

Oman Budget 2010

Royal Decree 1/2010

The government's budget for the 2010 fiscal year was endorsed by Royal decree on 2nd Jan 2010. It was another aggressive budget aiming development and growth, with spending maintained at a very high level as the government seeks to ensure that the economic recovery in the Sultanate gains traction.

The Major Highlight of the Budget:-

- Oil price assumed at \$50 per barrel
- General revenues for 2010 estimated to increase by 14% to RO 6.38 billion against the budget of 2009.
- Total expenditure projected to increase by 12% to RO 7.18 billion in 2010
- 2010 budget deficit will amount to RO 800 million, about 13% of the revenues and 4.8% of the 2009e GDP
- Higher than budgeted oil prices in 2009 is expected to cover most of the deficits which was estimated in the previous budget.
- Real GDP growth at 3.7% in 2009
- 2010 GDP is expected to register real growth of 6.1% and nominal GDP expected to grow at 18.4%.

A deficit of RO 800 million is projected, based on revenues of RO 6,380 million and spending of RO 7,180 million. Education, health, defense, and social security remain the major focus areas of government spending.

Confidence booster and expansionary budget

Government spending played a vital role in supporting the economy during 2009, but weak confidence and tight credit conditions have constrained the private sector response. By maintaining high spending, particularly in the form of investment spending, the government aims to reassure the private sector about its confidence in the economic outlook. The projected deficit is not a problem as it can be comfortably financed through the drawing down of CBO's net foreign assets, which stood at RO 4.63 billion at the end of October 2009.

Macro Economic Highlights - 2009

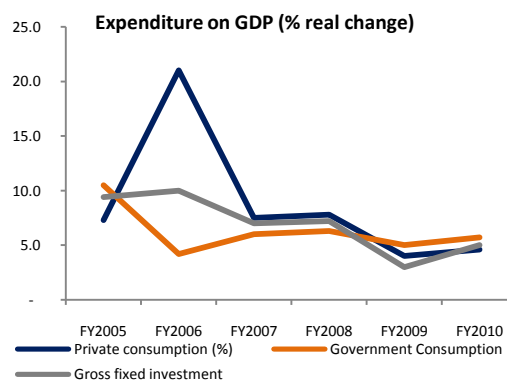
**Oil exports down by 41%,
Non oil exports grow by
16; and re-exports growth
at 14%**

Though 2009 was a year of major economic turbulence and subsequent recovery, Oman managed to post a real GDP growth of 3.7 percent despite a 20 percent contraction in nominal GDP. Nominal GDP is estimated to have reached RO 18.5 billion at the end of 2009 and is expected to grow by 18.4 percent in 2010, thus reaching very close to record levels of 2008. Total oil activities recorded contraction of 37% in nominal terms while non oil activities recorded marginal nominal contraction of just 2.2%. However, non oil activities in real terms expanded by 2.9% during 2009.

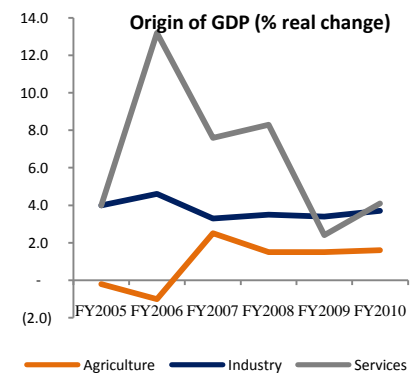
	2005	2006	2007	2008	2009	2010
Nominal GDP (RO ,000)	11,884	14,152	16,011	23,185	18,548	21,960
Real GDP growth (%)	5.8	7.5	5.8	6.4	3.7	6.1

Source: EIU reports

**Import value down by 23%;
BoP surplus down by 32% at
RO 4.4 billion**



Source: EIU reports



Source: EIU reports

**CA surplus at RO 212 mn;
down to 1.1% of GDP
against 9.1% in 2008**

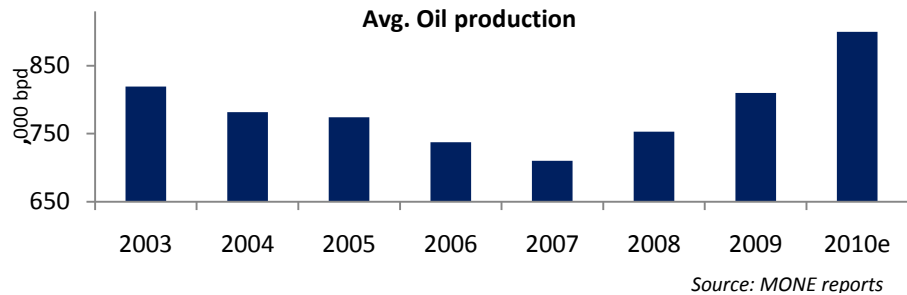
Fiscal indicators (% of GDP)	2005	2006	2007	2008	2009	2010
Public Sector revenue	38.00	35.20	37.00	37.60	34.90	35.20
Public Sector expenditure	35.40	34.90	36.70	36.30	34.20	33.00
Public Sector balance	2.50	0.30	0.30	1.30	0.70	2.20
Net Public debt	4.90	3.80	3.10	2.80	2.90	2.60

Source: EIU reports

The government is targeting real GDP expansion of 6.1% in 2010 by effectively employing its resources and continuing with the focus on physical and social infrastructural developments.

Details of Budget 2010

Preliminary economic data for 2009 were stronger than we had anticipated. Real GDP grew by 3.7 percent despite a large contraction in the oil sector. Non oil sector growth was 2.9 percent with all sectors of the non oil economy growing. Lower oil revenues pulled the current account surplus to RO 212 million in 2009 compared to RO 2.1 billion in 2009.



Oil production and price assumptions

We believe that the oil price assumption of \$50 per barrel is a conservative assumption and we expect Oman Crude to average \$70 per barrel during 2010. The government envisages around 10% increase in oil production during the year as compared to 2009 production levels. With the help of enhanced oil recovery systems being implemented in many of the oil fields, the government targets an average oil production of 900,000 bpd by the end of 2010. During the first 10 months of 2009, average oil production surpassed the targeted daily production of 805,000 bpd and recorded highest ever production rate of 807,400 bpd. Continuing with this momentum, we feel that achieving the targeted production for 2010 would not be overly optimistic.

Largest ever deficit in 2009 budget; 2010 budget deficit at slightly lower levels

Following a largest ever budgeted deficit of RO 810 million in 2009, the government has continued with its decision to keep spending at high levels in order to stimulate the economy. The RO 800 million deficits are still rated as one among the largest in nominal terms, though it is equivalent to only 4.8 percent of GDP. Across the world one of the key economic challenges for 2010 is the withdrawal of government stimulus. This is not a problem for the Sultanate as it is not facing major budgetary constraints (budget deficits are projected to exceed 10 percent of GDP this year in the US and UK) and any deficit can be comfortably financed from CBO's huge stock of foreign assets. We expect government spending to be at the budgeted level, and forecast a current account surplus of around RO 782 million for the year.

Revenue

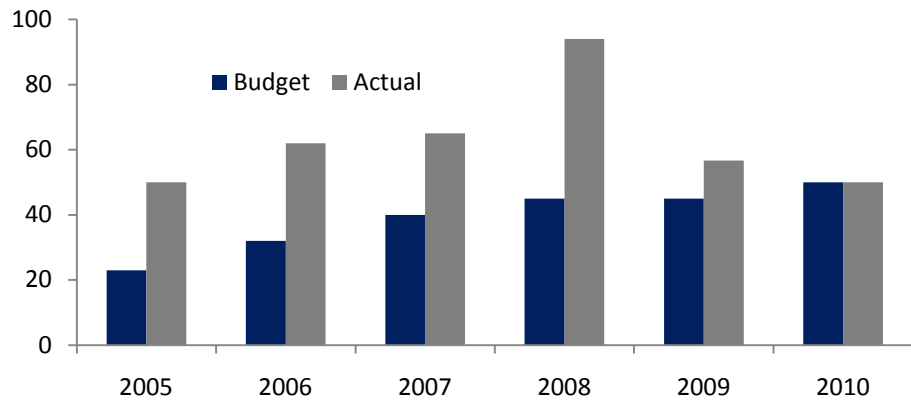
Total revenue is budgeted at RO 6.38 billion, up from RO 5.61 billion in 2009. Oil and Gas revenues constitute 76 percent of the total revenues. The oil



13.6% increase in revenue; Oil and Gas to form 76% of revenues

revenues were estimated at an assumed average oil price of \$50 per barrel and accordingly the oil revenue is estimated to be around RO 4.05 billion during 2010, contributing to 63% of the total revenues. Gas revenues are expected at RO 800 million, contributing to 13% of the total revenue. Non oil revenue is expected to grow by 8% over 2009 levels to reach at RO 1.53 billion. Over the years the contribution from oil revenues to total revenue has shown a declining trend and the same have reached at 68% in 2010 as against 83% in 2006.

Oil price assumptions



Source: MOF, Budget documents

It is usual for the budget to be based on a conservative oil price assumption. Over the last 6 years the actual oil price has averaged over 60 percent higher than the one used for the budget (for 2009, it is 26 percent higher). WTI is currently trading at \$81 per barrel, 62 percent above the assumed oil price for the budget. We think that the current price is above that justified by the demand and supply fundamentals owing to the influence of financial investors.

Investment income to be higher than 2009 levels

The main sources of non oil revenues are fees and charges for government services and customs tariffs, both of which are likely to grow modestly in line with stronger economic performance. Taxes and fee revenue are estimated to be at RO 682 million while revenues other than tax income are estimated to reach RO 781 million. Investment income is expected to be at RO 481 million, which gets benefitted from higher (albeit still very low) returns on the foreign government bonds that constitute the bulk of the government's foreign investments.

Expenditure

Total expenditure for 2010 is budgeted at RO 7.18 billion. This is 12 percent above the level budgeted for 2009. Budgeted capital spending has been

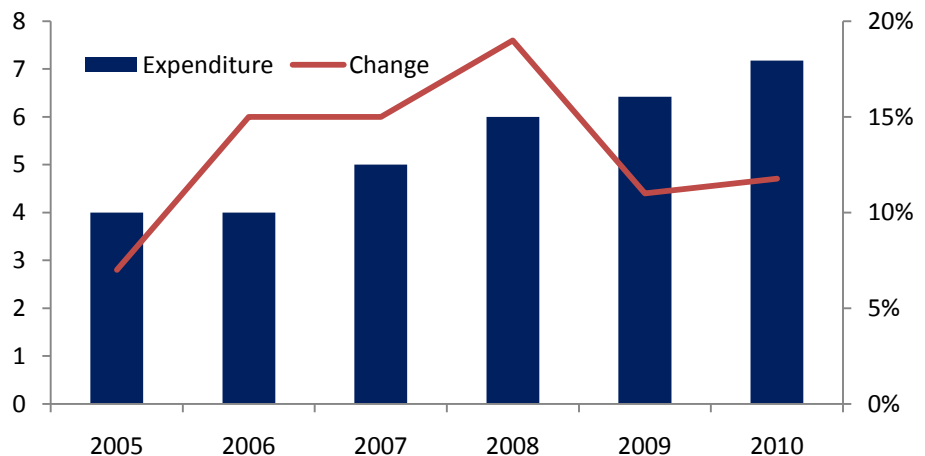
12% increase in expenditure; focus on physical and social infrastructure

raised by 10 percent to RO 4.7 billion. Current spending is projected to rise by RO 330 million to RO 2.5 billion. Spending maintains the focus of recent years and is centered on enhancing physical and social infrastructure. Education is allocated the biggest share of those departments disclosed in the budget. Spending plans for key public sector areas outlined in the budget include:

Education and training spending is budgeted to rise by 10.5 percent to RO 874 million. Work will begin on construction of a number of new schools at various regions.

Health sector receives RO 294 million, an increase of 8%. A number of new health centres at various regions are planned for during the year.

We believe that defense and security is the largest component of government spending, though this data is not reported in the budget. Defense and security accounted for 23% of the 2009 budget and may have been kept at similar levels.



Source: MOF, Budget documents

Development budget allocations to increase by 18%

Allocations for the development budget stand at RO 950 million, showing an increase of 18 percent over the 2009 budget. These allocations are set to cover the ongoing as well as new projects listed in the Seventh Five-Year Plan (2006-2010) under different sectors. This sends a strong signal that the government is determined in its plan of going forward with developmental projects. We see this as a major positive boost for manufacturing and contracting companies operating in the Sultanate.

The excess of planned aggregate expenditure of RO 7.18 billion over budgeted revenue receipts of RO 6.38 billion is estimated to leave a budget deficit of RO 800 million in 2010 which is 12.5 percent of revenues and 4.8 percent of 2009e GDP.



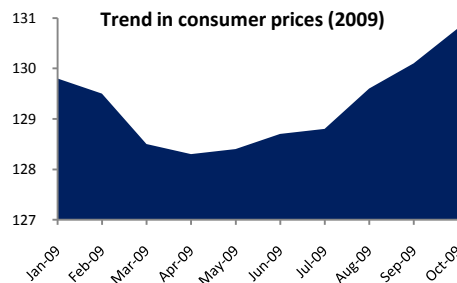
Deficit at 12.5% of revenues; 4.8% of 2009 GDP

We don't think that financing this budget deficit would be a problem as it can be done by withdrawal from State General Reserve Fund or by drawing down the stock of foreign assets built up in recent years. At the end of October net foreign assets at CBO stood at RO 4.63 billion. This stock of assets the government can call on gives Oman an advantage of easing the impact of extreme financing pressures while many of the advanced economies are facing problems.

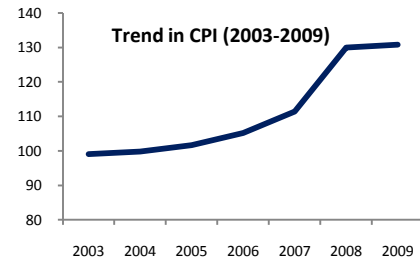
Inflation

Inflation down compared to 2008 levels; expect to have bottomed

Barring extraordinary inflation levels during 2008, Oman historically had very low levels of inflation. The data of the CPI in the Sultanate indicate a decline in inflation rate in 2009 to about 3.7% compared to 12.4% in 2008. The marked downturn in inflation rate could be attributed to the drop in commodities prices in global markets resulting from the global financial crisis that led to contraction in global demand, and the monetary policies adopted by the government.



Source: MONE reports



Source: MONE reports

We believe that the inflation levels have bottomed during 2009 owing to a strong dollar, low commodity prices and consumer spending. With commodity prices eyeing for 2008 highs, dollar getting weak against major currencies, and consumer spending to gain momentum with economic recovery, we expect the inflation levels in Oman to remain at higher levels in 2010 as compared to 2009.

Outlook – Confidence booster and expansionary budget

The budget addresses all segments of the economy like oil and gas, infrastructure development and social welfare, and stresses on economic diversification. In our budget review for 2009 we had indicated the average oil prices to be around \$60 and a possible surplus in the fiscal balance, which turned out to be a reality. We believe that the oil prices would float above budgeted levels during the year on account of recovery in the global economy and the reduced production policy adopted by OPEC. We forecast a



surplus in current balances at the end of 2010. This is because we expect the oil revenues to exceed budgeted levels and the tendency of the government for overspending above the budgeted levels to be curtailed as 2010 being the last year of seventh five year plan.

We continue to be positive about Oman’s economy in the long term as the government moves ahead with its investment expenditures. We believe that despite relatively lower levels of oil production, ongoing investments in infrastructure related projects are sustainable and this would spur the economy over the long term. This is supported by the government’s willingness to move ahead with its spending plan. Our view on various sectors based on the budget allocation are tabulated below

Sector	Our view	Remarks
Banking	Positive	Credit expansion to continue after a pause in 2009; Higher cost of funds expected to be offset by lower provisioning during the year.
Leasing	Neutral	Excess capacity to hinder new private sector investment in equipments; Higher cost of funds to pressure margins. Asset growth anticipated towards the second half of the year.
Industry	Positive	Demand driven capacity utilisations.
Cement	Positive	Infrastructure projects to boost demand for cement; margin improvements as a result of capacity expansion
Oil marketing	Positive	Throughput volumes for commercial and aviation segment to increase
Port services	Neutral	Capacity driven expansions to smoothen vessel traffic and cargo movement; Higher vulnerability to investment income a rider
Engg & Contracting	Positive	Increased project activity to help in acquiring better orders
Investment Holding	Neutral	Lower base to affect positively on relative valuations
Telecom	Neutral	Mobile penetration rate to moderate while broadband penetration to increase. Blended ARPUs to get stabilise during the year.
Utilities	Neutral	Stable income and profitability to continue in the absence of any capacity expansions



	Budgeted Figures			
	2008	2009	2010	Change
Figures in RO millions				
Net oil revenues	3,610	3,522	4,050	15.0
Gas revenues	620	670	800	19.4
Current revenue	1,130	1,355	1,477	9.0
capital revenue	32	54	40	-25.9
capital repayments	8	13	13	0.0
Total revenue	5,400	5,614	6,380	13.6
Defense and Security Expenditure	1,360	1,545	1,615	4.5
Civil Ministries	1,905	2,149	2,480	15.4
Oil Production expenditure	180	196	212	8.2
Gas Production expenditure	50	76	80	5.3
Interest on loans	55	54	45	-16.7
Total current expenditure	3,550	4,020	4,432	10.2
Civil development expenditure	725	800	950	18.8
Civil capital expenditure	20	21	20	-4.8
Oil production expenditure	670	679	725	6.8
Gas production expenditure	450	419	433	3.3
Total capital expenditure	1,865	1,919	2,128	10.9
Total participation and subsidies	385	485	620	27.8
Total expenditure	5,800	6,424	7,180	11.8
Deficit	400	810	800	-1.2

Source: MOF, Budget documents

Current Account	2005	2006	2007	2008	2009	2010
Trade Balance	4,101	4,503	3,980	6,543	4,206	4,321
Exports	7,189	8,303	9,497	14,507	11,293	9,617
Imports	(3,088)	(3,800)	(5,517)	(7,964)	(7,087)	(5,296)
Services balance	(848)	(997)	(1,248)	(1,595)	(1,154)	(1,394)
Income balance	(393)	(256)	(326)	(852)	(1,032)	(888)
Current transfers balance	(868)	(1,072)	(1,412)	(1,993)	(1,793)	(1,258)
Current account balance	1,992	2,177	995	2,103	140	782

Source: EIU reports



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