KCS Group Europe

KCS Country Risk & Threat Advisory

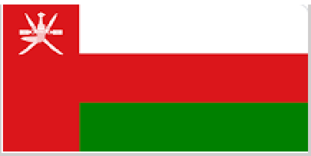
KCS Group Europe
Risk & Threat Advisory Paper

OMAN

Strategic uncertainty in a testing time

March 2020

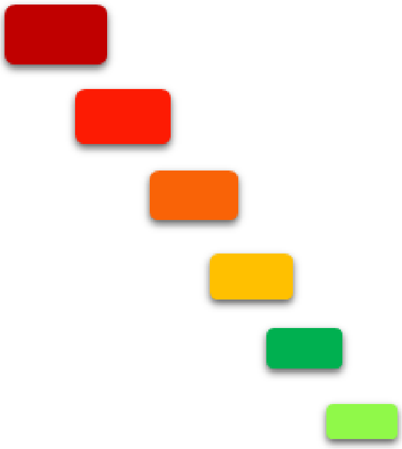
Political Risk Advisory Briefing



Country:	Oman
Population:	5 million (of which 3 million are native)
Source:	United Nations

Oman has a Risk Rating of 3

6	**Very High**	The assorted threats described in the report are almost certain to have a derogatory effect.
5	**High**	The threats are extremely likely to negatively affect the business.
4	**Very Possible**	There is a strong likelihood of problems arising in this country.
3	**Possible**	There is a fair chance of problems arising in this country.
2	**Low**	There is a low likelihood of any threats impacting business.
1	**Very Low**	There are virtually no impediments to successful business in this country.



Political

Oman is now entering uncharted waters. After fifty years of strong governance, albeit originating from a military coup, Sultan Qaboos Al Said is gone and the country has a new ruler, for many the first in their lifetime. Given that Qaboos' cousin, Haitham Al Said, was swiftly appointed to the throne – as much driven by his name being the Sultan's personal choice as to secure a quick and peaceful succession – there will, in the short term, be political continuation and a sense of *'business as normal'*. However, this succession could not have come at a more tense or difficult time for the Middle East region and across the coming months the traditionally neutral, calm Oman could find itself at the centre of the world's attention in more ways than one.

Sultan Haitham's first public speech was to declare that his two main policy objectives would be continuing Oman's pressing for peace in the region, and developing the economy. While the second is discussed in greater detail below, peace is a more nebulous goal to achieve and Oman is in the curious position of being the least involved (with a strict policy of neutrality) but the most strategically important – bordering both Yemen and Saudi Arabia, and facing Iran across the seismically strategic Straits of Hormuz. It sits at the literal epicentre of the region and realistically, cannot pursue a policy of further isolation if it hopes to see peace.

In keeping with neutrality, Oman remains politically apart from the rest of the Middle East: most notably taking no stance in the ongoing Saudi Arabia-Qatar blockade, facilitating the talks that led to the landmark 2015 nuclear deal, and actively hosting Yemen's Houthi rebels, at war with the Saudis for years. This has led the country to be seen as something of an honest broker, and one that is respected in terms of its position – if not universally liked.

But it is inevitable that there will still be political tensions under the surface. Somewhat expectedly, these are predominantly driven by outside actors. Long a British protectorate, the British influence over Oman remains strong in terms of trade and military support – and Britain sees Oman as a major driver (and facilitator) of its foreign policy objectives in the region. Meanwhile, the USA uses Oman as a staging point for military intervention and is insistent that the latter must reduce its ties with Iran (indeed President Trump has all but ignored Oman during his tenure). With such powerful nations each trying to sway Oman to their geopolitical will, Oman may find its neutrality – and its peace – difficult to keep.

Economic

Sultan Qaboos was rightly acclaimed for his modernisation of a country that, up until his rule, barely merited a mention in international politics and was internally paralyzed: hardly unexpected for a state with a literacy rate of 5% and just three schools. Qaboos ensured that Oman saw a veritable explosion of infrastructure, investment and political engagement (albeit that the Sultan was always in command) and, in short order, had transformed Oman into a modern state, viable on the world stage.

Oman boasts far less reserves of oil than its neighbours – believed to be a little over five billion barrels – and is reliant on both oil and gas for practically all of its energy needs. By the early 2030s there will be no oil left; and the idea of an oil-based economy will by necessity be outdated. Therefore, the need to diversify is now an overriding economic goal, more so than just modernisation alone. A forthcoming five-year plan, one of many in service to the Vision 2040 program, will see an intensification of efforts in manufacturing, tourism and mining and attempt to solidify Omani excellence in all of these industries, enough to see a pivot away from hydrocarbons and towards a more diverse economy.

Saudi Arabia invests a great deal in Oman but is increasingly perturbed that the latter continues to enjoy a wealth of trade with Iran. There have been suggestions that if this were to continue, the KSA might withdraw its investments. While this would be a political ploy, with Oman unlikely to compromise so openly on its neutral outlook, the financial impact could be significant – not least the Dh44.7m promised by the Saudis and projected to boost Duqm Port as a key driver in diversification. Once again, political games might interfere with economic necessities.

It seems that there is little chance of dethroning the UAE as the Middle East's premier financial destination, but aside from these extant and burgeoning industries, Oman would for instance be ideally placed to take a lead in renewable energy, particularly hydro-driven given its expansive coastline, and the start-up tech sector (in which it has already professed an interest). It is certainly encouraging that the *'gap'* has been spotted early on and is being taken very seriously. The key now will be twofold: to ensure that momentum is not lost in the transition to the new Sultanate, and to manage current and ongoing problems such as a budget deficit and rising unemployment that might risk destabilising the carefully managed situation.

Social

Given the manner in which he succeeded his father, and the undeniable improvement in the quality of life of practically every Omani, Qaboos was a well-loved and respected ruler who, despite running an autocratic monarchy, appeared to be held in genuine affection. But even Oman experienced the wave of protest that swept the Arab world in 2011, albeit to a more minor extent. Thousands took to the streets between February and May, and while Qaboos proposed economic reform and removal of unpopular ministers, he nevertheless detained and jailed a number of protestors between 2012-2013.

Since this point there have been no outright protests, and nothing suggests that Sultan Haitham will face the same kind of unrest. However, given the almost unthinkable outright protests against the Iranian government across the Straits of Hormuz, this cannot be ruled out should the regional temperature continue to rise. But it is not envisaged that any movement will be large, or vocal enough, to cause more than a minor inconvenience to the Sultan.

The media remains broadly sympathetic, although this can be put down as much to benevolent dictatorship as much as genuine loyalty. However, a broader problem could arise if a troubled economy, fuelled (ironically) by a failure to successfully diversify, leads to social grievances on a fundamental, rather than political, level. This would most likely lead to an intensification of troops-on-the-street (with the Omani police already making a strong showing in general) and a downturn in the market. We have seen in Hong Kong what happens with sustained protest, even where there has historically been no *'tradition'* of this.

Terrorism and security

Oman is a stable state with a strong security infrastructure, and has never been subject to a terror attack. This is not by chance: under Qaboos, non-Muslims had the right to worship in their holy places, education was promoted massively, and the peace-making role helped to diffuse domestic tensions. While no state can ever be said to be truly safe, Oman is as safe as the Middle East comes.

Although not currently afflicted by organised crime in the manner of, say, Russia or Japan, Oman is aware of the degree to which crime is becoming transnational and evolved across not only state lines, but also in its means. Given Oman's strategic location in three ways - the heart of the Middle East, the gateway to Asia and directly facing Iran across the Straits of Hormuz – it is beloved of smugglers and traffickers as a crossroads where crime can flourish. The National Centre Bureau works closely with Interpol to shut down organised crime in Oman, but not with 100% success. Notably, in the field of trafficking, Oman has been on the USA's *'Tier 2'* watchlist since 2017, indicating that there remains an inherent weakness in the security posture. Certainly, no business would actively want to collude with or benefit from, traffickers, but the reputational consequences of accepting business from those later found to rely upon it would be extremely damaging.

While the threat directly from within Oman is therefore minimal, it is the state's positioning that is largely likely to cause problems, with a chance that a firm could be used as a scapegoat or unwitting partner, or be directly targeted because of their work, by external criminal interests.

Added to this is the cyber-dimension, and it is reported in recent times that attempted blackmail via phone apps is on the rise, as are phishing and spoofing emails. For what it is worth, Oman is ranked as the third most prepared country in the world according to the Global Cybersecurity Index prepared by the International Telecommunication Union, largely down to its cyber-security strategy that mandates continuous investment in cybersecurity, and early adoption of forward-thinking and educative practices. This does not mean the country is totally secure – but it is certainly head and shoulders above its neighbours.

Legal

The Sultan's rule is paramount in Oman. There is no separation of powers and no system of checks and balances. The Sultan promulgates laws known as primary legislation, or Royal Decrees, and these in turn import secondary legislation to be enacted by ministers, all under a Sharia system.

While the Omani legal system is for the most part a relatively fair one, given that it is an absolute monarchy there will be pitfalls. Media critical of the Sultan – be it print or online – is routinely suppressed and there are harsh penalties for slandering the sultan or 'undermining the prestige of the state'. It is possible that one could unwittingly fall foul of these laws, or experience political problems by partnering/hiring an individual with previous *'distasteful'* history.

As of the most recent Financial Action Task Force report on Oman, the country was found to have implemented all but seven of forty recommendations that would bring it in line with international standards, but there remained gaps in areas of politically exposed persons, prohibiting anonymous/falsely-named accounts, and the lack of mandated due diligence concerning money laundering or terrorist financing.

Environment for business

Sultan Haitham is regarded as a business-positive leader and the already extant Omani system is relatively positive towards creating a conducive business environment. A significant benefit to Vision 2040 is that Oman's economic and expansive goals will require a lot of foreign investment, and as such these is encouraged through a number of channels. Firstly, the creation of three Free Zones at Salalah, Sohar and Al Mazyunah that offer foreign investors specific benefits in importing, exporting and trading. Free Zone companies also benefit from tax exemptions and can be 100% foreign owned. Moreover, the Foreign Investment Law introduced in January 2020, designed specifically for expats and foreign nationals, ensures that investors will receive 'incentives, privileges and guarantees' and will itself encourage further foreign investment.

Oman – because of its strategic location – is open to approaches from any state, acting as a starting point for Chinese and Indian regional interest, most notably with Duqm Port (which has seen significant Chinese investment) acting as one end to the Belt and Road Initiative. It keeps a strong Asian focus, with the aforementioned countries its top two export destinations, China in particular accounting for 39%, and Japan and South Korea also in the top five. As regards imports, the UAE leads the way on 34% and with the Asian tigers all showing strongly as well. Meanwhile, the USA enjoys a Free Trade Agreement removing all non-tariff barriers and customs.

Low-level corruption (particularly bribery) remains a key issue and it was in light of this that the revised 2019 penal code was introduced, cracking down harder on facilitation payments, embezzlements and misappropriation of public funds (to name but three).

There is always more to be done. The Implementation Support & Follow-up Unit (ISFU), responsible for the economic diversity of Oman, confirmed as such in its most recent annual report in which it stated a greater need to boost Oman's global appeal in key sectors including tourism, mining, energy and business – exactly the ones it needs to encourage foreign investment – and calling for increased ease of implementing legislation. If the momentum can be maintained, the investment climate will grow ever more beneficial.

Snapshot overview

Strengths • Strong economy, a secure and stable system of government. • Arguably the most cyber-secure state in the region. • A long history of, and legal system conducive to, expats and foreign investment.	*Weaknesses* • Still almost entirely reliant on extractives to power the current economy. • Low-level corruption still to
Opportunities • Keen to push for diversification of industry over the next twenty years. • Open to multiple new/growing sectors and investments.	*Threats* • Risks being seen as a pawn in international political games. • Potential for a left-field turn under a new Sultanate.

GREY AREA DYNAMICS

Over the years, KCS has made it their business to find workable solutions to impossible problems. To do this, KCS has sought to establish clearly the intelligence gap between perception and reality.

In today's market where terrorism, organised crime, cybercrime and government sponsored cyber espionage and war appear to confront us daily, we need reliable tools to identify the risks well in advance. It was for these reasons that KCS created and developed the analysis of risk by Grey Area Dynamics or GADs, as they are often referred to.

GADs are all the risks, weakness and threats that will, at one time or another, interfere, disrupt or at worst close down businesses. In the projects and work in which KCS have been involved in all over the world, it has been evident that the GAD's identified, can and do kill. This method of risk assessment and measurement goes well beyond standard due diligence and is a collective description of factors, which can be passive and non-passive, legal and illegal. Because GADs are difficult to quantify or assess from a purely economic viewpoint, these considerations do not normally feature in most credit ratings, investment and banking reports, which focus only on sovereign risk.

The main categories of Grey Area Dynamics usually encountered are:

Passive/Legal

- *Tribalism and Integration* – The late Sultan was responsible for bringing the tribes of Oman together – unlikely, but possible, that an alliance could fracture if further modernisation meets resistance.
- *Regulations, Taxes and Duties* – laws have been toughened up against suspected tax evaders, with penalties increased for late filings/returns and increased police freedom to raid premises.
- Currency & Capital exposure – although the general risk of money laundering (and terrorist financing) in Oman remains low, cyber-compromise is on the rise and this will have a direct effect on capital loss.

Non-Passive/Legal

- *Absence or effectiveness of Legal Safeguards* – no separation of powers and no checks and balances on the wishes of the ruler.
- *Overt and disguised/beneficial ownership* – there remains little legal mandate to confirm beneficial ownership or proxies in any business transaction.
- *Bureaucracy and Local Government* – in places remains 'heavy' and there is an acknowledged need to smoothen and streamline the bureaucratic system.

Passive/Illegal

- *Bribery & Corruption* – still present throughout multiple levels, although officially bribery is forbidden.
- *Vested Interests and Cronyism* – the law is cracking down on officials accused of corruption in the oil and gas sector, but as befitting such a valuable industry it is likely to be more widespread than will be caught.
- *Patronage* – those vying for power and influence with the Sultan could use companies as bargaining chips or political tools.

Non-Passive/Illegal

- *Counterfeit & Fraud* – faked products are on the rise in Oman and the Ministry of Commerce acknowledges the need for greater protection of intellectual property.
- *Organised Crime* – Oman is at a trafficking crossroads and this plays into the hands of organised crime, as well as affecting those that may unwittingly benefit from this.
- *Civil Unrest* – there is a small chance that political demonstrations could arise again, if Iran's instability sparks a second wave of protest across the Middle East.

For a risk assessment to be thorough, it must encompass the potential for a broad array of economic, political and business situations that might affect a business venture. Evaluations limited just to political issues or financial factors may be completely misleading.

The degree of severity of a risk portfolio will also depend on the origin of the investing entity; for example, European companies often face different risk profiles to American corporations considering the same investment opportunity.

Grey Area Dynamics pose a challenge of diagnosis[1]. The key to avoiding problems before they occur or solving them after they have begun to take a toll on performance, lies in their early identification and evaluation. Ignoring the impact of GAD's can be a costly business.

[1] KCS Group Europe won the European Service Provider of the Year, 1999-2000 at the European Risk Management Awards magazine International Risk Management for their work on GADs. In 2004, the company won an award for Product of the Year from StrategicRisk.