15 AUG 2022

Fitch Upgrades Oman to 'BB'; Outlook Stable

Fitch Ratings - Hong Kong - 15 Aug 2022: Fitch Ratings has upgraded Oman's Long-Term Foreign-Currency (LTFC) Issuer Default Rating (IDR) to 'BB' from 'BB-'. The Outlook is Stable.

A full list of rating actions is provided below.

Key Rating Drivers

Oil and Reform Drive Upgrade: The upgrade reflects significant improvements in Oman's fiscal metrics, a lessening of external financing pressures and ongoing efforts to reform public finances. Higher oil revenue will underpin budget surpluses in 2022 and 2023 and a sharp fall in government debt/GDP to below the 'BB' median. While we expect oil prices to trend down over the medium term and there has been some dilution of fiscal reform in 2022, we believe that commitment to fiscal consolidation via the state's medium term fiscal plan (MTFP) will be sufficient to limit renewed deterioration in public- and external-finance metrics.

Budget Swings to Surplus: We forecast budget surpluses of 5.5% and 3.4% of GDP in 2022 and 2023, respectively, Oman's first surpluses since 2013, as oil revenue growth easily outweighs additional spending. We assume average Brent crude prices of USD105/barrel in 2022 and USD85/barrel in 2023 and that crude and condensate output will grow by 8.8% in 2022 and 3.5% in 2023, reaching a record high of 1.1million barrels/day. Favourable prices will also boost budget revenue from gas.

In 2024 we forecast a small budget deficit as lower oil prices (assumed to average USD65/barrel) and modest GDP growth offset gains from ongoing fiscal reforms that will boost non-oil revenue and lower overall spending. Non-hydrocarbon tax revenue will increase, following the introduction of VAT in April 2021; personal income tax planned for 2023; and the likelihood of stronger corporate tax revenue.

Fiscal Reform Progress and Challenges: Spending will be higher than budgeted in 2022 (by 6% on Fitch forecasts), owing to fuel subsidies to cushion the domestic impact of high energy prices, slower reform of other subsidies and higher capex. The timeframe for phasing out electricity subsidies has been extended to 10 years from five.

We expect the MTFP, even on our assumption that it falls short of full timely implementation, to lower the fiscal breakeven oil price to around USD66/b in 2024 and to narrow the non-oil primary deficit as a percentage of non-oil GDP to 23% in 2024 from 31% in 2019. Oman would nonetheless remain heavily dependent on hydrocarbon revenue and vulnerable to commodity-price shocks.

Improved Government Debt Metrics: We forecast government debt/GDP to fall to 46.7% in 2022 and 44.9% in 2023, from around 70% in 2020, on the back of better budget performance and oil-fuelled nominal GDP growth of 24% in 2022. Government debt/GDP will be lower than the 2022 'BB' median of 55%. The government used part of the oil revenue windfall to buy back USD0.7 billion of bonds maturing across 2025-2032; pre-pay the remainder of the pre-export financing facility taken out in 2017 (USD1.3 billion) and repay a maturing USD3.6 billion loan from China. This has created some interest savings and the latter two payments have reduced the amount of variable-rate debt Oman holds and streamlined its debt portfolio. Net foreign borrowing in 2022 will be negative to the tune of around 4% of GDP.

We forecast government debt/GDP to then start rising, to 50% by 2025, as the budget swings back into deficit. Nonetheless, this projection compares favourably with the outlook at the previous review (above 65% of GDP). The government is seeking to lower state-owned enterprise (SOE) debt and we estimate it will decline in 2022 to 30%-35% of GDP, from around 42% in 2021, largely due to nominal GDP growth. Nonetheless, this remains high and a risk for government finances.

External Financing Pressure Eases: The government has fulfilled its external financing requirement for 2022 and has reduced the size of maturities in 2023 to USD1.7 billion. Oman's funding position is considerably more comfortable relative to recent years', although medium-term funding requirements remain sizeable and Oman's level of external indebtedness is high: we forecast gross external debt/GDP at 92% in 2022, compared with a 'BB' median of 55%. Sovereign external maturities average USD3.5 billion in 2024-2026. In addition, SOEs under the purview of the Oman Investment Authority (OIA), Oman's sovereign wealth fund, have USD2.2billion in average annual external debt payments in 2022-2024.

SNFA Improves, External Debt High: Sovereign net foreign assets (SNFA) are likely to turn marginally positive in 2022, slightly better than the 'BB' median, after deteriorating dramatically to -9% of GDP in 2020 from 53% in 2014. The Central Bank of Oman's gross foreign reserves will strengthen in 2022-2023 on the back of current-account surpluses and average above 4.5 months of current external payments, in line with the peer median. OIA's foreign assets remain broadly stable, close to USD17 billion. Oman's total net external debt position will also improve, but at 33% of GDP is double the 'BB' median.

Oman's 'BB' IDRs also reflect the following key rating drivers:

Growth Boost Will Fade: Real GDP growth will accelerate in 2022 to 4.4% from 3% in 2021, driven largely by the oil sector as Oman increases crude oil production alongside the OPEC+ taper. Non-oil GDP growth should strengthen mildly, to around 3%, given loosening pandemic-related restrictions, renewed population growth and a mild loosening of fiscal policy. We forecast growth to slow to 2.8% in 2023 and to around 2% in 2024-2025 as gains in hydrocarbon production level off, oil prices fall and the government pursues its MTFP. We forecast inflation to rise in 2022 but remain contained at 3.5% on average, helped by government price controls, before moderating to under 2% in 2023-2024.

Structural Challenges Will Persist: Most of Oman's structural indicators are above the 'BB' median, including World Bank Governance Indicators (WBGI). Nonetheless, potential social pressure resulting from the low employment rate of young Omanis remains a risk to public finances and political stability, in Fitch's view. The economy and fiscal revenue will remain heavily linked to the hydrocarbon sector, despite ongoing structural reforms to boost diversification.

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 WBGI have in our proprietary Sovereign Rating Model (SRM). Oman has a medium WBGI ranking at the 57th 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: A higher trajectory of government debt/GDP than the baseline scenario, for example, stemming from weak implementation of the MTFP, a materialisation of large contingent liabilities or lower-than-expected oil prices

-External Finances: Substantial deterioration of Oman's external balance sheet and liquidity conditions, for example, in the form of a large decline in central bank reserves and OIA assets

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Public Finances: Greater confidence in medium-term stabilisation of government debt/GDP and SNFA/ GDP through staying broadly on track with the government's fiscal reform programme

-External Finances: A sustained decline in net external debt/GDP, reflecting lower SOE external debt, lowering risks to Oman's external finances

- Public and External Finances: A sustained period of high oil prices that enables a material strengthening of the sovereign and external balance sheets

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

Fitch's proprietary SRM assigns Oman a score equivalent to a rating of 'BBB' on the LTFC IDR scale.

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

- Structural: We have added a -1 notch to adjust for the significant improvement in the SRM score which in part relates to cyclically high oil prices, which are boosting many of the model inputs based on nominal GDP

- Public Finances: -1 notch to reflect risks to government finances from contingent liabilities (with SOE debt at 30%-35% of GDP in 2022), high dependence on hydrocarbon revenue and other fiscal rigidities related, for example, to subsidies and wages

- External Finances: -1 notch largely to reflect Oman's large net external debtor position, which is double 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 LTFC IDR. Fitch's QO is a forward-looking qualitative framework designed to allow for adjustment to the SRM output to assign the LTFC IDR, reflecting factors within our criteria that are not fully quantifiable and/or not fully reflected in the SRM.

Best/Worst Case Rating Scenario

International scale credit ratings of Sovereigns, Public Finance and Infrastructure issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of three notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

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 WBGI 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 WBGI 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 indicators, 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 WBGI is relevant to the rating and a rating driver. As *Oman* has a percentile rank below 50 for the respective 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. As Oman has track record of 20+ years without a restructuring of public debt and captured in our SRM variable, this has a positive impact on the credit profile.

Except for the matters discussed above, the highest level of ESG credit relevance, if present, is a score of 3. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity(ies), either due to their nature or to the way in which they are being managed by the entity(ies). For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Fitch Ratings Analysts

Toby Iles
Senior Director
Primary Rating Analyst
+852 2263 9832
Fitch (Hong Kong) Limited 19/F Man Yee Building 60-68 Des Voeux Road Central Hong Kong

Hawa Ly
Senior Analyst
Secondary Rating Analyst
+44 20 3530 1280

Paul Gamble
Senior Director
Committee Chairperson
+44 20 3530 1623

Media Contacts

Alanis Ko
Hong Kong
+852 2263 9953
alanis.ko@thefitchgroup.com

Wai Lun Wan
Hong Kong
+852 2263 9935
wailun.wan@thefitchgroup.com

Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Oman	LT IDR	BB	Upgrade		BB-
	ST IDR	B	Affirmed		B

ENTITY/DEBT	RATING			RECOVERY	PRIOR
	LC LT IDR	BB	Upgrade		BB-
	LC ST IDR	B	Affirmed		B
	Country Ceiling	BB+	Affirmed		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 Ceilings Criteria (pub.01 Jul 2020)

Sovereign Rating Criteria (pub.11 Jul 2022) (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, v1.7.2 (1)

Debt Dynamics Model, v1.3.1 (1)

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

Sovereign Rating Model, v3.13.1 (1)

Additional Disclosures

Solicitation Status

Endorsement Status

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

DISCLAIMER & DISCLOSURES

All Fitch Ratings (Fitch) credit ratings are subject to certain limitations and disclaimers. Please read these limitations and disclaimers by following this link: https://www.fitchratings.com/understandingcreditratings. In addition, the following https://www.fitchratings.com/rating-definitions-document details Fitch's rating definitions for each rating scale and rating categories, including definitions relating to default. ESMA and the FCA are required to publish historical default rates in a central repository in accordance with Articles 11(2) of Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 and The Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019 respectively.

Published ratings, criteria, and methodologies are available from this site at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance, and other relevant policies and procedures are also available from the Code of Conduct section of this site. Directors and shareholders' relevant interests are available at https://www.fitchratings.com/site/regulatory. Fitch may have provided another permissible or ancillary service to the rated entity or its related third parties. Details of permissible or ancillary service(s) for which the lead analyst is based in an ESMA- or FCA-registered Fitch Ratings company (or branch of such a company) can be found on the entity summary page for this issuer on the Fitch Ratings website.

applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.

For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001.
Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the “NRSRO”). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see https://www.fitchratings.com/site/regulatory), other credit rating subsidiaries are not listed on Form NRSRO (the “non-NRSROs”) and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

Endorsement policy

Fitch’s international credit ratings produced outside the EU or the UK, as the case may be, are endorsed for use by regulated entities within the EU or the UK, respectively, for regulatory purposes, pursuant to the terms of the EU CRA Regulation or the UK Credit Rating Agencies (Amendment etc.) (EU Exit) Regulations 2019, as the case may be. Fitch’s approach to endorsement in the EU and the UK can be found on Fitch’s Regulatory Affairs page on Fitch’s website. The endorsement status of international credit ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.