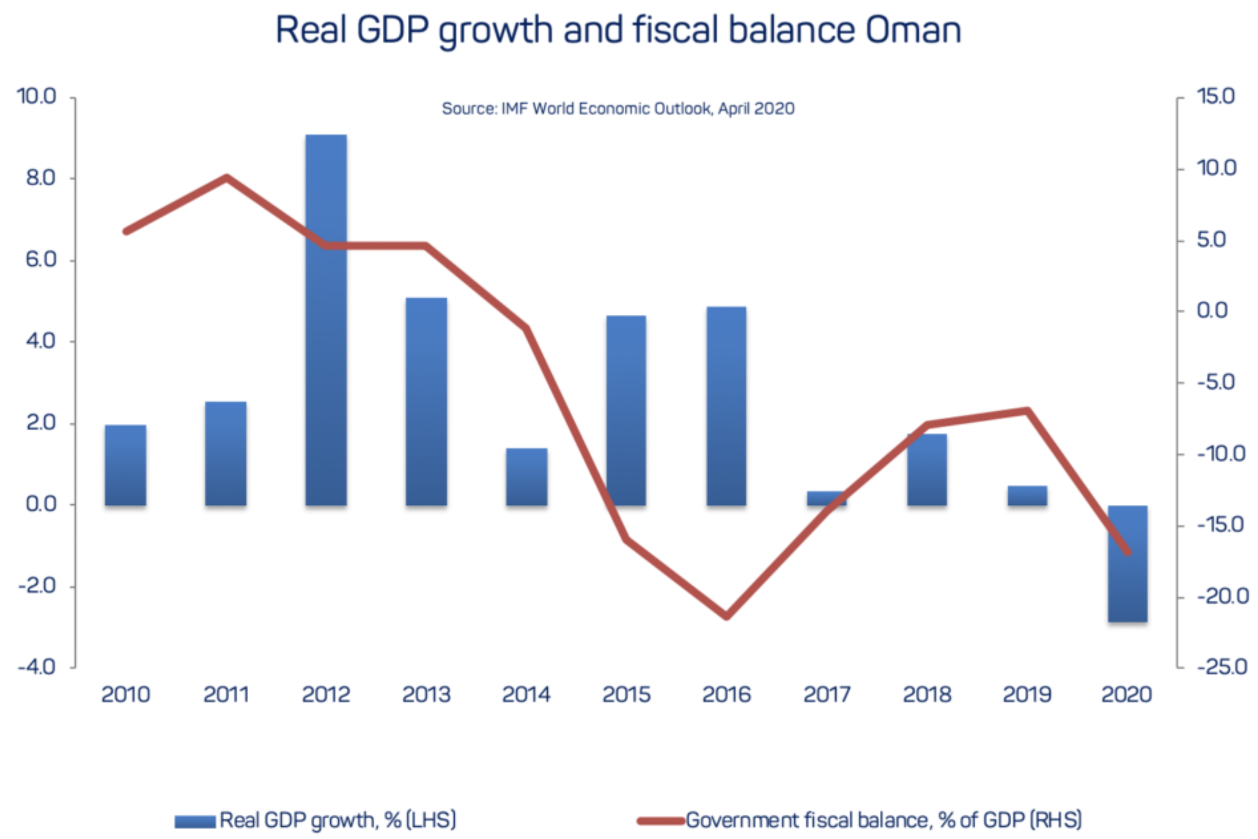
The severity of the economic challenge facing Oman will persist long after the COVID-19 pandemic has receded, requiring the country to rethink its long-term approach to economic development. Vision 2040 remains a top priority for the leadership under Sultan Haitham but with insufficient funds to carry out legacy spending commitments, it will have to rely upon the private sector to drive diversification. This means we could see an acceleration of reforms to attract investment, including further dismantling of foreign investment restrictions, privatisation, closer ties with China and a new tourism strategy.

The challenging new normal for Oman’s economy

Oman’s economic growth model was already on shaky foundations going into 2020, and the double whammy of the virus and the oil price collapse has brought forward an economic reckoning.

The IMF forecasts that Oman will experience its worst recession in over two decades this year, with growth will remain stuck in a low gear thereafter. With oil prices expected to remain low over the coming years, the main driver of Oman’s economy will stagnate. Meanwhile, the non-oil economy will take years to recover from the surge in bankruptcies accompanying COVID-19.



New reality will require new strategy

This more challenging environment will force Oman to adapt its long-term economic strategy. A prolonged economic slump would risk a resurgence of the large-scale protests that occurred in 2011 and, to a lesser extent, in 2018.

After succeeding Sultan Qaboos bin Said Al Said in January, Sultan Haitham bin Tariq Al Said has promised policy continuity, including a reaffirmed commitment to Oman’s Vision 2040 programme, which seeks to diversify the economy away from oil and towards non-oil sectors such as manufacturing, logistics and tourism. However, structurally lower tax revenues in Oman mean that the government will have insufficient funds to carry out legacy spending commitments that form part of Vision 2040.

The IMF forecasts a significant widening of the fiscal deficit this year and next, and the government’s ability to fund deficits through borrowing is deteriorating. Despite a 10% cut to 2020 public spending commitments since the start of the year, Oman’s credit rating has sunk to sub-investment grade or “junk” status, according to all three major ratings agencies. Oman’s Vision 2040 will thus have to rely more on the private sector to invest in diversifying the economy over the coming years.

Potential routes for attracting foreign capital

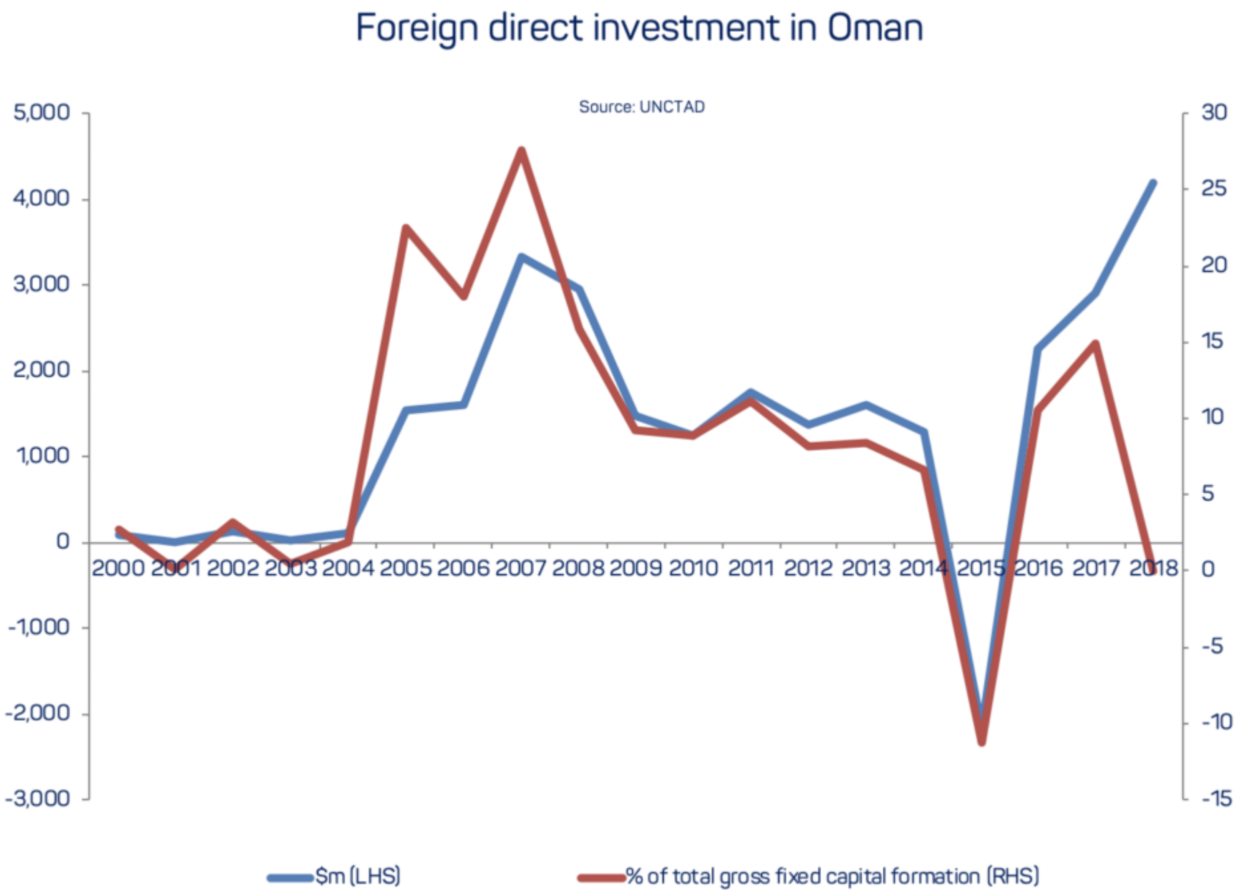
There are several potential routes for attracting more private investment into Oman’s economy, some of which are already being partially utilised. Some key potential strategies include the following:

Relaxing foreign ownership restrictions: Attracting more private capital will require greater incentives for foreign investors. There is already strong momentum for relaxing restrictions on foreign ownership, which is a more feasible carrot for the government to provide than generous subsidies and tax breaks. In January a new Foreign Capital Investment Law allowed 100% foreign ownership in a raft of previously restricted industries including defence, oil and gas, and restaurants. Further liberalisation could include 37 industries still barred from complete foreign ownership, such as transportation, vehicle repairs, recruitment services, fishing and social care.

Privatisation: The existing trend of divesting state assets will likely be ramped up. Significant progress has already been made, with the government selling a 49% stake in the state-owned Oman Electricity Transmission Company to the State Grid Corporation of China for $1bn in December last year. In addition, Oman is reportedly considering privatising Muscat International Airport. Future infrastructure development could also be partially privatised through public-private partnerships such as the proposed Salalah–Thamrait truck toll road. The oil and gas sector would be the largest opportunity for privatisation, and although the government would ideally wait for a recovery in hydrocarbon prices before selling any assets in the sector, near-term financing challenges may force privatisation sooner rather than later.

Deepening ties with China: A significant slowdown in Chinese economic growth this year, combined with deteriorating Sino-Western relations, will see China engage in more targeted foreign investment in the coming years. Nonetheless, Chinese investment into Oman could be forthcoming in return for subsidised energy and manufacturing exports. This could include petrochemical products from the Duqm refinery and petrochemical complex, and natural gas from the Khazzan-Makarem field.

Relaxing tourism restrictions: A collapse in tourism arrivals due to COVID-19 could prompt a rethink of Oman's tourism strategy. Over the past decade the country has targeted the luxury tourism market as a way of maximising revenue and minimising disruption from foreign visitors. However, as international tourism volumes will take years to recover from the pandemic, Oman may seek to save the sector by opening its hotel, hospitality and tourism industry to investment from more mass-tourism-focused firms.



Omanisation an obstacle to investment

A requirement for firms to increase employment of Omani nationals, known as Omanisation, will be a significant brake on foreign investment in the country. In line with wider employment trends in the Gulf, this year's economic shock has encouraged the government to accelerate Omanisation of the economy. This is a way of making the private sector pay for social subsidies that the government is now less able to provide.

However, given the scarcity of local skilled labour, this policy will raise costs for foreign businesses operating in Oman and make investment less attractive. In April the finance ministry gave public sector companies until July next year to draw up timetables to appoint Omanis in the place of foreign staff, including in managerial positions. Restrictions on private sector hiring of foreign nationals, who make up more than 40% of Oman's population, will also likely be tightened.

Seeking regional assistance to be a last resort

The desire to maintain Oman's longstanding foreign policy independence means that foreign financial assistance will likely only be sought as a last resort. Oman has kept the IMF at arm's length in recent decades and has not accepted financial aid from wealthier GCC neighbours since the Arab Spring in 2011. Such independence has allowed Oman to maintain strong diplomatic and economic ties with both the GCC on the one hand and Qatar and Iran on the other.

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