



بنك الإمارات دبي الوطني  
Emirates NBD

## Credit Note

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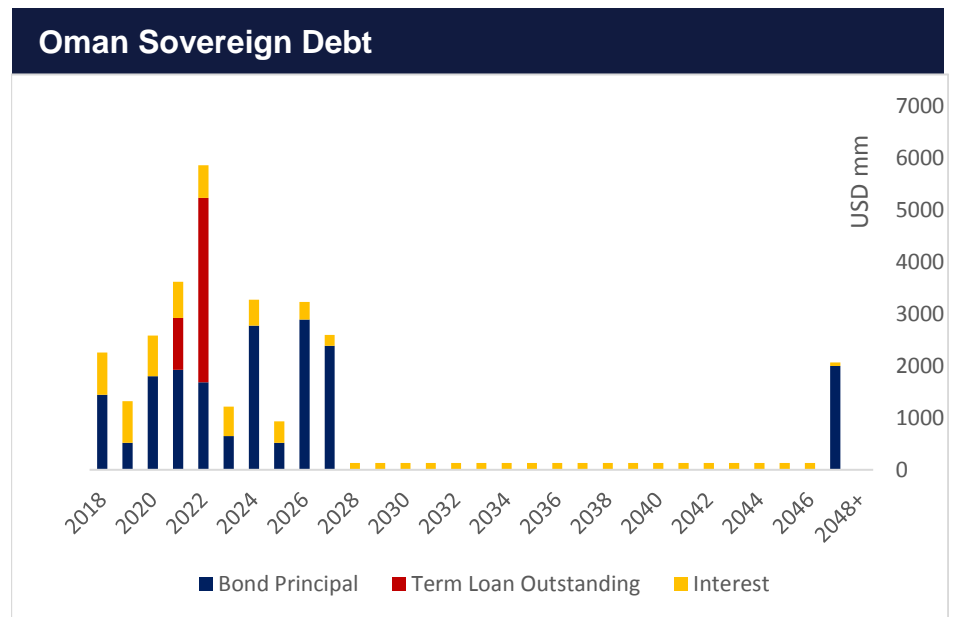
# Sultanate of Oman Update

The Government of Oman, rated BB/Baa2/BBB- by S&P, Moody's and Fitch respectively, yesterday raised \$6.5 billion via issuance of bonds with tenure of 5yr at T+190bps (\$1.25bn), 10yr at T+310bps (\$2.5 bn) and 30yr at T+395bps (\$2.75 billion). Much as in 2016 and 2017, Oman is likely to follow the bonds issuance with a sukuk offering soon, possibly of size between \$1.0 - \$2.0 billion to fund projected budget deficit of circa \$7.8 billion in 2018. In light of the new issues, presented below is a recap of key credit characteristics of the Oman sovereign.

## Oman Debt

To fund its budget deficits, Oman government has raised debt via bonds as well as sukuk in the recent past. It also has bilateral loan obligations as well as some treasury bills.

- Oman currently has total debt obligation of USD \$31.4bn made of a) bonds (including TBs) of \$18.6bn; b) loans of \$4.55bn and c) committed interest expense of \$8.28bn.
- 73% of the debt obligation is denominated in USD with remainder in OMR.
- 95% of the debt is at fixed interest rate and the earliest USD bond maturity is not until June 2021.

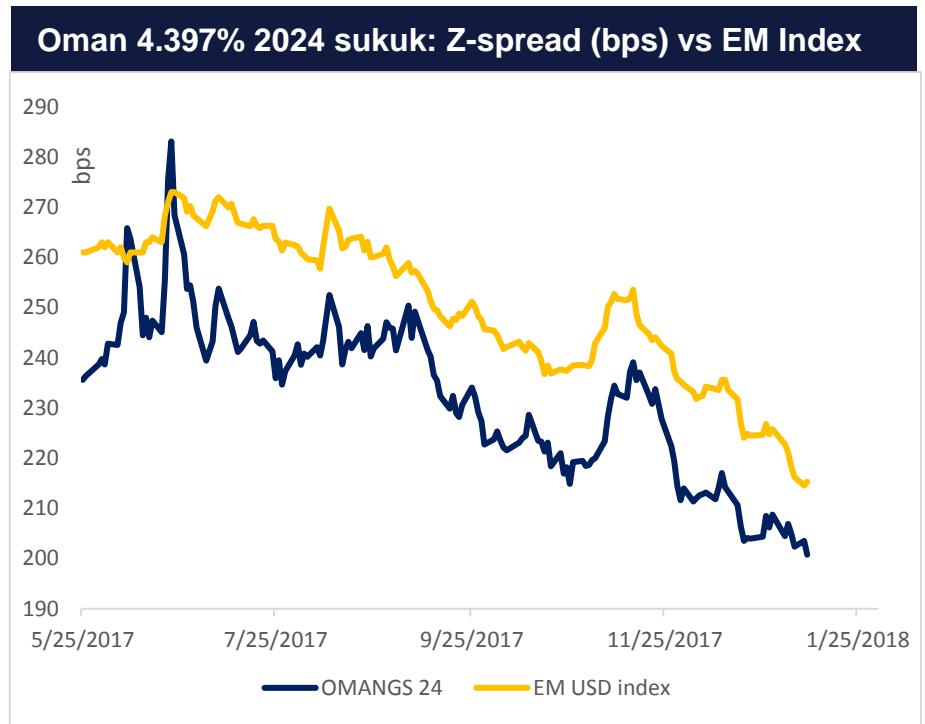


Source: Bloomberg, Emirates NBD Research

Oman tapped international capital markets in 2016 and 2017, raising \$4.5 billion and \$7 billion respectively via bonds as well as sukuk.

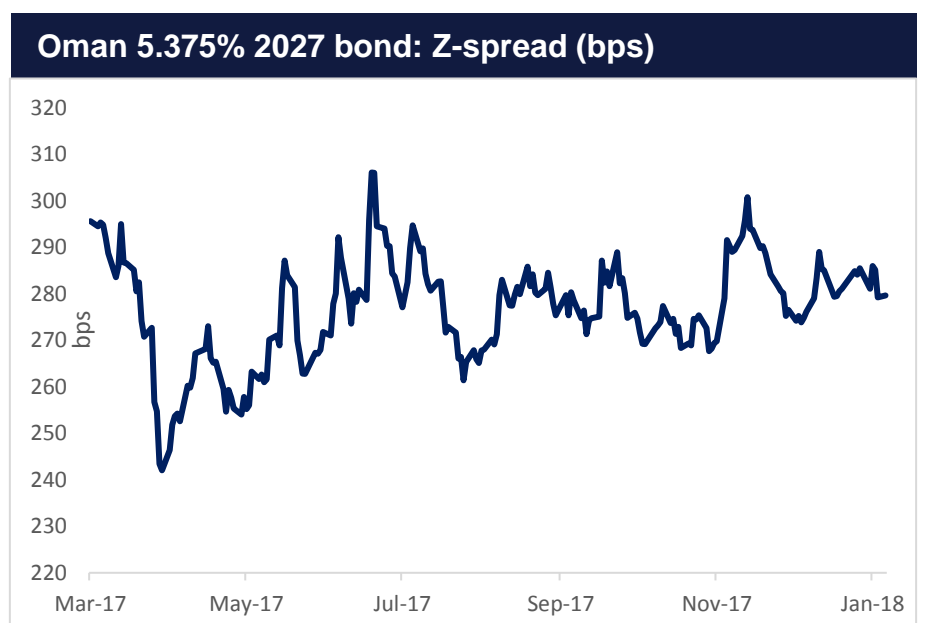
	Ticker	Cpn	Maturity	Amount \$mm	YTW %
Bonds					
	OMAN	3.625	6/15/2021	1500	3.56
	OMAN	3.875	3/8/2022	1000	3.67
	OMAN	4.75	6/15/2026	2500	5.14
	OMAN	5.375	3/8/2027	2000	5.2
	OMAN	6.5	3/8/2047	2000	6.44
Sukuk					
	OMANGS	4.397	6/1/2024	2000	4.37

Despite several rating downgrades in 2017, overall demand for Oman bonds has been resilient. Credit spreads on Oman bonds have tightened in sync with the improvement in wider emerging market bonds.



Source: Bloomberg, Emirates NBD Research

Credit spreads on Omani bonds did widen in November / December last year as S&P and Fitch downgraded Oman's rating in quick succession which dampened investor sentiment and raised the risk of the rating falling into the junk category by all three agencies. However since then, rising oil prices have stabilised the sentiment and yield on Oman bonds have tightened in sync with the market.



Source: Bloomberg, Emirates NBD Research

## 2018 Budget

Last week, Oman released its 2018 budget that reflects an increase of 9% in revenue to OMR 9.5bn and 6.8% in spending to OMR 12.5bn over the previous year, thereby leaving the budget in deficit of circa OMR 3.0 billion i.e. US\$ 7.8bn. The budget is based on assumption of oil prices at \$50/b

- In 2018, 71% of government revenue will come from hydrocarbons compared with 70% in 2017, thereby validating that limited progress has been made in diversifying the economy's reliance away from oil. Looking ahead, hydrocarbon revenues are likely to continue to increase due to higher oil prices and by the recent start of production from the Khazzan gas field (owned 60% by BP and 40% by Oman). There is minimal expectation of increase in revenue from higher corporate taxes introduced last year. Also introduction of VAT is not likely until end of the year.
- Despite higher than expected oil prices in 2017 and consequently higher revenues, actual fiscal deficit in 2017 was OMR3.5bn vs budget of OMR 3.0bn largely due to higher expense on defense and hydrocarbon exploration. These may be difficult to cut much due to regional security challenges and due to the need to spend on exploration now in order to increase future hydrocarbon revenues. Also room for cutting subsidies is low as subsidies only account for less than 1% of the GDP.
- In 2017, Oman financed 90% of the deficits by domestic and foreign borrowings and remainder 10% by drawing on State General Reserve Fund of Oman (SGRF). SGRF foreign assets were USD18 billion at end-2016.
- 2018 budget deficit is expected to be financed from borrowing (84%) and reserves (16%). The government is also hoping to privatise some of its domestic infrastructure assets.

<b>Oman Budget Highlights</b>			
<b>OMR mm</b>	<b>Budget 2018</b>	<b>Budget 2017</b>	<b>% change YoY</b>
Oil	4870	4450	9%
Gas	1910	1660	15%
Taxes & fees	1413	1423	-1%
Other	1307	1167	12%
<b>Total Revenue</b>	<b>9500</b>	<b>8700</b>	<b>9%</b>
Defense & Security	3440	3340	3%
O&G production	2100	1820	15%
Civil Ministries	4350	4400	-1%
Other	2610	2140	22%
<b>Total Expenditure</b>	<b>12500</b>	<b>11700</b>	<b>7%</b>
<b>Deficit</b>	<b>-3000</b>	<b>-3000</b>	

Source: Bloomberg, Emirates NBD Research

## Other Credit Considerations

- Oman remains a neutral player when it comes to regional disputes and politics.
- Oman's Fiscal breakeven oil price is around \$ 75 – \$80 / b (second highest after Bahrain) and external breakeven price is around \$70 – \$75 / b (highest in the GCC). Though Oman is not a member of OPEC, it has voluntarily reduced its production by about 30 thousand barrels per day, resulting in lower export revenues and wider current account deficits.
- Oman's hydrocarbon reserves are small and are expected to last for about 15-24 years at the current rate of production.
- The government expects GDP to grow at 3% in 2018 supported by no intent to cut development spending. Projects such as the new international airport, expressways, water networks, hospitals and renewable energy generation would continue to get government funding. Also the diversification strategy includes developing the port of Duqm and building internal Oman rail system between three major ports to support its vision of becoming a logistic hub.
- The sectors which contribute materially to GDP are construction, mining & quarrying, manufacturing and utilities. In addition fisheries, tourism and logistics have been identified as the sectors for future growth.
- The government is likely to predominantly finance its deficits largely via the issuance of foreign currency debt. This is likely to see Oman's net foreign asset position change from a positive 24% to GDP in 2017 to a net debtor by 2020.

Key Economic Data				
	2015	2016	2017	2018
Nominal GDP (\$bn)	70	67	72	77
GDP growth %	5.7	3	0.5	3
CA balance / GDP %	-15.7	-19.4	-13.8	-13.5
Budget balance / GDP %	-15.5	-20.2	-12.8	-11
Debt / GDP %	12.8	29.6	37.6	45.3
Net Debt / GDP %	-51.4	-36.5	-23.7	-11.3
Usable reserves (\$ bn)	2.95	5.90	6.45	4.96

Source: Emirates NBD, S&P, Bloomberg

- To mitigate large external borrowings, the government is exploring selling some assets and increasing the capacity of the domestic debt capital markets. Six state owned assets are shortlisted for privatization in 2018.
- Omani banking system has relatively limited reliance on external funding, as banks are largely funded by domestic customer deposits. That said, last year S&P downgraded its score for Omani banking sector from 5 to 6 (1 being the best on a scale of 1 to 10) and Moody's revised the outlook on the Omani banking sector to negative from stable mainly as a result of expectation of higher NPLs.
- A deterioration in the domestic or regional political environment would be highly credit negative but is not factored in the current ratings
- Oman has recently joined the Base Erosion and Profit Shifting (BEPS) Inclusive Framework of OECD along with KSA and Qatar. The European Union has placed Oman in the grey list of non co-operative tax jurisdictions. As at now there are no sanctions even on the black listed countries, however risk remains for sanctions to be imposed at some later stage. However, with proper implementation of BEPS measures, Oman should be able to get out of the grey list.
- **Currency Peg** : Oman's current account balance is running in negative. Though devaluation of the currency is not yet anticipated, the persistent current account imbalances may become a hurdle in defending the currency. Devaluation of the currency would warrant credit rating downgrades as it will materially increase the government's debt servicing burden. That said, devaluation risk is not yet factored into the sovereign's credit ratings mainly because of the expectations that stronger GCC countries will provide support to the weaker ones via provision of deposits, loans or grants. GCC countries had pledged \$20 billion to Bahrain and Oman in 2011 through a new GCC Fund. Although transfers do not pass through the Bahraini and Omani government budgets, they support their external payments positions.

## Credit Ratings

- S&P downgraded Oman's rating to BB/stable in November 2017. As per S&P Oman's external debt will exceed its liquid external assets for the first time in 2018, with the gap widening to 25% of current account receipts by 2020. S&P's rating could be upgraded if there was a sharp reduction in external debt or sharp increase in usable FX reserves.
- S&P's rating is constrained by their view that sultanate's decision-making is centralized, resulting in less predictable policymaking. Sultan Qaboos bin Said Al Said is 76 yrs old, has ruled Oman since 1970 and exercises absolute power and holds the offices of prime minister, chief of staff of the armed forces, minister of defense, finance and foreign affairs, and chairman of the board of governors of the central bank. The institutional weakness related to the centralization of the powers was highlighted during 2015, as the Sultan's eight months stay for a cancer treatment in Germany paralyzed the decision-making process, effectively delaying the policy response to the oil price slump.
- Moody's has a Baa2/Negative rating on Oman since July last year. Moody's concerns revolve around lack of clarity on strategy to address fiscal deficit and external vulnerabilities in the face of low oil prices. Moody's notes that the change in corporate tax rate has not translated into any material increase in non-oil revenues for the govt. Given the limited absorption capacity of the domestic

market Moody's expects continued reliance on international debt issuance which has already increased Oman's susceptibility to international capital flow volatility. The cost of funding will likely continue to rise in light of Oman's structural challenges and in a global environment of rising interest rates, which could significantly weaken Oman's government debt affordability indicators and pressurize Moody's rating.

- Fitch downgraded Oman to BBB-/Negative in December 2017 mainly due to government expenditure and budget deficits being higher than previously planned. Further downgrades are possible if fiscal and external position deteriorates further as a result of failure to implement fiscal reforms or due to a renewed fall in oil prices.

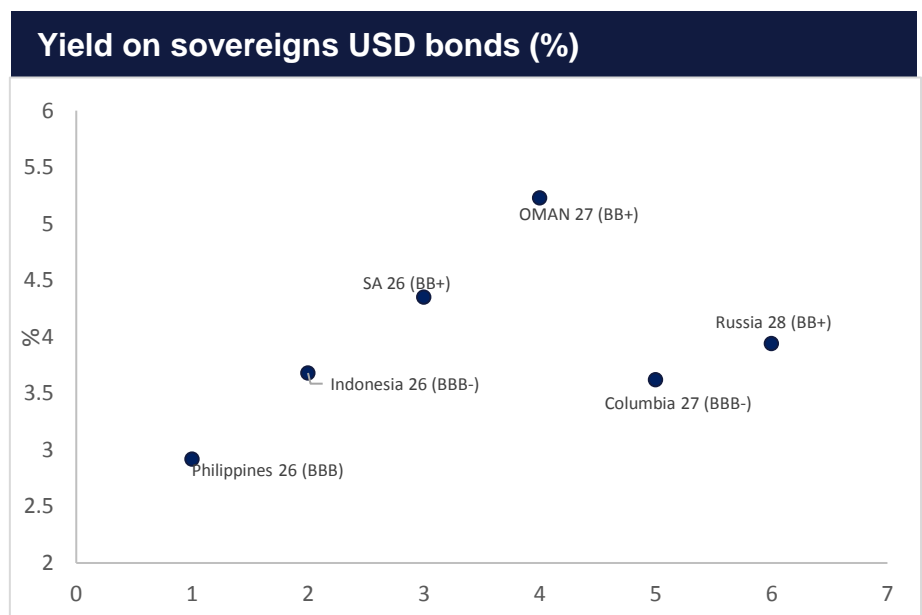
Ratings Calendar - 2017			
	1st	2nd	3rd
<b>S&amp;P</b>	11 May	9 Nov	

Source: S&P, Moody's

Ratings on Oman are likely to remain volatile until the government's strategy to balance budgets is better established and accepted.

### Relative Value

Despite all the challenges, Omani bonds are likely to retain international investors' interest mainly on relative value basis.



Source: Bloomberg, Emirates NBD Research

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