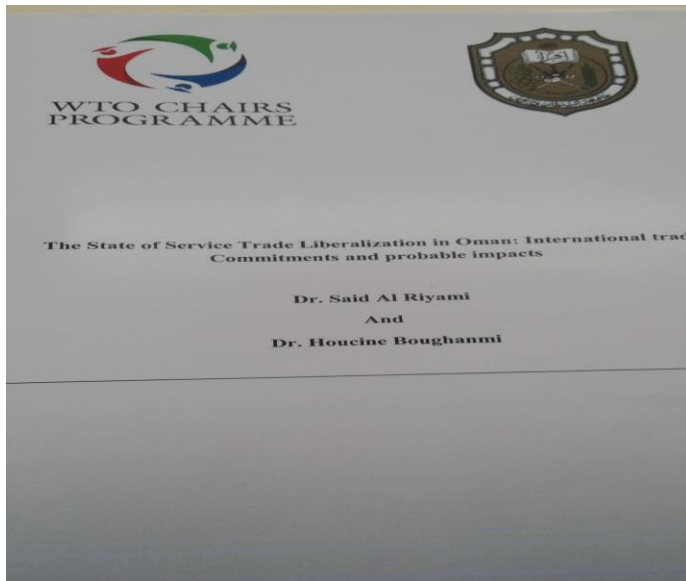


## OUTREACH

### Collaboration

The chair conducted a study on service trade liberalization in Oman collaboration with the Ministry of Commerce and Industry. The study was completed on June 2016 and submitted to the Ministry for review and comments.



## Executive Summary

1. The service sector in Oman contributes around 41% to the Gross Domestic Product (GDP) and has shown a sustained annual growth of 12% during the last four years. This compares favorably with the industrial and agricultural sectors where the annual growth during the same period reached 9 and 7% respectively. Three subsectors, “Public administration”, “wholesale and retail trade”, “transport, storage, communication” constitute more than half of the total service value added. The demand for the service activities is expected to increase as the economy diversifies away from oil.

2. Trade in service as reflected in the balance of payment showed an increasing negative balance over the years, with an annual deficit growth of 12% during the last 4 years. In 2014, service trade deficit amounted to R.O 2754 Million. Transport service is the main import item, covering more than 38% of total service imports, while “travel” is the main export item constituting around 44% of total service exports. Export of service contributes around 12% of total non-oil exports of goods and services.

3. Trade in service is not totally reflected in the balance of payments statistics as services are intangible and can be traded in a variety of ways, which make it difficult to measure and record. A lot of trade in services takes place through foreign investment in the form of commercial presence in the country.

4. This study is concerned with the status of service trade liberalization in Oman and its probable effect on market conditions and performance within the sector. The status of service trade liberalization was described by analyzing and comparing Oman's liberalization commitments under GATS and under the preferential trade agreement with the USA. As many of these commitments do not reflect actual policies, the commitment under international agreements is complemented by a Service Trade Restrictiveness Index (STRI) analysis focusing on the most important services and using the most recent available data on applied service trade policy.

4. Upon its accession to the WTO, Oman scheduled commitments in 97 subsectors out of the 160 sub-sectors included in the GATS sub-sectors' classification list. It is shown that with commitments in 97 subsectors, Oman has the third most extensive GATS commitments in the Arab region, following Saudi Arabia (127 sub-sectors) and Jordan (128 subsectors). A worldwide comparison shows that the number of Oman's sub-sectoral commitment is higher than the average of all WTO members (52) but lower than the average in developed economies (106).

5. In terms of the depth of these commitments (full commitment, commitment with limitation and no commitment), Oman level of commitments stands relatively strong compared to other countries with similar conditions of accession. The depth of commitments' as indicated by WTO liberalization score is for example comparable to Jordan but higher than Bahrain, Morocco and even higher than the European Union in many sectors. Oman's level of commitment is highest for computer services (Score of 100), Telecom services (100), insurance services (90), distribution services (70), environmental services (75), professional services (68), and education services (60). The services with lower liberalization scores include recreation services (0), health and social services (25), audiovisual services (30), maritime transport services (31) and banking and other financial services (33).

6. The liberalization commitments of Oman in the GATS have been consolidated and improved under the USA-Oman Free trade area. Several of the commitments in the USA FTA well exceed those contained in GATS, particularly in areas like recreation services, health and social services, maritime transport services, construction services, and education services. In comparison with other USA FTAs, more liberalization commitments were taken by Oman compared for example to Jordan and Morocco commitments in their respective FTAs with the US. The decomposition of Oman

commitments under US-Oman FTA shows that approximately 21% of the subsectors committed in both mode 1 and mode 3 are new sectors with reference to GATS while 48% (mode 3) committed under GATS have been improved.

7. Commitments in international agreements could deviate from applied policies and their restrictiveness to international trade. The Service Trade Restrictiveness Index (STRI) developed by the World Bank has been used to quantify the restrictiveness of applied service policies. Data show that the STRI in Oman stands at 47.4 which is a score somewhat high but still below 50 indicating absence of major restrictions. Comparatively, Oman service policies are overall less restrictive than most GCC countries but little more restrictive than the average MENA countries and considerably more restrictive than the EU. According to the STRI index the highest barriers to trade are observed in the telecommunication sector with a STRI score of 62.5 while the most open sector is the financial sector with a STRI score of 38.9.

8. Trade restrictiveness in services affects consumer prices, the real cost of doing business, firm competitiveness and therefore social welfare and economic growth. It has been shown elsewhere that service liberalization induces greater competition and exerts pressure on the incumbent to improve performance while technological and knowledge transfers accompanying trade liberalization particularly in Telecommunication, financial, and transport services affect positively welfare and long-term economic growth.

9. The telecommunication sector in Oman, with monopoly dismantling and privatization, witnessed a structural change leading to the emergence of a modern and competitive telecom sector. As a result, the International Communication Union (ITU) has classified most telecommunication services in Oman (domestic and international fixed long distance, internet services, mobile data services, fixed wireless broadband) as having full competition whereas the DSL, the mobile and 3G sectors are classified as partially competitive.

10. The Financial sector is the least restrictive sector according to service trade restrictiveness index. Although the banking sector is competitive, it is still highly concentrated where the top 5 banks hold 80% of the total assets. The sector has shown new entries of foreign banks following Oman liberalization commitments in GATS, but the sector is still dominated by domestically owned banks. Data did not provide evidence that entry of foreign banks affected negatively the profitability and growth of domestic banks. Similarly, the insurance sector is virtually open with no restrictions with respect to ownership of insurance companies. Partly because of stiff competition and liberalization, the insurance sector contribution to the GDP grew from 0.8% in 2008 to 1.4% in 2014.

11. The retailing sector has expanded significantly and currently makes more than 16% of the total service GDP. This growth is basically driven by the new entries of retailing supermarket giants in the Muscat area, facilitated by the liberal investment commitments in international

trade agreements where foreign ownership exceeds 70% and could reach 100% in some cases (US-Oman FTA).

12. The transport sector, particularly maritime transport, being at the cross road of international trade has considerable potential of growth as the sector is liberalized. Oman commitments under GATS allow foreign ownership up to 70% in both passengers and freight transport services while in others services such as cargo handling, ownership is allowed up to 51%. Under the US- Oman FTA the transport sector is totally liberalized except in maritime freight transport services where foreign services can only be provided in joint venture with Omanis nationals with equity up to 70%.

13. Professional services in Oman such as legal services, accounting, auditing, and book-keeping services are quite open in comparison to MENA or even to the European Union as reflected in the STRI. Still, foreigners can only own up to 70% equity in companies established in Oman and in joint venture with Omani partners (for legal companies). Under the US FTA, no equity limitation is required for accounting, auditing and book-keeping services.

14. Finally, the liberalization of the service sectors in general was shown to attract foreign investment and bring an effective competitive environment conducive to better service quality and more service choices for consumers. The attraction of further foreign investment in the services sectors enhances the Omani economy and generates employment opportunities for Omanis. Service liberalization may lead to job losses in some sectors which are not efficient and not competitive but these losses are more than compensated as a result of additional jobs created in those sectors which under WTO impulse are more efficient and competitive. There is ample evidence that Foreign Direct Investment has increased in Oman following liberalization of the services sector (as a result of Oman commitments under GATS and US FTA). In order to enhance the economic performance of the service sector and allow the country to take full advantage of international service agreements the following recommendations are proposed for the six service sectors selected in this study.

- a) Banking: Omani banks should not shy away from venturing into foreign markets and should follow the example set by Bank Muscat that has established a branch in Singapore and further considering expanding in other foreign markets. Considering the domestic market is limited in size, establishing presence in foreign markets is a viable option for other Omani banks to explore as well.
- b) Insurance: The growth of the insurance sector has been significant. However, there is still room for improvement in order to increase the contribution of the sector to the GDP which stood at 1.3% in 2014.
- c) Telecom: Currently there are only two mobile phone operators and a third one is under consideration. The entry of a third mobile phone operator into the market should be accelerated as such a move will have the effect in further reductions in

- tariff rates and the provision of even better quality of services as a result of enhanced competition and more consumer choice. It will also increase employment opportunities for young Omanis coming out of high schools and colleges.
- d) Retailing: The foreign equity limitation of 70% in the retailing sector in the case of giant super markets should be discarded as such a move will generate greater competition in the domestic market to the overall benefit of the consumers.
  - e) Transport: In certain transport activities such as in maritime transport services (passenger transportation and freight transportation) where foreign equity is limited to 70%, serious consideration should be given to remove this equity limitation in future WTO multilateral trade negotiations.. Because of Oman's strategic geographical position adjacent to one of the global major seaborne trade routes, Oman's maritime transport sector has potential for growth and therefore foreign investors should be encouraged to come to Oman by removing the equity impediment.
  - f) Legal and Auditing/accounting: In the professional services of accounting, auditing and book-keeping the foreign equity limitation of 70% under WTO should be removed in future multilateral trade negotiations. Presence of foreign/auditing firms and other professional services is particularly attractive for foreign investors, who may be attracted to Oman knowing that they get attractive world class services in Oman.