2019 Oman State Budget: "A prudent budgetary approach"

06 January 2019

Summary of state budget released in Royal Decree 1/2019

	2019 budget			2018 budget		2018 actuals*	
	Target oil prices at $58/bbl			Target oil prices at $50/bbl		Actual oil prices at $68/bbl	
	OMR (m)	%of total	% change from 2018	OMR (m)	% of total	OMR (m)	% change from 2018
Revenues							
Oil	5,465	54	12	4,870	51		
Gas	1,980	20	2	1,910	20		
Total oil & gas	**7,445**	**74**	**10**	**6,780**	**71**		
Taxes & fees	1,450	14	3	1,413	15		
Non tax revenues	850	8	(26)	1,147	12		
Others	355	4	122	160	2		
Total non-oil & gas	**2,655**	**26**	**(2)**	**2,720**	**29**		
Total revenues	**10,100**	**100**	**6**	**9,500**	**100**	**10,300**	**8**
Expenditure							
Defense and security	3,450	27	0.4	3,440	28		
Oil and gas	2,230	17	6	2,100	17		
Civil ministries	4,490	35	3	4,350	34		
Loan interest	630	5	31	480	4		
Investments	1,325	10	(3)	1,365	11		
Subsidies and other	775	6	(22)	765	6		
Total expenditures	**12,900**	**100**	**3**	**12,500**	**100**	**13,200**	**6**
Deficit	**(2,800)**			**(3,000)**		**(2,900)**	
Deficit funded by:							
Foreign borrowing	2,000	72	(5)	2,100	70		
Local borrowing	400	14	-	400	13		

Reserves	400	14	(20)	500	17

*Source of information: Royal decree 1/2019 and Ministry of Finance press release

Overview

Oman's 2019 budget sets a prudent and measured tone in both its revenue and expenditure projections with a resultant deficit of OMR 2.8 billion.

Strong oil prices in the first three quarters of 2018 significantly improved the performance of the 2018 budget, with Oman crude averaging c. $68.7/bbl (for the period to November 2018; NCSI data). The forecast for oil prices in 2019 remains positive, with analysts predicting an average price of c. $60 - $65/bbl. Analysts cite commitments to decrease production quotas by OPEC and allied oil producing countries, including Oman, and further sanctions on Iranian oil exports as rationale for their outlook. However despite this, Oman's FY19 budget has been based on a cautiously optimistic average oil price of $58/bbl, stating the need for "precautionary measures to mitigate any decline in oil prices". Indeed continued geopolitical risks in the region, including the withdrawal of Qatar from OPEC with effect from 1 January 2019, underline the continued volatility in supply and demand and underlying oil prices.

The key aims of the FY19 budget are to (1) maintain fiscal sustainability and spending efficiency, (2) continue to provide economic stimulus, and (3) maintain the level of social services for nationals.

Revenue is budgeted to increase by 6% to OMR10.1 billion (cf. FY18 OMR9.5 billion), with oil & gas revenue representing c.74% (OMR7.4 billion).

Expenditure is budgeted to increase by 3% to OMR 12.9 billion (cf. FY18 OMR12.5 billion), with a commitment to complete a number of strategic infrastructure projects to help incentivize economic growth.

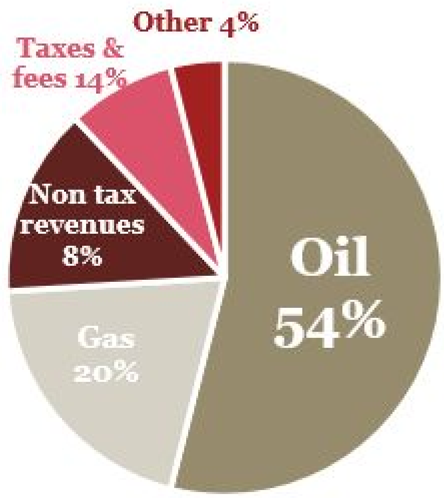
There is continued focus on the need to enhance the contribution of non-oil revenue, and the budget includes allocations for the five sectors identified by the National Program for Enhancing Economic Diversification (Tanfeedh): manufacturing, logistics, tourism, fisheries and mining. The Government acknowledges that revenues from these sectors depend significantly on private sector investment, and is committed to improving the business environment to facilitate this. In addition, the Government appears keen to outsource other services and projects to the private sector to further ease expenditure and with the aim of bringing improved efficiency and cost savings.

Further insights in Sultanates 2019 state budget

Revenues

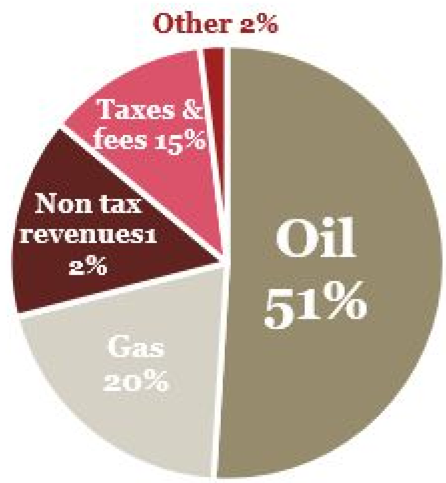
Oman's 2019 budget estimates total revenues at OMR 10.1 billion, an increase 6% compared to estimated revenues in 2018. Oil and gas revenues comprises c. 74% at OMR 7.4 billion and the remaining OMR 2.7 billion is estimated from non-oil and gas revenues.

2019 Revenue Estimates



*2019 budgeted revenues at OMR 10,100 million

2018 Revenue Estimates



*2018 budgeted revenues at OMR 9,500 million

Revenues estimates are based on the Country's commitment to cut down on oil production in accordance to OPEC's decision to reduce production volumes and increasing gas revenues from the Khazzan oil field (Standard and Poor's expects a significant increase in gas revenues from the ongoing Khazzan project). Further; these estimates are based on the consideration of the following:

- The improved efficiency of tax and fees collection
- Standardised fees of municipal services
- Revised fees of services provided by the Ministry of Agriculture and Fisheries and Ministry of Health

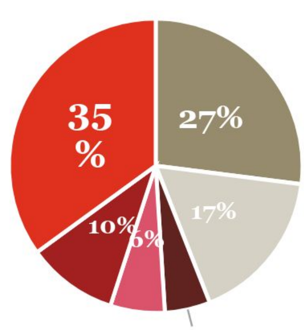
Actual revenues in 2018

The actual oil and gas revenue were up by c. %8 compared to 2018 budget estimates. The revenue increase is mainly due to the increase in oil prices to $68 per barrel. Behind this increase was a successful month of crude oil trading on the Dubai Mercantile Exchange in September 2018 where oil prices reached as high as $90 per barrel. The non-hydrocarbon revenue target has not been met. This is mainly due to the delay in implementation of the approved measures aimed at energizing non-hydrocarbon revenues.

Expenditure

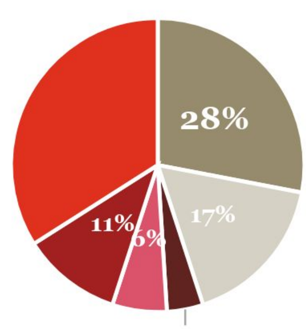
Total expenditure is estimated at OMR 12.9 billion, OMR 400 million (3% higher), than projected in the 2018 budget. OMR 4.5 billion of this is to be allocated to expenditure of the ministries and government units.

2019 Expenditure Estimates



2019 Budgeted Expenditures at OMR 12.9 billion

2018 Expenditure Estimates



2018 Budgeted Expenditures at OMR 12.5 billion

Defense and security | Oil and gas | Loan interest
Civil ministries | Investments | Others

Investment spending is estimated at OMR 2.1 billion, ensuring that all ongoing projects are paid for, avoiding any delays in development. Oil and gas production expense is estimated 6% higher than last year at OMR 2.2 billion, by purpose of not only maintaining future oil and gas production, but also to enhance the oil and gas reserves.

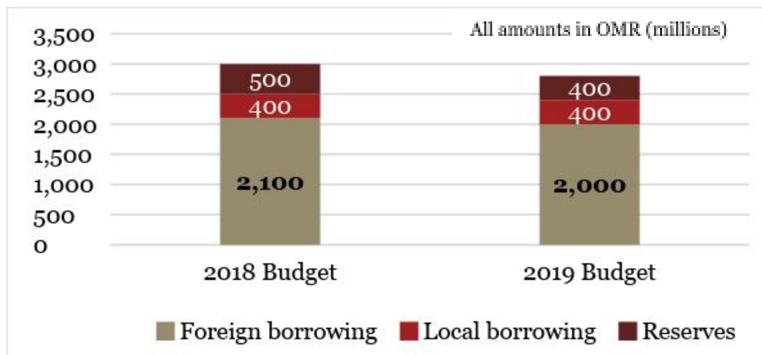
Actual expenditure in 2018

The actual spending totaled OMR 13.2 billion in 2018, a 6% increase compared to the 2018 projection. This is widely due to the rise in investment spending in development projects, increased expenditure in government units and high cost of public debt servicing.

Deficit

The actual deficit in 2018 was roughly OMR 2.9 billion, while the 2019 budget estimates the deficit at OMR 2.8 billion, or 9% of total GDP.

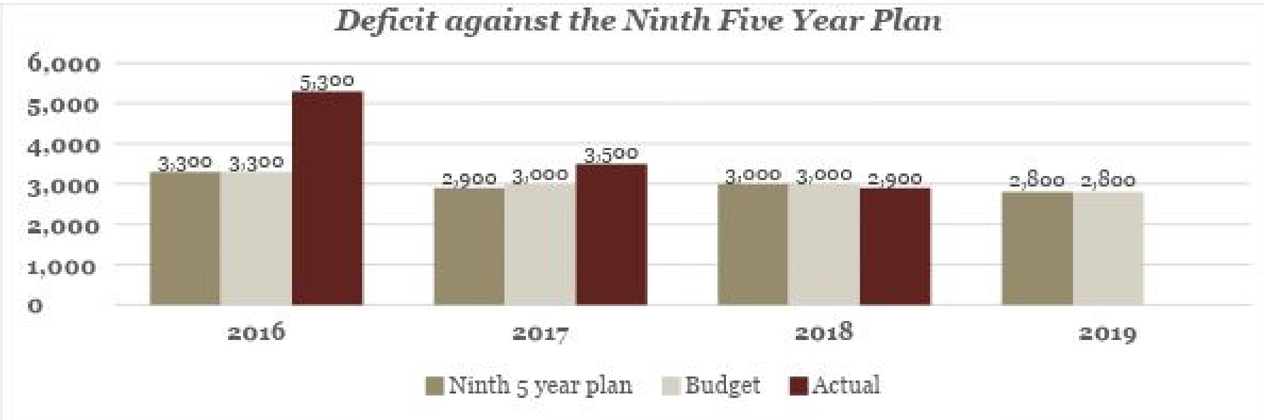
Following the spike in the actual deficit in 2016 at c. OMR 5.3 billion (initially budgeted at OMR 3.3 billion), the deficit appears to be managed and is showing recovery. The estimated deficit in 2019 is lower than the deficit of 2017 by c. 18%, or OMR 600 million.



Deficit financing

Despite the unfavorable set of global economic conditions and the uncertainty over the debt market, Oman covered the approved deficit in 2018 by borrowing mainly from external sources (albeit at higher interest rates). This accounted for 69% of total deficit funding, whilst domestic borrowing amounted to only 17%, and the remaining 14% was covered by withdrawal from reserves.

The 2019 budget deficit is estimated to be 86% covered by external and domestic borrowing, while the balance will be covered by drawing on the reserves. This is in line with the Government's guidelines to maintain the sovereign reserve funds, and to rely upon borrowing to finance any deficit.



2019 Budget Objectives

Fiscal sustainability

Fiscal sustainability is the most important objective of the state budget; however for this to be realised, the Government acknowledges that spending must be prioritised against the competing needs of the continued provision of public services and strategic investment to keep the economy on a positive footing.

In addition, and in order to keep the deficit within 'safe limits', the Government acknowledges the need to improve the contribution of non-oil revenue "in a way that leads to reduce dependency on the oil sector". Whilst this is a plausible objective, with the continuation of existing measures, such as Tanfeedh, and the introduction of new initiatives, such as excise tax; the Government will need to consider accelerating additional reforms, for example, the introduction of VAT, and intensify its investment activities in line with its interim five year plans and vision 2020 objectives, to feel some relief from the burden of oil price volatility.

Economic stimulus

The budget outlines a number of key themes and objectives to ensure continued economic growth at a rate of 2-3%, in line with the Ninth Five Year plan. The Government has committed to the completion of a number of strategic investment projects and promoting the involvement of the private sector and small and medium enterprises (SME's) in the delivery of some government services. SME's will also continue to have access to funding via loans from the Al Raffd Fund and Oman Development Bank.

Maintaining levels of Basic Services

The budget is designed to maintain the level of priority social services for citizens. These include services within the education, health care housing and social welfare sectors which account for c.36% of the 2019 budget. Public sector recruitment of nationals, and training via the National Training Fund will continue in 2019, with plans to train c. 6,000 nationals, and the allocation of c. 5,000 public sector job opportunities.

Key developments going forward

Indirect tax reforms

Oman and its neighboring GCC member states have long been under pressure to accelerate fiscal reforms to decrease reliance on hydrocarbon revenues. Key components of these reforms include the introduction of VAT and excise taxes. Progress has been made by GCC wide agreements for both taxes and domestic implementation by some GCC member states.

Excise tax

The introduction of excise tax (commonly also referred to as 'selective' or 'sin' tax) in Oman was widely expected to be implemented during 2019, and has now been confirmed in the FY19 budget. In addition to levying the tax on tobacco, energy drinks and certain carbonated drinks, it has been reported that the tax may also extend to alcohol and certain other "luxury" goods. Businesses involved in the importation and / or domestic production of such goods are advised to seek guidance on the anticipated excise tax compliance framework, and to consider the impact of the tax on their pricing and margins. The Kingdom of Saudi Arabia (KSA), United Arab Emirates (UAE) and Bahrain introduced excise tax in 2017, ahead of their respective VAT regimes. Qatar has also recently implemented excise tax with effect from 1 January 2019.

Value Added Tax

The introduction of Value Added Tax (VAT) in Oman has been postponed beyond the originally anticipated date of 1 January 2019, and is now widely expected to be introduced by 1 January 2020. The FY19 budget statement does not provide a timeframe for the introduction of VAT, but refers to "*capacity building for tax and customs systems"* – which may include preparations for VAT. Similarly, the 2019 budget revenue forecast under "taxes and fees" does not reflect any significant increase that may be attributable to the introduction of VAT in this year.

In September 2018, the Secretariat General for Taxation (SGT) stated that it was targeting an implementation date of 1 September 2019, although this date remained "under review". To date, only three of the six GCC member states have introduced VAT: UAE and KSA from 1 January 2018; and Bahrain from 1 January 2019. It is expected that, of the three remaining countries, Oman will be the next to implement VAT. Accordingly, many businesses have started to prepare for VAT implementation, and have started to mobilize resources and budget to initiate this process in earnest in early 2019.

Tanfeedh initiatives

The 2019 budget includes allocations to continue the focus on enhancing economic diversification within the Sultanate into the sectors identified in the Tanfeedh initiative. The Tanfeedh initiative was established to fulfill the objectives of the Ninth Five Year Development Plan 2016 – 2020. It also works towards sustainable participation between the public and private sectors. The strategic sectors identified in the programme are: manufacturing, tourism, transport, logistics, mining and fisheries.

Although the initiatives recommended by Tanfeedh are heavily reliant on private sector investments into the projects, the government is committed to taking further steps to facilitate procedures to support and provide efforts to develop the respective sectors and the business environment as a whole.

Other measures

Oman is the 103rd country to join the 'Inclusive framework on Base Erosion and Profit Shifting ("BEPS").

Oman has committed itself to the implementation of the four minimum criteria's of BEPS standards, namely, countering harmful tax practices, tax treaty abuse, transfer pricing documentations and country by country reporting, and finally, improving dispute resolutions mechanisms to priorities of the BEPS measures.

Alongside with the BEPS framework, transfer pricing regulations are expected to be implemented in 2019. The transfer pricing regulations are anticipated to follow the general principles put forth by the Organisation for Economic Cooperation and Development ("OECD") model.

The takeaway

Oman's 2019 state budget maintains a focus on economic diversification and the need to manage expenditure to ensure the deficit is maintained within sustainable levels, whilst still providing sufficient investment to promote economic stimulus and growth. The budget follows a similar strategic approach to that of FY 2018, with prudent increases in revenue and expenditure targets. The Government remains cautious in its outlook citing volatility in oil prices, which remain the principal source of revenue. Strategic steps to diversify the economy, such as the introduction of excise tax, and the outsourcing of various Government services to the private sector and SME's are a welcome sign, as is the continued commitment to targeted investment to boost employment and social development.

Let's talk

For a deeper discussion of how the 2019 Oman budget might affect your business, please contact:
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