

## The Dubai Challenge

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In the past few months, the state capitalism of emerging countries has caused increasing nervousness. Whether practiced by state-owned companies or sovereign wealth funds, it has triggered defensive reactions everywhere in the western world. But fear is bad council. Rather than closing one's mind, it would be preferable to try to better understand what exactly is at stake.

Two facts to begin with. First, there is no observable trend towards statism in economies where market capitalism has strong roots. On the contrary, what we see is countries whose economic system was nationalised or underdeveloped or both, and which are now integrating fast with the global marketplace. Private-sector capitalism is increasingly vigorous everywhere, including arguably in Russia. Second, the strategies of the new "state capitalists" are many and various, and they are not always consistent. City states have different priorities from superpowers. In each country concerned, investment strategies are vividly fought over, in particular between those who would prefer to invest the state funds at home and those who wish to see the money used for acquisitions abroad.

Forty years ago, Jean-Jacques Servan-Schreiber published the best-selling *American Challenge* and noted that 'this challenge is not essentially industrial or financial. It calls into question above all our intellectual fertility and our ability to turn ideas into reality.' Similarly, if state capitalism is destabilising the global environment, it is not primarily on account of its financial clout. After all, many western banks manage more assets than the Abu Dhabi Investment Authority, the largest recorded sovereign wealth fund. What creates unease is the feeling that the emerging state operators are more agile than Western counterparts because they are less hamstrung by governance, financial and democratic constraints. The old 1970s metaphor was 'no worries if they have the oil and we have the ideas', but it all changes when those who have the oil (or macroeconomic surpluses) also have the ideas. This was the core of the 'American challenge' in 1967, and is also at the core of the new challenge which the western world, including the US, is faced with today.

The Emirate of Dubai, through its dynamism and the speed of its arrival on the international scene, is perhaps the most prominent emblem of this new challenge. The complex deal which it embarked upon last month, when it became at a stroke the largest shareholder in the Nordic exchange OMX, the London Stock Exchange and Nasdaq, sums up the ambitions of Sheik Mohammed Al Maktoum. According to a close adviser quoted by *BusinessWeek* magazine, 'his main concern is making sure this city competes quickly with New York'. Dubai is well positioned. Closer to Karachi than to Baghdad or Mecca, and closer to Bombay than to Damascus or Cairo, this former pearl divers' port ambitions to be the hub of the huge area stretching from Europe to the Indochinese Peninsula. It already is for air travel and sea transport. It may become so for finance.

By becoming overnight a force to be counted with in the global stock exchange business, Dubai is building up an infrastructure centered on brands, technologies and skills: a sort of intangibles-based industrial policy. The cultural shock is contained by the fact that Dubai will retain only minority stakes. And stock exchanges are only one part of the game. Dubai has also convinced most western investment banks to choose it as their launchpad in the region. It seeks to attract global headquarters of companies such as Halliburton, which this column focused on in April.

Success is far from guaranteed. There can be doubts as to the sustainability of a global financial centre without deep historical roots. The previous steps have not been without setbacks. In 2004, a reform of local financial regulation was harmed by the impact of doubtful property transactions. Political risks are high, too. Last year, Dubai Ports World met the opposition of Congress following its purchase of US ports, which it has later had to resell. But the audacity of Dubai's endeavour remains arresting, and it cannot be easily discounted.

How should the West react? In 1967 Servan-Schreiber noted that 'nothing would be more absurd than picturing US investment as a culprit and opting for a repressive response'. The contest cannot be won by ducking the race. To meet the Dubai challenge, developed countries must show as much inventiveness, boldness, analytical rigour, global outlook, technological vision and speed of execution as the best of the emerging players. A demanding programme, but by no means impossible.

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