Fitch Ratings

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Fitch Upgrades Oman to 'BB+'; Outlook Stable

Fitch Ratings - Hong Kong - 25 Sep 2023: Fitch Ratings has upgraded Oman's Long-Term Foreign-Currency Issuer Default Rating (IDR) to 'BB+' from 'BB'. The Outlook is Stable.

A full list of rating actions is at the end of this rating action commentary.

Key Rating Drivers

Public Finances Underpin Upgrade: The upgrade reflects the use of high oil revenues to pay down debt and spread its maturity, spending restraint reducing external risks, and an increase in Fitch's oil price forecast. We project general government debt to fall to 36% of GDP in 2023 and stabilise at around 35% in 2024 and 2025, below the 'BB' peer median of 54%. This compares with our forecast of 45% of GDP in 2023 when we last upgraded Oman in August 2022.

The upgrade also incorporates our view that the government will not backtrack on recent fiscal consolidation measures. The reduction of Oman's fiscal breakeven price to below USD70/bbl over our forecast horizon from USD80-90/bbl over 2017-19 significantly reduces vulnerability to oil price swings, although risks remain.

Falling Debt: Oman continues to pre-pay some its debt, using the budget surplus from high oil prices. We project debt to decrease by about 8% in nominal value in 2023. The Petroleum Reserve Fund has not been used for these repayments and was over USD2.5 billion in August 2023. Oman's debt management has smoothed its debt profile, reducing the risk of liquidity pressures.

Improving External Balance Sheet: Lower external debt has eased external liquidity risks, although debt repayments prevented accumulation of foreign assets. We project sovereign net foreign assets (Oman Investment Authority's (OIA) foreign assets + FX reserves - direct government debt) to return to a positive position in 2023, after falling to -9% of GDP in 2020, from 53% in 2014. Foreign-exchange reserves will rise only modestly in 2023 as debt repayments continue, to cover 3.3 months of current account payments, below the 'BB' median of 4.3 months.

State-owned entities (SOE) have also contributed to the improvement of Oman's external position, with OQ, Oman Telecommunication Company and Asyad Group significantly reducing debt between end 2021 and June 2023. We project overall SOE debt to be broadly stable at about 40% of GDP, including 17% of GDP in external debt, with Energy Development Oman SAOC increasing its debt to develop its assets while most other large SOE will reduce debt and asset sales will generate internal funding. OIA foreign assets are stable, at close to USD17 billion (15% of GDP). We project total net external debt to stabilise around 26-28% of GDP over 2023-25, well above the 'BB' median but materially lower than the recent past.

Fiscal Restraint Remains: Spending has been relatively prudent in the face of higher oil prices and we project key current spending items to grow in line with nominal GDP, well below the rate in previous periods of high oil prices. The fuel price cap introduced in 2022 is temporary with a clear cutoff price. We project a government budget surplus of 4.1% of GDP in 2023, 2.4% in 2024 and 1% in 2025, narrowing in line with our Brent crude price forecasts of USD80/bbl in 2023, USD75 in 2024 and USD70 in 2025.

We project oil production to plateau from 2025 at 1.08 million bpd and gas production to rise modestly, largely to service domestic demand although new export facilities are being considered. Our fiscal balance metric differs from the government, as we exclude some dividends, liquidity and debt management items from revenue and spending.

Medium-term Fiscal Plan on Hold: High oil prices and global inflationary pressures have led the government to pause some measures included in its medium-term fiscal plan, which was drafted with much lower oil prices assumptions. The authorities are likely to focus on qualitative measures to improve tax collection for VAT rather than raise rates while the budget remains in surplus, but personal income tax could be introduced in 2025. We would expect the tax to initially yield revenues of only 0.2% of GDP.

Budget Risks Remain: Combined with the introduction of VAT in 2021, PIT would provide Oman additional fiscal levers compared with the pre-pandemic period, increasing the resilience of public finances. However, in our view, there remain some uncertainties around Oman's willingness to implement new revenue measures if oil prices dip below our forecasts.

New spending commitments will be introduced, with the authorities passing a law widening the social safety net in July 2023. From 2024, the government will make a higher social security premium contribution, which will increase spending by about 1% of GDP, although this cost will largely be offset by a lower cost of the fuel price cap. Public finances will remain dependent on hydrocarbon revenue and vulnerable to oil prices shocks. Potential social pressure from the low employment rate of young Omanis remains a risk to public finances.

External Vulnerabilities Remain: We forecast sovereign external maturities to average USD2.9 billion in 2024-2026. In addition, annual external debt payments by SOEs under the purview of the OIA average USD3.1 billion in 2024-2025. These external commitments are less burdensome than in recent years, but remain significant, especially in a scenario of lower oil prices and continued tight global financing conditions.

Growth to Slow: We project GDP growth of 2.1% in 2023, slowing from 4.3% in 2022. Oil production will contract as Oman has cut production since May 2023 as part of the OPEC+ cuts, while liquefied natural gas export facilities will be at full capacity. We project non-oil sector growth of 2.7%, as the construction sector starts to recover from a 23% contraction in 2022, the OQ8 Duqm refinery ramps up production and other sectors slow as the pandemic recovery fades. In 2024, the continued rebound in construction, mostly driven by private demand, tourism, downstream hydrocarbons and higher oil production quotas will push GDP growth to 2.7%.

From 2025, Oman could benefit from large scale investments in the green hydrogen sector through projects aimed at using the green energy locally to produce green steel or to export. Investment agreements of over USD20 billion (17 % of 2023 forecast GDP) have been signed, but no final investment decisions have been made and uncertainty about off-takers for export products remains high.

ESG - Governance: Oman has an ESG Relevance Score (RS) of '5[+]' for both Political Stability and Rights and for the Rule of Law, Institutional and Regulatory Quality and Control of Corruption. Theses scores reflect the high weight that the World Bank Governance Indicators (WBGI) have in our proprietary Sovereign Rating Model. Oman has a medium WBGI ranking at the 52nd percentile, reflecting strong scores for rule of law and regulatory quality, but a low score for voice and accountability.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/ Downgrade

- Public Finances: An upward trend in government debt/GDP; for example, stemming from a loosening of the fiscal stance, a materialisation of large contingent liabilities or lower-than-expected oil prices.

- External Finances: Deterioration of Oman's external balance sheet; for example, in the form of a decline in central bank reserves and OIA assets.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

- Public Finances: A strengthening in the government's balance sheet; for example, through the introduction of new fiscal consolidation measures or a sustained period of high oil revenue.

- External Finances: A continued decline in net external debt/GDP, reflecting lower SOE external debt or an accumulation of foreign assets.

- Macro: Growth of the non-oil economy that notably improves non-oil fiscal revenues and reducing social spending pressures on the government.

Sovereign Rating Model (SRM) and Qualitative Overlay (QO)

Fitch's proprietary SRM assigns Oman a score equivalent to a rating of 'BBB' on the Long-Term Foreign-Currency (LT FC) IDR scale.

Fitch's sovereign rating committee adjusted the output from the SRM to arrive at the final LT FC IDR by applying its QO, relative to SRM data and output, as follows:

Fitch removed the-1 notch on Structural to reflect its view that the oil prices used in the model no longer cyclically distort its output.

- Public Finances: -1 notch to reflect risks to government finances from high dependence on hydrocarbon revenue and other fiscal rigidities related, for example, to subsidies and wages, and for contingent liabilities.

- External Finances: -1 notch to reflect vulnerability to renewed oil moves that the model may not fully capture and Oman's large net external debtor position, which is well above the 'BB' median

Fitch's SRM is the agency's proprietary multiple regression rating model that employs 18 variables based on three-year centred averages, including one year of forecasts, to produce a score equivalent to a LT FC IDR. Fitch's QO is a forward-looking qualitative framework designed to allow for adjustment to the SRM output to assign the final rating, reflecting factors within our criteria that are not fully quantifiable and/or not fully reflected in the SRM.

Country Ceiling

The Country Ceiling for Oman is 'BBB-',1 notch above the LT FC IDR. This reflects moderate constraints and incentives, relative to the IDR, against capital or exchange controls being imposed that would prevent or significantly impede the private sector from converting local currency into foreign currency and transferring the proceeds to non-resident creditors to service debt payments.

Fitch's Country Ceiling Model produced a starting point uplift of +1 notch above the IDR. Fitch's rating committee did not apply a qualitative adjustment to the model result.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Oman has an ESG Relevance Score of '5[+]' for Political Stability and Rights as WBGIs have the highest weight in Fitch's SRM and are therefore highly relevant to the rating and a key rating driver with a high weight. As Oman has a percentile rank above 50 for the respective Governance Indicator, this has a positive impact on the credit profile.

Oman has an ESG Relevance Score of '5[+]' for Rule of Law, Institutional & Regulatory Quality and Control of Corruption, as the WBGIs have the highest weight in Fitch's SRM and are therefore highly relevant to the rating and are a key rating driver with a high weight. As Oman has a percentile rank above 50 for the respective Governance Indicator, this has a positive impact on the credit profile.

Oman has an ESG Relevance Score of '4' for Human Rights and Political Freedoms, as the Voice and Accountability pillar of the WBGIs is relevant to the rating and a rating driver. As Oman has a percentile rank below 50 for the respective Governance Indicator, this has a negative impact on the credit profile.

Oman has an ESG Relevance Score of '4[+]' for Creditor Rights, as willingness to service and repay debt is relevant to the rating and is a rating driver for Oman, as for all sovereigns. Oman has a 20-plus year record without a restructuring of public debt. This is captured in our SRM variable and has a positive impact on the credit profile.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/topics/esg/products#esg-relevance-scores.

Fitch Ratings Analysts

Cedric Julien Berry
Director
Primary Rating Analyst
+852 2263 9950
Fitch (Hong Kong) Limited 19/F Man Yee Building 60-68 Des Voeux Road Central Hong Kong

Toby Iles
Senior Director
Secondary Rating Analyst
+852 2263 9832

Paul Gamble
Senior Director
Committee Chairperson
+44 20 3530 1623

Media Contacts

Jack Li
Beijing
+86 10 5957 0964
jack.li@thefitchgroup.com

Peter Fitzpatrick
London
+44 20 3530 1103
peter.fitzpatrick@thefitchgroup.com

Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Oman	LT IDR	BB+	Upgrade		BB

ENTITY/DEBT	RATING			RECOVERY	PRIOR
	ST IDR	B	Affirmed		B
	LC LT IDR	BB+	Upgrade		BB
	LC ST IDR	B	Affirmed		B
	Country Ceiling	BBB-	Upgrade		BB+
• senior unsecured	LT	BB+	Upgrade		BB
Oman Sovereign Sukuk S.A.O.C.					
• senior unsecured	LT	BB+	Upgrade		BB

RATINGS KEY	OUTLOOK	WATCH
POSITIVE		
NEGATIVE		
EVOLVING		
STABLE		

Applicable Criteria

Country Ceiling Criteria (pub.24 Jul 2023)

Sovereign Rating Criteria (pub.06 Apr 2023) (including rating assumption sensitivity)

Sukuk Rating Criteria (pub.13 Jun 2022)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Country Ceiling Model, v2.0.0 (1)

Debt Dynamics Model, v1.3.2 (1)

Macro-Prudential Indicator Model, v1.5.0 (1)

Sovereign Rating Model, v3.14.0 (1)

Additional Disclosures

Solicitation Status

Endorsement Status

Oman	EU Endorsed, UK Endorsed
Oman Sovereign Sukuk S.A.O.C.	EU Endorsed, UK Endorsed

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The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. Sector-specific best- and worst-case scenario credit ratings are listed in more detail at https://www.fitchratings.com/site/re/10238496

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