that South Korean companies are developing in the Gulf Arab states (primarily the UAE) and possible expansion strategies for the future by once more examining moves by South Korean companies energetically expanding into the Gulf Arab states in recent years as well as relations between South Korea and the Gulf Arab states.

This paper will be structured as follows. Section 2 will examine the impact of the Arab Spring on the Gulf Arab economies, primarily from a macroeconomic perspective. Section 3 will study the impact of Japan and South Korea on the UAE economy in terms of trade structure. Section 4 will discuss the activities of

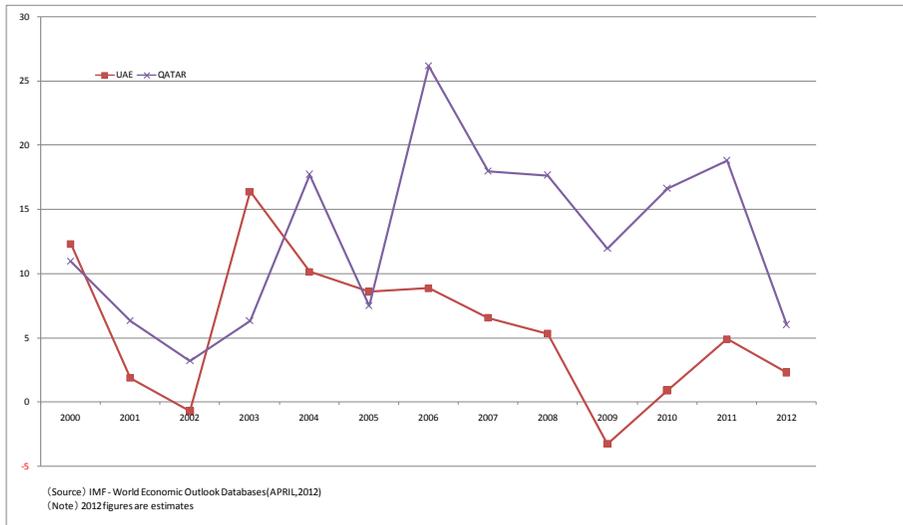
Japanese and South Korean companies in the UAE market and explore that market's potential. Finally, Section 5 will summarize the arguments made up to that point.

## **2. Impact of the Arab Spring on Gulf Arab Economies**

The Arab Spring that swept through Middle Eastern Arab states has thus far (as of July 2012) had relatively little direct impact on the UAE. The Gulf monarchies have countered the spillover of the Arab Spring and repressed anti-regime movements by distributing additional income to the people. The oil-producing Gulf states hold abundant supplies of oil money due to the surge in oil prices in the 2000s, and they have achieved a certain degree of success in responding to the challenges of the Arab Spring by making incremental political reforms and boosting the economic benefits distributed to disaffected segments of society. Although 2011 saw the "petition incident" and the rise of numerous political reform movements in the UAE, these movements appear to have quieted down before they could become population-wide movements (Horinuki [2012a,b]).

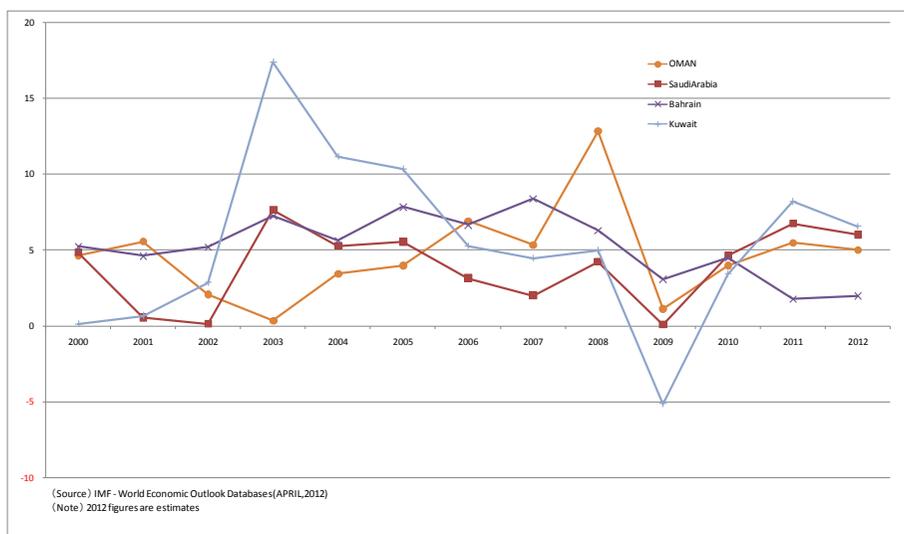
The macro economies of the Gulf region can be broadly divided by economic growth rate into two groups. There is the high-growth group consisting of the UAE, which has maintained relatively high growth rates (an average real GDP growth rate of 6.1% during the 2000s), and Qatar (13% for that same period) (Figure 1), and the low-growth group comprising the remaining countries: Oman (4.6%), Kuwait (5.1%), Saudi Arabia (3.5%), and Bahrain (5.9%) (Figure 2). There is a clear disparity between the two groups that was particularly apparent in the first half of the 2000s, when the UAE's average real GDP growth rate was 8.1% and Qatar's 8.7% vis-a-vis Oman's 3.3%, Kuwait's 7.1%, Saudi Arabia's 4.0%, and Bahrain's 6.0%. The Arab Spring has prompted small- and large-scale demonstrations in Gulf Arab states other than the UAE and Qatar. From February to March 2011 up to 10,000 demonstrators took to the streets in Saudi Arabia, and several thousand participated in demonstrations in Kuwait, Bahrain and Oman.

**Figure 1. Real Economic Growth Rates in GCC Countries (UAE, Qatar)**



Given that the Arab Spring did not have a major domestic impact on the high-growth group of the UAE (6.1% real GDP growth rate from 2000-2010) and Qatar (13.0%), it is a curious coincidence that those countries with low real GDP growth rates for the same period-Oman (4.6%), Saudi Arabia (3.5%), Bahrain (5.9%), and Kuwait (5.1%)- experienced anti-government demonstrations on a large scale.

**Figure 2. Real Economic Growth Rates in GCC Countries (Oman, Saudi Arabia, Bahrain, Kuwait)**



The economic prospects for the UAE are bright overall. It has been pointed out that the most powerful influences on the UAE economy at present are the US, European and Chinese economies (AI-Astad [2012]). Future developments in these overseas markets bear watching, but the UAE Ministry of Finance's economic forecasts project real GDP growth rates of 3.5% for 2012 and 4.7% for 2017.

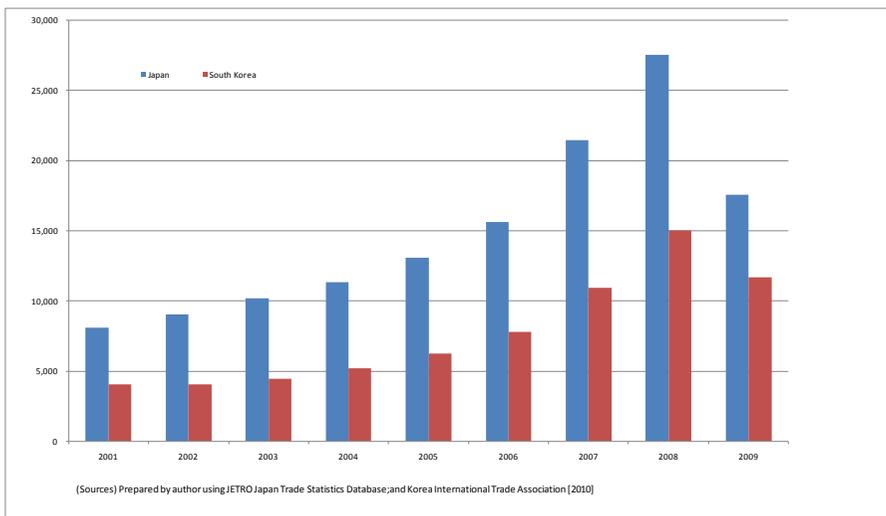
### **3. Japan's and South Korea's Contributions to the UAE Economy**

In 2010, Japan accounted for 16% of the Gulf Arab states' exports and 6% of their imports, while South Korea provided 10% of the region's exports and 4% of its imports. The two countries have become long-term trading partners for the Gulf Arab states, and about 50% of the GCC's trade surplus in 2010 was a result of trade with Japan and South Korea (*Arab News*, March 24, 2012).

(1) GCC countries and the UAE as export markets

The GCC countries, especially the UAE, continue to grow in importance as export destinations for Japan. Exports to the UAE totaled US\$2.57 billion in 2001, but this figure had expanded by 2011 to US\$7.44 billion. Although 44.5% of Japanese products exported to the GCC countries had been going to Saudi Arabia, in the mid-2000s exports to Saudi Arabia declined, with the UAE and other Gulf states expanding their product imports from Japan (Figure 3). The UAE's share of Japanese exports to the GCC countries climbed from 31.8 % in 2001 to 38.0% in 2011.

**Figure 3: Japan's and South Korea's Exports to GCC Countries (unit: million US\$)**



A breakdown of the goods exported to the UAE in 2011 showed US\$1.29 billion (17.4% of total exports to the UAE) in automobiles (gasoline-engine, larger than 3000 cc), US\$440 million (5.9%) in automobiles (gasoline-engine, 1500 cc-3000 cc), and US\$310 million (4.1 %) in trucks (diesel-engine, 5 tons-20 tons). Next among the principal export goods after these were automotive-related products and AV equipment (JETRO Japan Trade Statistics Database).

South Korea's share of total exports to the GCC is 3.2% (2009), not much different from Japan's 3.0% (2009). However, South Korea's exports to the GCC countries are increasing at an even faster pace than Japan's. Japan's exports to the GCC countries grew by an annual average of 12.5% for the period 2002-2009, but South Korea's grew by an average of 15.9% over that same period. The rates of increase for exports to the UAE were 15.2% for Japan and 17.5% for South Korea (both figures for the period 2002-2009).

South Korea's exports to the GCC countries jumped from US\$4.04 billion in 2001 to US\$11.7 billion in 2009 (Figure 3); exports to the UAE moved up from US\$2.17 billion in 2001 to US\$4.98 billion in 2009. This means that South Korea's exports to the UAE have expanded to about 80% of Japan's.

One characteristic of South Korea's exports to the GCC countries in recent years is the concentration of these exports in GCC countries such as the UAE and Saudi Arabia that have relatively large markets. The UAE claimed 42.5% of South Korea's exports to the GCC countries (33.0% went to Saudi Arabia) and 37.0% of Japan's. This emphasis on the UAE as an export market for South Korean products has been observed throughout the first decade of the 21<sup>st</sup> century; 53.6% of exports bound for GCC destinations went to the UAE (and 31.5% to Saudi Arabia) in 2001 and 43.9% (33.6% to Saudi Arabia) in 2005.

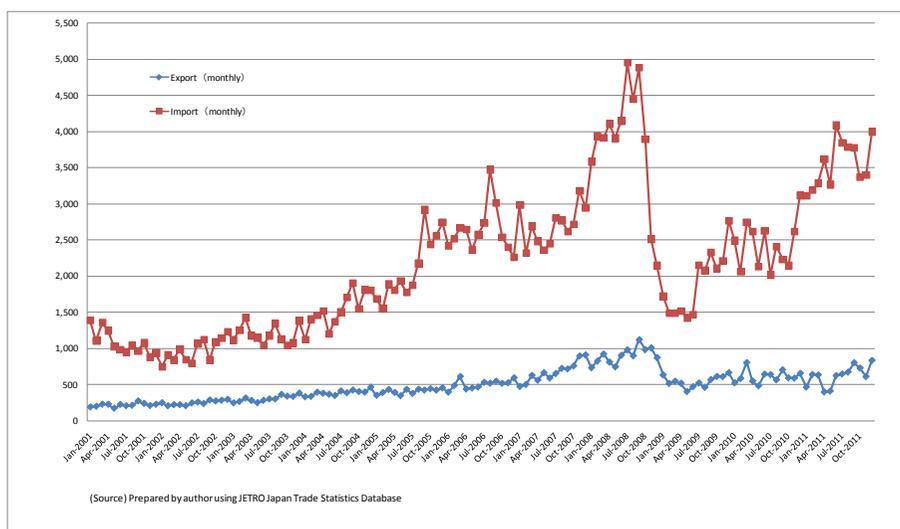
Another feature of South Korea's exports to GCC countries is the rapid increase over the past several years in automotive-related and nuclear power-related exports (Han [2012]). South Korean automobile exports to GCC countries expanded from US\$1.25 billion in 2005 to US\$4.03 billion in 2011, with the share of these exports among total exports to the GCC increasing from 20.1% (2005) to 23.3% (2011). Exports of nuclear reactors and machinery have expanded from US\$1.14 billion (2005; 18.3% of total exports) to US\$3.43 billion (2011; 19.9% of total exports).

Seeking to increase trade with the GCC countries, South Korea is currently engaged in negotiations with these countries on the conclusion of a free trade agreement. These talks have been underway since an agreement was reached in March 2007 on the need for concluding an FTA between South Korea and the GCC; the first round was held in Seoul in July 2008, the second in Riyadh in March 2009, and the third in Seoul in July 2009. The principal topics of discussion at the moment are South Korea's request that tariffs on automobiles, electric/electronic equipment, and iron and steel products be promptly lifted, and the GCC's request that tariffs on petroleum products and aluminum be abolished (Han[2012]).

## (2) Advent of the Arab Spring and Its Impact on Trade with the UAE

The changes over time in Japan's exports to the UAE show no apparent sign that exports to the UAE have significantly diminished following the Arab Spring (Figure 4). Japan's exports to the UAE did drop considerably in the wake of the international financial crisis triggered by the September 2008 Lehman Shock, but they have enjoyed upward momentum ever since. While there was a temporarily fall-off in exports when the Arab Spring occurred, the rate of decline was minimal compared to that seen during the international financial crisis, and exports have been steadily recovering.

**Figure 4. Japan's Monthly Trade with the UAE (unit: million US\$)**



Examining monthly exports from the UAE to Japan also reveals that the Arab Spring has had an insignificant direct impact on bilateral trade (Figure 4 ). The principal commodities imported from the UAE are petroleum (US\$33 billion in 2011, accounting for 77% of total imports from the UAE) and natural gas (US\$4.39 billion in 2011, accounting for 10% of total imports from the UAE), but it bears noting that re-import goods amounted to US\$49 million (2011, 0.1 %). Generally speaking, the UAE's primary re-export goods are pearls, diamonds, gems, precious metals, and machinery/audio equipment, with pearls, diamonds, gems, and precious metals making up 39.6% of the UAE's US\$50.5 billion in re-exports in 2011 and machinery/audio equipment 21.7%. The UAE's principal re-export destinations are India, Iran and Iraq, but re-exports to Japan have been on the rise in recent years.

Besides the UAE, Qatar and Kuwait also account for a certain share of

re-exports from the Gulf Arab states to Japan, and these re-exports, inclusive of petroleum and natural gas, rank among the top ten products exported to Japan. Many of the Gulf oil-producing countries with petroleum-/natural gas-related industries as their primary industries have had a particularly difficult time nurturing their manufacturing industries. Although the range of products-processed products such as pearls, diamonds, gems, and precious metals as well as machinery/audio equipment, etc.-is limited at the moment in the Gulf Arab states as they are still in the process of developing industrial bases for manufacturing, the export of manufactured products through re-export will help foster their manufacturing industries.

#### **4. Japanese and South Korean Corporate Activities in the UAE Market and Their Contributions to the UAE Economy**

The expansion of Japanese companies into the UAE has been in an uptrend since the turn of the millennium. According to Hosoi [2011], Japanese companies had 347 offices in the UAE in 2010, of which 110 were operating within Dubai's Jebel Ali Free Zone (JAFZA). With 153 corporate offices in Dubai outside JAFZA and 84 corporate offices in UAE emirates other than Dubai, Japanese companies in the UAE are clearly concentrated in Dubai.

It should be pointed out that the expansion of Japanese companies into the UAE has been extraordinarily dynamic compared to that into other Middle Eastern countries. Japanese companies in general do not appear to be overly enthusiastic about setting up operations in the Middle East. Japanese companies had 108 subsidiaries in the Middle East as of 2010, drastically lower than the 11,497 in Asia and the 2,860 in North America (Table 1 ). Given that the number of Japanese companies doing business in the Middle East numbered 63 in 2001, this increase has been quite slow.

**Table 1. Local Subsidiaries of Japanese Companies by Region**

	(number of subsidiaries)									
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
North America	2,596	2,663	2,630	2,743	2,825	2,830	2,826	2,865	2,872	2,860
Middle & South America	738	750	766	781	823	834	892	900	900	972
Asia	6,345	7,009	7,496	8,464	9,174	9,671	9,967	10,712	11,217	11,497
Middle East	63	67	71	72	76	76	83	97	99	108
Europe	2,147	2,246	2,332	2,368	2,384	2,405	2,423	2,513	2,522	2,536
Oceania	456	456	460	449	446	430	413	435	456	481
Africa	131	131	120	119	122	124	128	136	135	145
BRIC s	na	na	na	3,064	3,502	3,899	4,196	4,684	5,010	5,175
<b>TOTAL</b>	12,476	13,322	13,875	14,996	15,850	16,370	16,732	17,658	18,201	18,599

(source)Ministry of Economy, Trade and Industry,JAPAN

South Korea's direct investment in the GCC countries in 2010 was US\$190 million, a mere 1% of South Korea's foreign direct investment. South Korean investment in the GCC countries begin in 1974 with a project to build a highway in Saudi Arabia, and the focus since has been on expansion through infrastructure construction projects such as those in Kuwait (1975), Qatar (1976), and the UAE (end of the 1970s). A breakdown by industry of South Korea's investment in GCC countries in 2010 shows that 30% has gone to electricity, gas, water and other public works, 28% to manufacturing, 20% to construction and 12% to real estate. The Gulf Arab states have become the largest overseas markets for engineering, procurement and construction (EPC) in South Korean plant construction (Han[2012]); more than 60% of South Korea's overseas EPC contracts are with Gulf Arab states. According to 2010 data, the UAE is responsible for US\$24.35 billion (37.7%) of these overseas EPC contracts, Saudi Arabia US\$9.41 billion (14.6%), and Kuwait US\$2.6 billion (4.03%). South Korean companies have reportedly acquired a nearly 50% share of the EPC market in the Gulf Arab states (Han [2012]).

An UAE market analysis conducted by an investment company in Dubai has determined that South Korean companies are looking beyond the UAE's infrastructure/construction industry and eyeing future development in (1) the financial market centered on private banking and (2) the medical and educational

industries (Chang [2012]). Qatar, Kuwait, and the UAE have a high percentage of households with considerable personal assets and European banks also see this region's private banking market as attractive. The medical and educational industries form the core of social welfare and social infrastructure, and the expansion of companies in these sectors can be expected to contribute to the local economy and society, given the nature of these industries to improve social security and social development.

## **5. Conclusion**

This paper has endeavored to examine trends in the South Korean economy and among South Korean companies that have continually boosted their presence in the Gulf Arab countries, especially in the UAE, in recent years. South Korea's economy resembles Japan's in that its strength lies in manufacturing. There are numerous other similarities in their trade relations with the Gulf Arab states, characterized by a trade pattern of exporting automotive and machinery products to the Gulf Arab states and importing petroleum and natural gas. The key issue that this paper has sought to address is the reason behind the remarkable growth achieved by South Korean companies in the Gulf Arab states compared to their Japanese counterparts despite these similarities.

Although separate consideration should be given to the need for a more detailed study of the behavior of South Korean companies, the characteristics of South Korean companies doing business in the Gulf Arab states could be summarized as follows: (1) South Korea's trade with the Gulf Arab states disproportionately emphasizes the UAE, (2) South Korean companies have put the greatest emphasis on Gulf Arab states as target EPC markets for overseas plant construction, and (3) South Korean companies see the financial sector and the medical and educational industries as their next markets for development.

Japan could contribute to the UAE economy by (1) ensuring that the UAE's

financial base remains as stable as before through petroleum and natural gas imports, (2) providing further technical assistance pertinent to machinery/audio equipment, a key re-export commodity, and thereby increase exports to Japan in order to support the development of manufacturing in the UAE and other Gulf Arab states, and (3) expanding into overseas plant construction, finance, education and medicine, which are promising sectors within the UAE market, in order to promote the growth of these industries in the UAE.

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