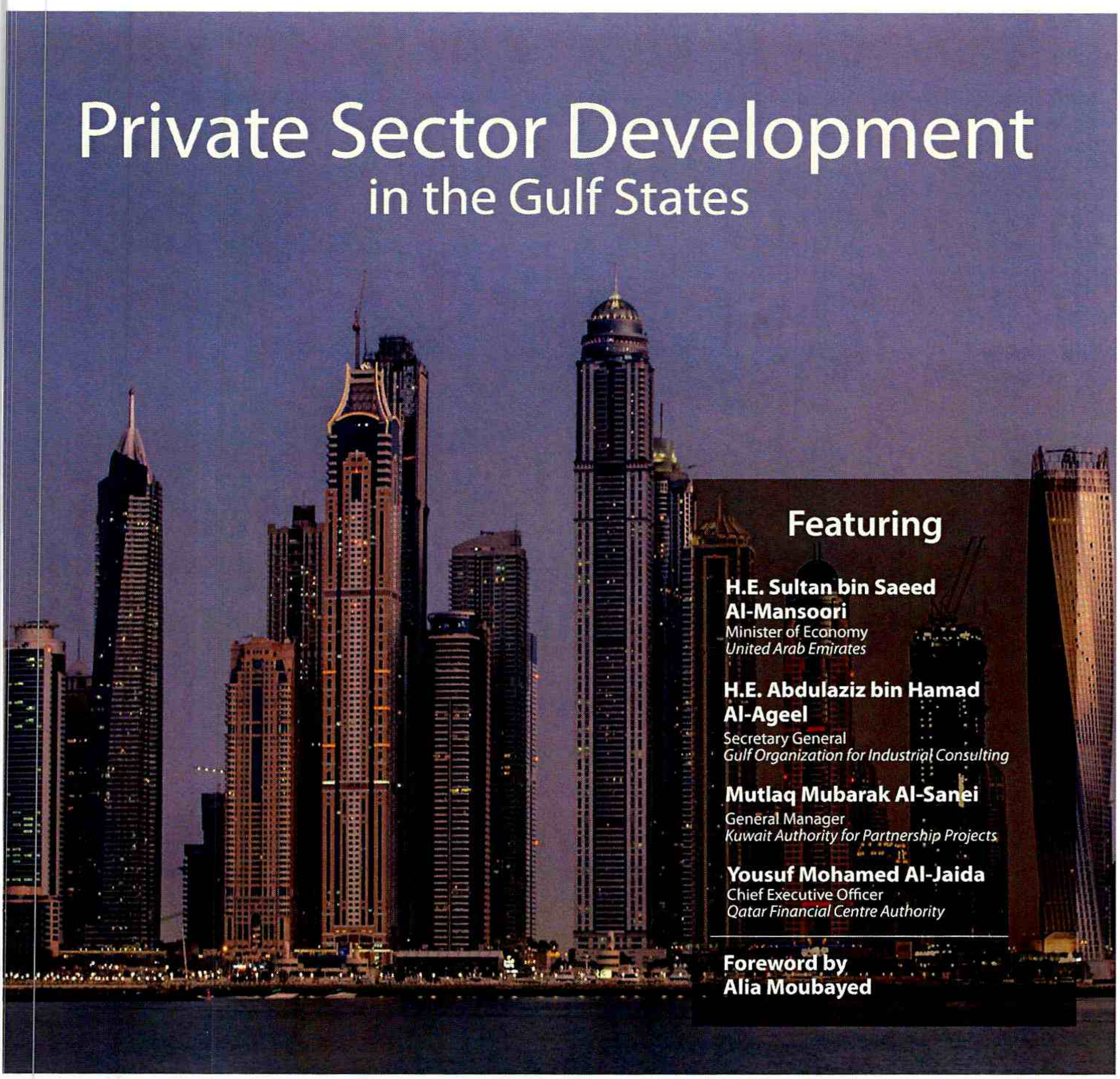
OXFORD
GULF & ARABIAN
PENINSULA STUDIES
FORUM

UNIVERSITY OF OXFORD

GULF AFFAIRS

Summer 2017

A Publication based at St Antony's College



Private Sector Development
in the Gulf States

Featuring

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The Case for a New Economic Model in Oman

by Yousuf Al Balushi

Promoting private sector-led inclusive growth

The Sultanate of Oman, like other Gulf Co-operation Council (GCC) countries, has experienced robust economic growth over the last four decades under a state-led development model. But a number of challenges lie ahead, including the need to create adequate employment opportunities for Omani nationals, ensure high economic growth-rates are sustained and secure enough funds to cover future development projects. The private sector can play a major role in meeting these challenges, mainly through reducing the government's reliance on oil revenues, diversifying the economy and further developing national human capital.

Over several decades, the Omani government has provided significant support to the private sector in terms of infrastructure development, various forms of financial incentives, erecting a business-friendly legal framework and encouraging free competition to stimulate innovation. Yet Oman, much like other GCC countries, still has a weak and somewhat inefficient private sector that is largely dependent on the government.

The private sector in Oman is mostly characterized by small businesses that are owned by individuals or families, which typically offer low-wage and low-skill employment. This has led to a fragmented private sector that lacks the financial means and skills to do business on a large scale. In fact, private sector enterprises prefer hiring migrants who accept lower wages, require less training and are subject to more flexible labor market regulations than Omani nationals.

Although the private sector in Oman continues to grow, much of this growth is driven by heavy government subsidies of capital, energy and infrastructure (sometimes even for free). This approach provides little incentive to increase productivity, which requires investment in technology and conducting research and development. To this day, Oman's private sector depends on government spending that is financed by external rents (oil and gas revenues). In turn, this makes the state the leading source of business growth.

Toward a thriving private sector

The Omani government is aware that the state-led development model can no longer be relied upon to sustain long-term growth. Shifting toward a private sector model will therefore be crucial—in particular, to align profit maximization incentives with the twin social objectives of shared growth and job creation for Omani nationals. Undoubtedly, achieving this alignment will require careful coordination between the three pillars of economic development: government, business and society.

Accumulating technical know-how in the areas of production and marketing will ensure a successful transition. A variety of institutions associated with finance, labor, regulation and trade are needed in this endeavor. These institutions balance and protect the rights of all concerned government bodies, private sector firms and society at large.

In the financial sector, there needs to be more emphasis on channeling domestic savings toward productive sectors instead of consumption. Equally important is to tackle the common barriers to market for businesses, including the availability of and access to affordable credit, collateral constraints and the inappropriateness of existing lending products. Moreover, supporting private investment in the non-oil sectors and in small-to-medium enterprises is central to developing an active and more efficient private sector.

In the labor market, existing challenges have multiple dimensions. First, there is a weak link between the job market and vocational and training programs, which results in job seekers who don't have the necessary work skills. Second, the quality of basic education in Oman is poor, and is not producing students who can handle the soft skills (transferable skills like communication and problem-solving) required in most professional settings. In addition, the availability of low-cost migrant labor has driven wages in many sectors well below what nationals would willingly accept. The government should pay more attention to the balance between political stability, huge fiscal costs and its long-term commitment to recruiting the increasing numbers of job seekers.

It is also important to promote entrepreneurship and to encourage Omani nationals to choose private sector work over serving in the government. There needs to be a better balance between guaranteeing public sector employment for nationals and ensuring the private sector is competitive and flourishing. But to meet labor market demand, the government should first re-evaluate existing manpower institutions or create new ones that encourage high technical and managerial proficiency.

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Thinking globally

Recognizing the constraints of Oman's small domestic market and the economic opportunities globalization offers, the Omani government should focus on encouraging regional and global integration in order to boost productivity and growth. By doing so, Oman can benefit in two important respects. First, by importing much-needed ideas, technology and know-how from abroad; second, by tapping into global demand, which provides a deep elastic market for Omani goods.

Oman should also look to attract foreign direct investment (FDI) from countries that promote productivity spillovers and that have less restrictions in partnering with domestic firms. At the same time, Omani policymakers should encourage multinational corporations already operating within the country to establish business support centers that assist local businesses in securing investors. These steps could help Oman maximize the potential benefits of FDI for competitiveness and sustainable development alike.

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