



Analysis of Monetary Policy of Central Bank of Oman on Economic Growth and Stability

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Abstract: Growth and stability are both impacted by monetary policy. The analysis of monetary policy evaluation and its effects on Oman's economy is the main goal of this study. The primary objective of the central bank is to safeguard price stability by keeping an eye on the following indicators: GDP growth, employment, inflation, interest rates, and oil production. Numerous indicators and determinants, including the dependent variable of oil production, GDP growth, inflation, interest rates, and employment level, are used in the study. It was discovered using these variables that a country's economy is entirely dependent on these elements. The goal of the study is to determine how efficient the Sultanate of Oman's monetary policy is and to evaluate the effects of various monetary instruments on the Sultanate's economy.

Key Words: Monetary Policy, GDP, Economic Growth and Economic Stability.

1. INTRODUCTION :

Monetary policy is a tool used by central banks to control economic volatility and establish price stability or low and steady inflation. In many developed economies, central banks have clear targets for inflation. Inflation targeting is also becoming popular in many emerging nations. Through the purchase or sale of assets on the open market, central banks often modify the amount of money in circulation in order to implement monetary policy. Short-term interest rates are impacted by open market operations, and this has an impact on longer-term rates as well as economic activity. The monetary policy is loosening when central banks reduce interest rates. Monetary policy is becoming more stringent as they increase interest rates.

Following the onset of the global financial crisis in 2007, industrialized economies' central banks loosened monetary policy by lowering interest rates until short-term rates nearly reached zero, which limited room for further reductions. In order to further reduce long-term rates, some central banks employed unconventional monetary strategies, such as purchasing long-term bonds. Some even used short-term rates that were less than zero. Central banks responded to the COVID-19 epidemic by easing monetary policy, supplying market liquidity, and preserving credit flow. Many central banks in emerging nations employed asset purchase programs and foreign exchange interventions to relieve pressure in the currency and bond markets. More recently, global central banks have tightened monetary policy by raising interest rates in reaction to rapidly rising inflation.

The exchange rate system of a nation is intimately related to its monetary policies. Interest rates have an impact on a nation's currency's value; so, countries with fixed exchange rates will have less room for independent monetary policy than those with flexible exchange rates. An efficient inflation-targeting system is supported by a completely flexible exchange rate regime.

The 2007–2009 global financial crisis demonstrated the necessity for nations to recognize and manage threats to the financial system as a whole. To support financial stability, numerous central banks created macroprudential policy frameworks and embraced the use of prudential measures. The purpose of macroprudential tools is to reduce vulnerabilities and provide buffers that increase the financial system's resistance to shocks. This lessens the likelihood that financial system shocks would interfere with the delivery of financial services and have detrimental effects on the economy. Because central banks can assess systemic risk and are frequently quite independent and self-governing, they are in a good position to implement macroprudential regulation. Because the organization in charge of macroprudential



policy needs to be resilient to political pressure and opposition from business associations, independence and autonomy are crucial.

Through its data collecting, technical help, and policy guidance, the IMF supports the efficacy of central banks. Regular conversation between the IMF and national central banks is referred to as Article IV consultation, which involves bilateral policy guidance. In addition to monetary policy measures, it might offer guidance on creating efficient frameworks for macroprudential and monetary policy. The IMF's Financial Sector Assessment Program (FSAP), which is a component of its financial surveillance, offers member nations guidance on managing threats to financial stability as well as an assessment of their financial systems. Technical comments like this for Finland, Netherlands, and Romania frequently include the assessments.

Countries that get technical assistance are able to build stronger institutions, capacity, and legal frameworks. It could involve macroprudential measures, exchange rate regimes, or monetary policy. Additionally, it can assist nations in achieving inflation targeting or enhancing open market and foreign exchange management activities carried out by central banks. As a requirement for central bank independence, the IMF's Central Bank Transparency Code (CBT) assists central banks in directing their transparency activities. IMF staff members undertake CBT reviews, which offer insights into central bank transparency and help improve communication between the central bank and its many stakeholders.

The IMF collaborates with its members to build and maintain databases that provide information for research and policy creation.

As an illustration:

The IMF monitors monetary policy agreements (AREAER), the legal frameworks of central banks (CBLD), and monetary operations and tools (MOID) of nations.

Every year, the IMF releases a survey that includes information on macroprudential policies and organizations, making cross-national and cross-temporal comparisons possible.

The most recent survey data is incorporated into the IMF's extensive historical database of macroprudential measures, or iMaPP. Utilizing the database, IMF economists assess the impact of policies. Additionally, researchers have free access to it.

Comprehensive, organized data on central banks' direct market interventions is available from the IMF. For instance, during the COVID-19 epidemic, IMF economists tracked measures to support financial markets using the Central Bank Interventions Database (CBID).

2. Conceptual Framework of Dependent and Independent Variable for Economic Stability

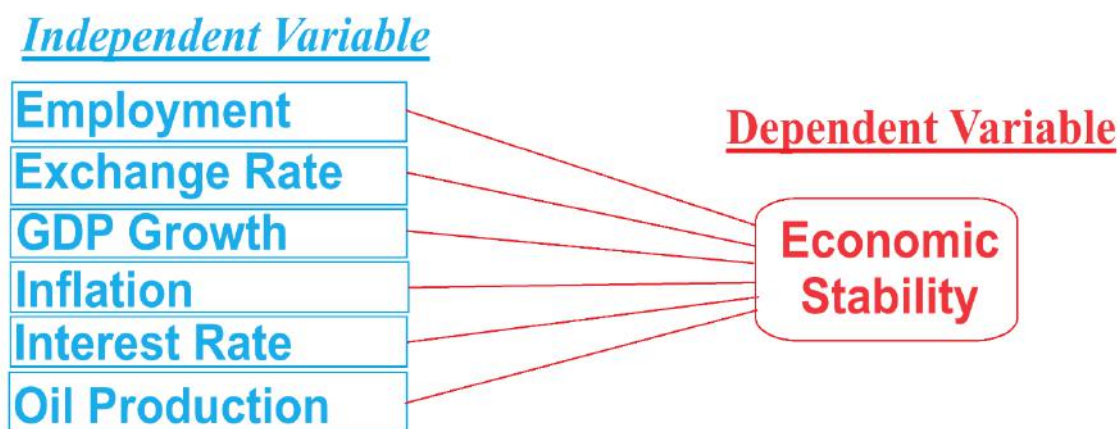


Diagram 1

Employment

In keeping with the Oman Vision 2040, the Sultanate of Oman's government has made obtaining employment opportunities for its people a top priority. Oman's economy is multifaceted and depends on a number of industries, including the banking industry, oil and gas, tourism, building, fishing, and agriculture. The Sultanate's administration has been working to diversify the economy so that more job possibilities can be created for the people living there. Although the oil industry continues to be the backbone of the nation's economy, more and more other sectors are contributing to the creation of jobs. During the epidemic, the government promoted remote labour, which lessened the negative effects on working conditions. In addition, the government has been emphasizing skill development through a



number of programs in order to involve individuals in new job prospects in the digitalization and information and technology sectors. In addition, a number of programs have been introduced to support small and medium-sized businesses (SMEs) and encourage young people in the nation to pursue self-employment and entrepreneurship. The government has been implementing a number of programs, including funding, training courses, and business development services, to foster a more supportive atmosphere for SMEs. In 2022, there was a 16.2 percent increase in overall employment opportunities, which can be attributed to the continuous rebound of economic activities following the epidemic. Employment prospects for foreign workers and citizens grew by 23.3 percent and 3.6 percent, respectively. A notable surge in foreign labour force participation in 2022 was mainly due to the industry's rebound from a low point during the pandemic.

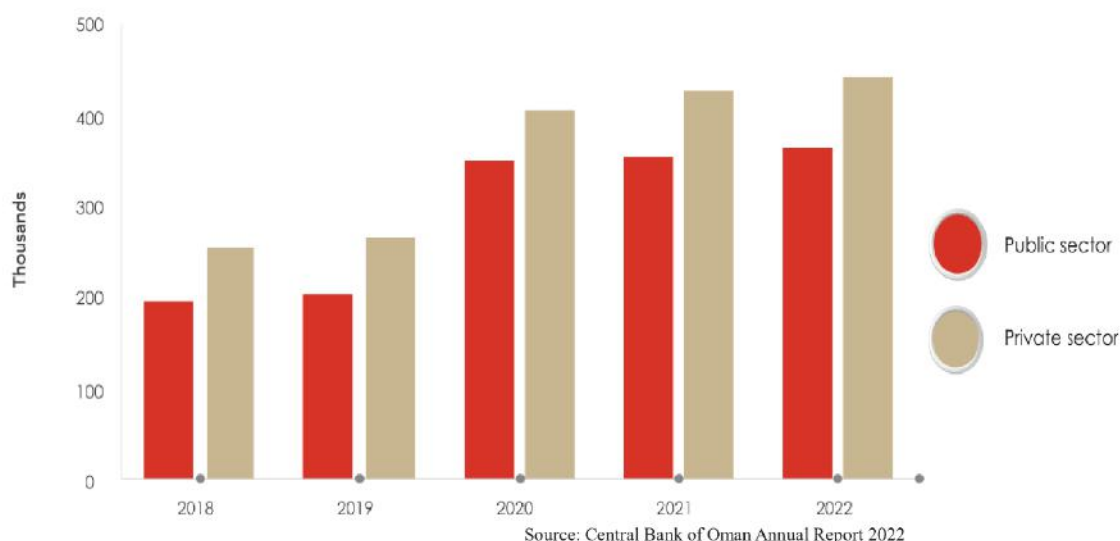
Public Sector

In the public sector, the number of Omani workers rose by 3.5 percent, whereas the number of foreign workers increased by 5.8 percent. From an opposing viewpoint, Omani citizens made up 89.2 percent of all public sector workers in 2022 as opposed to 89.4 percent in 2021. The administration persisted in trying to improve the employment prospects for young people in the nation. In April 2022, the Ministry of Labor launched the "Sahim" project, which aims to improve competitive advantage, open up new investment visas, and encourage job seekers to use their skills, abilities, and real-world experience to build the economy. Five thousand job seekers have been successfully hired by government entities in different governorates through the Sahim program through a temporary contract labour scheme.

Private Sector

The Sultanate's private sector is crucial to the country's economic diversification and the creation of job opportunities for both locals and foreign workers. To support the sector's recent expansion, the government has been putting laws and programs into place to maximize Oman's private sector's potential. In the post-pandemic period, a number of private sector segments demonstrated strong recovery, which resulted in a notable increase in the employability of the sector. Consequently, there was a 19.0 percent rise in private sector employment overall in 2022. With the relaxation of the Covid-19 pandemic limits, there was a 23.8 percent increase in the number of positions for expatriate workers in the industry, compared to a 3.7 percent increase for citizens.

Employment of Omanis in Public and Private Sector



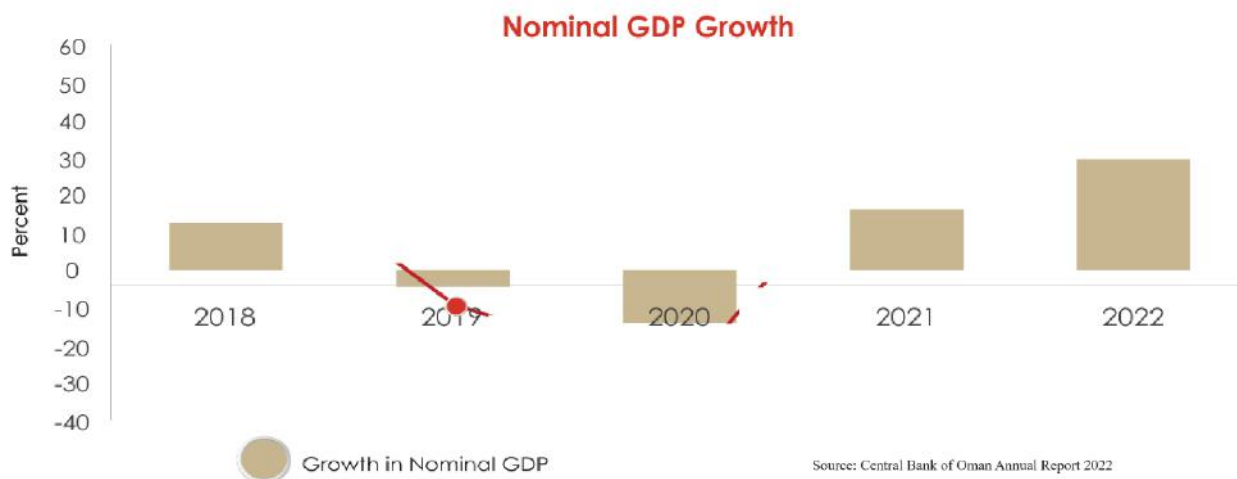
Graph 1

GROSS DOMESTIC PRODUCT (GDP)

In 2022, the Omani economy saw strong development, with both non-hydrocarbon and hydrocarbon-related activities exhibiting positive real growth. Increases in the production of natural gas and crude oil—the latter of which saw a notable annual increase—supported the expansion in the hydrocarbon sector's output. While the actual growth of the industrial sector, agriculture, forestry, and fisheries decreased, the non-hydrocarbon sector experienced growth mostly from the services sector. Results Compared to 2021, when it grew by 16.2 percent, the Omani GDP grew by 30% in



nominal terms in 2022. Both the non-hydrocarbon and hydrocarbon industries, with growth rates of 16.9 percent and 61.6 percent, respectively, were credited with the 2022 boom. The 48.4% increase in oil price was the primary driver of the hydrocarbon sector's growth, although the year-over-year increase in oil production was only 9.6%. These changes caused the hydrocarbon sector's percentage of the nominal gross domestic product (GDP) to rise from 30.3 percent in 2021 to 37.7 percent in 2022. Crude oil accounted for the majority of the hydrocarbon sector's nominal output rise, with natural gas output increasing at a more moderate rate. In 2022, the hydrocarbon industry made up 77.2 percent of government revenue, up from 73.6 percent in 2021. The manufacturing, transportation and storage, wholesale and retail commerce, lodging, and food service industries were the main drivers of the nominal expansion in the non-hydrocarbon sector.



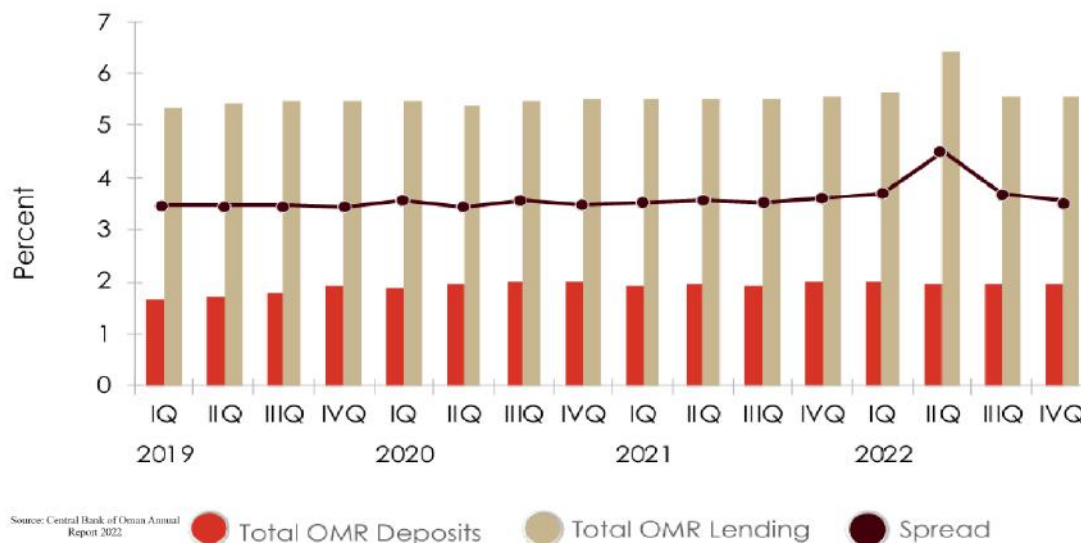
Graph 2

Interest Rates Developments

The hydrocarbon sector's share of the nominal GDP increased from 30.3 percent in 2021 to 37.7 percent in 2022 as a result of these modifications. The hydrocarbon sector's nominal output rose mostly due to crude oil, while natural gas output increased at a more moderate rate. The hydrocarbon sector accounted for 77.2 percent of government revenue in 2022, up from 73.6 percent in the previous year. The non-hydrocarbon sector's nominal growth was mostly driven by the manufacturing, hotel, food service, wholesale and retail, and transportation and storage sectors. As of the end of December 2022, the weighted average interest rate on total deposits (Omani Rial + foreign currency deposits) has risen to 2.065 percent from 1.910 percent in December 2021. Conversely, lending rates increased slightly from 5.153 percent at the end of December 2021 to 5.705 percent at the end of December 2022. Foreign currency lending rates increased significantly from 3.520 percent in December 2021 to 7.055 percent in 2022, while local currency lending rates declined somewhat from an average of 5.570 percent to 5.543 percent. Conversely, the margin in interest rates between savings and loans in local currency fell from 3.594 percent in December 2021 to 3.550 percent in December 2022. 54.5 percent of all Omani Rial deposits held with conventional banks at the end of December 2022 received interest rates of 2.0 percent or less annually, according to an examination of the distribution pattern of those deposits. The percentage of outstanding Omani Rial time deposits that produced a return of 4.0–5.0 percent at the end of December 2022 was found to be 35.6%, down from 49.6% the previous year. This is a fall of 13.9 percentage points. Regarding interest rates on Omani Rial loans, personal loans accounted for the majority (57.1%) of loans, with rates ranging from 5.0 percent to 7.0 percent as of the end of December 2022.



Weighted Average Interest Rates



Graph 3

Inflation

Oman's inflation was impacted by changes in both local and international prices. Price stability continued to be one of the CBO's primary goals in order to guarantee sustained and balanced economic growth, even in the face of the currency peg regime's limitations on the independence of monetary policy. Owing to the Sultanate's open capital account, currency peg, and heavy reliance on imports of goods and services, imported inflation continued to play a major role in domestic inflation and, as a result, Oman's inflationary conditions mostly followed trends in global inflation. However, the outcome of domestic inflation was greatly influenced by domestic demand conditions as well as government policy in the form of taxes, subsidies, administrative fees, and other measures. Sharp jumps in global inflation in 2022 were caused by the release of demand that had been stored up throughout the epidemic, significant stimulus plans, growing energy costs, labour shortages, supply chain disruptions, and geopolitical concerns resulting from the conflict between Russia and Ukraine. Global inflation started to decline in the second half of the year after hitting all-time highs as a result of many central banks tightening their monetary policies to rein in the soaring prices. In advanced economies, average retail inflation grew from 3.1% in 2021 to 7.3% in 2022 (IMF, WEO April 2023). Similarly, from 5.9 percent in 2021 to 9.8 percent in 2022, inflation in developed economies and emerging markets (EMDEs) surged.

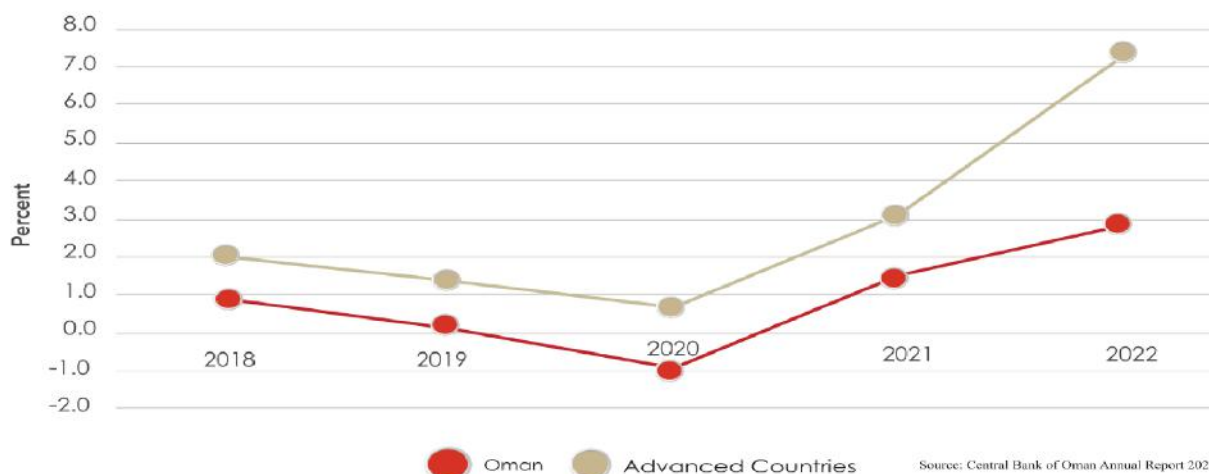
Despite this, Oman's inflation situation was benign throughout the year, which was a result of both administrative actions and the appreciation of the US dollar. However, in the first two months of 2022, there was a slight uptick in inflation, which decreased as the year went on. The average annual rate of inflation, calculated using the consumer price index, increased from 1.5 percent in 2021 to 2.8 percent in 2022. Notably, during the year, inflation was greater in the food and non-alcoholic beverage category while it was down in the communication sector. With Oman's nominal GDP growing by 30.0 percent and government spending growing by 7.0 percent due to increased oil prices, demand conditions remained solid in terms of supply and demand variables. The monetary aggregates exhibited muted expansion, with broad money growing at a moderate rate of 0.6 percent due to a decline in deposit growth and a decrease in currency demand. A supply-side element that contributed to the increase in global food prices in 2022 was the appreciation of the NEER, which reduced the inflationary pressure on domestic prices.

According to intra-year changes in inflation, the Value-Added Tax (VAT), which went into force in April 2021, had a base impact that made inflation in the first quarter of 2022 particularly high. After that, throughout the duration of the year, the inflation rate was benign and tempered by a number of variables, chief among them the administrative actions taken by the government and positive developments in the exchange rate. The administrative actions included capping fuel prices at October 2021 levels, granting more items an exemption from the VAT, and lowering the fees associated with issuing and renewing work permits for foreign nationals. Furthermore, because the Omani Rial is fixed to the US dollar, the USD's strengthening in 2022 caused a positive shift in the OMR Nominal Effective Exchange Rate (NEER), lowering the cost of imports into Oman and containing inflation. The food and non-alcoholic beverage group had an



increase of 5.2 percent, according to a breakdown of the CPI components; transportation showed the second-highest rate of inflation at 3.9 percent. The epidemic, changes in geopolitics, and challenges related to climate change were the main causes of the disruptions to the food and energy markets. The producer price index climbed by 36.4 percent in 2022 compared with a 15.3 percent increase in the year before, which is much higher than inflation based on the Consumer Price Index (CPI). This spike was attributed to the index's substantial weighting of oil and gas goods. As was previously said, issues relating to global supply and demand caused oil and gas prices to surge in 2022.

Annual Consumer (retail) Inflation

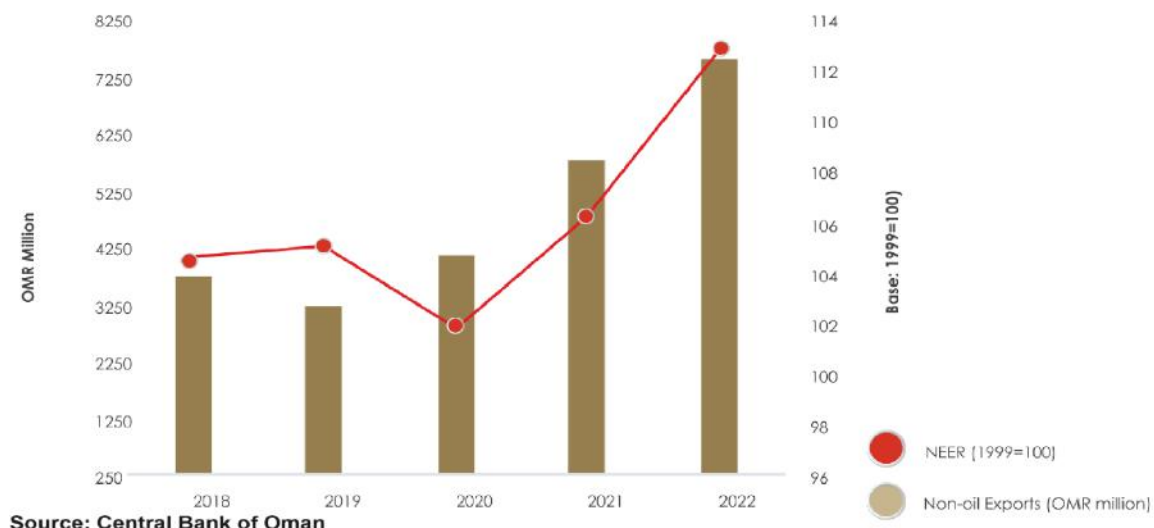


Graph 4

Nominal Effective Exchange Rate (NEER)

Exports become more valuable when considering a single unit of currency exchange due to the appreciation of currency. The Omani Riyal weighted average nominal exchange rate versus 18 major importing economies' currencies is determined by the Oman Nominal Effective Exchange Rate index, with 1999 serving as the base year. Over the past few years, the Omani Riyal has been rising, particularly in light of the FED interest rate increase. In December 2022, the Nominal Effective Exchange Rate value increased 6.3% over the prior year. In December 2022, the index read 112.8, up from 106.2 in the same month the previous year. But it lost value from its September 2022 level of 118.2. Because the goods from the partner economies were more affordable, the value of imports increased as a result of the currency's appreciation. Despite the increased cost of exports, the strong level of demand worldwide reduced the related expenses.

Nominal Effective Exchange Rate (NEER)



Graph 5



Oil Production and Exports

Due to supply-side pressures brought on by geopolitical tensions resulting from the Russia-Ukraine conflict, the global oil market saw tremendous growth in 2022. Furthermore, following a period of stagnation in the first half of 2021 due to Covid-19 lockdowns and limitations, worldwide economic activity resumed its upward trajectory. From 97.1 mb/d in 2021 to 99.4 mb/d in 2022, oil demand rose. In contrast, the world's oil supply grew from 95.05 million barrels per day in 2021 to almost 99.9 million barrels per day in 2022 in order to fulfill demand (EIA Short Term Energy Outlook). In addition to rising demand, supply-side factors that resulted from restrictions on Russian crude supplies as the Russia-Ukraine conflict developed, extended supply chain interruptions, and uncertainty in the world energy markets all contributed to an increase in oil prices in 2022. The IMF estimates that the average price of oil in 2022 (calculated by summing the prices of WTI, Dubai Fateh, and UK Brent) was USD 96.4 per barrel. As supply constraints loosen and oil inventories rise due to anticipated excess production, the average price of oil is expected to drop to USD 73.1 per barrel in 2023 (IMF, WEO update, April 2023).

The tightening measures implemented by major central banks to control persistently high inflation were another issue that merited notice. These efforts may have contributed to a decrease in demand as capital became more expensive to obtain with rising interest rates. From a low of USD 73.1 in February to a high of USD 112.9 in August, the average price of Omani oil rose by 48.4% to USD 95.4 per barrel in 2022. In 2022, the real GDP was approximately 34.5 percent comprised of oil and gas. In 2022, their revenues made up around 77% of all government revenues, up from 73.6 percent in 2021. In 2022, total oil output reached 388.4 million barrels, a 9.6% rise from the average daily production of 1,064.2 thousand barrels the previous year. Crude oil output accounted for the largest portion of total oil production in 2022, rising 12.8 percent to 309.5 million barrels, while condensate production fell 1.4 percent to 79 million barrels. In 2022, Oman exported 319.5 million barrels of crude oil, a 10.6% increase above its record in 2021.

In comparison to 289 million barrels the previous year, Oman's total oil exports for the whole year 2022 increased by 10.6 percent to 319.5 million barrels. From 81.5 percent in 2021 and 82.5 percent in 2020, the percentage of oil exports in total oil output rose to 82.3 percent in 2022. Nearly 82 percent of the Sultanate's total oil exports in 2022 came from exports to China, the Sultanate's top crude importer, down from 84 percent in 2021. Conversely, exports to India rose from 28.9 million barrels in 2021 to 31.2 million barrels in 2022, a 7.9% gain. In 2022, oil shipments to South Korea and Japan increased by 179% and 93%, respectively, to 12.6 million and 11.7 million barrels.

Omani Crude Oil Production and Exports



Graph 6

3. Conclusion and Recommendations :

Oman's Central Bank (CBO) monetary policy shows its major impact on economic stability and growth. The CBO uses interest rate adjustments, open market operations, and macroprudential measures to stabilize prices, boost economic growth, and reduce financial system vulnerabilities. These steps have stabilized the Sultanate's oil-dependent economy, but diversification is necessary for long-term sustainability. The government's Oman Vision 2040 initiatives have increased private sector employment. However, talent development and SME support must continue to sustain this



growth. Hydrocarbon and non-hydrocarbon sectors drove 2022 Omani economic growth. Growth was driven by rising oil production and prices, underlining the need for diversification to lessen oil dependence. The CBO's interest rate changes have affected deposits and lending, raising foreign currency loan rates. Stimulating economic activity and managing inflation must be balanced. Administrative efforts and the US dollar's strengthening kept Oman's inflation under check despite global inflationary pressures. Management of imported inflation and domestic price stability requires constant vigilance. The Omani Riyal's increase has raised export prices and lowered import prices, boosting economic stability. Export-driven growth requires a competitive exchange rate. Global market dynamics and geopolitical concerns have affected the oil sector's performance, emphasizing the need to improve production efficiency and explore new markets to continue development. Tourism, manufacturing, and IT should be accelerated to lessen oil dependence. Investment incentives and specific policies can do this. Continue improving monetary policy to adapt to global and domestic economic changes. This includes improving data gathering, analysis, and forecasting. Increase financial services for SMEs and underprivileged communities to promote inclusive economic growth. For this, digital financial solutions might be crucial. Develop worker skills for developing industries through education and training. Government, business, and education must collaborate. Monitor inflation and exchange rates. Timely measures can reduce economic damage. Increase SME funding, mentorship, and market access. Entrepreneurship promotes innovation and economic resiliency. Promote public-private collaboration to harness resources and expertise for economic development. In conclusion, the Central Bank of Oman has stabilized and grown the economy with monetary policy, but diversifying the economy and improving policy frameworks are necessary. Oman can achieve sustainable economic growth and resilience to global economic crises by following these ideas.

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