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Global Financial Crisis and Its Impact on the Economy of Oman

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Abstract: The effects of the financial crisis in America, which happened to be spoken as one of the most advanced countries, spread from there to the other countries of the world and none were spared of its effects. For some of the countries, the effect was immediate whereas in some much smaller countries the effect was slow to come. One of the countries that have been lately affected by this is the Sultanate of Oman. This is a small high income economy that is highly dependent on its oil resources. It is a small member of the OPEC (Organization of Petroliam Exporting Countries) oil-cartel with a share of only 0.4% of the world's proven oil stocks and 1% of the world production according to the EIU (Economist Intelligent Unit), CIA (Central Intelligence Agency) World fact book. This reflects the needs for carrying out policy changes in order to increase its exports and imports as well as to adopt measures whereby a diversification should be seen on its sources of revenue. Effective trade policies which shall include Omanization, promotion of the tax policy and improving both the SME (Small & Medium Enterprises) as well as the tourism industry shall help in the long run to nullify or reduce the negative impacts of the crisis. Further, if modernization in the existing political system is brought about and the investment by other countries, along with promotion of its own cottage industries like production of the Omani Halva, Date processing and Oudh and Frankincense export increased little if not much can help achieve to turn around the present scenario. Although, there is huge number of published researches in global crisis, little effort has been undertaken to study the impact of global crisis in Oman. In view of this, the main purpose of this paper is to illustrate, using empirical evidence, the extent to which the global crisis has had an impact on the performance of Oman. The aim of this study is to highlight; 1) The impact of global crisis on the various sectors of the Sultanate of Oman. 2) The extent to which Sultanate of Oman was affected by the global crisis. 3) Measures to overcome the crisis. The data used to answer these aims include all relevant statistics related to Oman. It is concluded that with the decline of the oil prices, the Sultanate was the first in the Gulf to address its negative repercussions, taking a series of measures to cut costs, restrict subsidies to its citizens, and raise the price of water, electricity, and other public services. Oman's adoption of cost-cutting programs as well as its use of external loans to address the national deficit are not new strategies and have been adopted by other Gulf States as a response to the oil slump. The study can be extended in future by investigating the banks and other non-bank financial institutions of the country to examine and document the overall effect of crisis on financial system of Oman.
Keywords: Global crisis, Omanization, OPEC, GEC, Diversification.

INTRODUCTION

The dawn of the year 2008 brought with it the most dangerous crisis since the great depression of the year 1930. This depression led to the increase in prices in the US which further spread to all the financial markets overseas as well. The depression affected the banking industry, the biggest insurance companies, and the enterprises. The global economic crisis was caused by the coming together of several structural as well as business cycle factors that conspired to produce a "perfect storm" of epic proportions. These factors ranged from the collapse of the housing market in the United States, imbalances between the West and the East in terms of trade deficits, reckless and risky speculation and finally, the sovereign debt crisis that was a culmination of years of fiscal profligacy and loose monetary policies. Nowhere was this more apparent than in the aftermath of the collapse of Lehmann Brothers when the entire credit system froze and the global financial system came perilously close to collapse [1].

The global economic crisis basically originated in the West but had its effects on all economies of the world. Of course, the US and the Europe were the primary victims of the crisis and it can be said that the Asian countries were relatively unscathed in the wake of the crisis. However, this is not to say that these countries have successfully “decoupled” from the west since the tightly knit global economy and the dependence of China on exports to the US for goods and India for services means that these countries have a fair amount of work to do before they can be called safe. The point here is that the United States and Europe were badly bruised by the crisis and it is still not clear when these countries and their economies would be out of the woods, if at all they would.

Although the financial crises wore a distinct mark of a ‘Made in USA label’ it did not stop there but spread to other countries as well. One of the countries that have been lately affected by this is the Sultanate of Oman.

Oman is a small country located in the far southeastern part of the Arab peninsula which is full of marvelous natural wonders and architectural beauty. Once ruled by the Omani Al Said Family it is now ruled by HH Sultan Qaboos Bin Said who took office as the official ruler on the 23rd of July 1970. According to the global terrorism index, Oman is said to be one of the safest and most secure countries in the Arab world. When looking at the map of Oman, it looks like a small peninsula surrounded by water from three different directions. However it has been said that humans have lived here for more than 106,000 years making it one of the oldest inhabited countries of the earth [2].

With the view to considering the effects of the global crisis on Oman we can say that the monetary policy flexibility is limited because the Omani Rial is pegged to the US dollar. That being said, the peg has provided a stable nominal anchor for the economy, particularly as contracts for oil, the main export, are typically priced in dollars. According to an article in the Times of Oman written by Christopher Smart on November 13, 2017 Oman’s real effective exchange rate has appreciated by 12% since early 2014. This represents deterioration in international competitiveness of the country’s most tradable sector which is likely to dampen non-oil GDP growth due to the absence of factors, such as improved efficiency or technological capacity. All this comes at a time in which Oman is facing its own financial crisis. Oman’s large youth population will be a key determining factor in any succession crisis, yet in a post-Arab Spring Middle East, hostility to established powers remains a key element among the region’s youth.

Oman Economy – At a glance

Strengths	**Weaknesses**
• Abundant energy (oil and gas) resources. • Strategic location on the Straits of Ormuz and closeness to Gulf, Asian and African markets. • Comfortable foreign exchange reserves (import cover of 8 months) as well as assets in the sovereign wealth fund. • State commitment to industrialization, economic diversification and development. • Modern infrastructures (roads, airports, sea ports, telecommunications).	• Sultan Qaboos does not have an heir and the succession process is opaque. • Energy dependence (oil and gas represent almost two thirds of export earnings) while proven reserves have a limited time horizon (15 years). • Closeness to regional conflict (Iran, Yemen) • Export dependence on China which accounts for 39% of total Omani exports (a rebalancing in China could have adverse effects on Oman’s trade balance).

The performance of companies in the Omani services sector and the behavior of stock price between the period before, during and after financial crisis had caused changes in many branches of economy, where, it impacted economic growth and asset prices which in turn led to growing concerns about the deceleration in economic growth. In Sultanate of Oman, the monetary and financial sector was characterized by high growth in money and credit, which reflected the fast expansion and strong economic growth. From other side, financial crisis resulted in downward trends in oil prices and significant deceleration in global demand conditions, and the crisis prompted a decline in the price of gas. Also, the influence of economic slowdown and rising unemployment started to affect the economic outlook of the sultanate. It is expected that MSM (Muscat Securities Market) of Oman will also reflect impact of global financial crisis.

The aim of this study is to highlight

- The impact of global crisis on the various sectors of Oman
- The extent to which Oman was affected by the global crisis.
- Measures to overcome the crisis.

REVIEW OF LITERATURE

1. Compounded by participating in OPEC oil production cuts in 2017, protracted low oil prices and fiscal austerity continue to weigh on Oman's economy. Fiscal and current account deficits remain large, and with Oman increasingly resorting to external borrowing to finance its deficits, public debt is rising rapidly. However, growth is expected to pick up over the medium term following a boost in oil and gas, and from expected gains in the non-oil sector resulting from the government's economic diversification plan. (October 2017 – Reese Erich - Oman's Economic Outlook) [3].
2. With the tumbling down of crude oil prices of around 70% over the past eighteen months the profits for the world's top oil companies have declined. In Oman and most of the Gulf countries crude oil prices have dropped around 40% from their peaks of last year. The Petroleum Development of Oman has noted that many oil companies are not digging new wells and workers are laid off. In this situation Omani government received $3.45 billion from oil sales in the first quarter of this year which is less than last year by 35%. (Zuwaina Al Daraar – How low oil prices have shaken Oman's economy) [4].
3. According to Stand & Poor's rating the decline in oil prices will have a significant impact on Oman's economic and fiscal indicators due to its high dependence on oil. It also forecasted that Oman's GDP will fall in 2016 when compared to that of the year 2014 while the annual average increase in general government debt will be about 5% of GDP in 2016 when compared to the year 2019. (Standard & Poor's ratings – March 3, 2016 – "Decline in oil prices will have significant impact on Oman's economic and fiscal indicators") [5].
4. The Yemen war and with Oman agreeing to Saudi led coalition against terrorism lead to many security concerns. Though Oman is playing a proactive role since it is supplying basic necessities and consumer goods over the border as opposed to accepting refugee, this still had both its positive and negative effects. Though it gained because of the increased supply situation it has had to increase the cost on border security. The problem has come at a time when Oman itself is facing financial difficulties. Oman's expenses will only continue to rise and this is a significant problem as military spending already accounts for 11.5% of the GDP. Moreover the recent agreement among the OPEC and non-OPEC members to cut production with the view to increase the prices of oil has had both its advantages and disadvantages. The fact that Sultan Qaboos the present ruler not having a natural heir to the throne is also likely to bring with it heavy repercussions. (Jeremy Luedi – Impact on low oil prices - January 17, 2017) [6].
5. Crude oil prices in the Gulf have dropped about 40% from their peak last year and countries like Oman have seen their government budgets squeezed and workers laid off. Worker contracts have not been renewed and the contracts aren't as well. This year's budget has seen a cut in public spending of around 25% in defense spending and 48% slash in subsidies and social welfare. According to Sadeq Sulaiman, a former Omani ambassador to the US in Muscat a massive 77% of Oman's budget comes from oil revenue and this should change which can be done by diversifying the economy to become less dependent on oil. It was also according to him specified that there should be a change in the educational system which does not seem to be doing very well. (Reese Erlich – June 5, 2015) [7].
6. Oman is a small high income economy that is heavily dependent on oil resources. It is a small member of the OPEC oil-cartel with a share of 0.4% of the world's proven oil stocks and 1% of world production. Aware of the dwindling oil reserves the government actively pursued a development plan that focuses on industrialization, privatization and diversification away from oil. Agriculture is not a priority in terms of diversification effort. However among other services tourism is being promoted and is a successful key component of the diversification strategy. (Country report on Oman – Leendert Colijn – Economic research department – Rabobank) [8].
7. As Oman's oil reserves dwindle, the government is using enhanced oil recovery techniques to boost production, but it also is focusing on fiscal reform and economic diversification to reduce the country's heavy reliance on hydrocarbons. With businesses frequently complaining about bureaucracy and a cumbersome regulatory environment, the government plans to reduce red tape to attract investors. Other obstacles to economic freedom include a weak legal framework and subsidies and other forms of favoritism to state-owned enterprises. (2018 Index of Economic freedom) [9].

8. The GCC countries performed well during the 2003–08 oil boom, but the boom also presented challenges. Buoyant economic activity, rising consumer and investor confidence, and abundant liquidity spurred excessive credit growth, inflation, and asset price increases. In addition, in some countries, banks' growing dependence on foreign financing and exposure to real estate, construction lending, and—to a lesser extent—the equity market, contributed to balance sheet vulnerability in the event of a slowdown in economic growth and a decline in asset prices. In the corporate sector, the boom was associated with higher leverage, which increased the sector's vulnerability to the availability and cost of financing. (Impact of the Global Financial Crisis on the Gulf Cooperation council countries and challenges Ahead – An update – May Khamis and Abdelhak Senhadji with contributions from Joshua Charap and Serhan Cevik – International Monetory fund, 2010 publication) [10].
9. (Mazhar M. Islam, 2003) mentioned in his paper that Oman is a free market economy, with low taxation levels, fairly liberal investment laws and no control on capital movements and is a member of the Arab Gulf Co-operation Council (GCC). The economy is managed through a series of plans emphasizing agriculture and industrial development. However, Oman remains heavily dependent on its oil revenues. Oil revenues also drive economic activity in the non-oil sectors. The government recognizes the need to diversify the economy away from oil as rapidly as possible and its vision 2020 plan aims to reduce the oil sector's contribution to less than 20% over the next two decades. (The impact of International Financial Crisis on the efficiency of Omani Banks' Performance: An empirical study – June 2014 – Zaroug Mohamed) [11].
10. As of August 2008, oil prices plunged rapidly as demand from the Organization for Economic Co-operation and Development (OECD) countries came to a sudden halt and recession loomed as the financial crisis severely impacted the global economy (IDS, 2008, p. 5). In an attempt to curb falling prices, the Organization of Petroleum Exporting Countries (OPEC) introduced a series of cuts in output. However, even if that demand is expected to increase, it will not be sheltered from the consequences of the global economic turmoil, as it is forecast to grow at a slower pace over the short-to-medium term. Broadly speaking, growing oil demand in developing countries has recently been driven by two major components, namely increasing demand in both China and India and Arab oil-exporting countries. Hence, the extent to which oil demand in developing countries will be impacted largely depends on the underlying elements in each of the abovementioned components. This will translate into lower demand for oil: Arab oil consumption grew by 3 per cent in 2009 and 2010, from 5.4 per cent in 2008. (The impact of the Global Financial crisis on the world oil market and its implications for the GCC countries) [12].
11. The global crisis was transmitted to Arab economies through several distinct channels: the financial markets, the crude oil market, Arab investments in global asset markets, tourism, the remittance income of Arab workers, and the region's non-oil exports, originating primarily in North Africa and destined for Europe. Financial institutions and real estate developers are among the largest publicly listed companies in Arab markets, and both were adversely affected by the global financial crisis. The global crisis sharply reduced the flow of foreign investment into real estate; the global recession led to a decline in the demand for crude oil, which triggered a sharp decline in its price. Moreover there was the decline in value of the foreign assets of GCC countries. Depending on their exposure to each of these transmission channels, different Arab countries were impacted differently by the crisis. (The Impact of the Global economic crisis on Arab countries – A year end assessment – Professor Nader Habibi – December 2009) [13].
12. The decline in oil prices since late 2014 has created a changed policy environment for oil exporting countries, particularly those of the Gulf Cooperation Council in which structural reforms are being made. There has been the introduction of subsidy reforms and subsequent increase in the price of fuel, electricity and water across the GCC states. (Article Prioritizing renewable energy in a time of fiscal austerity – Karen E. Young) [14].

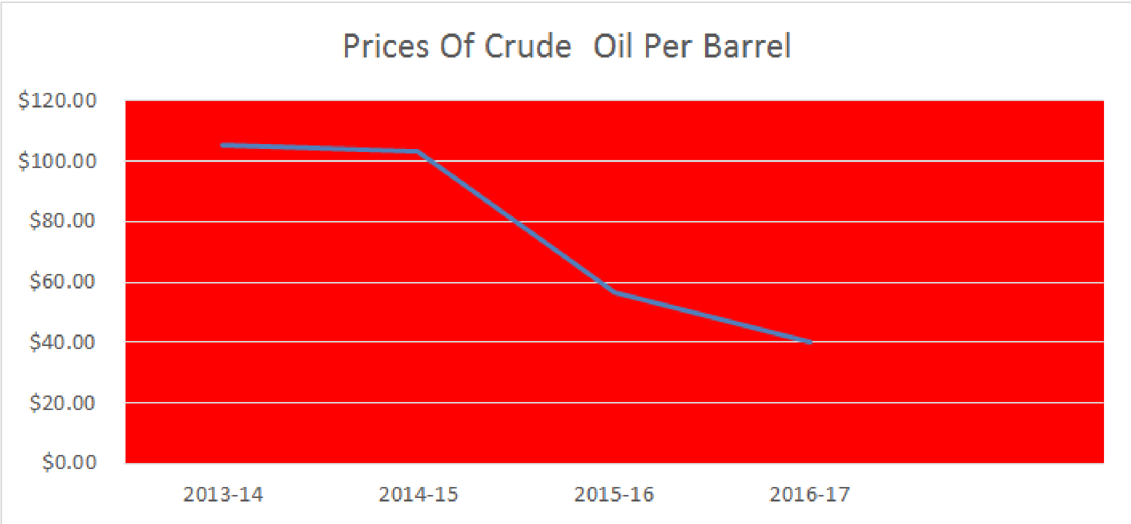
THE IMPACT OF GLOBAL CRISIS

The crisis, which influenced the whole world in 2008, affected Oman economy, which has leaped forward in economy during the recent years. For the reason that prices of natural resources, which are the driving force behind this country development, decreased during violent days of crisis and failed to satisfy the growth rate. Although Oman experienced this crisis lighter than the other countries which felt it deeply, its economy which has made a big development during the recent times was interrupted. The global economy has suffered a "Big bang" of synchronized shocks. The crisis which started in the US was transmitted to the GCC (Gulf Cooperation Council) through a contraction in global economic activities and the decline in oil prices, plunging asset prices and financial deleveraging. The external shock has also exposed domestic financial sector vulnerabilities arising from rapid credit growth. The forthcoming sessions highlight the impact of crisis, both negative and positive effect in Oman.

Negative Effect of the global crisis in Oman

Continuing low oil prices – With prices falling Oman is hit hard as 77% or two thirds of the country's budget depends on oil revenue. The IEA (International Energy Agency) has further warned that another sharp fall is possible. A low price of oil has badly affected the balance of trade position of the country over the period of years [15].

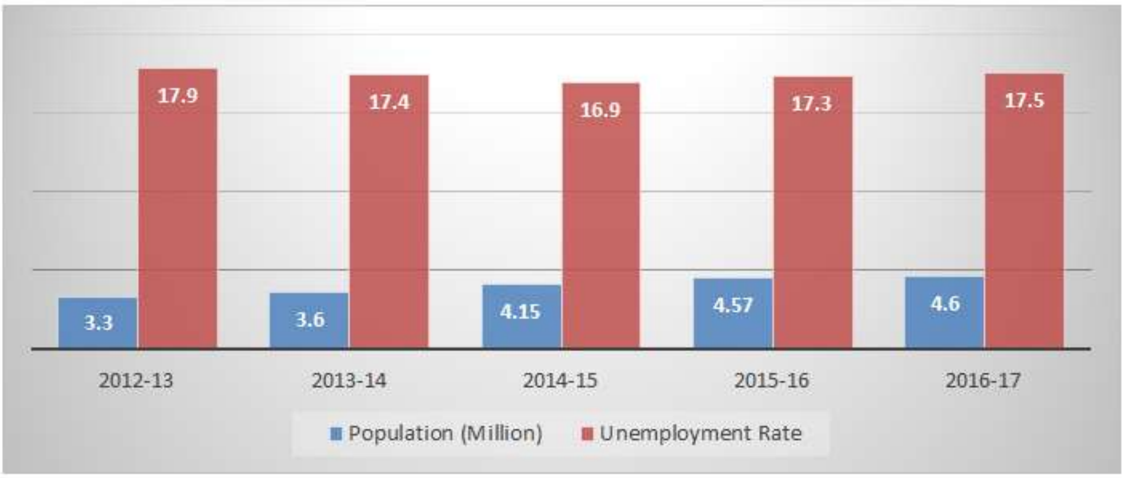
Year	2012-13	2013-14	2014-15	2015-16	2016-17
Prices Of Crude Oil Per Barrel	$109.61	$105.51	$103.23	$56.45	$40.14



(Source: Ministry of Oil and Gas and National Centre for Statistics and Information)

Rising unemployment due to the fact that the prices of oil are dropping and the oil exploration and drilling companies do not want to dig for new wells and hence the existing workers have to be laid off thus facing unemployment. The labour contracts which used to be previously renewed automatically are now not being done as new contracts for oil are not forthcoming. A direct effect of the global slump on the economic activity of developed countries and the diminishing house hold purchasing power resulting from rising unemployment as well as added uncertainty about the future [16].

Year	2012-13	2013-14	2014-15	2015-16	2016-17
Population (Million)	3.3	3.6	4.15	4.57	4.6
Unemployment Rate	17.9	17.4	16.9	17.3.	17.5



(Source: - Reese Erich - Oman's Economic Outlook - October 2017)

Trade Balance

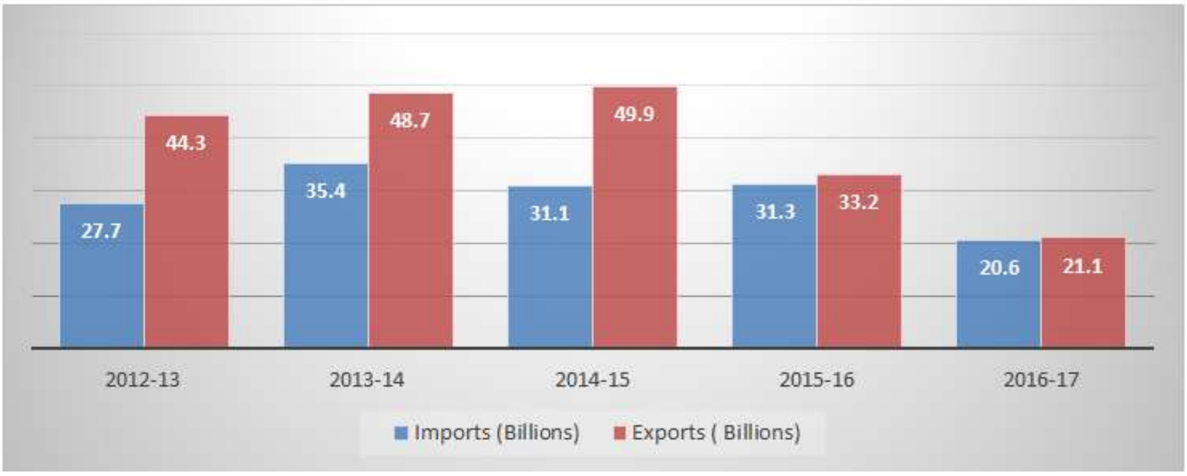
The trade balance for Oman is calculated as the difference between the exports and imports of goods and services, as percent of GDP. A positive number means trade surplus and a negative number means trade deficit [17].

Year	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**
Trade Balance (Billions)	16.6	13.3	18.8	1.9	0.5

(Source: - Reese Erich - Oman's Economic Outlook - October 2017) https://www.focus-economics.com/countries/oman

Trade balance of the country is decreasing sharply from 2014-15 to 2015-16. It must be further stated that though it appeared that the imports of the country was reducing over the years, so did the exports which also complemented to the adverse effect over the years till the period of 2016-17. There was a reduced demand for exports and also fluctuations in the foreign exchange reserves have not been favorable [18].

Year	**2012-13**	**2013-14**	**2014-15**	**2015-16**	**2016-17**
Imports (Billions)	**27.7**	**35.4**	**31.1**	**31.3**	**20.6**
Exports (Billions)	44.3	48.7	49.9	33.2	21.1



(Source: - Reese Erich - Oman's Economic Outlook - October 2017)

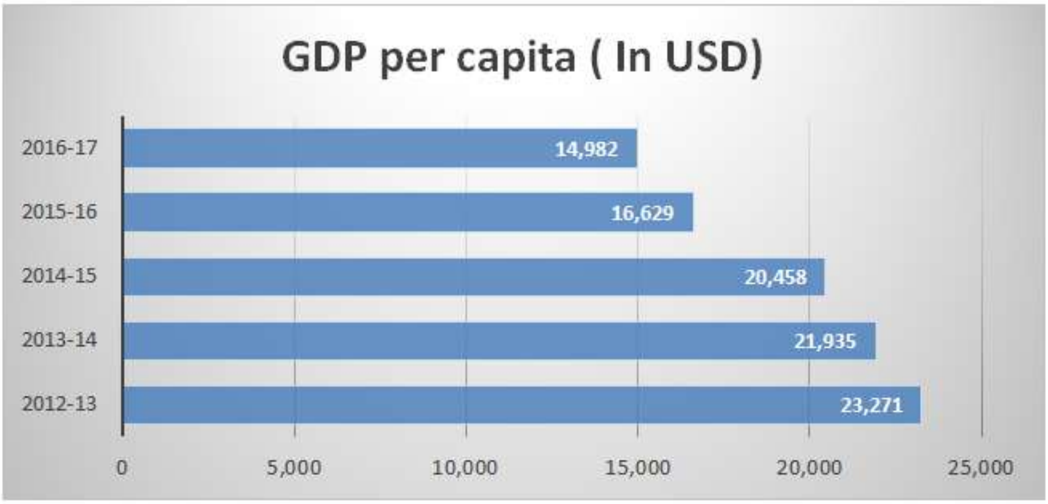
Slashed public spending

Previously when the economy was booming the government spent freely on subsidizing of gasoline as well as in social spending to appease the Arab Spring demonstrations. The decline in public spending may also mean a reduction in investment expenditure which constituted roundly one third of the total budgeted public expenditure. The government spending on the defense of the country has been slashed by 25% and public spending has been done so by 50%. The crisis will affect the middle class the most because the rich can easily survive with what they have [19].

Decrease in GDP per capita

It will lead to fewer projects in both the private and the public sector which could lead to less profit and has been the cause of the overall decrease in the GDP over the years [20].

Year	2012-13	2013-14	2014-15	2015-16	2016-17
GDP per capita (In USD)	23,271	21,935	20,458	16,629	14,982



(Source: - Reese Erich - Oman's Economic Outlook - October 2017)

The crisis has affected indirect financing, whether funded by local banks – which have become more reluctant to lend – or by foreign banks, with limited lines of credit. This has further led to the decrease in trade over the years.

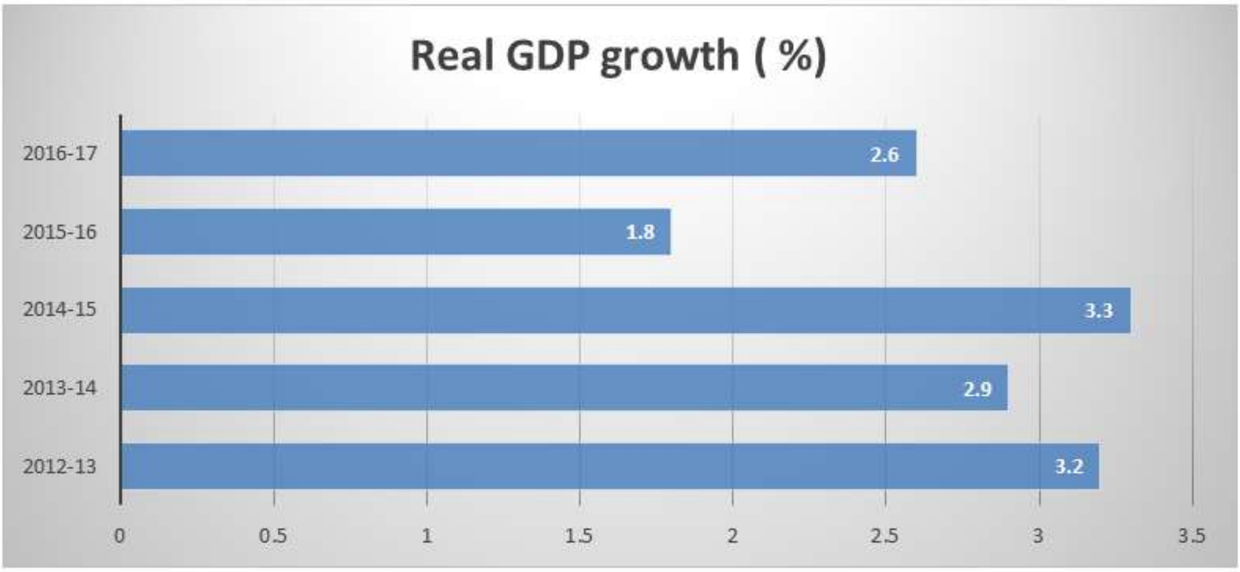
The real estate markets have also been hit. Real estate transactions dropped sharply in the past year, a housing ministry report has revealed. Real estate transactions worth OMR 2.6 billion were recorded in 2017, which was a drop of 61 per cent, compared to transactions in 2016. Realtors have put this down to the fact that buyers continue to wait and watch [21].

Positive Effects of the global crisis in Oman

Increased pressure to diversify the economy

With the increased diversification the world integrated trade solutions statistics has shown that Oman country growth v/s world growth v/s GDP growth which after a fall in the previous years is now slowly showing a tendency to rise because of the measures taken [22].

Year	2012-13	2013-14	2014-15	2015-16	2016-17
Real GDP growth (%)	3.2	2.9	3.3	1.8	2.6



(Source: - Reese Erich - Oman's Economic Outlook - October 2017)

The Oman government now learning from its past ups and downs of the oil prices have decided to as the proverb goes 'Make hay when the sun shines" and store the money for the dark days when the oil prices may further go down [23].

- Corruption and lavish spending on the country's activities which previously drained millions of dollars from the national budget is now being curbed.
- The country planned to develop refineries to process oil into diesel and other petrochemicals so that instead of exporting an oil barrel for 100 dollars, value could be added to it by refining it and having different derivatives, which could also lead to different chemical products
- The government is also building a huge and modern port in Duqm, on Oman's central coast. Currently ships exporting oil had to pass through the Straits of Hormuz which was closed due to wars and political instability and the new port would now provide an alternate shipping route. This port would serve as both a landing and loading point thereby making Oman a main logistics hub for the region. The government further decided to upgrade the infrastructure, the transportation and even the introduction of railway to link Oman with the other GCC countries.
- It has decided to diversify the economy by developing and concentrating on the manufacturing, transportation and tourism sector.
- One might point that the recent agreement among OPEC and non-OPEC members to cut production acts as a ray of hope for Oman. This will help to increase prices [24].
- The demand for immigrant labor will slow down as a result of the decline in economic activity and the flow of Omani riyals overseas will be reduced thereby increasing the foreign exchange rate of the country in relation to the currencies of other countries [25].

SUGGESTED MEASURES THAT COULD BE ADOPTED BY OMAN TO OVERCOME THE CRISIS

Omani policymakers will need to implement major economic reforms and diversify the oil-dependent economy, which has suffered as the result of the fall of global oil prices. With a currently unsustainable public sector, authorities are challenged with introducing economic reform while avoiding possible social unrest.

- Omanization: Due to the increased dependence on immigrant workers, there has been an increased movement of funds from Oman to India and other countries which can be reduced if the labor force of the nation was composed of more Omani nationals who would earn more and spend more within the country thereby increasing the production and purchasing power of the country
- Extending loans to the nationals especially the youth for starting new and small scale industries – With the increased participation of the nationals in setting up small scale private organizations the development of the country is bound to take place and lead to the increase in the revenue. Moreover the licensing costs and other costs to be paid by these nationals would surely serve as a source of income to the country
- Reducing the overdependence on oil as a revenue producer – The country should diversify into the production of other manufactured goods and reduce its dependence on oil. Foreign investments into Oman can be encouraged thereby leading to more industries in the country. The Port and Free zone authority of Sohar wherein more industries can be opened up is a case in point.
- Processing of oil into diesel and other petrochemicals can lead to adding value and lead to different chemical products being produced
- The new logistics hub at Duqm can serve favorably to increase trade.
- Transportation and infrastructure facilities should be upgraded. The plan to link the GCC with metro services would surely increase the revenue.
- Tourism and gas-based industries should be a part of the government's diversification strategy. More tourists spots should be developed along with Salalah and the tourism industry should be promoted. The visa charges for people coming into the country to see these spots would surely serve as an ample source of income.
- The exporting of Dates and Oudh which are inherent commodities unique to the land of Oman should be encouraged
- Women entrepreneurship has to be encouraged and this can be done with the promoting of education among them.
- Taxes which are a source of income for other countries need to be introduced into the country on the income of all sectors thereby increasing the revenue and preventing a large part of the income of the non-nationals from moving out of the country.
- The obstacle of economic freedom in the form of a weak legal framework and subsidies and other forms of favoritism to the nationals and state owned enterprises should be done away with.
- The Education system has to be improved and the youth in colleges have to be encouraged to do research on how to overcome the present crisis situation. Establishment of technology
- Abolishing electricity subsidies and increasing the price of electricity and water.
- Reduce hiring and freeze the salaries of civil servants

CONCLUSION

The purpose of this research study is to investigate the impacts of the global crisis on the efficiency and performance on the economy of Oman. The effects of the global crisis which started in the west had also far reaching effects on the east though it was much slower. One such country which was recently affected was the Sultanate of Oman. The study highlights the extent of global crisis and also the impact of global crisis on economic performance of Oman both negatively and positively.

A major threat to Oman's stability is the economic crisis caused by the drop in government revenues from the sale of oil. With 80 percent of its income coming from oil, the government is now hard pressed to balance the need to pass economic reforms with the need to meet the terms of the unwritten social contract with its populace, which promises welfare in exchange for a preservation of the existing political order.

Despite the possible social discontent that may emerge as a response to wage cuts, a greater range of reforms need to occur. Fuel, electricity and water subsidy schemes need to be restructured for greater efficiency. Additionally, Oman must accelerate and expand its efforts to further diversify its economy. There will be a need for the reforms to be implemented in phases to ensure economic and social stability through the transition. As elsewhere in the Middle East, Oman's economic health is vitally important to its political stability. There are concerns over the health of 74-year-old Sultan Qaboos who has no children and has not named an heir. A leadership change at a time of economic turmoil could also contribute to political and social instability.

To quote the words of Salim bin Nasser Al Aufi, the Under-Secretary of the Ministry of Oil & Gas, in his speech exclusively to the OPAL Oil & Gas Magazine on the notable triumphs of the past six months in the oil sector he said "With the downturn spawned by the collapse in international oil prices well into the third year, oil and gas operators continue to stay the course much to delight of Oman's authorities. In the upshot, Oman is well-poised to ramp up production especially when limits on production imposed under the OPEC led deal has been lifted" He further stated that "Oman has to the potential to exceed the constrained production level and soon Oman would be able to come out of the effects of the global crisis"

Thus, Omani authorities urgently need to implement reforms and diversify the economy to contain the expected consequences of the drop of global oil prices. Omani policymakers face the complex challenge of implementing reform without thwarting current political and social stability, and without damaging the current health of the economy.

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