CASE STUDIES OF BANKING INDUSTRY REGULATORY REFORM, TRANSFORMATION AND MERGERS IN OMAN

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Thesis
entitled
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CASE STUDIES OF BANKING INDUSTRY REGULATORY REFORM, TRANSFORMATION AND MERGERS IN OMAN

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ABSTRACT

This research examines the banking industry in relation to Regulatory Reform, Transformation and Mergers in the Sultanate of Oman, and how these important aspects of bank management considerations influence efficient banking systems and contribute to country and economic development. The literature review encompasses Oman, the Gulf Cooperation Council (GCC) and other countries. A Theoretical Framework was established and research questions formed that examine existing theory and also raise opportunities to complete phenomena-based case studies that address areas of bank management in Oman that have not been previously investigated. The study uses qualitative methods by a process of semi structured interviews with senior bankers and business operators in Oman. The author's twenty-year experience in the Omani banking industry contributed to the theoretical inquiry and the findings of this research address gaps in the current literature and will be useful to regulators, bank management, businesses and educators.

KEY WORDS: Banking / Oman / Regulatory Reform / Transformation / Mergers

153 pages

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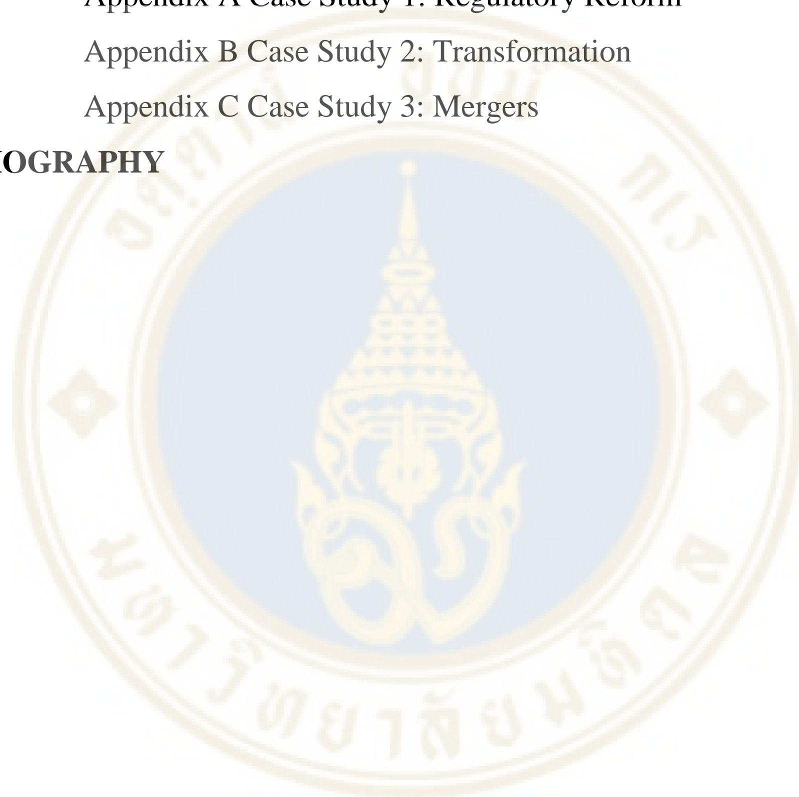

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LIST OF ABBREVIATIONS

Abbreviations	Terms and Meanings
ADB	Asian Development Bank
AFC	Asian Financial Crisis
ANZ	Australia and New Zealand Banking Group
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
ATM	Automatic Telling Machine
BPR	Business Process Reengineering
CBQ	Commercial Bank of Qatar
CITI	Collaborative Institutional Training Initiative
CMA	Capital Markets Authority
DIFC	Dubai International Financial Center
FCA	Financial Conduct Authority
FSA	Financial Services Authority
GCC	Gulf Cooperation Council
GFC	Global Financial Crisis
IMF	International Monetary Fund
IRB	Institutional Review Board
OECD	The Organization for Economic Cooperation and Development
OMAN	The Sultanate of Oman
PRA	Prudential Regulation Authority
QFC	Qatar Financial Center
SET	Stock Exchange of Thailand
SME	Small to Medium Enterprise
TQM	Total Quality Management
UAE	United Arab Emirates

CHAPTER I
INTRODUCTION

This thesis is the outcome of studies relating to Regulatory Reform, Transformation and Mergers in banking sectors and specifically addresses events and research questions of banking phenomena in the Sultanate of Oman. Qualitative methods have been used and the format of data collection was by a series of semi-structured interviews with experienced banking and business professionals that are based in Oman, and the study of literature and the banking events, and the findings of the interviews have provided the opportunity to write case studies on each of the topics of Regulatory Reform, Transformation and Mergers in Oman.

Regulatory Reform, Transformation and Mergers are common traits of the banking industry especially since the Asian Financial Crisis (AFC) of 1997. Following the Global Financial Crisis (GFC) of 2008 banks have needed to change their earlier behaviors, and they have been under greater supervisory control and scrutiny. Literature attests to each of these elements creating positive advances in the development of banking and financial systems.

For example, in the case of regulatory reform, Bakir (2009), Kroszner and Strahan (2011) and Levine (1999 & 2012) show that the underlying purpose of banking supervisory reforms is to provide improvements to policies and procedures that create greater efficiencies and benefits in the banking systems.

Transformation in the banking industry is a strategy for development and through benefits to the transforming entity, adds value to the industry generally (Audzeyeva & Hudson, 2016; Franke, 1998). It is also relevant to bank transformation initiatives that the theories of John Kotter's "Eight Steps to Transforming Your Organisation" often come into play, with successful strategy implementations (Kotter, 1995), and for more recent case examples see also Appelbaum et al., (2012).

Relating to mergers, Du and Sim (2016) show that in developing markets especially, bank mergers are regularly seen as tactics that can stabilize banking sectors.

There are also quantitative studies that show mergers add value and improve the quality of lending portfolios and the financial system generally (Focarelli et al., 2002; Houston et al., 2001), and the outcomes of mergers have become better over time, particularly since the 1990's (Gupta & Misra, 2007).

Academic literature such as Goldsmith (1969), McKinnon (1973), and Shaw (1973) provide evidence of financial development having positive effects on country economic growth and it is well recorded that a robust and a progressive banking industry is necessary (Arestis & Demetriades, 1997; Crowe & Meade, 2007; Gurley & Shaw, 1955; Levine, 1998, 2004; Schumpeter, 1911).

In King and Levine (1993), the authors confirm Joseph Schumpeter's (1911) arguments that expansion of financial services are required for technological innovation and economic development. Schumpeter, like Walter Bagehot (1873) before him, was a visionary economist who foresaw the importance of technology in the financial sector. It was futuristic of Schumpeter to theorise about technology in the early parts of the last century.

Many of the tests for country development relate to measurements of GDP per capita and much of the research and results, as confirmed by Durusu-Ciftci et al. (2017), conclude that governments and policy makers benefit by increasing the expansion, openness of markets and effectiveness of the banking sector. Therefore, it is incumbent on regulators to act in a way that fosters the development of a country's financial sector that will accelerate economic development.

King and Levine's (1993) study unambiguously confirms that measures of financial development are closely and robustly associated with real GDP growth and therefore lead to the ability for country development. Similarly, empirical studies from both Calderón and Liu (2003) and Claessens and Laeven (2005) confirm that financial sector development leads to economic improvement. Levine (1999) also endorses and stresses that effective banking systems provide a framework for long-term economic development. Calderón and Liu (2003) and more recently Durusu-Ciftci et al. (2017) further discovered that financial progress contributes more to developing countries than in already industrialized countries. This finding would be expected as there would seem to be a "catch up" phase in developing economies that would normally show faster growth ratios than developed nations and this is also seen in the instance of Oman.

It is important to show here why Oman is a country that is fit for research and also for writing case studies. Oman is a relatively newly developing country and it was only in 1970 when Sultan Qaboos took over that the country began a program of modernization. Before Sultan Qaboos, illiteracy and infant mortality were high, and average life expectancy was at only 50 years of age (from World Bank Data https://data.worldbank.org/country/OM). In 2010 the UNDP rated Oman as the fastest developing country since 1970.

Historically Oman has been geographically important for traders from Asia making their way to the Arabic countries, Africa and to Europe. It has been resource rich since oil was found in the 1960's and it has used these revenues to fund its modernization and social benefit programs. There is currently only about 30 years of oil reserves at current consumption in Oman and this has caused the government to consider diversification strategies. For the reasons that the country is young and the banking sector does not have a long history, there are gaps in research and in the literature to be addressed. For these reasons, Oman is an interesting and a suitable country for research.

Oman's banking system is relatively modern and sophisticated and Oman has effective governance (Baydoun et al., 2013). Oman's banking regulators are strong and proactive and they have ensured that the rapid development of the financial system has added value to the development of the country.

The initial research through reviewing existing literature and assessing banking events in Oman enabled the formation of relevant research questions on the topics of Regulatory Reform, Transformation and Merger activities in the banking system in Oman. Research questions have been formed by deep study of the literature and also from knowledge of the country's banking sector and its workings.

The research questions posed are:

1. Regulatory Reform - How can regulators ensure that Islamic banks are able to compete equitably with conventional banking practices, and preserve Shariah laws?

2. Transformation - Why is the principle of urgency and the laws of agility important for transformation strategies in developing economies? How can they deliver value for customers and stakeholders?

3. Mergers - Why is the banking sector in Oman motivated to merge and what are the expected benefits to the merging banks and their shareholders?

A series of semi-structured interviews were conducted with some of Oman's top bankers and business heads, and the outcomes have been used to form answers to the stated research questions.

Outcomes of the research have also been used to write case studies on each of the topics, and by examining those cases, provide a broader understanding of the banking system, from an insider's perspective, and provide examples of best banking and governance practices. Examination of the cases will answer research questions on future and wider theory. Case studies in Oman may be characteristic of broader general observations. By using research and the researchers own experiences to write real life cases, they add to the existing academic literature. Results answer the *how* and the *why* (Yin, 2013; see also Baxter & Jack, 2008) of existing theory.

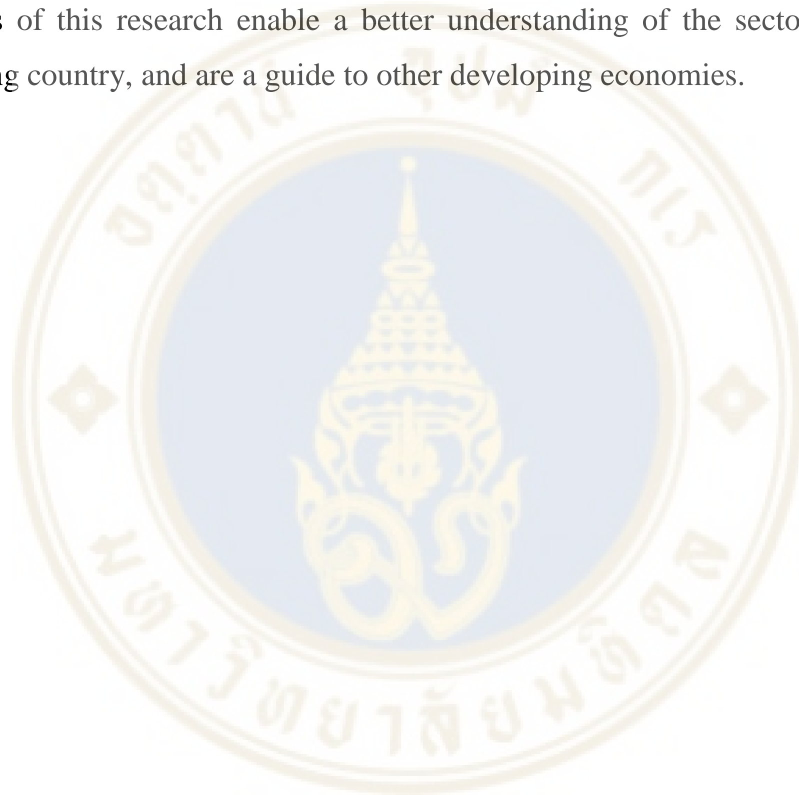
The research calls on existing literature and documentation (business reports, Central Bank of Oman and the Capital Markets Authority information and country statistics), and from experiences of living and working in the banking industry in The Middle East region, specifically in Oman. Current industry contacts and the outcomes of the interviews provided a collection of data, and also evidence for validation of the research.

Interest in researching these topics comes from a banking and finance career of over 40 years, including roles as the Chief Executive Officer of large banks in the Middle East countries of Qatar, the United Arab Emirates and Oman. Since 2005, the researcher has been working in the region and has become closely associated with regulators, decision makers and business leaders, particularly in Oman.

Oman has a recent history of rapid social and economic development (Al Lamki, 1998), and in the last two decades especially, it has seen notable reform, transformation and merger activity in the banking industry. However, because it is a small and newly developing country (since Sultan Qaboos overthrew his father to be the country's leader in 1970), there is little in the way of any sizable data-set information to base quantitative research. Hence, studies of the banking sector and case studies of Oman lend themselves to research that is qualitative in nature.

Harrison et al. (2017) have described case study research as most often to be qualitative, and it should reflect meaningful events (Yin, 1981a), and the choice of recording experiences by the use of a single case study is a commanding approach (Siggelkow, 2007) to examine phenomena.

The use of case studies has become an accepted method to explore events and outcomes in the business arena, and the research of these uses a variety of information sources (Eisenhardt, 1989a; Yin, 1981b). To date little has been published in academic journals about Oman and especially the banking industry in Oman. The findings of this research enable a better understanding of the sector in this rapidly emerging country, and are a guide to other developing economies.



CHAPTER II
LITERATURE REVIEW

In keeping with the study, the literature review forms three parts, Regulatory Reform, Transformation and Mergers, and has generally kept to the banking sector. However, it addresses a global approach with concentration on Middle East and Gulf Cooperation Council (GCC) countries. The reasoning for this is that while similar, there is little academic literature that focuses on the banking sector in Oman, and with regard to the banking industry GGC countries in particular, while being more advanced than Oman, studies can provide lessons in the development of banking and financial governance in the region.

2.1 Regulatory Reform

Regulation refers to rules, guidelines, directives, protocols, instructions, laws and byelaws that are all set in place by authorities to ensure proper ethics, social objectives, control and robust governance. Countries without strong regulation experience some of the lowest levels of socioeconomic development, and most of these countries show poor economic growth (Yousef, 2004). The Organization for Economic Cooperation and Development (OECD) Regulatory Reform Program (2018) shows that regulatory reform programs are an ongoing process and are intended for authorities to frequently review and evaluate regulatory quality. The purpose is to assess current regulations and modify those that impede competition, innovation and growth, while ensuring that efficiency and central social objectives are served.

Lesser-developed countries are not as prone to have the desire or the capabilities for proper reform environments, however, international authorities can leverage reform requirements. For example, Naceur and Omran (2011) show that in the 1980’s several Middle East countries undertook noteworthy reforms under the directions of the International Monetary Fund (IMF) and these were enforced by the

IMF in exchange for financial assistance that was required for social and economic development.

Regulation is bureaucratic in nature, normally set by legal systems and government authorities. Often, reforms are reactive to economic or social events, they are the result of inquiry, and they are lengthy in formation and can be slow in their delivery (Bakir, 2009). In support, Atkinson and Coleman (1989), contend that bureaucratic agencies form the core of policy formation and key agencies become government and industry regulators, in the case of banking, there are traditionally country central banks and capital markets authorities.

In times of critical need, regulators will offer wide ranging, and what can be seeming radical reform. In Australia, following the 1997 Wallis Inquiry on the banking and financial systems, two new regulators were formed shortly after the Asian Financial Crisis. The Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investment Commission (ASIC) were formed and replaced 10 existing regulators. Remarkably, in these sweeping reforms, the Reserve Bank of Australia lost its bank regulation powers (Bakir, 2009), which was given to the APRA and this reform of the regulators was unprecedented in modern global banking at the time.

After the 2008 GFC, the United Kingdom reviewed its financial governance systems and closed its primary regulator, the Financial Services Authority (FSA) (Parker & Masters, 2010). As in the Australian model, two new agencies were established, the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) (Vina, 2010). The time taken for this change was five years and is one example of the often lengthy and bureaucratic process of regulatory reform; refer to Bakir (2009).

In periods of vigorous economic growth, robust regulatory systems are imperative, and as country and economic structures develop more rapidly, the need for quicker review and reform is vital. In the late 1990’s and early 2000’s, Middle East countries and particularly the United Arab Emirates (UAE) and Qatar saw rapid growth fueled by rising oil and gas prices, new capital investment, predominantly from overseas stakeholders, and significantly new domestic purchasing power. These countries had financial regulatory systems that in world terms were immature and needed significant change. The existing regulatory systems would not allow for the pace of commercial

development required to keep up with the fast rate of economic growth and development and they needed to fully revamp and set in place modern and sophisticated systems to support their financial development requirements.

Separate to their existing banking regulators (central banks and capital markets authorities), both Dubai, in the UAE, and Qatar developed distinct regulatory entities for conducting business, separate from traditional systems. The Dubai International Financial Center (DIFC) was established in 2004 and the Qatar Financial Center (QFC) was established in 2005, and they were both set up with their own independent, international regulatory authorities and judicial systems, common law framework and global financial exchanges.

It is well documented that national development is at the forefront of government accountability and development of the banking system is necessary for the advancement of country and economic progress (Arestis & Demetriades, 1997; Bagehot, 1873; Crowe & Meade, 2007; Gurley & Shaw, 1955; Levine, 1998). The importance of banking reform and financial regulation is increasing, especially as markets become truly global and more open, and empirical studies covering long periods, and large data bases in various economies and countries also confirm that financial progression strongly correlates to economic advancement (Calderón & Liu, 2003; Claessens & Laeven, 2005; King & Levine, 1993).

The world's first central bank was established in Sweden in 1668 and since then regulatory reforms have featured strongly in financial systems. During the 1960's, the development of economies advanced from a reliance on traditional banking systems to non-bank sources of funding and these were dominated by market driven factors and newly conceived products that were not within the normal purview of traditional regulation (Kroszner & Strahan 2011). No more visible has this been than after the eruption of the sub-prime phenomena which led to the GFC of 2008 (D'Arista & Griffith-Jones, 2008; Levine, 2012; Lo 2009; Metrick & Rhee, 2018). Monitoring and reform had been a major part of the regulatory system that failed the financial sector in the lead up to the GFC and the decline of the banking sector had a foremost negative impact on global economic progress.

Financial catastrophes are unavoidable when human behavior is combined with liberal markets and freer enterprise, and additional to that, when legislation and

regulation is unresponsive, slow or unorganized (Lo, 2009). This coupled with a decade of mounting greed, skirting of regulation, development of new and complicated financial products and disenfranchised risk rating authorities, all led to the downfall of large investments banks, Bear Stearns and Lehman Brothers in 2008. The downfall of these two banks marked the start of a financial crisis that was felt throughout the world and on a scale larger than any other financial catastrophe before. Both institutions had become very creative with their product offering, and lax with their portfolio management, and their risk appetite had outgrown their capabilities, despite what was thought of at the time as robust regulation by the US Federal Reserve. An emergency government loan was provided to Bear Stearns in March 2008, but this did not prevent its collapse, leading to a merger with JP Morgan Chase.

Lehman Brothers was at the time, the United States' fourth largest investment bank (behind Goldman Sachs, Morgan Stanley, and Merrill Lynch), the institution filed for Chapter 11 bankruptcy in September 2008 after becoming illiquid from trading in sub-prime portfolios. At the time, Lehman Brothers was considered part of the fraternity of banks that were thought of as "too big to fail". This term was phrased to describe corporations that become so large that their failure would have significantly detrimental effects, and they were prone to gain government support when they face times of financial downturn (Mintz, 2015).

Arun & Turner (2004) define governance as a narrow, but clearly expressed approach where mechanisms ensure that managers will act in the interests of shareholders. They also argue that banking institutions are special and complex in nature and that a broader perspective of governance is required to protect the interests of the economy in general, and those of depositors, as well as shareholders.

John and Senbet (1998) define corporate governance as a group of mechanisms used by stakeholders to ensure that management teams efficiently manage company resources to ensure that the stakeholders' interests are protected. The relationship between strong governance at board level, and coupled with dedicated and independent risk functions leads to superior bank performance. Battaglia and Gallo (2015) also identify with Pathan (2009) and Pathan and Faff (2013) that strong governance is defined by (i) appropriate board size, (ii) independence (from management and shareholders), (iii) having separate board committees (remuneration,

nomination, audit, risk, etc.), (iv) impartiality of reporting lines (risk, compliance and internal audit functions), and (v) a high frequency of board and committee meetings.

After the GFC, not only was the governance of regulators under scrutiny, but also the governance of the financial institutions themselves (De Andres & Vallelado, 2008). The dual role of boards, of monitoring the management and also advising and directing, has come under scrutiny, as have the elements of independence, size and complexity, Al Tamimi (2012) confirms that bank performance and good corporate governance are related.

Levine (2004), Macey and O'hara (2003), Boot (2000) and Prowse (1997) all acknowledge and confirm the existence of the difficulties of complexity and regulation in the corporate governance of banks, and in addition, the concept of opaqueness is addressed. However, with proper control and appropriate regulatory capital, the likelihood of systemic banking calamities is reduced (Dungey & Gajurel, 2015). Dungey and Gajurel (2015) also consider that to a significant extent domestic situation can be controlled by regulation, although the contagion of international situations is more difficult to manage. In banking these days, these deficiencies are well known to risk managers and are also measured and monitored within the banking systems by regular stress testing of scenarios, as a tool to foresee and manage any impending downturn.

At no other time is the efficacy and strength of good governance more important to financial, economic and political markets, than in a period preceding a financial markets downturn, however history has shown that reforms of regulations more often come after the crises. Bowornwathana (2000) discusses the experience in the regulatory reform of policies in the post Asian financial crash of 1997, and the expectations and influence of donor agencies such as World Bank, Asian Development Bank (ADB) and the IMF.

In Asia, post 1997 there were extensive changes to governance regulations and especially those relating to board members and the management of banks and financial institutions, these reforms assisted the Asian countries well during the later Global Financial Crisis. The hardest hit countries were Thailand and Indonesia and these needed fast and strong reforms. The Bank of Thailand issued its “Fit and Proper Criteria” detailing that bank's board members should have at least five years of

experience with a well-run financial institution and they should not serve on more than three other boards at the same time. In addition, bank lending to related parties, including directors, is now strictly forbidden and 100% foreign ownership of banks was allowed. The banks needed capital to survive and the outcome of the reforms were that twelve of the fifteen local banks were recapitalized by foreign investment or by merger (Pathan et al., 2008). In Indonesia, there were a number of systemic failures revealed in the banks and governance reform intervention was enforced by the IMF. Banks that did not submit rehabilitation plans by the end of December 1997, and those whose plans were not accepted by the Bank of Indonesia, were to be closed, this resulted in sixteen banks being shut down in November of the same year. A new Banking Law was introduced in 1998, the amendments also allowed 100% foreign ownership and the power to grant bank licenses was transferred from the Ministry of Finance to Bank Indonesia (Omori, 2014). In many Asian countries, the financial crisis forced governments to grant greater independence to the central banks (Haggard, 1999).

Crowe & Meade (2007), in their study of central bank governance studied the length in office of central bank management, independence and mode of decision-making, transparency and commitment to policy. All these are shown as measures that evidence a solid platform for central bank governance and those countries that employ them diligently fare better than others. Enhancements have been seen in emerging and developing countries indicating a desire to develop and progress. The more advanced countries improved by lesser amounts, and interestingly the US Federal Reserve scored lowly in the study, (it scored in the third quartile). More developed countries, while having longer history and more mature mechanisms for implementing stronger governance systems, find size and the complex nature of developed systems a greater obstacle. There are costs, but also benefits associated with strong and diligent governance processes, and the more sophisticated the system of governance, the greater the benefits (Puranam & Vanneste, 2009).

According to Stout (2017), good corporate governance can promote knowledgeable decision-making and it can also discourage shareholder influence and inspire management team optimization. Stout (2007), additionally confirms that governance has costs as well as benefits. Most importantly, in times of stress, downturn,

and even crises, good governance that has strong foundations can protect companies from social and financial ruin.

The benefits of good corporate governance have been tested in a number of ways in recent years. In Ananchotikul et al., (2010) a study of 333 companies listed on the Stock Exchange of Thailand (SET) were assessed for governance violations over a period from 1990 to 2002 and again from 2003 to 2006. The significance of this split was that the SET introduced a new corporate governance code in 2002. This was for listed companies and had 15 principles for good governance, which were also a further reaction to the 1997 AFC. Interestingly, the SET did not make adoption of the principles mandatory, but it was on a “comply or explain” basis. The results of the study show that adoption of good governance principles equate with lower code violations.

A later study, by Kouwenberg and Phunnarungsi (2013), tested market reactions to corporate governance violations in Thailand. The results of that research was that markets react negatively to governance code violations and the logic of the two studies is that good governance would lead to positive market reaction and improve company valuations at the status quo, or better.

It has become evident that “literature suggests that corporate governance codes require teeth to have a positive effect on firm value” (Kouwenberg, 2006, p. 1). Since the GFC, banks have been fined 243 billion USD by regulators, (Goldstein, 2018). These include the large institutions of Bank of America USD 76.1 b, JP Morgan Chase USD 43.7 b, and Citigroup USD 19 b. In Europe, Deutsche Bank USD 14 b, Royal Bank of Scotland USD 10.1 b and BNP Paribas USD 9.3 b. Countries with stronger regulation and with penalties for non-compliance have a better chance at development and economic growth, again leading to higher company value (Helleiner & Pagliari, 2011; Jackson, 2007; Kane 1997).

If management and board members are not properly accountable to the owners, they may not manage the company appropriately. Directors have an enforceable responsibility to shareholders, and poorer board governance can create situations that directors have opportunities to manage firms in a way that not beneficial to all stakeholders.

By many measures, Australian Boards more closely replicate “best practice” for corporate governance than Boards in other developed markets. This could be a direct

outcome of the Wallis inquiry and the regulatory changes implemented shortly after (Kiel & Nicholson, 2003). Kiel and Nicholson (2003) also introduces agency theory as a major issue in managing and monitoring companies, arguing that in the best practices of governance, CEO and Chairman should not be the same person; it also contends that the agent/principal relationship can be detrimental to proper regulation and good governance.

The overwhelming central theory perspective of governance is that of agency theory (Daily et al., 2003), and it is key in the study of governance. The concept in agency theory is that there should be a separation between ownership and control. In essence, dealing with management (and board members) being classified as agents, and shareholders as principals. Agents make decisions that can affect principals and there can be circumstances where agents are motivated to act in their own best interests, which are contrary to those of the principals (Bonazzi & Islam, 2007). It is evident that optimal conditions are found when the management is independent from the board members. It is also apparent that the best situations are where board members have the education and experience to be able to correctly monitor and advise management. Since the 1997 Asian crisis and the 2008 GFC many such measures to ensure independence and correct fit of board directors in banking have been implemented by regulators. Singapore, Hong Kong and Indonesia now insist that prospective board members of banks become qualified through relevant examinations and certifications before they are approved by the central banks as fit for appointment. Since 2008, appointments of board members in many countries require approval by their respective country regulators. In the Middle East, ratio numbers and clear definitions for independency of directorships are also in place. In addition, in many locations regular monitoring and auditing of all aspects of bank controls and management has become stronger.

McColgan (2001), states that agency problems arise because contracts between the principal and the agent cannot be perfect, and because every action of the agent can be from decisions that affect both the welfare of the agent and of the principal. The question is how to incentivize the agent to act in the best interests of the principal. McColgan also shows that managers bear the entire cost of failing to pursue their goals, but partake in only small amounts of the benefits of successful initiatives. These point to the principal/agent relationship being floored at the most basic levels. McColgan

(2001) also shows that agency problems are long in history and they are inevitable, and that agency costs can be reflected in company value.

More definitions that are specific to agency theory are as far back as the 1970's by Jensen and Meckling (1976) where the agency relationship is defined as a pact where the principals employ agents to perform services and where the employment contract involves delegation and decision authorities provided to the agents. If both the principal and the agent are utility maximizers (that is, they both strive to gain maximum value for themselves individually), there is opportunity that the agent may not act in the best interests of the principal. In these cases, the principal can limit the departures from his interests by establishing appropriate incentives for the agent and by incurring "monitoring" costs designed to limit the negative activities of the agent. The agent may set in place measures to limit or to "bond" the agent from harm to the principal and although monitoring and bonding will be actions that would be in favor of the principle's welfare, there will be costs associated. Additionally, the result of reduced benefit to the principal, in real terms, brought about by the agency relationship can be measured as a "residual loss". The resulting cost is referred to as agency cost and is measured as the sum of all of monitoring costs, bonding costs and residual losses.

As recently as Panda and Leepsa (2017), which reviews theory and empirical evidence, agency theory is shown a principle dating back to Adam Smith (1776) in his book, "The Wealth of Nations". Through their own literature review, Panda and Leepsa (2017) describe types of agency problems arising from principal/agent problems, principal/principal problems, and principal/creditor problems, and the solutions to these can be found by monitoring and bonding the agents (Jenson & Meckling, 1976).

However, agency problems can still exist, and they are difficult for independent regulators to monitor. Nicholson and Kiel (2007) in their study reveal examples of the decisions that management and board members can make, that will have detrimental effects to shareholders. These are in relation to day-to-day bank management, risk appetite and strategic decisions, and very much relative to management and board member remuneration and bonuses. Recent years have shown that banker's remuneration packages have outgrown many other industry sectors, showing significant growth of salaries and bonuses, even in times of poor performance.

Agency theory is concerned with incentives which are approved by management and the board (agents), which will cause detriment to shareholders (principals), and this has been identified in the literature since the 1970's (Eisenhardt, 1989b).

Until the 1950s, the Middle East countries had basic economies, which were born quite late in relation to Western economic systems. This also leads us to regulation, reform and governance that were aspects of corporate development in the Middle East countries, which were in their infancy at the time. In the 1960's and 1970's Middle East countries experienced rapid economic growth, fueled by global development of international trade, and oil and gas field discoveries. In the 1970's particularly, higher oil prices were the driving factor that sustained the economies of the oil countries and resulted in higher wealth and GDP (Battaglia & Gallo, 2015; Yousef, 2004), and banking systems in the region developed accordingly. During these periods of growth, banking regulation and accountability authorities were established and the prime control of the ruling leaders was slowly being handed over. In the 1980's the oil price bust led to severe economic downturns, and gaps widened between embedded institutional practices and reduced government capacity. The developing regulatory authorities could not keep up and regulatory reform and governance in the Middle East were seen as some of the worst in the world at the time (Yousef, 2004).

Oman is however known to have good levels of bank governance in the GCC (Al Malkawi et al., 2014; Baydoun et al., 2012), and is in line with Crowe and Meade's (2007) higher measures of independence, transparency and length of tenure for the central bank management. Because of these higher levels of governance, Oman was less effected in comparison with other GCC and neighboring countries throughout the GFC. Oman has a strong history of robust governance from its banking regulators, the Central Bank of Oman and Capital Markets Authority, and they have in place swift and strict penalties for code violations.

However, at the bank management level in Oman it is evident that although banks are willing to abide by central bank guidelines, there have been cases evidenced through public annual financial reports and the Capital Markets Authority reports of high dividends paid to shareholders, although year-on-year performance has been lagging. Decisions to pay significant dividends are an example of short-term benefit to shareholders, which can be made at the long-term detriment to liquidity and capital

adequacy of these banks. This is driven by a large representation of the shareholding by sitting board members, although independence is officially maintained, and in accordance with the Central Bank of Oman regulations, there are common shareholdings and closely tied board representation across some of the banks.

During the 1960's and 1970's, the Middle East saw the extra complexity of the introduction of Islamic style banking that was presented as a facility for Muslim communities, and it became a competitor to the existing conventional banks. The Quran was written shortly after the death of the Prophet Mohammed in 632 (AD), and it clearly forbids charging, or paying interest (known as riba or usury) for finance and investment dealings. It was not until 1963 that the first dedicated Islamic bank was established, in Egypt, and in 1975 Dubai Islamic Bank, in the UAE was opened as the first modernized Islamic bank, producing a revised suite of extended products (Khan, 2010). The introduction of Islamic banking in other GCC countries followed closely, however, the Omani ruling council were not comfortable with the prospect of a dual banking system, and Oman was the last of the GCC countries to introduce Islamic banking (Sastra Mihajat, 2018 and Mubeen et al., 2014), in 2012.

Gheeraert (2014) asserts that Islamic banking, similar to conventional banking is important for the development of the banking sector and is necessary for country development and economic growth (Boukhatem & Moussa, 2018). Islamic banking has philosophies and principles that protect Muslims from activities that are forbidden in Islam (riba, usury, gambling, alcohol, etc.). Sharia (Islamic law) regulations are also intended to encourage companies to engage in business and promote development generally (Ito, 2013), while maintaining the beliefs of Islam.

Shariah supervision can bring additional costs that are not seen in conventional banking (Garas & Pierce, 2010) but can be profitable, and a worthwhile business venture for new and existing banks, (Hardianto & Wulandari, 2016; Ito, 2013; Khasawneh, 2016; Zarrouk et al., 2016).

However, Islamic banking presents further complexities to the conventional banking systems, requiring a separate Sharia board, balance sheet, risk and compliance divisions, and ways to ensure that Islamic funds do not become "tainted" with conventional funds, and this brings a dilemma for central banks and Islamists of how

Islamic banking can preserve the Shariah laws and also maintain equity with conventional banking structures.

2.2 Transformation

Once there is an understanding of what transformation is, the search for how and why transformation happens, and what it leads to, is all-important for executives so that they can recognize the processes and the benefits of transformation. Executives strive to achieve significant returns on the investment and efforts of change. What transformation is and the incentives it creates are well documented by academic literature.

Transformation in the commercial world relates to the process of fundamental operational change that will alter relationships with stakeholders in order to help anticipate, react to, and manage shifts in external business and economic forces (Rouse, 2005).

Over recent years, new terminology has been coined for the strategic and operational reviews of businesses and implementation programs. In the last few decades we have heard about, change management, business model innovation, operational excellence, Total Quality Management (TQM) and others, however these are all used to describe processes that make continual change a normal part of doing business (Deming, 1986).

Since the 1980's companies have been driving unprecedented internal change (Earl, 1994; Kettinger et al., 1997), but to be transformational, the changes, actions and the delivery need to be at a level that will transcend the organization's basic structure, and results need to be substantial, measurable and widely noticed. Transformational change can disrupt the market and dislodge the competition (Crowe & Meade, 2007).

Transformation is much more aligned with the definition of Business Process Reengineering (BPR), which began to appear as a business term in the mid 1980's, and is a much more revolutionary process (Hammer & Champy, 1993; Rouse, 2005).

Enterprise transformation is the essential change to the way an organization operates, whether that be entering a new market or operating differently. It fundamentally changes relationships with and aligns an organization's activities relating to customers, people, processes, products and technology with its business strategy and vision (Rouse, 2005) and it intends to meet the long-term objectives of the company.

From the above definitions, it is shown that transformation is about fundamental change, and that it is central to extensively altering the function of a company. The theory of enterprise transformation helps to understand what businesses look for and where they look, to find solutions for business improvement by means of the transformation processes.

Part of the reasons why transformation occurs, is in reaction to external factors of the economy and the surrounding markets, contends Rouse (2005) who also describes the economy and the markets as drivers of the enterprise and “intraprise”, which is the internal context of transformation.

Often times there are value deficiencies that are supplementary drivers of transformation, these are denoted as internal factors and they arise during routine business and management reviews. They can address gaps in the needs of the stakeholders, that is, the customers, the employees, the suppliers and the investors of an enterprise.

Enablers of transformation are work processes, and generally, a closely managed and regular course of monitoring and measurement is required. The requirement to regularly review work processes is well understood (Hammer & Champy, 1993) and the need to amend processes to achieve routine desired outcomes is continuous.

The need for transformation is determined by value deficiencies, which are defined as potential that is desired, but not delivered. The process of transformation is the how that leads to fulfilling the value deficiencies. Transformation also scrutinizes and make positive changes to work processes (Arestis & Demetriades, 1997). This inspection involves reflection and deliberation of what the company will look like after the proposed changes, and pursuing incentives that compensate for the work involved, and account for risk versus return, relative to the investment in the transformation process. The potential and desired value improvement will influence how investments

and resources are allocated in order to deliver the best returns. The level of diligence and the efforts of management will lead to the outcome (positive or negative) of the results, superior problem solving, decision-making and delivery capabilities will result in the best standard of implementation and returns (Rouse, 2005).

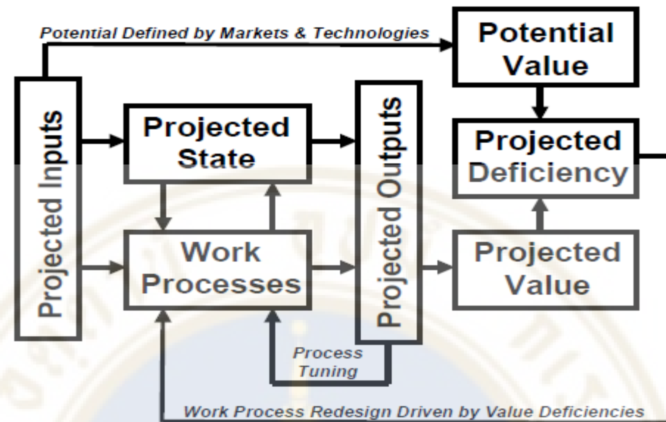


Figure 2.1 Theory of Enterprise Transformation. Adapted from Rouse, (2005)

The notion of “state” is introduced here and it is fundamental to enterprise transformation theory. The projected state of an organization is the planned outcome of utilizing variables and their values to provide an assessment of the future state of the company. This is an essential strategic planning element, together with work processes, and after addressing any deficiencies, will lead to the projected value of an enterprise. Often “state” is referred to as the strategic intent of an enterprise, or a process.

Different enterprises will implement transformation in different ways, and this brings about different styles of managing transformation and of course different outcomes. The figure below shows the relationships between the MEANS of transformation, or the areas of focus. The SCOPE of the transformation, whether it is a simple activity, a function or part of the enterprise, or the whole enterprise that is undergoing change. The ENDS refers to the outcomes and incentives of the transformation exercise, it could be greater cost efficiencies, better market acceptance, new products and services, or higher returns and profits.

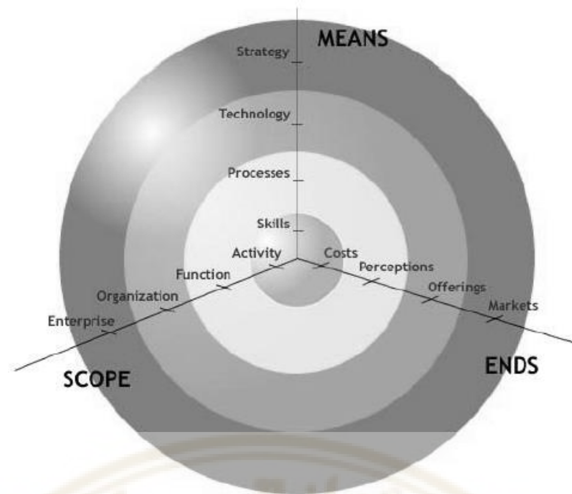


Figure 2.2 Transformation Framework. Adapted from Rouse, (2005)

The costs and the risks associated with change programs increase as the project moves away from the center. Projects that revolve around the center will classically include well-known and simplified methods of implementation. In contrast, initiatives at the outside will involve significant and more complex changes of products, services, systems, as well as larger investments and risks.

In reviewing Kotter's 8-step change model, Appelbaum et al., (2012) argue that companies need constant change, not only to ensure their current market positions, but also to grow and develop. Commitment to change is not optional and the growing pace of technology development will overtake many businesses if they are not prepared for it, and already implementing change, and they need to be nimble in their application of change processes (Biedenbacha & Soumlderholma, 2008). Much of the current literature refers to the consistent and the endless nature of change (Armenakis & Harris, 2009; Weick & Quinn, 1999), but the focus of management in any transformation initiative will be the incentives or the rewards, to be derived (Rouse, 2005). Without some kind of improved incentives, potential or projected increased value, there will be no desire for change. In some cases, this will be essential change to ensure the survival of an enterprise, in other cases, it will be to provide a stable platform for the business to grow and in some other cases, and it will include a reaction to changing external markets and economies.

For example, during the 2008 GFC, many banks cut their risk appetite and reduced their portfolios and balance sheet size. These were the actions of conservative operators who while keeping a safe and steady form of strategy, generally took a larger reduction in revenues and profits. Enterprises that undertook this type of strategy took longer to recover from the crisis.

Others took a more aggressive approach, they repriced their portfolios, to compensate for the increased risk, they looked to purchase distressed assets, at bargain prices, and they took the opportunity to review operating costs and staff structures. The majority of these operators came out of the GFC stronger and more resilient.

There are of course pitfalls in transformation, and there are many instances of the change process failing. Common reasons for these pitfalls are shown in Kotter (1995), including declaring victory too soon, and not embedding the change in the very culture and fabric of the organisation. Failure often comes from managers not accounting for the importance of maintaining a process and having a distinct focus from the beginning to the very end of the transformation project.

It is often said that the focus of any large transformation will be directed towards the different groups of stakeholders, which are the customers, the employees, suppliers and investors (Ackermann & Eden, 2011). However, in practical measures the transformation assessment, strategic decisions and the implementation process will in these more modern times concentrate on three aspects, people, processes and products, and this is shown in the transformation example of Bank Dhofar in Oman (Babicci & Wongsurawat, 2018).

The focus on people, processes and products brought drastic and positive results, in less than two years Bank Dhofar had moved from number five position (and at the time it was spiraling downwards), to turning the trends around, and achieving number two position in the country. Share price had also outperformed all of its peers and provided superior returns for shareholders. The strong focus on these three drivers became a formula for a very successful enterprise transformation.

Central to the drivers in Bank Dhofar’s case was the strategic intent. This is defined as a management statement about the desired direction of an enterprise that also conveys what that organization wants to achieve in the long term. Rouse (2005) refers to this as “projected state”.

Strategic intent provides purpose and continuity of objectives when an enterprise is addressing internal and external developmental pressures. Yet, literature on strategic intent does not account for differences, or the heterogeneity of goals, within an organization. That means that the goals are made up of parts that are very different from each other and unless the most senior management is fully accountable for the transformation process and delivery, there can be misunderstandings over internal ownership of the strategic intent (Mantere & Sillince, 2007).

Initiatives are implemented to drive competitive advantage; however, these often fail to provide the desired results in the competition of enterprises that are in similar markets, implementation efforts that lack top management support often lead to failures, or at the minimum reductions to projected values. Also in the same market, competitive forces are similar, and often a larger, stronger enterprise can create corporate damage to smaller and weaker competition.

The strategic intent statement of an organization will provide a link to value-added performance changes; it also looks at the relationships that exist between strategy and measurement, and operational performance (Fawcett et al., 1997). The 1990's corporate catch cry of "what gets measured, gets done" was part of better strategic management and Fawcett, et.al. (1997), also confirm that measurement is an imperative factor of strategic intent.

Kotter's first step in the change process is to create a sense of urgency, and this needs to be carried through to a management mindset which ensures that everyone involved in the process realizes that there is a stakeholder that will be affected by every decision, and with regard to customer experience, Stephen Denning in his 2016 paper "How to make the whole organization Agile" states (p. 10), that "Everyone doing work has a clear line of sight to the customer." Kahan (2018), p. 49 also confirms, "Leading organizations are using agile teams to continuously refine the ease of their products and services to keep customers happy and engaged".

Customer focus was a major part of Bank Dhofar's delivery to its stakeholders and it stemmed from building a new agile platform for delivery. Speed to market became all-important and examples of reduced approval and turnaround times for its customers became a chief differentiator in the market for Bank Dhofar to propel itself to success. The importance of speed and agility are further stressed in this age of

creativity, technological advances and network connections, where customers demand urgency in delivery of services and continuous innovation is a minimum for organizational survival (Denning, 2016a). A well-considered and delivered sense of urgency and agility in its strategy plans brought Bank Dhofar from a sluggish bank known as a follower in all aspects of customer delivery, to a competitive leader where others needed to change their style and methods to keep pace.

2.3 Mergers

Mergers are complex strategic tool, they can be multi-faceted and there are many reasons for companies to consider mergers to drive competitive advantage. Defining the core and the style of mergers is important in understanding the explanations for why mergers are so popular, and their benefits, and their desired successes.

Mergers can be approached as a structural procedure that allows companies to combine competences to realize strategic and operational goals (Sawler, 2005), in the banking sector, mergers generally result in industry consolidation. Because of technology advancements that modify production processes of financial companies, one major enabler can be financial deregulation, and history has shown us that mergers in this industry occur in waves (De Young et al., 2009), that are generally aligned to economic cycles and events. Moreover, research into bank mergers is important in relation to the recent refocus on compliance and regulations in the banking sector globally (Karolyi & Taboada, 2015).

There are three significant merger theories that define the types of mergers according to Green and Cromley (1982). Conglomerate describes a strategy to seek product line expansion is also classified as diversification. This relates to mergers between two or more companies that are usually engaged in unrelated business activities. The merging entities may operate in different industries or in different geographical regions. A pure conglomerate merger involves two firms that have nothing in common. Banks will sometimes engage in this type of merger to join other markets and product offerings that they do not already participate, the merger might be in the form of a portfolio or a sale of part of the seller's overall business. Standard Chartered Bank's purchase of the Grindlay's Bank franchise from Australia and New Zealand

banking Group in 2000 is an example of a conglomerate merger where Standard Chartered wanted to enter certain markets in the Middle East and the Indian Sub-continent and through this purchase was able to merge with Grindlay's Bank in those locations, this merger also allowed Standard Chartered Bank to expand its presence in the Private Banking sector in its existing markets. The intention of the merger was to allow Standard Chartered to grow in terms of geography and in terms of product range (Financial Daily – Business Line, 2002).

Vertical mergers expand control into similar product lines and occurs when two companies produce parts or services that combines products. It is when two companies operating at different levels within the same industry's supply chain combine their operations. The acquiring company will increase control over more sources of supply and distribution, often using those distribution channels to sell existing product offerings. Such mergers are completed to increase synergies achieved through cost reductions and other efficiencies, which result from the merger with one or more supply companies.

Horizontal mergers expand control of business activity in the same product groups. The buying company wants to increase its market share. A horizontal merger occurs between companies that are working in the same industry, and they can be within the same geography, or across borders. The merger is typically part of consolidation between two or more competitors offering the same products or services. Such mergers are common in industries with fewer firms, and the goal is to create a larger business with greater market share and economies of scale, since competition among fewer companies tends to be higher and more direct. Mergers between companies that sell the same products but compete in different markets are often known as "market extension mergers" and it is more evident that in the banking sector mergers will be horizontal mergers. Qatar National Bank in the Middle East was established in 1964 and until 2005 had a presence in only Qatar with representative offices in London and Paris, locations where Qataris would traditionally spend their summer months. In the mid 2000's the bank began a rapid expansion program through horizontal mergers with international entities. Qatar National Bank cleverly used the newly acquired markets to modify and sell its existing product base, especially its advisory services, private banking and Islamic banking products, it is now the largest financial institution in the Middle East.

There is a growing division of academic literature on whether mergers create value, according to Devos et al. (2008), there is little proof in the literature of the significance of merger gains. However, the growing theory suggests that motives for mergers include synergies, increased market power, and efficiency improvements, and these are all considerations when firms decide to merge. If a main criterion of business management is to improve shareholder wealth, then it follows that any merger must hold motives that lead to improvements that will deliver that value increase.

The opinion that mergers in the banking sector will also lead to better results is instinctive (Du & Sim, 2016) and has been evidenced in studies by many researchers, including Andrade et al. (2001), Beltratti and Paladino (2013), DeYoung et al. (2009), Rhoades (1998) and Olson and Zoubi (2011). While the expected benefits might be able to be gained, with time by organic measures, mergers bring a speed that can propel the combined entities past the competition and significantly improve their league ladder status amongst their peers.

Bank mergers are generally seeking to result in both shareholder value and efficiency gains (DeYoung et al., (2009) quickly and to make gains on competing banks and organizations. Gattoufi et al. (2009) describe three broad categories of motivation. The first being improved cost reductions (synergies and financial efficiencies). The second motivation that they refer to has a number of elements that make the markets attractive for mergers. In the banking sector, these include increased competition from competitors and changes in regulations. The third, and quite a controversial consideration is managerial self-interest, Gupta and Misra (2007) confirm, where managers could use merger strategies to build on their own objectives and personal interests, and as a way to boost or to defend their authoritative positions. Also in agency theory research, Eisenhardt (1989b) shows that in mergers principal and agent (owner and manager) interests can deviate.

A motive in Oman for bank mergers is that while the Omani banking sector is relatively small and concentrated, mergers are desired to allow banks to gain scale to be competitive with other banks in the GCC (Al Muharrami, 2019). The GCC has 95 commercial banks, the largest Omani banks are Bank Muscat is ranked 25, and Bank Dhofar, ranked 50th, and all Omani bank assets are less than 4% of the regions total bank assets. Banks in Oman need to find scale to be able to become competitive in the region

and to also participate in larger tracts of financing local infrastructure projects, and this has been a large motivation for the numerous merger discussions in Oman in the past decade.

Studies confirm that mergers are a widely used strategy accepted by banks to achieve growth as well as cost benefits. Rhoades (1998) studied nine case studies of bank mergers, with a view to reviewing efficiency effects, all resulted in substantial cost benefits.

However, there seems to be insufficient literature on the impact of bank mergers on staff, in Bryson's (2003) review of the literature of the time and her study of the 1996 merger of Westpac Bank and Trust Bank in New Zealand, she found that acquisitions often have an undesirable effect on employee behavior. This can result in counterproductive practices, nonattendance, low morale and job dissatisfaction and loss of key staff. Important factors in the success of mergers is management ability to gain employee trust, ensure strong communications with employees and instill job security. The conclusions of Bryson's study show that successful mergers can provide sustainable benefits, but they also have the potential to result in trauma and stress to both individuals and the company. People issues are often a neglected factor of mergers, as management focus on the greater business issues of sales, cost containment and revenues. In Oman the high level of the Omanisation ratio for banks and the government's requirements to create jobs for locals inhibit banking merger gains through staff rationalization.

Marks and Mirvis (2011) & Schuler and Jackson (2001) show that many executives pay low consideration to combining human attributes in corporate cultures when considering their merger activities, however those same executives when reviewing the outcomes, admit that undervaluing the human capital management difficulties in the merger of cultures was a major mistake in their integration efforts.

Other factors that can rapidly change merger outcomes are market perceptions and customer reactions, regulatory changes, technological advancements and funding structures. For all these reasons, and because negative impacts of change can be swift and damaging to the predicted outcomes, management that is dealing with bank mergers need to be active in constant review of their integration strategies and be agile in their counter actions to ensure that projected gains eventuate (Kahan, 2018; Houston et al., 2001; Brouthers et al., 1998). In the Standard Chartered Bank and ANZ's

Grindlays merger customers perceived that Grindlays was an elite bank and much more prestigious than Standard Chartered, numbers of customers were taking their business elsewhere as Standard Chartered was a smaller bank and not well known in India at the time (Tschoegl, 2003).

It is rare that any merger will involve entities of equal standing, and especially where payment terms would be neutral, the norm is that one will be more dominant, most likely the acquiring entity, and that is usually the one that has most to gain, or risk. Mergers, especially in developing markets, present firms with significant opportunities for entry, growth, expansion and progress. Along with benefits to be gained, details of the characteristics of the target entity and the motives of any related or owning party, as well as policies of the regulators are important considerations in the decision to buy process. In this regard, critical relationships are formed among the individualities of the parties involved; that is the acquirer, the target, the owners and the local regulators (Uhlenbruck & De Castro, 1998). Mergers are expected to provide acquirers with value by way of revenue growth, cost synergies and additional customer bases. They also give opportunities for other types of value creation, including the transfer of technological knowledge as well as competitive market practices.

Publications on banking mergers relate to benefits, risks, corporate background and regulatory environment and all of these features can be vastly different in the approach and the completion of any merger with the result also differing. Of course, when an entity seeks to merge with another, the management will have a strategic intent and a view of the end structure and results, but these can be derailed by the outcomes of the relevant due diligences and events that occur during the onboarding and integration processes. While there is a quantity of publications and references on mergers, there is little evidence of research involving any standard conceptual framework for mergers in general and in bank mergers explicitly. A merger is similar to a living organism with characteristics that can morph and change many times during the integration process, and constructing a standard framework that management can work to is problematic and complex. It is worthy of discussion here to gain a further understanding of the complexity of mergers and more so when combined with the banking industry.

Mergers have both positive and negative attributes; it is shown that structuring a framework for mergers, especially relative to bank mergers, is a difficult concept, and has not been widely addressed in academic study. The theoretical framework for the model discussed here is adapted from Uhlenbruck and De Castro's (1998) study of strategic management literature on mergers and acquisitions, which remains relevant today. The model is sectioned to show phases of decision-making, action and anticipated results. The three entities involved are the target, the acquirer and the regulator, which all affect the transition of the merger and the post-merger performance. The target, because of its historical conditions and its desirability to the acquirer, the acquirer because of its position as an investor seeking economic opportunity and, the regulator because of its role as arbiter of market conditions.

The framework shows phases that are relevant to all of the target, the acquirer and the regulator. The target includes its resources and capabilities, meaning in bank situations its customers, staff, capital and its internal infrastructure and its ability to transform its resources into value for its stakeholders. The level of social engagement is important, as reputational issues are all important to well managed and controlled acquirers. Forms of funding are also paramount as efficiencies, cost to income variances and returns on investment are elements that are closely measured in the merger process and in post-merger performance. The complexity for managers to assess and control becomes evident.

The regulators as the governing bodies for legal frameworks are particular in their objectives for the industry and the markets and their policy capabilities. The role of the regulator is to ensure good governance and that any actions by the target and the acquirer will be in benefit to the public and to wider markets, generally. They also have responsibilities to ensure that employment is protected and that alternatives are available.

Conditions of the operational phase of integration are important considerations both before completion of the due diligences and during integration actions. Strategic intent is about the benefits of mergers resulting from the similarity of the assets and operations of the merging entities (Jemison & Sitkin, 1986). Often these benefits result from synergies between the merging firms' resources and capabilities. The kind and number of organizational adjustments required for integration are affected

by the strategy and organizational fit of the merging entities (Datta, 1991), and the characteristics of a target may differ markedly from those of the acquirer in organizational structures, systems, culture and strategy.

The characteristics of the target and the strategic intent of the acquirer may interact to affect the integration processes. Deeper integration will require either a higher degree of organizational fit or severe, and likely costly, adjustments during the integration processes, all these aspects are required to be taken into consideration in the planning and implementation stages. To ensure that the cost of the acquisition will be outweighed by the benefits of the post-merger performances, synergy strategies in banking will often relate to rightsizing of staff. Standard Chartered Bank in their merger with Grindlay's Bank reduced the combined staff numbers by over 35%, and this was done with the approval of unions, regulators and the government. They also substantially reduced the number of combined branch offices. These actions made the Indian operations of Standard Chartered Bank group one of its most profitable.

Terms of the contract relates to the usually accepted terms and conditions of which the major consideration will be price. Achieving a willing seller and a willing buyer where both parties feel that they are being dealt with fairly and where they both feel that they will gain benefit – the seller most likely to achieve a benefit in the shorter term than the buyer due to time required to achieve full synergies and created values. Mergers can involve substantial governance anxieties for regulators especially where political requirements is to preserve employment continuity (such is the case of most of the Gulf Cooperation Countries where they all have some form of localization quotas in the banking industry). Regulators will require forms of guarantees to ensure that such matters and general and specific term of governance are adhered to; in fact, many regulators will look to acquirers to instill superior management practices and experiences.

CHAPTER III
THEORETICAL FRAMEWORK

The objectives of this research are to examine how systems have advanced, to better understand regulatory reform, transformation and mergers in the banking industry, and to provide a platform to answer current gaps in academic research in Oman. While considering the development of meaningful research questions, deliberation included the rapid economic and social development of Oman, and compared the governance and banking systems in other GCC countries and wider.

Academic literature for almost 150 years, since Walter Bagehot's "Lombard Street" (1873), shows evidence that country development is enhanced when there are greater developed banking systems. Arestis & Demetriades (1997), Crowe & Meade (2007), Gheeraert (2014), Gurley & Shaw (1955), Levine (1998 & 2008), Schumpeter (1911) are a few that have conducted researched and confirm that the development of banking systems hold positive influence on country development, in more recent years.

Further, considering the research of concepts that have the greatest effects on developed country banking systems, constructs that form the mainstay of bank management considerations were identified and a framework developed. Literature provides many influences on country banking systems and it is clear that there are three phases of development; these are banking regulation and governance, which are subject to regular reform, and essential for a strong and resistant banking industry. Second, is transformation, which is constant and proactive, and ensures that the infrastructure of the banking system is up to date and a strong driver of economic, social and technological developments. The third phase is consolidation and mergers, which is a result of the success of banking systems where over-growth can actually become detrimental to economic markets, and they are subject to many motivators.

Relationships between these three constructs intertwine, and it is shown that each has a relationship with each other (regulatory reform, transformation and mergers). Using the conduit of the banking sector to address country development, the theoretical

framework (shown below), assists in support of the research questions, and to guide the approach to research and solutions to the research questions (Lederman & Lederman, 2015).

Literature confirms that the constructs have relationships and confirms that the relationships of regulatory reform, transformation and mergers have interactive associations. Atkinson & Coleman (1989), Bowornwathana (2000), Yousef (2004), Bakir (2009), Parker & Masters (2010), Naceur & Omran (2011) and Babicci & Wongsurawat (2018) all reference the relationships of these banking activities and improvement and development of banking systems, and how these banking activities have influence on country development.

According to Anfara et al. (2014) in "*Theoretical frameworks in qualitative research*", p 15, research frameworks assist with the study and analysis of phenomena, and they provide a guide through the methodology process (Miles and Huberman, 1994 and Baxter & Jack, 2008). The theoretical framework for this research highlights literature that relates to the constructs of this study and the outcome of the enriched country development of Oman.

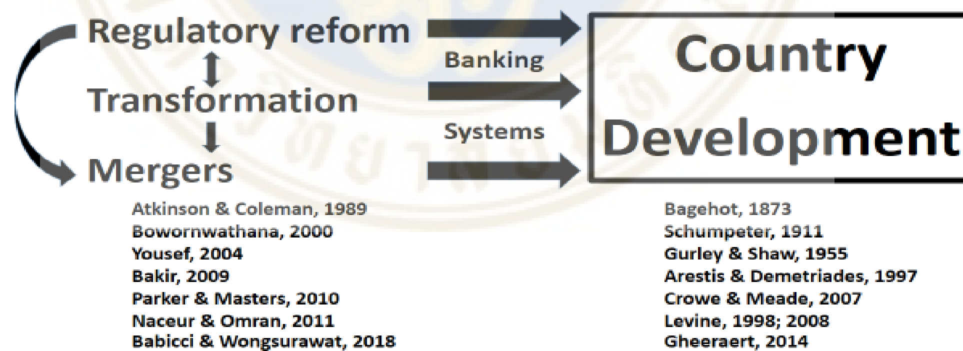


Figure 3.1 Theoretical Framework

Mergers can also be treated as a form of transformation, and regulatory reform is a driver of mergers but mergers are not a regular driver of regulatory reform.

The definitions provided in literature show that each of the topics of regulatory reform, transformation and mergers are closely linked and this is also seen

specifically in the OECD Regulatory Reform Program (2018), Rouse (2005) and Sawler (2005). Commonly these constructs can all be seen to be drivers of change that are used to improve efficiencies. Also, in the framework above (Figure 3.1), all the three topics are closely linked when they are reviewed in relation to the banking industry. Further, these are the three main aspects of banking that will bring about the greatest change to individual banks, and they can also bring about the greatest disruption to banking markets.

In the case of Oman, the development of the banking sector since 1970, has led to the enhancement of country infrastructure, economic growth, and social benefit.

CHAPTER IV
RESEARCH OBJECTIVES AND QUESTIONS

The research contained in this paper studies three aspects of banking specifically in Oman. Discovering the interplays of those three aspects shows evidence of roles both separately and jointly in the country's development. The study includes both local banks and international banks (including Islamic banks and Islamic windows of conventional banks), and the influences of the local authority of the Central Bank of Oman.

Important lessons have been learned from recent developments in Islamic banking in Oman where the regulatory authorities set up a framework for allowing conventional banking and Islamic banking to cohabitate in a single market, with both efficiency and legal efficacy in terms of Shariah requirements. This is delivered with strong initial influence from the central bank. However, for Islamic banking in Oman customers have met the new offerings with some reluctance, and a study by Belwal and Al Maqbali (2019) also shows that customers in Oman had mixed feelings about the Islamic Banks. Some customers questioned if the banks and the windows closely adhere to Shariah laws, and a majority of the Muslim population have not opened accounts with the Islamic banks or Islamic windows. The research shows shortfalls in the banks' operations, marketing practices, staff knowledge as well as customers' understanding of Islamic banking.

More than ever, in recent times and especially since the Asian Financial Crisis of 1997 and since the Global Financial Crisis of 2008 the art of bank management has been ever changing, it is complex in its nature and often opaque to the outside community. Understanding what transformation is and explicitly how banks transform, and their processes to obtain improved financial and commercial results is important to gaining an effective and progressive banking system, that will assist in greater economic and country growth as local economic indicators develop.

In the banking industry worldwide, mergers are common and are used for many reasons that include growth, portfolio and risk management, and contraction of market size. There is also evidence that at times mergers are considered to satisfy the personal benefits of managers. Many mergers fail, in ways that are often masked by management, and while some aspects of individual mergers will often be successful, the total success and achievement of fully anticipated productivity and cost economies is rarely reached and, the integration process can be lengthy, costly, disruptive, and often problematic.

However, merger activity in the industry continues, and at this current time, projected mergers have become a development tool again, and there are more proposed mergers listed now than have been transacted in the past decade. This opens a platform for research of why banks are keen to merge and what this means to development in the industry, and specifically, what has happened historically and what is happening currently in Oman's banking sector.

The research objectives of this thesis are to examine how banks have developed in Oman and how they have contributed to the country's development, and to also understand gaps in current academic literature and to contribute to the industry with this research, and with the resultant learnings, by way of case studies based on each of the three topics of regulatory reform, transformation and mergers.

Harrison et al., (2017) states that case studies are, "a versatile form of qualitative inquiry most suitable for a comprehensive, holistic and in-depth investigation of a complex issue (phenomena, event, situation, organization, program, individual or group)" p. 8.

As to in what way case studies are important as research models, where suitable quantitative sources are not available, or do not provide a fit that will effectively report the phenomena, Yin, 1981b, first identified that case studies are best used as a method to report events that are not purely related to issues of quantitative research. Quoted from this publication is, " if one is desirous of answering "how and why" questions instead of or in addition to questions of frequency, case studies are the most appropriate strategy" (Yin, 1981, p. 100). Baxter and Jack, (2008) add that, "a case study design should be considered when: (a) the focus of the study is to answer "how" and "why" questions", p. 545. Yin followed up again in more recent times, (2013) with, "the

desired analytic generalization should present an explanation of how and why the initiative being evaluated produced results (or not)" p. 326.

The above evidences that an appropriate use for this research is case studies to ask how and or why questions that will delve deeper into the phenomena and evaluate the results.

A study of Audzeyeva and Hudson, (2016) shows how research questions related to a case study influence and affect the end benefits produced. Case studies, that are a result of this research, show that there have been benefits gained in market value and in effectiveness and questions have been posed that seek answers to provide a deeper association with existing literature and how, or why, the relationships with those findings also demonstrate benefit to the banking industry in Oman.

This section raises three research questions to address phenomena in Oman for each of Regulatory Reform, Transformation and Mergers in the banking sector. Answers to these questions will be found in current literature and the interview process of this research, and lead to answers and case studies that are for the benefit of Oman, the banking and business industry and educators, generally.

4.1 Regulatory Reform

Oman was the last of the GCC countries to initiate Islamic banking and it was evident that the structure of Islamic banking in the other countries had taken on different forms. Some of these were not fully effective, and in the countries of Qatar and Kuwait, Islamic banking windows were withdrawn on the basis that their regulatory authorities could not assure that the tenants of Islamic banking were being observed. Bahraini laws do not cover Islamic windows, although they are allowed in practice and the UAE does not have a specific Islamic banking framework.

The decisions to allow Islamic banking in Oman and the implementation of their framework were delayed until 2012 and until after the Omani authorities had studied how the other countries were dealing with this aspect of banking. Regulatory decision-making is an assessment of the costs and the benefits of proposed regulation and evaluation of the performance of existing procedures and policies, (Kirkpatrick & Parker, 2004), who also show that in developing markets, benchmarking to an already

established regulatory location is with best practices as there is not a one-size fits all approach that is suitable in all situations, and that consultation ensures that full and proper information is analyzed, and this can be from the experiences of other jurisdictions.

We also see from Bakir, (2009), Parker and Masters, (2010) and Vina, (2010) with the examples of Australia and England changing the financial regulatory authorities, that England had assessed the earlier experiences of Australia when reviewing their regulatory structures.

The Central Bank of Oman followed other GCC countries with their late introduction of Islamic Banking and similar to the UK following Australia in their review of the banking regulatory system, this allowed the Omani regulator to study the benefits and the disadvantages of the other countries regulation and governance, and allow them to install a strong framework to ensure that Islamic Banks and Islamic windows in Oman would be sustainable and competitive in a well-established conventional banking market. In view that certain and large banking markets have already questioned the efficacy of Islamic banking and conventional banking cohabitating, and maintaining Shariah compliance, the following question arises for Oman.

Research question 1: How can regulators ensure that Islamic banks are able to compete equitably with conventional banking practices, and preserve Shariah laws?

4.2 Transformation

Competitive forces are a major factor in shaping strategy and Kotter, (1979) shows us that coping with change is the essence of transformation strategy. To engage competition is not an easy task; they are often moving forward at an expedient rate and for an organization to overtake its competitors or, as a minimum, to keep the status quo, institutional urgency and agility that is necessary (Denning, 2016a, and 2016b). Kotter's eight steps to transforming an organisation sets out the criteria for urgency as "an excellent starting point for managers implementing change in their organizations, and applying the model is likely to improve the chances of success" (Appelbaum et al., 2012, p. 776).

Not surprisingly, Kotter's first step in his change model is "Establishing a sense of urgency" (Kotter, 1995) and this includes "examining market and competitive realities and identifying and discussing crises, potential crises, or major opportunities" (Kotter, 1995, p. 63). Creating a sense of urgency seems to be a natural prerequisite and it also seems to be a simple requirement, but Kotter also reports that over 50% of companies that he has observed fail at this step.

Corporate agility is a necessary requirement in competitive markets for senior decision-makers who face accelerating change (Kahan, 2018). Kahan (2018) also provides management theories of agility which lead to innovation management. First gear speeds and institutional sluggishness do not provide corporations with the nimbleness that is required in today's marketplaces. Denning, (2016a) confirms that the agile approach to management started in software development in 2001 and it enables quick-to-market, customer-focused strategies. He introduces what he calls "Agile Practice", that is three core "laws"; the law of the Small Team, the law of the Customer, and the law of the Network. In Denning, (2016b) shows how agile organizations can deliver new value to customers and other stakeholders, and this agile culture with a platform of urgency form a suitable basis for the research question.

Research question 2: Why is the principle of urgency and the laws of agility important for transformation strategies in developing economies? How can they deliver value for customers and stakeholders?

4.3 Mergers

Various academic studies have been written on mergers, including banking mergers. There are a number of bank mergers that have taken place in the GCC countries in the last decade, including Oman, and the past has shown that the local banking industry has developed and benefited through mergers. However, activity in more recent years has been slow and although there have been a number of merger discussions reported, since 2003 Oman has seen only two bank mergers (in 2012 Oman International Bank merged with Hong Kong and Shanghai Banking Corporation, Oman, and in 2020 Oman Arab Bank merged with Alizz Islamic Bank). Merger interest in banking is rising again and in the GCC countries the following 2018 table shows mergers that have been

approved by the relevant regulators and are currently being negotiated by individual management, trade unions and government agencies.

Table 4.1 GCC banks seeking to merge.

Country	Banks seeking to merge/buy stake	Combined/Additional assets
Kuwait - Bahrain	Kuwait Finance House KSCP merger talks with Bahrain's Ahli United Bank BSC	$92.6 billion
Dubai - Turkey	Emirates NBD PJSC agreed to buy Turkey's Denizbank AS for $3.2 billion	Adds $42.8 billion in assets
Saudi Arabia	Saudi British Bank took over Alawwal Bank in a $5 billion stock deal	$72.5 billion
Qatar	Barwa Bank and International Bank of Qatar in talks to merge	$22 billion
Oman	Oman Arab Bank SAOC exploring potential merger with Alizz Islamic Bank SAOG	$7 billion
Oman	Bank Dhofar SAOG starts merger talks with National Bank of Oman	$20 billion
Abu Dhabi	National Bank of Abu Dhabi PJSC and First Gulf Bank PJSC merge to form First Abu Dhabi Bank	$188 billion

Source: Bloomberg News 11 September 2018

It is interesting to see that Oman is preparing for two of the seven proposed mergers. Regarding the Bank Dhofar and National Bank of Oman merger, it was announced in 2019 that discussions between the two banks had been discontinued. For Oman Arab Bank and Alizz Islamic Bank, this was a merger of a conventional bank with an Islamic bank, and evidences the intricacies of dealing with two separate legal entities (conventional and Shariah), and regulatory frameworks, while ensuring that banking assets are not co-joined in the processes and become "tainted". The motives for this merger are not traditional and they are related to Oman Arab Bank's requirement to become a listed entity, and Alizz Islamic Bank's struggle to gain size, in a competitive market.

Motives for mergers are many and include economic, personal and strategic motives (Brouthers et al., 1998), and among the usual economic motives are economies

of scale and cost reductions (De Young et al., 2009). However, achieving economies of scale and efficiency gains through reductions of labor costs can difficult (Focarelli et al., 2002).

Managerial self-interest (Eisenhardt, 1989 and Gupta & Misra, 2007) was also investigated in relation to the various discussions for proposed mergers in Oman. Other aspects of good governance, for example appropriate board size and board behaviors (Battaglia & Gallo, 2015; Pathan, 2009 and Pathan & Faff, 2013) are likely to change during a merger and the culture of Board behavior was very relevant in Oman. Agency theory characteristics (Jensen & Meckling, 1976) can also affect the motives for mergers and in Oman there is a particular situation with banks where the board makeup (and sometimes the management) is representative of a large portion of the shareholding. This can blur the lines between the management and board (agents) and the shareholders (principals).

The Central Bank of Oman has been supportive of past bank mergers and has provided merging banks incentives such as tax concessions and support with deposits, Oman is the only GCC country that has a policy for bank mergers (Molyneux & Iqbal 2016, p. 131). Currently the Central Bank of Oman remains supportive of bank mergers (Fahy, 2020), to help rationalize the industry, and to reduce the gap between the level of business controlled by Bank Muscat, the largest bank, and its competition. Bank Muscat controls more than 35% of Omani banking assets (Bank Muscat annual report, 2020).

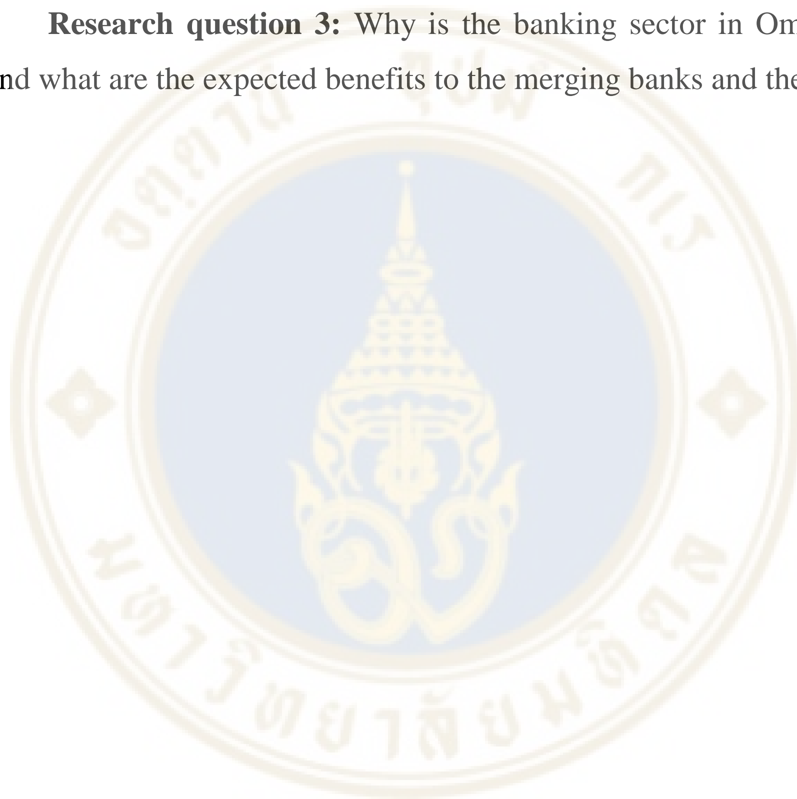
In a country where the expatriate population is approximately 44%, and where the private sector employs 89% of the working expatriate population (Ali et al., 2017), for the banking industry to regulate 90% Omanization creates social contracts where the government bears the cost of ensuring local employment and social welfare (Forstenlechner & Rutledge, 2010 and Swailes et al., 2012). Ali et al., (2017) also show that the trend for public sector employment in Oman, is that only 13% of government jobs are filled by expatriates.

The Oman constitution guarantees all Omani nationals the right to work and it was in 1995 that the government started Omanisation regulations. The emphasis was to reduce the reliance on expatriate workers and to provide employment for local citizens (Glaiser et al., 2019).

The cost of labor of banks in Oman is high, the average employment costs of the three largest banks in Oman is 63% of their operating costs, (obtained from the 2020 annual reports of Bank Muscat, Bank Dhofar and National Bank of Oman).

This creates a dilemma for Oman; where there is an appetite and regulatory support for bank mergers. The motives to merge include cost reductions to attain efficiencies, and the largest costs in the banks is staff costs. Regulations of high Omanization and the local labor laws make cost savings by reducing staff numbers difficult, and other usual motivators have also been difficult to achieve.

Research question 3: Why is the banking sector in Oman motivated to merge and what are the expected benefits to the merging banks and their shareholders?



CHAPTER V
SCOPE OF RESEARCH

The sizes of banking markets are expansive and that development of markets which banks operate in and the differentials involved in the banking sector are wide, and the literature is expansive. When the initial thoughts of how to address the topics of this research was formed it became apparent that a developed and efficient banking industry is necessary for country economic and commercial development, however, what are the factors that make an efficient financial system? To answer that, and to provide a vehicle to lead this research to offer contributions to the academic and management arenas, it is seen that banking systems are forever evolving, moving forward and reinventing itself. In order to be leaders in advancement, remain competitive and be creators of shareholder value, banks are continually in a state of transformation. In tandem with that transformation, regulators are also constantly reinterpreting laws and procedures. History shows that when banks control the markets, without adequate and proper regulation, crises can occur. This was recently shown in the cases of the Asian Financial Crisis of 1997 and the Global Financial Crisis of 2008, both of which were hugely detrimental to country growth and economic development. The most effective economies over long periods are those that have proactive polices and regulators with firm rules and guidelines, and there are strong penalties in reaction to regulatory breaches.

"Financial institutions have been hit with $10.4 billion in global fines and penalties related to anti-money laundering (AML), know your customer (KYC), data privacy, and MiFID (Markets in Financial Instruments Directive) regulations in 2020, bringing the total to $46.4 billion for those types of breaches since 2008". Quoted from Jaclyn Jaeger in Compliance Week, 23 December 2020.

Mergers have become a transformation tool that is used regularly and constantly in all banking markets, and for many reasons are promoted as banking advancements to regulators, shareholders, customers and staff committees. As a system

of transformation, that has a much quicker effect on the banks' targeted outcomes than projected organic styles of growth, mergers present significant effects, and they need to be managed in ways that are specific to the challenges encountered.

All of regulatory reform, transformation and mergers in the banking sector are widely researched and there is significant literature available. In addition to the academic literature, there is a large supply of statistical information available from bank reports and regulatory publications, and the use of data from interviews completed the gathering of information to be able to form and answer suitable research questions.

The initial research was wide and not restricted to the financial or banking sectors and this gave a broad understanding of the effects of each of the three facets, in the broader sense. Next was to approach the banking sector in general, in relation to the selected topics. The review of literature while extensive on a global basis is much less so in relation to the Middle Eastern, and especially, the Gulf Co-operation Council countries. On deeper revisions, it was found there is a lack of literature about the Sultanate of Oman, which is a relatively new, but fast track, oil wealthy country and has had a high degree of development and growth.

Banking is a historic industry stretching back centuries and knowledge of the early development of most geographic markets has been lost in time, however, in Oman, the history is contemporary and can be studied in relation to recent events of the early development and rapid expansion to a modern financial sector. Oman provides an opportunity to research the gaps in the knowledge of the banking system relative to how regulatory reform, transformation and mergers have influenced country and economic development.

The scope of this research uses literature reviews, databases (annual reports, central bank reports, and country statistics) and the outcomes of a series of semi-structured interviews with senior bankers and business leaders.

CHAPTER VI
METHODOLOGY

6.1 Research Method and Design

There are many studies in regulatory reform, transformation and mergers which have used both qualitative and quantitative methods. However, there are fewer studies relative to the banking sector, and even less in relation to the banking sector in Oman.

The banking sector in Oman is young compared to the global development of the industry (Babicci & Wongsurawat, 2018; Kalmoor, 2010). Additionally, the banking market is small in number of banks and for these reasons, empirical evidence to conduct in-depth quantitative research studies is limited. Hence, research into the banking industry in Oman lends itself to qualitative studies.

Qualitative research engages respondents' reactions to situations that are explored and studied by researchers, and they provide a series of events that can be studied to provide outcomes that will support, or otherwise, the inquiries that seek to collaborate the researchers' perspectives with the respondent's experiences and knowledge (Yeung, 1995). Ambrosini et al. (2009) report that in qualitative research situations, smaller sample studies are more likely to provide appropriate materials for understanding targeted situations, on the basis that the respondents selected are experienced and knowledgeable in the fields being researched.

In the case in Oman there are experienced and knowledgeable professionals that can be found in the areas of conventional banking, Islamic banking, and the Central Bank of Oman, accountants, lawyers, educators and businesses. Experts from all of these areas were approached to provide their experiences and knowledge through semi-structured interview processes to find answers to the proposed research questions in this study. Their responses have been collated to provide validation to support the research questions posed. Supporting information was gained by completing a fieldwork of a series of interviews with suitable and senior candidates from each of the above

professional areas. It is important to obtain an appropriate cross section of the industry so that full and proper evidence is gathered to test and validate the theory posed in each of the research questions.

This was supported by a series of discussions guided by structured questions, where responses were video recorded. Field notes, interview transcripts and other supporting documentation were also taken. The questions were constructed to generate discussions in order to obtain in-depth information on the development and current status of the banking industry in the Sultanate of Oman

The responses were collaborated and validated in two ways; the first was from secondary data of academic publications, media reports (newspapers and trade related magazines), company reports, and central bank and stock market reports, and the annual reports of banks in Oman. The second was by observation including the researcher's experiences in Oman as a senior banker and industry advisor over the past fifteen years and in the Middle East for over twenty years, this is the validation phase.

The benefit of the observation phase is that it does not require further interaction with the interviewees (Adler and Adler, 1994) and the researcher was able to use own experiences and that of others to gauge the efficacy of the data collected and the data collection process. Observation also generates rigor when it is used with other collection methods and they can also highlight if there are any inconsistencies between the interviewees responses, and later conversations, and what has happened in reality (Pettigrew, 1990).

The following table shows how the research will be supported by secondary research and by observations.

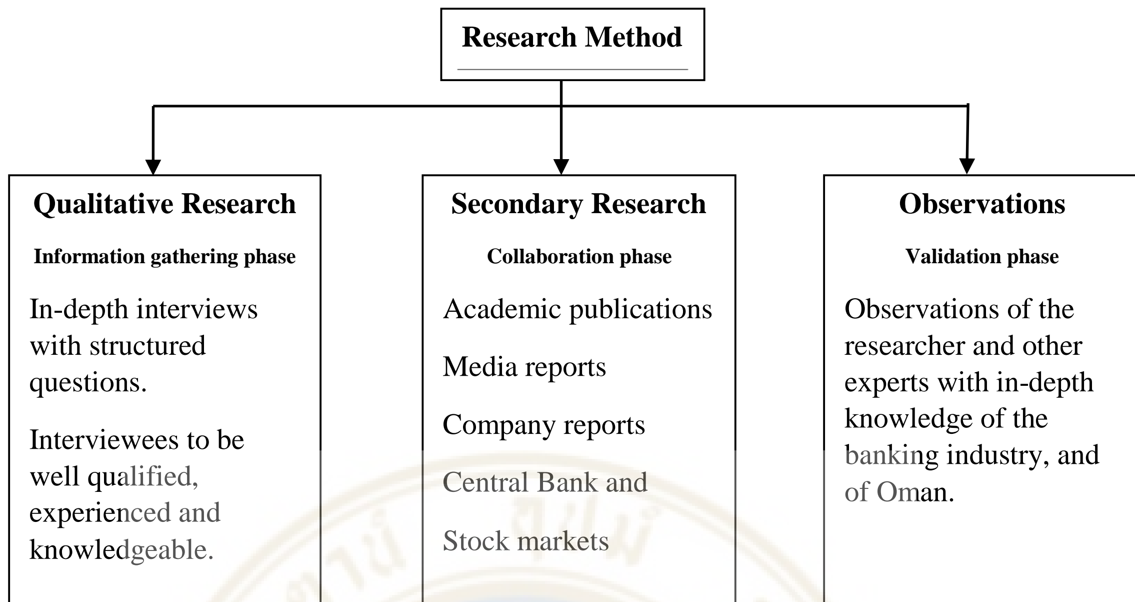


Figure 6.1 Research Method. Adapted from Santipiriyapon 2016

Data was collected from all three sources of information and the interview outcomes provided the primary information data and validity of information already collected. To also prove cross validation of information Triangulation Method was used. Triangulation Method is the process of using more than one method to collect data. This is a research technique to further assure the validity of the research information through the use of a variety of methods to collect data on the same topic, which involves different types and sources of samples as well as methods of data collection (Paul, 1996). This research used the three phases of data collection, Interviews for primary data collection, Collaboration and Validation. The purpose of triangulation is to capture different dimensions of the same phenomenon. It was useful to assist with adding dimension to the information collected by the primary source in answering the research questions. The following figure shows how triangulation method is used to validate the information from different sources against each other and shows that the process is not linear in nature but cross examines each source of information in relation to the other sources.

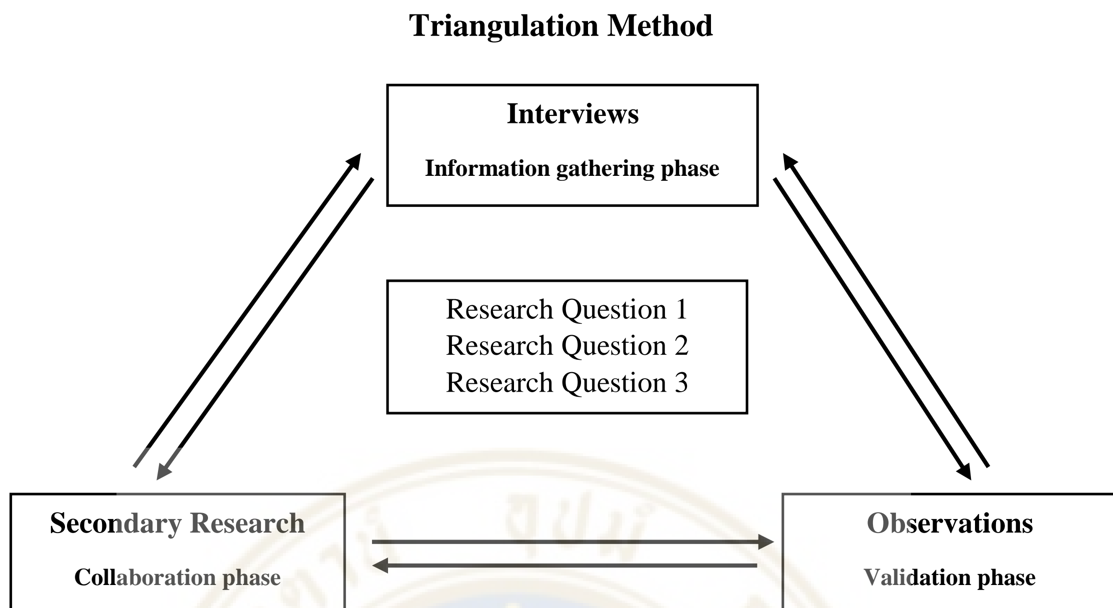


Figure 6.2 Triangulation Method. Adapted from Olivier-Hoyo & Allen 2006

Triangulation is a qualitative research strategy to test validity through the convergence of information from different sources (Carter et al., 2014), and Patton (1999) refers to Triangulation Method as the use of multiple data sources in qualitative research to develop a comprehensive understanding of phenomena. He also refers to the credibility of qualitative inquiry which depends on distinct but related inquiry elements, the first is techniques and methods for gathering data that are carefully analyzed, with attention to issues of validity and reliability; the second is the credibility of the researcher, which is dependent on training, experience, track record and status.

During a review of this process of research, it is important that the objectivity of the researcher as a possible industry insider is addressed. While the researcher was the Chief Executive Officer of a major bank in Oman and a senior executive in the banking sector, there has been a suitable gap in time since holding responsibility in the sector in Oman. The researcher left Oman and the position of CEO for Bank Dhofar in 2011, and fully retired from the banking sector in 2015. This shows a suitable distance to enable objectivity in this research, however, contacts that have been maintained generally and, in the industry, and they are valuable to obtain relevant and accurate data. The researcher does, however, at the time of conducting this research

process, maintain a position in the Sultanate of Oman as a Strategy Advisor to the petroleum industry.

6.2 Research Process

In order to conduct qualitative studies, there must be a research process that can be followed. The flow chart shown below represents the process employed in this research. The research questions were examined through literature reviews and confirmed that answering the questions posed in this study, banking literature will be enhanced, it is also original research and will add to knowledge relative banking in Oman and the development of Oman's economy.

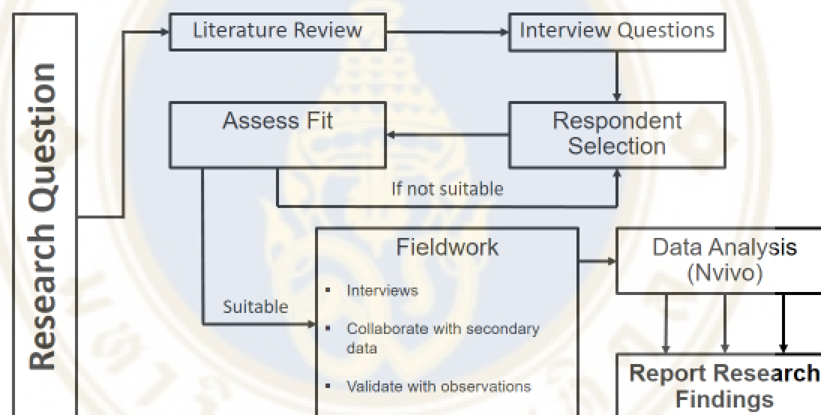


Figure 6.3 Research Process

For the interview process, it is important to obtain a suitable cross selection from not only the banking industry but from business sectors as well. Table 6.1 below, shows that the selection of respondents from banks and companies includes representation from all business and bank types associated with the banking sector.

All of the types of banks in Oman were represented (Conventional, Islamic, Islamic Windows and International), there was also representation from business (large corporations and SME's) and also from legal and accounting firms, all of the respondents from these have a long close association with the banking sector in Oman

and have experiences or knowledge relating to regulatory reform, transformation and mergers.

Executives of conventional banking and Islamic banking supervisory departments of the Central Bank of Oman were also selected, however, they declined to be interviewed and formally responded to the researcher that internal CBO approvals for the interviews were unavailable due to the possible market sensitive nature of the proposed discussions.

A representative from the College of Banking and Finance of Oman was also included in the interviewee selection to provide a view of the educational sector for banking.

The selection number of respondents was spread across the banking and supporting industries and considering Ambrosini et al. (2009) and Alam, M.N. and Alam, M.S. (2017) and Rowley (2012), consisted of twelve interviews.

The following table shows the selected respondents that were interviewed and also shows what sector the respondents came from and the level of their seniority in their institution.

Table 6.1 Interview respondents

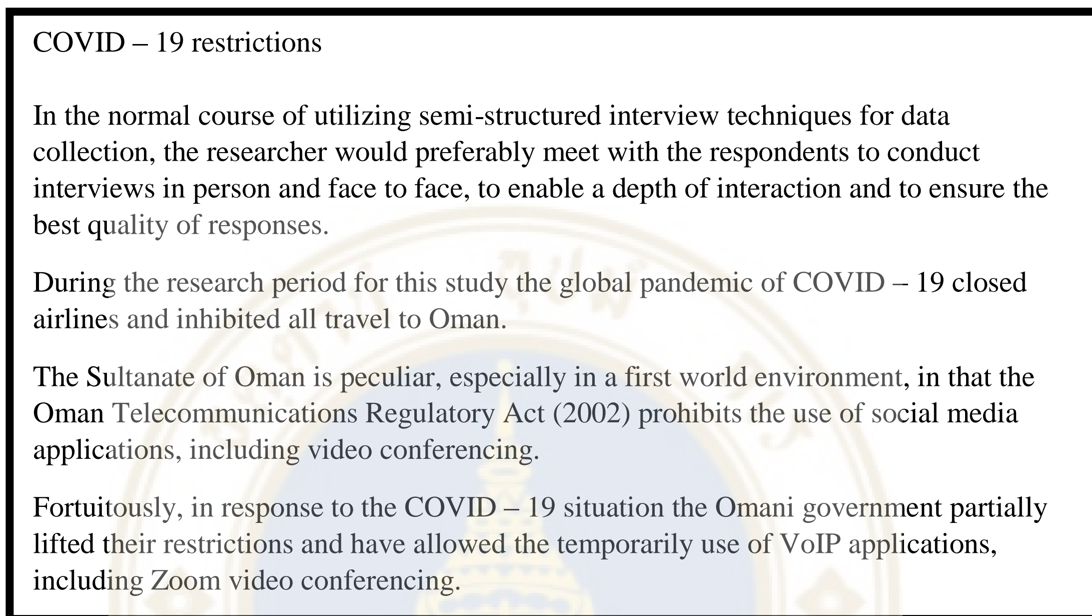
Banking or Other Entity	Respondent and Seniority Level
Conventional Banks	Chief Executive Officer Business Head
Conventional Bank Windows	Board Member Chief Executive Officer
Islamic Banks	Chief Executive Officer Business Head
International Banks	Business Head
Large Businesses	Chief Executive Officer
SME's	Chief Executive Officer
Accounting Firms	Partner
Legal Firms	Partner
College of Banking and Finance Oman	Past Dean
Total Respondents	**12**

Sampling sizing in qualitative research is regarded as the specific standard and has been proposed for different methods of data collection for qualitative study, Qu & Dumay (2011) propose a single individual interview is appropriate where unstructured interview technique is used, however in the search for a full and varied view of data, more than one individual could be used depending on the level of knowledge and experience of the interviewee, and as the researcher deems fit. The amount of people used add to the depth and thoroughness, and validation of the material provided, although larger numbers can often cloud analysis of final results without adding proportionate value (Marshall et al., 2013), with the lesser the number of interviewees preferable when the subjects are at the upper range of specific expertise and knowledge. This research used semi-structured interview technique and is described as open discussions guided by pre-qualified themes interposed with questioning to elicit greater depth responses (Qu and Dumay, 2011). The number of interviewees for the sample requires a sufficient quantity so that people with different roles, experience, backgrounds, and any other source of variability that might draw accurate answers are included in the study. There is no one size fits all with selecting sample size for qualitative case study research and the key criterion is that the interviews must result in satisfactory interesting findings. Rowley (2012) reports that as a guide qualified research should aim for around 12 interviews of approximately 30 minutes in length, or the equivalent, six to eight interviews of around one hour.

The number of respondents (twelve) was appropriate for this research methodology and the discussions showed a deep knowledge of the Omani banking and business environments, this provides satisfactory comfort that the outcomes of the interviews are appropriate and accurate. The process to select respondents, test them for fit against the criteria, and approach them for acceptance and to complete the interviews was lengthy and took four full months due to the seniority of the respondents and their busy and full schedules. There was a balanced mix of Omanis and expatriates (7 Omanis and 5 expatriates), seven of the respondents were from within the banking industry and five were from other sectors.

To gain the greatest depth and width of knowledge of the subject, a greater than usual selection of interviewees was set for this research project, and a criteria to ensure the best knowledge panel available. Interviewees selected were expected to have

been in their respective industries, in Oman, for ten years or more, and in their current role for at least four years. Interviews were conducted on an individual, one on one basis, with the researcher and conducted and recorded by video using Zoom video conferencing applications.


COVID – 19 restrictions

In the normal course of utilizing semi-structured interview techniques for data collection, the researcher would preferably meet with the respondents to conduct interviews in person and face to face, to enable a depth of interaction and to ensure the best quality of responses.

During the research period for this study the global pandemic of COVID – 19 closed airlines and inhibited all travel to Oman.

The Sultanate of Oman is peculiar, especially in a first world environment, in that the Oman Telecommunications Regulatory Act (2002) prohibits the use of social media applications, including video conferencing.

Fortuitously, in response to the COVID – 19 situation the Omani government partially lifted their restrictions and have allowed the temporarily use of VoIP applications, including Zoom video conferencing.

Figure 6.4 COVID – 19 restrictions

Pulakos and Schmitt (1995) show that structured interviews relate to two types of respondent, the first is experience based and the second is situational based. Experience based questions are those that relate to real life circumstances of what the respondent has experienced, and situational questions relate to how the respondents feel events have transpired. All the respondents for the interviews have had direct experiences in their fields in order to answer the structured questions, and they also showed that they all have opinions and considered views of how events in the banking sector have transpired.

The respondents were assessed for experience based fit (referring to the process in Figure 6.3), and they all meet the criteria of knowledge and experience for their subject matter. All have been in their respective industries in Oman for over ten years and in their positions for over four years. The selection criteria of ten years in the industry is rational because that is approximately 25% of a projected career life, and the interviewees will have built up substantial knowledge and experience in their field. This

also runs true for working in Oman for at least ten years where employees are able to build knowledge and experience specifically about the Omani markets.

All the respondents were at the very senior CEO or business head level and those from outside the banking sector were selected from large business, the SME sector, accounting, and legal firms – as users of banking services, and from the academic community (College of Banking and Financial Studies) that closely relates to banking education.

6.3 Interview Procedures and Questions Development

A series of questions that are suitable for interviewee responses is required to obtain research information and the design of the questions follows the subjects of regulatory reform, transformation and mergers in the banking sector in Oman.

When using interviews as a data collection method, creating trust with the interviewee becomes very important (Meyer, 2001), this is to assist with getting the most honest and appropriate responses. It should be noted here that researcher is known to all the respondents, or the respondents know of the researcher. The lead-in to a formal interview can be delicate, especially with Arabic respondents and to assist with the process I used the following steps. First, contacted the proposed interviewee directly (by telephone) to request their assistance and to advise them of the background of my request, and all agreed to participate in the interviews. Second, an email was sent explaining the features of the research and out-lining the broad issues that would be raised in the interview, and describing the process. I also included that the interview would be video recorded, so that the respondent would not be surprised, and I also explained the anonymity measures and ethical matters of the research. It was important to communicate how I intended to use the responses, and I also explained the documents that were required to be signed by the interviewees (Interview Consent Form). I explained the project's origin and purposes, procedural details to be carried out, its expected benefits and any risks to the interviewee that may occur, including methods to prevent and handle any harmful consequences, and that there is no remuneration or expense. I included an information sheet and copies of the consent form, all in accordance with Mahidol University's Institutional Review Board criteria.

Below is a table that shows the questions and the literary sources that helped to develop the appropriate questionnaire. It is designed to create discussion around the subject areas and not to be a yes/no reaction or to gain formal rigid answers. The interviews for each of the respondents was very much an interactive session of in-depth discussions that would flesh out a complexity of information and opinions. It was not expected that respondents would be expert in all the fields and the questions were devised to obtain the best data of knowledge from the selection of industry professionals.

Because the sessions were to be interactive discussions I designed the questions to generate open discussion and I restricted the number to ensure that I utilize the respondents time most effectively.

Table 6.2 Interview questions

Regulatory Reform	Question
1	Bank performance and good corporate governance are related (Al Tamimi, 2012 p. 173) and effective banking systems provide a framework for long-term economic development (Levine, 1999 p. 720). How do local policies help with governance and economic growth?
2	Benchmarking with international best practice is often used in regulatory decision-making (Kirkpatrick & Parker, 2004 p. 336) and the Central Bank of Oman has wide ranging powers and promotes transparency (CBO Governance Statement and Mission and Core Values, CBO website). Independence and transparency are two major areas of central bank governance (Crowe & Meade, 2007 p.69). How have these been used effectively in Oman to promote development and yet maintain control and how does the Central Bank of Oman benchmark against other GCC countries?

Table 6.2 Interview questions (cont.)

Regulatory Reform	Question
3	Oman introduced Islamic banking later than other GCC countries (Sastra Mihajat, 2018 p. 75) and decided to include Islamic windows to the framework (CBO Islamic Banking Regulatory Framework, 2012 p. 22 para. 4.3) at a time when countries like Qatar and Kuwait had closed Islamic windows (Babicci & Wongsurawat, 2020 p.118). How can the supervision of Islamic windows uphold Shariah laws relating to riba, profit sharing and products, and make sure that Islamic funds are not "contaminated", while being broadly "managed" within conventional bank structures?
4	Islamic banking has a positive impact on the banking sector (Gheeraert, 2014 p. 513) and can boost economic growth (Boukhatem & Moussa, 2018 p. 235), but Shariah supervision can bring additional costs that are not seen in conventional banking (Garas & Pierce, 2010 p. 389). Can Islamic banking compete effectively with conventional banking?
Transformation	
1	Transformation strategies help develop and benefit banks (Audzeyeva & Hudson, 2016 p. 41) and transformation of banks is gaining speed with the introduction of modern innovations (Franke, 1998 p. 131). How do banks in Oman keep pace and are they benchmarking to global standards?
2	To keep up with the speed of change banks need to establish a sense of urgency with their strategies (Kotter, 1995 p. 60) this worked well with our Bank Dhofar strategy and we caught the competition by surprise at that time. Oman projects have attracted strong foreign investment and is looking for more. Do banks in Oman have the range of products and the speed to deliver expectations for customers that are used to working in larger and more developed markets?

Table 6.2 Interview questions (cont.)

Regulatory Reform	Question
3	Banks also need to adapt quickly to changes to be competitive (Kahan, 2018 p. 48) and it is common theory that agile organization's deliver value (Denning (a), 2016 p. 10). Is the regulatory framework and the statutory environment flexible and quick enough with decision making to ensure that Omani banks are competitive?
4	How is urgency and agility in Oman delivering value for the banks customers and for the shareholders?
Mergers	
1	The Central Bank of Oman has been supportive of bank mergers (Molyneux & Iqbal, 2016 and Fahy, 2020), and recently there has been discussion about possible mergers (for example, Bank Dhofar/Bank Sohar, Bank Dhofar/National Bank of Oman, Oman Arab Bank/Alizz Bank). Is Oman currently overbanked, and is this the right time for more mergers?
2	Oman's Council of Ministers has also committed to provide jobs for new Omani graduates (Al Shaibany, The National, 5 October 2017), and many of these will be expected to be in the banking industry. In addition, to ensure job creation for Omani's, The Central Bank of Oman maintains strict Omanisation requirements in banks, which is currently 90% (Central Bank circular 762 dated 14 July 1995 and Central Bank of Oman Booklet of Circulars dated 30 April 2009 p. 10). How can banks ensure that Omani employment and Omanisation requirements are met, and also deliver efficiencies and cost containments?
3	There are many motives for bank mergers including increasing revenues, cost savings, synergies and rationalization (Houston et al., 2001 p. 288 & p. 308). Staff costs in Oman banks are high at 63% of operating costs (2019 annual reports of Bank Muscat, Bank Dhofar and National Bank of Oman), and mergers can create higher staff costs (Focarelli et al., 2002 p.1, 065). Oman has the desire for bank mergers, but with Omanisation, job creation expectations and high staff costs; what are the likely motivations for these mergers?

All the respondents are senior executives in their fields and in their organizations and they were able to afford limited time for the interview session itself. In my email to each of them, I asked that they allocate approximately one hour for the interviews. The discussions were detailed with total interview time of 14 hours and thirteen minutes (average time was one hour and twelve minutes).

After completing all the interviews, transcriptions of the video recordings were completed and uploaded to the NVivo software program for analysis. The following screenshot is an example from the NVivo program showing the transcription of one of the interviewees.

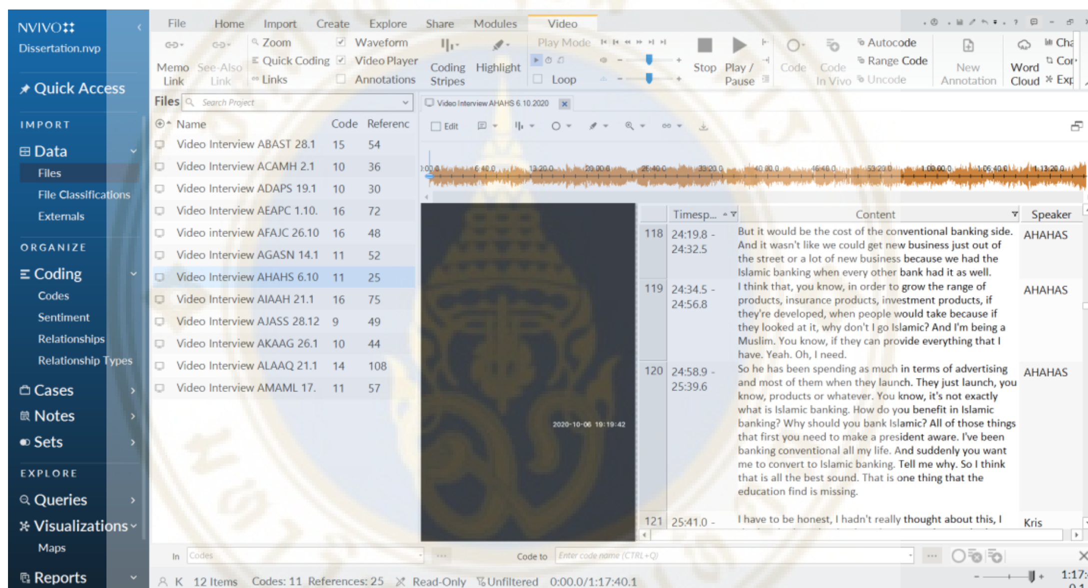


Figure 6.5 NVivo Screenshot – transcription

This shows how the identity of the interviewees has been masked by coding their names (in this case AHAHAS), I have removed the image from this screenshot example to further protect the anonymity of this interviewee. The transcripts were then reviewed for repeated ideas and concepts, and codes were assigned to the common themes, sub-codes, ("child" codes) were also developed and relationships and sentiments (positive and negative) were derived.

The coding process was lengthy and it involved working and reworking and refining the data many times to produce a structured and detailed framework which supported the research directions, and these were further analyzed and then re-reviewed

into impressions, and then into categories in order to find answers to the research questions.

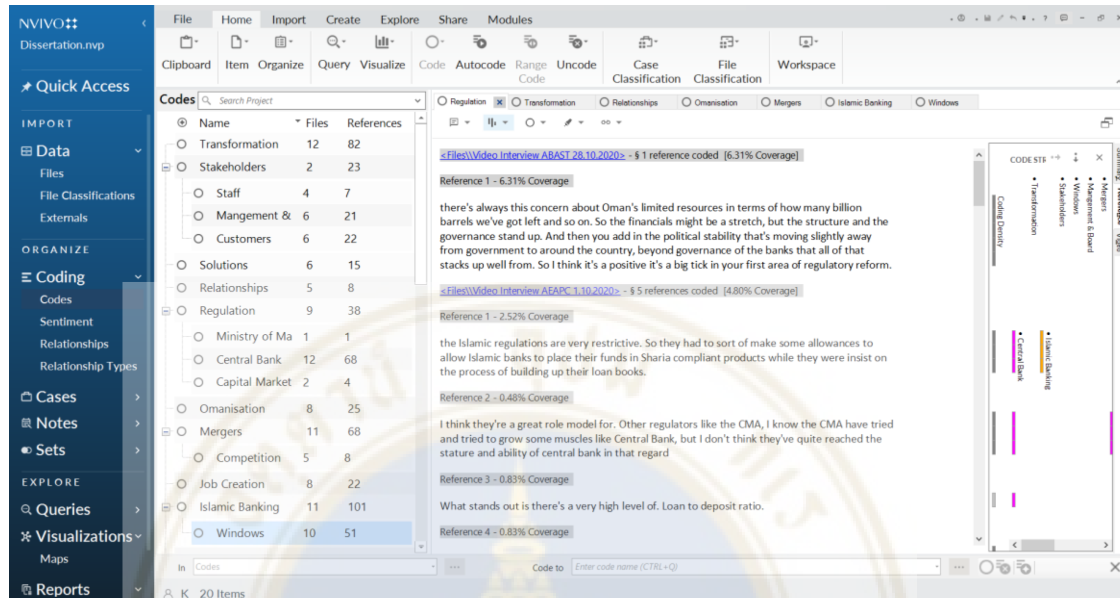


Figure 6.6 Nvivo Screenshot – coding

The above (Figure 6.6) is a screenshot of the coding files from NVivo. Selections from the transcribed interviews are filed under codes (the names and numbers of codes are derived through the analysis of the transcriptions, and then further refined into the sub-codes. The program also shows the number of times a code is referred to, and the percentage (density) of each reference. The colour coding at the right of the screen shows the location and density of each reference.

The NVivo related work process for this research involved approximately two hundred hours and produced over seventy pages of work notes.

CHAPTER VII
ETHICS

Members at the most senior levels of bank management (Conventional Banks, Islamic Banks, Islamic Windows and International Banks), as well as banking industry stakeholders (business customers, accounting practices, legal firms and the Oman College of Banking and Finance) were interviewed as part of this research. Ethical concerns need to be protected in relation to participant identification and any confidential information obtained during the interviews.

Confidentiality of the responses to the interview process are to be maintained, the author is the person to conduct the interviews, prepare and collate the responses and complete the reporting. Information that could identify any respondent or organisation will only be known to the author and only released after confirming with the relevant respondent and obtaining appropriate authorities from the organisation, if required. All respondents have signed the Interview Consent Form.

The targeted respondents are all professionals and senior level executives in their organizations and their industries, and because the research questions are general in nature, ethical issues relative to sensitivities of questions are not expected. The identity and the answers from all those interviewed have been kept anonymous, and information is only reported in a way that ensures that anonymity.

The ethical practices designed to be employed in the research and reporting of this dissertation have been submitted to the Institutional Review Board (IRB), Mahidol University Center of Ethical Reinforcement for Human Research and approval has been granted. As part of that submission, the author completed the Collaborative Institutional Training Initiative (CITI) program in social and behavioral research.

CHAPTER VIII
FINDINGS

While analyzing the outcomes of the interviews it was evident that the chosen respondents were very knowledgeable about the banking sector and about Oman in general, the discussions were deep and covered all aspects of the current trends and banking history in Oman. Seven of the twelve respondents are working in the banking industry, they are all long-term career bankers and the minimum time worked in the industry is twenty four years. One of the respondents is also the Chairman of the Omani Bankers Association, and one of the other bankers is a member of the Majlis A'Shura, the Lower House of parliament. One is a board member of the Capital Markets Authority. Two of the respondents had international banking experience and one had worked in the banking sector outside Oman for an extended period. Of the non-bankers interviewed four were expats, and of those all have spent more than twenty years living and working in Oman. The one Omani in this group is currently a Member of State and is a past long standing Dean of the College of Banking and Finance. The quality and the knowledge of the respondents is extensive, and the research was able to uncover interesting and original findings.

Discussions began with general conversations about local current affairs and the general economic situation in Oman, and then moved more specifically into banking and the topics of this research. A large portion of the general discussions were about the recent issues in the Omani economy and how those issues interact with the banking sector. Themes included the volatility of oil prices and Oman's reduced government revenues, which have led to economic challenges for both the public and the private sectors, and the need for Oman to reduce its reliance on oil production, and the government's strategies for large infrastructure projects to drive economic growth. The recently constructed Duqm Special Economic Zone, which includes a major petrochemicals refinery, is a large-scale project with a cost of USD 7 billion. This project was recognized by all the respondents as a success, but it was also acknowledged

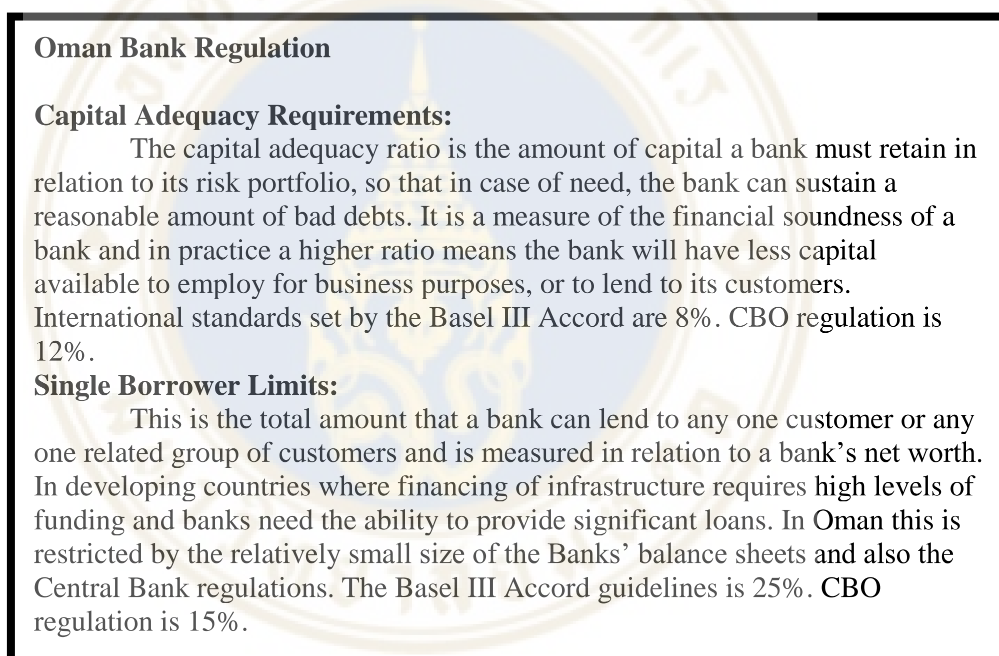
that foreign investment is needed to span the gap between infrastructure costs and local bank funding capabilities. Oman currently has active infrastructure projects worth USD260 billion (Oman Projects – Middle East Business Intelligence), and these include large energy related facilities, social enhancement amenities such as housing, schools and hospitals and tourist related spending for airports, hotels and resorts. The newly completed upgrades to the airports in Muscat and Salalah to cater for larger numbers of local and international travelers was at a cost of USD 3.1 billion. Because of the size and number of these infrastructure activities, Oman has become a sought-after destination for foreign investment, which is needed in the absence of a sufficiently sized banking sector and local capital markets.

All of the respondents had views and experiences regarding the cultural and socio-economic issues related to living in Oman specifically, all the conversations included issues that are created by Omani's large families, which in earlier days, when medical facilities were low, were for continuity and family succession reasons. However family sizes have not reduced in current times and it is culturally expected for Omanis to have a large number of children. Oman's first census was in 1993 and showed at that time women between the ages of forty and forty four gave birth to an average of 8.13 children, Sultan Qaboos voiced his concerns stating "a big family is a burden on us all" (Drysdale, 2010). The culture of large families and the introduction of modern medical facilities has created a social issue of overpopulation of Omani youth, and as a result creates a scarcity of and great competition for employment opportunities. The government has been addressing these employment challenges by strong Omanization measures, job creation in the public sector, and more recently by implementing early retirement programs to free up positions along the employment chain.

One of the most consistent threads brought out of the discussions was confirmation of the complexity of bank management and the strong influence of board members in decision making, and this came from both bankers and non-bankers. In addition to the Central Bank of Oman's frameworks and regulations, guidance and instruction is also directed by the Capital Markets Authority with regard to general corporate governance, which includes banks. Central bank management is additionally concerned with banking sector stability, loan portfolio quality and depositor protection, and board influence. Rooted in the interview discussions were vocal and undisputed

views about Central Bank of Oman regulations and the interviewees regarded that bank regulation in Oman is well managed, but conservative, and the CBO guidelines are more traditionalist and restrictive than international norms, including its peers in other GCC countries. In the interviews all the bankers were unanimous and three of the five non-bankers confirmed this conservative stance, and specific examples were given that Oman based banks cannot lend outside Oman, they cannot open operations internationally, and they are restricted in lending to non-resident individuals or companies.

The most prevalently raised subjects in the CBO's conservatism related to capital adequacy requirements and single borrower limitations.



Oman Bank Regulation

Capital Adequacy Requirements:
The capital adequacy ratio is the amount of capital a bank must retain in relation to its risk portfolio, so that in case of need, the bank can sustain a reasonable amount of bad debts. It is a measure of the financial soundness of a bank and in practice a higher ratio means the bank will have less capital available to employ for business purposes, or to lend to its customers. International standards set by the Basel III Accord are 8%. CBO regulation is 12%.

Single Borrower Limits:
This is the total amount that a bank can lend to any one customer or any one related group of customers and is measured in relation to a bank's net worth. In developing countries where financing of infrastructure requires high levels of funding and banks need the ability to provide significant loans. In Oman this is restricted by the relatively small size of the Banks' balance sheets and also the Central Bank regulations. The Basel III Accord guidelines is 25%. CBO regulation is 15%.

Figure 8.1 Oman Bank Regulation

Sources: CBO Regulatory Framework on Financial Stability Basel III Accord Guidelines

The Central Bank of Oman Regulatory Framework on Financial Stability shows that banks in Oman are required to maintain a capital adequacy requirement which is high at 12%, and single borrower limits are restricted to 15% of the banks net worth, and these are shown in comparison with Basel Accord guidelines above. The Basel Accord has been accepted by all banking jurisdictions as global guidelines for

bank financial management. Capital adequacy and single borrower limits are key determinates of the banking sector's ability to grow organically, and conversely central bank regulations will strive for a balance of bank financial strength, economic protection, and growth, and these aspects of governance require particular attention, especially in times of economic downturn.

A relevant and telling insight from the interviews was from the senior bankers who had strong views on the local regulations, with regard the ability for Omani banks to build scale and participate in the number of current infrastructure projects, which are set to drive the economy for future growth. One of the bank CEOs stated,

"If we don't have scale, we can't play in the game at all, (meaning participate), and a lot of the reason we can't play in the game is regulation, you've got single borrower limits and we need the projects."

To put the need for foreign investments in context of the infrastructure projects, at the end of 2019 the local banking system had total assets of USD 91.6 billion and a net worth of USD 31.2 billion (CBO annual report 2019). Net worth is calculated as total assets less liabilities, and with single borrower limitation of 15%, allocations is limited to USD 4.7 billion – for total projects of USD 260 billion, and it is evident that outside investment is needed. The added dilemma is that the Oman government is operating on a growing deficit due to the reduced oil income, which accounts for 84% of government revenues. This means that government funding for these projects has become limited, and additional funds are needed to create employment opportunities.

Findings from the interview discussions are detailed below under the topics of regulatory reform, transformation and mergers, and the outcomes of the interviews provide data to fill gaps in the current literature, relative to the banking sector in Oman, and to find answers to the research questions posed in this study.

8.1 Regulatory Reform

The Capital Markets Authority of Oman provides governance and guidance for corporate entities and also provides supervision of the Muscat Securities Market (Oman's stock market), while the Central Bank of Oman forms monetary policy and is the primary regulator for the country's financial system and banking sector.

The CBO sees its role as responsible for promoting financial stability and fostering a sound, progressive and sustainable economy and in line with the definition of regulatory reform intervention, the Central Bank seeks to develop and implement policies that will improve and enhance social requirements and the country economic situation in Oman. However, the CBO is also well known for being conservative and cautious, it is seen as rather traditional more than contemporary in management style, but it is also seen as a strong administrator of banking policy.

During the interviews there was a consistency of comments about the central bank. All the respondents showed positive sentiments, and the messages all had the same common thread with regards to conservatism, “they stack up as conservative against the rest of the GCC”, “a very strong filter”, “they’ve got the headroom for relaxation”, “always been conservative”. Al-Muharrami (2019) confirms the supportive but conservative attributes of the policies and regulatory frameworks of the Central Bank of Oman, and as far as being a strong regulator, the studies by Baydoun et al. (2012) and Al-Malkawi et al. (2014) both show that Oman rates high on corporate governance measures within the GCC countries.

At the same time, all the respondents were complimentary on the central bank’s role and management, “they are not unreasonable”, “very supportive”, “emphasizing transparency”, and also they were positive on the wider role of the regulator in promoting social benefit and supporting Oman’s strategic and economic visions, “they are very socialistic bent”, “worried about the everyday person on the street”, “act as a consumer protection body”.

The quoted extracts below are from the interviews and they indicate that regulatory reforms to banking governance enhance country development, and are also relevant to the examples in Oman.

One of the respondents from the non-banking sector spoke about the benefits to Oman from the reforms by the Central Bank,

“The structure and the governance stand up and then you add in the political stability that’s moving slightly away from the government to around the country, beyond governance of the banks, and all that stacks up well. So it’s a big tick in your first area of regulatory reform.”

The following is another quote is from one of the non-banker CEO's and it is also a representative observation of The Central Bank of Oman's role in the country's economic progress,

"It may be frustrating in times of rapid growth, but the growth still happens and there's plenty of evidence to come that would be a very good example of the strategic nature of Oman's vision and how the central bank plays its part in those kinds of opportunities. My view is that the central bank in its governance and its policies are helping develop economic growth. But it's at quite a slow pace."

Further testament from the banking sector shows,

"In terms of the Central Bank being there for policies and governance it does help with economic growth because you need quality governance so there's a positive effect on the economy. For example, there is the government, which would be the central bank, and then you have the banks themselves, and obviously we need to have law. So when you look at all this, it facilitates growth."

When the Arab Spring erupted in 2011, rulers in the Middle East and North Africa took numerous measures to quell the popular discontent that was boiling over. Shrewd leaders understood that institutions needed to act as valves to release pent up political pressure. In Oman, Sultan Qaboos introduced a string of measures to address public grievances, including a minimum-wage hike and stepped-up efforts to create jobs (Al-Shaibany, 2013). For the first time in Oman's history, the Sultan also permitted Islamic banking to be established. And this led to the most radical and controversial regulatory reform in Oman's banking history.

Oman's religious majority is Ibadi Muslim with moderate and conservative attitudes, and in the view of Sultan Qaboos and his advisors, Sharia-style banking could foster exclusion and extremism. Not allowing Islamic banking at all, nonetheless, is unusual for a country with a majority Muslim population and the Quran explicitly forbids basic practices of conventional banking, which was the only banking service offered at the time. The discontent among some of the Muslim population was that an option that would be acceptable to Shariah compliance and the Quran was not previously available. That forced either the acceptance of conventional banking, with its non-Shariah conventions, or to not use the local banking system.

In 1994 and again in 2005, the Omani government had suppressed rebellious plots, arresting members of fundamentalist parties and seizing caches of illegal weapons. A major motivation for these parties was to promote Islamist ideals and, among other things, demand Islamic banking (Worrall, 2012). At the time, Oman was quite surprisingly the only country in the Gulf Cooperation Council (GCC), and the only country in the world with a Muslim majority, that did not allow Islamic banking.

However, the disruptions of 1994 and 2005 were relatively small and thus rapidly quashed. It was not until the much larger and more widespread Arab Spring uprisings in 2011 that the Sultan was forced to take notice. As an immediate response to the protests, he asked for a list of concerns to be presented to the government. The demands of the protesters centered on concerns that particularly troubled the large youth population of Oman: educational development and job creation and also the social/religious discontent caused by the ban on Islamic banking. By the end of 2012, there was a royal decree allowing Islamic banking, and the Central Bank consequently introduced a new Islamic Banking Regulatory Framework that was well considered and had been studied along with the experiences of other GCC countries, it included provisions for stand-alone Islamic banks and also Islamic windows of conventional banks.

It was a natural progression in 2012 that Oman would adopt Islamic banking and it seemed that the country's banking system was ignoring a large portion of the financial sector. The National Centre for Statistics and Information in Oman showed from 2016 data only about 56 percent of Oman's population held bank accounts, suggesting a great opportunity for banks to grow. The large number of non-participants was thought to be due to the fact that Islamic banking was historically not allowed; a conclusion of this data was that Muslims who closely adhere to the teachings of the Quran would prefer not to use banks at all, rather than conventional options.

The respondents to the interviews had many comments and views about the introduction of Islamic banking in Oman and the code section in Nvivo on Islamic banking became full with insights. These were all generally positive with evidence that Shariah style financing options are good for the religious expectations of the Omani population, "it was based on demand of people who felt very strongly", "there was demand, people wanted other options, and the government studied this carefully", "there

is a lot of appetite in the local market", "it's emotional at the end of the day", and "following these types of products will give them some kind of comfort."

Islamic banking is well accepted in the six GCC countries, according to the Islamic Financial Services Board survey 2018, it accounted for 42 percent of the world's Islamic-banking assets. The next-largest markets are the Middle East and North Africa (MENA) region, with 29 percent, and Asia, with 24 percent. The GCC, is a major player in Islamic banking worldwide, and is looked upon for innovations as well as regulation and control, the growth of Islamic assets here has also been the fastest globally. Other than for religious preference, the Omani government recognized the need for inclusion of a large part of the unbanked population, and by doing so, also add to the nation's development and economic growth.

One of the non-bankers, but a corporate customer of Islamic banking summed it up,

"Islamic banks are seen as a legitimate and positive addition to the financial landscape. There are some of the public companies listed on the Muscat Securities Market that are actually sort of labelled as Islamic friendly investments, we have got a lot of assets and it lends itself to the Islamic banking model."

And one of the Islamic banking CEO's confirmed the benefits of the new regulations,

"The central bank was seeing this as an opportunity, because if you do it the right way, you essentially are offering another option to a population of consumers. And I think indirectly, they are also seeing that this could bring a lot of unbanked. And 10 million capital became 55 million over the course of five years."

In corroboration with the above comments, Mubeen et al. (2014) confirm through a survey directly with Islamic banking customers and also through The Economist magazine, that Omanis convincingly agree (at least 75% Strongly Agree or Agree in the surveys) that Islamic banking contributes to increase the national revenues, they encourage investment in Oman, contribute to financial and monetary stability, and encourage citizens to save.

When Islamic banking was first introduced to the world in the 1960s, there were only dedicated Islamic banks. Conventional banks chose not to participate, as they did not realize the size of the market. They felt that Islamic finance was founded only

upon religious enthusiasm and destined to fail as it was not a commercial substitute for conventional banking.

However, Islamic banking won a large part of the conventional market, causing bankers to re-evaluate their thinking. Conventional banks needed to convince Muslim clients to trust their ability to properly implement Sharia principles. As a result, Islamic "windows" were established as independent and segregated "departments" of the conventional banking businesses, and to ensure Islamic values and practices were upheld, Sharia Boards consisting of Islamic scholars were formed to supervise the operations of windows and to ensure Shariah compliance. Islamic windows are under the umbrella of conventional banks and they separately offer products and services that are based on Islamic principles. It is essential for Islamic windows to ensure that there is strict Shariah compliance in every respect and there is also no cross-contamination of funds, and no comingling of Islamic and conventional products and technology systems, even management has to be totally separated. These strict requirements to maintaining adherence to Shariah principles in the Islamic windows of conventional banks has been the major challenge for bank management and for regulators.

There is increasing research also confirms that Islamic banking has a favorable effect on banking and financial development as well as on economic growth (Boukhatem & Moussa, 2018 and Gheeraert, 2014), and there were clear social and business reasons for introducing Sharia-style banking in Oman, and yet the supervision and governance of Islamic financial institutions continue to lack standardization (Garas & Pierce, 2010).

Oman is no different than other countries that have introduced Islamic banking, in that it has encountered certain barriers and obstacles. First, there was strong competition with the already established conventional banks, and the efforts required to woo customers away from existing relationships were found to be tough. Second, the availability of staff with relevant knowledge and experience is a challenge, there are few education opportunities specific to Islamic banking, the industry is young, and globally experience levels are shallow.

In Oman, where 90 percent of bank employees must be Omani, and Islamic banking has not been previously allowed, the newly formed Islamic banking structure needed find or quickly grow local experience. To this point, the College of Banking and

Financial Studies has been hugely supportive, providing vocational Islamic banking courses as well as a fully recognized bachelor's degree in Islamic banking. The third challenge concerns products, they must be specific to Islamic banking and acceptable to Sharia law. This challenge has been easier to address, as many products have been tested in other markets. The main requirement is to ensure that the Sharia board of each bank certifies that proposed products are Sharia-compliant. Solutions to these barriers were well addressed in Oman, partly because being late to the Islamic market, Oman was able to learn from other countries experiences (Magd & McCoy, 2014).

While conventional banking is still predominant in Oman, the market now also includes an increasingly vibrant Islamic banking segment that was immediately accepted and continues to grow rapidly, in the first nine months of 2017, it expanded by 29 percent, the fastest rate globally (The Report: Oman 2019). There are now two dedicated Islamic banks, and of the seven local commercial banks, six have Islamic windows.

With this major regulatory reform, the Central Bank was tasked to make sure that it not only instigated strong governance, but also supported the new banking system, and upheld Sharia principles. It learned from the experiences of other GCC countries that both a comprehensive Islamic banking regulatory framework and a higher Sharia supervisory authority are needed to ensure compliance. The Islamic Banking Regulatory Framework introduced in December 2012 included the immediate establishment of a Higher Sharia Supervisory Authority within the Central Bank. The Central Bank of Oman also wanted to ensure correct financial reporting in this new sector and worked closely within the standards of the Accounting and Auditing Organization for Islamic Financial Institutions. The result was the newly formed Islamic Banking Regulatory Framework, which extends to 591 pages, was thoroughly researched and it was a strong charter for Shariah compliance and to support this new parallel banking system in the country.

The decision to introduce Islamic banking was timely, and necessary, but the parallel consideration, to allow Islamic windows, created a greater cause for deliberation with the government and with the Central Bank. Prohibiting windows, nonetheless, would mean denying conventional banks the opportunity to set up outlets to serve existing customers, it would also deny the general public access to Islamic

banking until fully fledged Islamic banks became established. In taking the decision to also allow Islamic operations through Islamic windows, the Central Bank of Oman fulfilled its critical responsibility to mitigate the risks of non-adherence to Sharia principles (The Report: Oman 2019).

All of the interviews spoke about the regulatory approval for windows and that to not allow them would be “at the detriment of the conventional banks” but with the caveat that although some other GCC regulators had struggled with the concept of Islamic windows in their countries, the Central Bank understood the challenges of managing windows within a conventional banking environment, and the extra cost and management burdens of setting up separate management and systems. It was considered that implementation was necessary but it was clearly noted in the interviews that “Islamic windows aren’t as clean as they should be”, “it is easy to contaminate funds between the two” and “Islamic products are more expensive than conventional”, but all those interviewed stated that from the banks’ point of view widows were essential “as a defense measure”, to “protect the existing customer base” and as “an opportunity to offer another option to the population”. However, after the initial burst of new business, a certain amount of skepticism and acceptance grew. Much the interview evidence stated that windows are, “part of a conventional bank so it’s not pure Islamic”, “I don’t see windows as being true Islamic banking” and “I’m not sure that being good Muslim practice is really there”, “customers care about solutions, I don’t think they care about labelling religion on one product or another” – and these comments came from both Islamic and conventional bankers. More comprehensive statements were,

“Being (fully) Sharia compliant must be quite difficult. I know it's very expensive to have a window sitting beside you because you've got compliance to separate systems, separate entrance, separate buildings even.”

Mihajat (2018) details the additional compliance regulations that the Central Bank of Oman has set in its Islamic Banking Framework for Islamic banks and windows, as well as the capital requirements and it references the duplication experienced in having a conventional bank with an attaching Islamic window.

Another interview comment from an Islamic banking CEO described:

“The first batch of people converting, they took it more that it is halal and haram religious law. But now if you want to grow you want to be more attractive than

the conventional so you can grow a normal growth in your customers, not necessarily because you are Islamic. But also, you have to be competitive in terms of the products you have, the processes and procedures you have, the technology you apply."

The comments from the interviews closely confirms the findings of Belwal and Al Maqbali (2019) that shows customers in Oman had questioned the Shariah efficacy of Islamic banks and windows in Oman, and most of them had not opened accounts with the Islamic institutions. And relative to account opening and customer transfer to Islamic products Magd and McCoy (2014) shows that although there were indications for demand of Islamic banking services in Oman, there can be a significant difference between the actions and words of potential customers, and they stated "the assumption that Oman's majority Muslim population will leave conventional banking products behind purely due to religious obligations is too simplistic", page 1630.

Drawing lessons from the experiences of the other GCC countries, the Central Bank of Oman knew that regulations for windows would need to be comprehensive and clear.

The Oman Islamic Banking Regulatory Framework stipulates that conventional bank branches cannot carry Islamic banking business, unless they have an Islamic windows operation. There is to be no comingling of funds, windows are to have independence with their management, their IT systems as well as a dedicated treasury to manage Sharia compliant instruments. However, windows are constrained in relation to their net worth for prudential limitations, their single borrowing limits are reliant on the overall banks' net worth. Banks were also to install their own Sharia supervisory boards to oversee and monitor all aspects of Islamic banking and the appointment of appropriately qualified scholars to these boards also must be approved and monitored by the Central Bank. However, although the CBO put in strong procedures, it was also at a time when other countries in the region were reassessing their ability to ensure Shariah compliance with Islamic windows, and they were becoming aware of the same observations and sentiments of the bankers and the public generally.

The central banks of Qatar and Kuwait had withdrawn Islamic windows altogether. The fear of Islamic funds becoming "tainted" with those of conventional banking was a concern serious enough to the principles of Islam for these two GCC countries to stop windows altogether. Both these countries have taken radical decisions

to ensure the efficacy of Sharia compliance in banking by separating Islamic and conventional bank activities entirely. In Bahrain, the central bank has tightened its rules by requiring Islamic banks to be subject to external Shariah compliance audits and currently the whole Islamic finance industry is under review. Bahraini laws do not encompass Islamic windows, and accordingly, windows are outside the Central Bank of Bahrain governance, to which conventional banks and fully fledged Islamic banks are subject. The central bank recognizes this as a major deficiency and is currently looking at ways to change the laws (Reuters, 2018).

The banking system of the UAE was hit hard during the global financial crisis of 2008, and the government pushed for stronger governance and regulatory reform generally. However, change through the Central Bank has been slow; it was only in 2018 that a federal law was passed relative to banking. This law does not refer to any Islamic banking framework, but it does stipulate that a Higher Sharia Authority be formed within the Central Bank. The authority will regulate both full Islamic banks and Islamic windows (Decretal Federal Law No. 14 of 2018 Regarding the Central Bank & Organization of Financial Institutions and Activities; Article 17, Higher Shari'ah Authority, p.11).

Saudi Arabia is the only GCC country that relies purely on Sharia law as the mainstay of its legal system. Scholars have concluded that countries ruled fundamentally by Sharia law have no need for separate or more specific banking regulations and in the case of Saudi, there are conventional banks with windows, but the operations are regulated as stand-alone Islamic banks and the conventional "parent" is also managed under the country's Shariah laws (Alam, et al., 2019).

Although in this research the author was not able to interview the Central Bank of Oman management or get their views, and with the growing skepticism both locally and with the majority of the other GCC regulators, comments from the respondents about the efficacy of Shariah compliance with windows was not surprising. From discussions about this subject with all of the interviewees, it was learned, very convincingly, that the Central Bank of Oman's hierarchy is considering a revised strategy with regards to Islamic windows in the country. It was very openly spoken that the CBO is now considering closing windows and, as with Qatar and Kuwait, only allowing stand-alone Islamic banking.

All of the twelve interviewees had received information about the change of tact, some anecdotally and some directly, and they all spoke very openly about the certainty of its implementation. In fact, the respondent from the accounting practice, and who conferred with the central bank on the implementation of Islamic banking in 2012 gave this information, and he implies that the CBO was reluctant about Islamic banking in general, and certainly Islamic windows,

"Some people went directly to His Majesty at that time, His Majesty Sultan Qaboos, and requested his permission. I remember. And he said yes, so then Central Bank had no choice but to issue the Islamic banking finance regulations. But if you if you stand back and look at those Islamic banking regulations, it was in many ways to make windows only banking very difficult and almost to the point of telling conventional banks, we don't want you to have a window, but you can have one anyway."

Other telling comments were, "can see the writing on the wall for Islamic windows", "they want to move away from it, and maybe it could take another year or so", "some direction to consolidate the windows into independent banks", "basically what we are doing is a correction", "sooner or later the windows will be separated", "having multiple windows is not sustainable", and, "Qatar, by the way, by banning Islamic windows, they went the other way, and I think Oman is doing the same".

There were two more specific discussions with interviewees where they actually had inside knowledge and where they had been in discussions with the central bank on the topic, one from the CEO of a conventional bank with windows and the other from the CEO of a fully-fledged Islamic bank,

"There have been statements made all the way to the from the floor to the Governor level and even now with my interaction with the central bank, you know, they have they have talked about the fact that they are looking at a change in regulatory policies, to consider spinning off windows, similar to what Qatar has done."

And,

"The regulators have started talking about it, especially to the (bank) Boards that, you know, there is a (CBO) Board meeting every year after the audit. They call the (bank) Boards of the different banks independently. And I think they started spreading this, you know, to prepare yourself. It might not be maybe this year or next

year, but we have to be ready from 2022 to 2023 going forward, maybe some directions coming. So, in any case, we are working preparing ourselves for that.”

The evidence, although there have been no official advices from the CBO, is very clear that their assessments, with that of other GCC countries, is that they view Islamic windows as unable to properly provide Shariah compliant products and services, and therefore are in contravention of the reasons why, after the Arab Spring of 2012, Sultan Qaboos agreed to allow Islamic banking after a long history of conventional banking offerings only in Oman. If the changes are made in another round of regulatory reform, or not, the evidence from this research has become overwhelming that the central bank not only currently questions the efficacy of Islamic windows but the ability for the windows to compete with conventional banks, whilst being under the conventional bank “umbrella”, and also properly preserve Shariah laws. Like Qatar and Kuwait, it seems reasonable that proper and independent governance, which the CBO provides, would doubt the situation of windows operating amongst conventional banks, and discussions on options for the future included, allowing the current windows to be licensed independently to become stand-alone Islamic banks, to allow some windows to merge together to gain scale, or for some windows to merge with the existing stand-alone Islamic banks. Whichever way the direction of the future regulatory decisions take, there is no discussion about disbanding Islamic banking in Oman, and it is clear that Shariah compliant financing is there to stay, but perhaps without windows.

The details stated in the interviews in relation to the CBO reconsidering the original decision to allow windows in Oman is consistent with the literature on the separation of conventional banking and Islamic banking in Qatar and Kuwait. During previous visits to Oman (pre-COVID), and subsequent phone conversations, with other industry members involved in the banking industry in Oman, the researcher gained observations that, while the Central Bank of Oman would not participate in the interview process, agreed with the context of the interviews relative to possible changes in regulations on windows, and also the difficulties in maintaining Shariah compliance while windows remain under the overall umbrella of conventional banks. Discussions with one Chairman from a conventional bank (that also has an Islamic window), and separately with the Chairman and business heads of the two dedicated Islamic banks

spoke about the "open" talk in the market that the direction of discussions on windows management is that it is most likely to follow the way of Kuwait and Qatar.

8.2 Transformation

From the literature, we have found that transformation is about fundamental change of work processes that lead to important operational and financial improvements, and transforming a company's operations allows stakeholders to anticipate or react to external business and economic encounters. Banks in Oman have been under continuous transformation in the last decade and they have been striving to reach global standards, and to gain parity with more developed banking systems. There has been significant progress since 2007 when Booz Allen consultants conducted a study and labelled Bank Dhofar as "An underperforming 1980's bank" (Babicci & Wongsurawat, 2018), and that also described the wider Omani banking system in general, at the time. The banking sector in Oman is insulated in terms of global expertise and practice, and while the new generation of bank customers expect modern banking services, by nature the country's culture is conservative and approaches change with caution. Both of the non-banking CEO's that were interviewed are expats and have experiences as bank customers in Oman and also in other countries, and they had insightful comments on the conservative nature of Omanis and also the differences in banking development. One is quoted as "Omanis have qualities of friendliness and good sense that are not universal, and to that friendliness and good sense, comes conservatism", and, "the rest of the world banking is moving at a faster pace". The other CEO spoke about the development to a cash-based trading system over the past fifty years, before which bank accounts were not available to the majority of the population, he stated, "they've come into a cash society, and having difficulty transferring out of it or transforming". Although the same interviewee spoke, "the desire of the Omani banks to be absolutely current in terms of transformational technology that gives you agility and speed of response in terms of the actual customer products is there, and the young generation here will tolerate nothing different."

All of the respondents spoke about digital changes in the banks and the consensus was that the physical premises and branches had now become up to date with

regional and global standards, but there was a lot of work still to be done with modernization of technology. For example, payments in Oman are still largely based on cash, and the latest "tap-and-go-systems" are not yet available, and mobile payments are still not widely accepted. One non-banker, spoke that using manual methods for funds transfers was slow and while internet and mobile banking is available, it needs to be more widely accepted. Arab countries have a deep concept of "Majlis" or social meetings, and especially for the older population, a visit to the bank is still seen as an opportunity to catch up on current events and to socialize, for this reason alone there is a reluctance for customers to move from traditional banking to digital banking.

Balancing the desire to modernize with Oman's conservative culture and current economic and social issues, create a dilemma for banking management. A senior bank CEO confirmed this, "We have the vision, but we are not able to put it in place, because there is no ownership", referring to the older and more rigid style of most of the bank's board members, and the want for the Omani bureaucracy to protect job creation efforts and Omanization ratios for the local populace.

The vision is that, "we will have robotics and artificial intelligence that will take many of the decisions and the human interaction would be very limited", and here is shown the predicament that comes to the fore when the government is seeking to create jobs for Oman's youth.

From the College of Banking and Finance came a first-hand account of the challenges of digital transformation and the social balances of Oman's current issues, and attests to the protective role that the central bank takes in Oman, and some level of resistance for modernization in the banking system,

"Maybe some countries are slowing this (modernization) down because there will be many cuts on staff. I was planning to invite a speaker from Australia who had established their first mobile bank, and we were interested in listening to the experience, but we were advised by the Central Bank that this is not a topic to talk about because we, in Oman, are not in the process of encouraging banks to cut staff."

Notwithstanding the avenues of resistance, there has been a need for transformation in banks to address market changes, and to attend to customer desires for more modern products and services. In 2007 Bank Dhofar was well established with strong governance and good business associations, but its Board and top management

were concerned about the future, and signs of the bank lagging its competition were glaring.

On the face of it, the banking sector was growing fast in an environment based on a strong oil economy, by the mid 2000's Oman's annual GDP growth had reached 19 percent, and the banking system was expanding rapidly. However, the market had become increasingly competitive, banks were investing for the growth and the new Bank Sohar was established in the same year, and was already an aggressive player in town.

Bank Dhofar, however, was known in the market to be bureaucratic in decision making, lagging technology wise, and slow to act to the accelerating market. It was not only failing to achieve its potential in a growing market but it was also losing ground to its peers. With the exception of the new Bank Sohar, there were six local banks at that time, and by most measures Bank Dhofar was sitting in fifth place, and by most financial measures dropping further behind. As it continued to lose market share, some of Bank Dhofar's important staff and their experience was being enticed to join other banks, the morale and motivation levels of the remaining staff were falling fast, and this was also having a large effect on business performance.

The banking market grew by 28% in 2007, however, Bank Dhofar increased by a mere 8% and measured by total assets, they held just 9% of the banking sector's market share.

In January 2008, the Board approved a new five-year strategy and an investment spend to upgrade people, products and processes, the management were tasked with transforming the business and change the fortunes of the bank, and its lackluster reputation. They knew that they had a big job ahead of them and they would have to gain a sense of speed and direction to at least catch up and keep pace with its peers.

Clearly at the time, first hand observations of these facts were available to the researcher, as the CEO of Bank Dhofar. Additionally, many discussions in Oman still refer to the radical results of the transformation, which is now more than a decade ago, but still has effects today. One of the important parts of the 2008 strategy was to raise the profile and the presence of Bank Dhofar and still today many parts of Oman are inundated with the bank's signage, including the major airports and main roadsides.

A recent business discussion with members from another bank, also centered on the Bank Dhofar strategy implementation and the lessons that the market learned about urgency and agility to gain competitive advantage.

Some of the interviews commented about the pace of business and transformation in general in the banking sector in Oman, "it's slow and that might be because of the systems and processes, and the bureaucracy", "the need for speed is not there", the delay in doing what they want to do is really in their IT systems", and "the bureaucracy is endemic", and Singh and Fida (2015) conclude that the Omani banking sector is generally technically inefficient, and that is due to both poor input utilization (i.e., managerial inefficiency) and also a failure to operate at the most productive scale size.

Developing countries tend to grow quickly, from a low base, and there is a need for banks to grasp a sense of urgency and to be agile in their strategies in order to face the challenges of fast paced markets. Oman's economy was moving at a great speed and the banking industry was growing even faster, Bank Dhofar needed to not only catch up again but change their management style and manage their internal bureaucracy.

Other comments about the need for urgent action and change were, "it is survival, it's not a luxury, we will be out of the market – definitely", "you've got to have this sense of urgency to be up there with the big banks", and one CEO said referring to the need for agility, "you need to be in a four by four all purpose vehicle. And you need to move fast and change direction quickly."

Alam and Alam (2017) confirms that Bank Dhofar continued to use those traits of urgency and agility, and that it is well known in Oman as one of the fastest developing banks, which has given it a competitive advantage to remain in second place in the market.

The role of the Central Bank of Oman in transformation strategies was also discussed and a non-banker made statements about transformation efforts that link the governments strive for improvement,

"The central bank is very much there on this issue now as well. Encouraging best practices, latest best technologies being in place. So the recent story is getting better and better on this front."

All of the interviewees had close knowledge of banking transformation in recent years and they also had a close relationship and admiration of the 2008 Bank Dhofar transformation. That strategy was market leading at the time and forced other banks to raise their standards to maintain competitiveness to retain their best staff and their market share positions, and to employ higher standards of technology. By disrupting the bank system, economic development was enhanced enabling the local banks to be more competitive with international banks for the growing local business. The Bank Dhofar transformation brought a new level of competition to the market and new ways to serve the needs of the nation, and it played a part in answering the banks' role in pushing country and economic development. Strategies of urgency and lessening bureaucracy employed by the banks have been also adopted by government bodies in Oman and the digital innovations introduced by the banking systems are also being adopted by business and government entities country wide, for example, enhancing wider methods of payments and collections, also positively affecting Oman's development.

Well known academics have written about the need for urgency and agility in transformation efforts. The key points of Kotter's change model are to create a sense of urgency and find quick wins, recruit powerful change leaders and build a vision. Bank Dhofar did exactly that, they recruited a new and internationally experienced CEO, who brought with him a very senior change manager to implement and drive the benefits of their new strategy. Their vision was to become the number two bank in Oman, they knew that to topple Bank Muscat for the number one position would not be realistic. And they went out of their way to build speed of delivery and to find quick wins that would show the rest of the market that they had "woken up". This speed took the market by surprise and they were able to gain significant market share ground early in their five-year strategy.

Denning (2016a) and Kahan (2018) show that agility is the ability for firms to change quickly in pre-empting or responding to market movements and internal and other external forces. The outcomes of agile firms focus on delivering value to customers, and in doing so better the results for other stakeholders, and organizations that employ agile tactics consistently generate better results. The laws of agility are to work in small teams to cut through bureaucracy, being obsessed with delivering

customer value, and ensuring that the whole organization is working together towards common goals, (Denning, 2016b). Again, Bank Dhofar ascribed to all of these guides and built a process where they could move and act quickly, they had a view that at the center of everything they do is a customer, and they were resourceful in appointing two of their Board members to the management's strategy working committee, this cut through the ingrained bureaucracy and built transparency between management and Board in their decision making and implementation processes. This new level of collaboration and transparency allowed decisions to be made and executed quickly.

The results were startling and surprised the competition, and others in the market, it also made them realize that Bank Dhofar was a serious contender to reach their vision and disrupt the playing field. As early as the first half of 2008 showed remarkable transition of results. There was a noticeable jump in staff motivation, which was reflected in improved productivity and customer service levels. Assets had grown by 44 percent, mostly helped by growth in customer loans. Revenues grew 54 percent, and on the back of that, profits grew by 63 percent. The market also took notice of the changes as share prices increased by 32 percent and eventually Bank Dhofar share prices overtook all its peers and became to highest traded and highest priced equity in the Muscat Securities Market. All stakeholder, customers, staff, board members, shareholders and investors were gaining trust and also seeing the benefits of the bank's new direction, using urgency and the laws of agility as drivers. These benefits continued and within two years a highly visible and sustainable turn-a-round was evident.

During 2009 and 2010 Bank Dhofar won a number of important local and regional industry awards. It was named the Number One Bank in Oman in 2009 by Business Today and in an Ernst and Young survey. It was one of Oman Economic Review's "Top 20 Companies" in both 2009 and 2010, and their Best Bank in Oman in 2010. Euromoney also named Bank Dhofar the "Best Bank in Oman" in 2010. It had also climbed from number five position to become the second largest bank in Oman, and an independent study by Omani academic researchers also concluded that between 2009 and 2013, Bank Dhofar was Oman's most efficiently-run bank (Singh & Fida, 2015).

The Bank Dhofar case study is a prime example of a major business transformation which occurred in the banking industry in Oman. Literature and also the

interview process employed in this research show that urgency and agility are important factors, and in the case of Bank Dhofar and situations where there is significant catch-up, and in fast moving markets, are necessities in delivering improved value for customers and stakeholders. These factors are more so important in developing economies where growth happens at a rapid pace and quick change is part of market evolution and ensuring that competitive forces are matched and addressed while they are focused on their internal business processes. When an organisation adopts urgent and agile business styles, it is able to address internal changes that have dramatic effects and can significantly disrupt external markets.

8.3 Mergers

The literature is expressive in that the reasons companies consider merger activity is for efficiency gains, structural benefits, and enhanced market power, and in some cases managerial interests, and specifically relative to banking sector mergers, motives also include technology enhancements, better risk management, and portfolio quality enrichment, promoting stability in the wider financial sector, regulatory influence, and regulation or de-regulation changes.

In any country the central bank, or the responsible regulator, is charged with approval of any proposed banking merger and while the Central Bank of Oman is regarded as conservative, they have also shown that they are supportive of mergers, when they are proposed for the benefit of the industry, the community, and other stakeholders. While the CBO declined to participate in the research interviews, almost all of the respondents confirmed the conservative but supportive approach. One comment from a banker from one of the recently merged banks was, “the central bank has been supportive of mergers and the Governor has been personally supportive”, another and more descriptive quote from the interviews summarized the Central Bank and the government approach, and these sentiments confirm the results of Olsen and Zoubi (2011), including Oman, that states “Since the average bank in the MENA region is smaller than the optimal size, most bank consolidations and mergers should not be opposed by regulators.”, page 108.

The below quote is an academic observation from a senior administrator of the College of Banking and Finance,

"First of all, the Central Bank and the government is encouraging. They are encouraging mergers because first of all, from the macro level, what is the motivator for the government? The government wants to see a good number of large banks for two reasons. One, you know, it's like a monopoly now because Bank Muscat is the biggest by far. But the government doesn't want to see one bank having (such a large market share) because that also brings more risks. The other motive is that for the small banks, their opportunity or their potential for having more business and with international bodies, giving loans outside of Oman or even making more local loans, it is more difficult for the small ones. A merger will give some of them a chance to have better business, bigger business, and that is another strength for the government."

An outcome of the Central Bank of Oman regulations on capital adequacy and single borrower limits is that banks are restricted in the amount of free capital that they have to lend and large local projects cannot always be catered to in meaningful loan quantities from local bank resources. A way to overcome the challenges of being able to participate more in the current projects is for banks to merge and to gain larger and stronger balance sheets, most of the bankers raised this aspect in the interviews and one quote from a bank CEO of one of the smaller banks was, "you need to understand that banking is a game of scale …. If you don't have scale, you are going to face a lot of challenges, and that is exactly what we face."

Large projects (non-oil related) are required to produce a more diversified GDP that is not so reliant on Oman's oil industry, and fluctuating global prices. Foreign developers are also restricted in borrowing through Omani banks, in the past, the Omani government was able to support projects with contributions to funding, but now due to reduced oil revenues those options have also been restricted.

In order to compete for business, bank management is consistently looking for ways to increase their capital holdings, mergers are a tool to right-size capital, as well as other options for raising capital outside Oman that have been used in recent years, these include sourcing foreign debt and capital markets and interbank borrowings – but these sources come at a price and require subsequent repayment, and they are also assessed on bank's asset size.

With relation to the interview discussions specific to reasons for bank mergers in Oman, the responses were consistent that any significant efficiency gains would not be gathered from mergers of the local banks in Oman. The prospect of synergies from branch consolidations are limited as the Central Bank and also the government deter actions that would reduce employment numbers. With staff costs high at about 65% of bank expenses, and Omanisation requirements at 90%, synergies from human resource rationalisation will not be significant and unable to provide meaningful cost savings.

The aspect of Omanisation was discussed in detail and all of the interviewees had strong points of view, with positive sentiments – agreement was that Omanisation is an important feature to ensure employment for the local community. In the banking industry Omanisation is higher than any other sector in Oman, and this localization policy is also higher than in any of the other GCC countries, and it does create challenges for Omani bank management. Attracting experienced talent is competitive, providing for career advancement and also cost management are challenges that were outlined in the interviews. Some comments were that Omanisation is fully supported, but as an employment strategy it could be seen as a "civic duty" required to be delivered by the banks. Some of the direct quotes from the interviewees relative to Omanization were that it could be seen as "overly successful", "solving a temporary problem" and "there is a trade-off with the desire to create employment and enhancing profits". With direct regard to bank mergers Omanisation was seen as an obstruction to expected synergies, and one non-banker put it, "the benefits of economies of scale that mergers would normally bring, are compromised by the Omanisation imperative. Another said "when you've got rules like Omanisation, and you've got a small market that is overbanked, the normal motives for mergers like getting synergies and reducing your costs is challenged." These references are also discussed in Glaister et al. (2019) relative to conflicting logics of using talent management in achieving Omanisation goals and the synergistic drivers of merger benefits.

Due to the strong Omanisation requirements, the need to create employment opportunities, higher staffing costs and little chance to rationalize branches and workforce, it is considered that efficiency gains are not a major motivator for mergers in Oman.

However, it was also clear that providing opportunities for local youth is important and the discussions raised interesting suggestions such as finding ways to create roles for young Omanis with training and work secondments outside Oman where they can be trained and employed to later return, also suggestions to assist with promoting SME development and likewise funding to support young entrepreneurs.

For the motivation of structural benefits and discussions about the merger with HSBC and Oman International Bank in 2012, one senior international banker responded “the merger enabled us to get our capital right”. A number of the respondents agreed with the comment that banking in Oman is a “game of scale” – and this is important when considering the country’s current economic condition. Oman’s small population and limited economy size also restrict market growth, and for the survival of banks - “size and scale are necessary”. The importance of increasing bank capital and size was a feature of almost all the interviews, especially with the bankers, and showed in analysis as a major part of bank management concerns to enable competitiveness and for future growth.

Results in the success of the HSBC and Oman International Bank merger can be confirmed by the joint bank’s financials. After the merger in 2012 combined assets were USD 6,269 m., capital was USD 748.8 m. and profits were USD 18.6 m. Seven years later in 2019 assets were USD 6,623 m, capital reduced to 344.8 m but profits greatly increased to 90.1 m., (source: HSBC Oman Bank annual reports). Profits rose by 490% on asset growth of only 0.06%, showing a much-enhanced use of capital. While using each of the individual bank’s asset size at 2012, the merger strategy has not resulted in asset growth during the years after integration, and this is a factor of operating in a small and developing market. However, how HSBC Oman Bank increased its profitability on a smaller capital base was to change its policies on revenue streams and by using its international knowledge and reach to offer fee-based services, such as wealth management and insurance products, and especially financial advisory. In an empirical study that investigated efficiencies related to scale in the banking sector in Oman, Singh and Fida (2015) find that HSBC in Oman was showing high scale inefficiency up to 2011, but it becomes technically efficient in 2012 and 2013, and they further conclude that one reason for this is likely to be the merger of HSBC in Oman with Oman International Bank in 2012.

Many of the respondents spoke about the need to shift the revenue mix in the banking sector to a lesser reliance on traditional interest charging products, which is a high use of capital resources. There was significant discussion on the need for the Omani banking sector's desire to build investment banking offerings and advisory services. Currently these services are predominantly catered to by foreign banks and financial companies that are not based in Oman, and attaching revenues are lost from the Omani economy.

The more recent merger of Oman Arab Bank and Alizz Islamic Bank was also discussed and every one of the interview respondents had comments about the reasons for the union, it is a very current and relevant merger, and integration of the two banks only began in late last year. It was clear that the amalgamation was to benefit both entities differently, it was an opportunity for the newly combined bank to change the shareholding to classify Oman Arab Bank to become a majority owned Omani bank (previously Oman Arab Bank was classed as a branch of a foreign bank and a subsidiary of Arab Bank from Jordan). The merger allowed Oman Arab Bank to list on the Omani stock exchange though a local share structure and to be regulated as a local bank, other than a branch of a foreign entity. The benefits that Alizz Bank were looking for are that they will be part of a larger group with access to international markets – again the factor of scale was raised by all the bankers and also most of the non-bankers when discussing this merger, and that both banks will generally benefit from a larger combined balance sheet, but not for reasons of efficiencies or market power. Managerial interests was also not considered as a motive as the two banks, although merged together, will continue to operate in a form of a conventional bank with a subsidiary Islamic bank, and not classify Alizz Islamic Bank as a Islamic window. This merger is very much in the early stages of integration and evidence of any proposed financial benefits is not available at this time.

Both the mergers for HSBC and Oman International Bank and Oman Arab Bank and Alizz Islamic Bank resulted in structural motivations. In the case of HSBC Oman and Oman Arab Bank, their mergers created opportunities that HSBC is now classified as a fully local bank and they it been able to join the listing on the Muscat Securities Market, which has opened opportunities to raise funding through shareholding structures, capital markets and other avenues, to get their capital structures

in order and to participate in lending opportunities and project financing. Of course, one of the most basic roles of banks is to assess risk and to provide financing, the interview with the representative from the accounting partnership summed it up with, “you’ve got to lend to grow.”

It is apparent from both of the completed mergers above, that traditional motives for the banks to merge were replaced by the need of banks in Oman to improve and right-size their balance sheet positions, and in the case of HSBC and Oman Arab Bank to be reclassified as local banks and to participate on the Muscat Securities Market, and to gain other avenues for raising capital.

All respondents discussed that Bank Muscat is certainly the largest in the market, and by a wide margin, and that there would be no practical merger of two, or even more, of the other banks that would bring a combination to the level of market share and size to overtake Bank Muscat. Some felt that the market is currently over-banked, however one of the non-bankers who has been in Oman for more than 30 years had an interesting observation that “the current banking sector has seen quite a number of mergers in past years and historically the ratio of banks for the number of banked population was much higher than today.”

Respondents also felt that the completion of the numerous merger discussions over the past decade would not answer “balancing market share”. Discussions with a majority of the respondents concluded that the current market is “lopsided”, but within the next tier of banks, there is already the creation of proper competition, and Oman is seen as a free banking market with relation to pricing and products (within the scope of the CBO guidelines).

While there is evidence that the regulator, industry, and the economy in general, would benefit by levelling the competitive playing field, and reducing the “lopsided” banking landscape, the reality is that only a merger of the three next largest banks would be enough to give rise to challenge Bank Muscat with regard to asset size, and even if that was conducive to the relative management and Boards, it is evident through verification with annual reports and other financials that any such mergers could create a market with just two large players, and that would likely do harm to the remaining smaller banks.

The conclusion for this motivation is that market power is not a viable incentive for mergers in Oman. The following figure shows the market share by assets of banks in Oman, at December 2019.

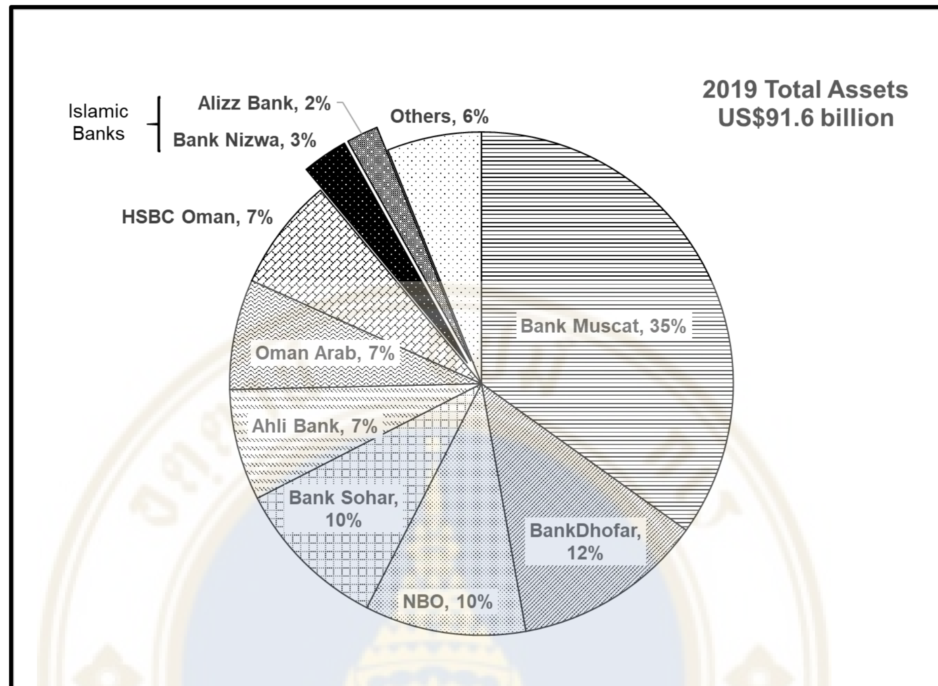


Figure 8.2 Banking market share by assets, 2019. Source: CBO and bank annual reports

Managerial self-interests were also questioned to see if these would be valid motivation for bank mergers in Oman, and this subject brought about some lighter discussions about the characteristics of some bank Boards. Many of the banks have longstanding Board members that are well known in the Omani market, some of the recent discussions with Bank Dhofar, in particular, and its negotiations with National Bank of Oman and also Bank Sohar could have been justified as being the basis for managers and Board members to grow their own interests by creating larger entities to manage and govern (Bank Dhofar has a strong Chairman and its CEO is a close relative, it is unlikely that either of these would be dislodged in the case of any merger).

After the success of their new strategy, in 2010 Bank Dhofar went in search of a suitable merger to strengthen their number two position, and to build balance sheet size to take on more business, and to compete closer with Bank Muscat. The then-CEO (who is the author of this research) and the Chairman went on the hunt for significant

mergers. They first approached Oman International Bank and initial discussions were positively received. At Bank Dhofar's end internal analysis had been completed, Bank Dhofar was strong in the corporate banking sector and Oman International Bank had a larger retail base. The thinking was that the two businesses were complementary and a merger would be seen as a first step to set a firm foundation for rapid growth. The talks with Oman International Bank were soon stopped after the Chairmen of both the banks could not find agreement of the general terms. Oman International Bank, however, was clearly agreeable to a union (just not with Bank Dhofar), and they did merge with the Hong Kong and Shanghai Banking Corporation's (HSBC) Oman office in 2012.

In late 2010 there was a high-level meeting at the Grand Hyatt hotel in Muscat with the same CEO and the Chairman of Bank Dhofar along with an external banking consultant and The Commercial Bank of Qatar's CEO and owner's representative from the Al Fardan group in Qatar. CBQ owned 35% of National Bank of Oman and it was founded by the Al Fardan family, who were also significant shareholders. Everybody left that meeting in agreement that a merger in Oman was the right strategy for Bank Dhofar and NBO, and that both parties would hold further discussions with their respective boards. The Bank Dhofar team had completed a strategic study on the merger benefits and already had agreement from their Board to proceed. After the meeting in Muscat, they were quietly confident that this time a merger would go ahead. However, within 48 hours the news came back through NBO's top management that the possibility of a merger would not progress because the Commercial Bank of Qatar board did not support the deal.

The next series of merger negotiations began in mid-2013 between Bank Dhofar and Bank Sohar. The market sentiment was that this merger would happen and propel the joint bank solidly into number two position with about 22% of the market. Talks continued in earnest and both banks entered into a non-binding Memorandum of Understanding in 2015, and legal and financial consultants were appointed on both sides for the due diligence process. In June 2016 when both boards agreed on a Share Swap Ratio, subject to regulatory approvals, it appeared that after a long gap this merger would go ahead. However, in October 2016, after three years of negotiations, Bank Dhofar advised its shareholders that due to the banks being unable to agree on certain key issues, negotiations were discontinued.

Again in June 2018 The Commercial Bank of Qatar announced on their stock exchange (in Qatar) that it would commence discussions for a possible merger between Bank Dhofar and NBO. Bank Dhofar responded a month later with an announcement that their Board of directors had resolved to also enter the discussions. However, by December of the same year, the Commercial Bank of Qatar made a further stock market announcement that they do not support the merger, similar to their decision in 2010.

Stock market reports in both Oman and Qatar show the reasons that both of these merger attempts did not proceed were that the management and the Boards of the respective banks could not come to agreement on future management terms.

Through discussion with the interview participants and from stock market releases, it was discovered that managerial self-interests became a de-motivator for these mergers, and the reason for this is that the characteristics of many Board members would not want to risk losing a Board position in any amalgamation. The stock market reports were backed up by the interviewees and one telling quote from the interviews was, "Management did not want the merger to happen for a lot reasons that were very selfish."

And with regards to the proposed merger with Bank Sohar, comments from the legal consultant to the merger were,

"at one of the very, very first meetings I attended on the Bank Dhofar and Bank Sohar merger, I asked the question if you guys thought, you know, who's going to be on the Board of the merged bank? The room went silent, then a year and a half later, hearing that the reason why the whole thing did not proceed, they could never agree who was going to be on the board."

For bank specific reasons for mergers, participants advised that the make-up of banks in Oman are all similar, they all have retail banking businesses, corporate banking and treasury services, they are all at the same level of technological advancement with their computerization, digital and mobile banking offerings, and they all operate in the same risk environment. Discussions were had with all the bankers and the non-bankers on these topics and the outcome of the discussions concluded that there would be no advantage to balancing individual portfolios (retail banking or corporate banking portfolios) with mergers, other than to increase portfolio size. Regulatory

guidelines have been consistent in past years and while the regulator is supportive of some mergers, there has been no regulatory changes or any de-regulation in the past decade that would actively promote merger activities.

Results from the earlier research for this study, and the series of in-depth interviews reveal that the Omani banking sector could clearly benefit from more consolidation activities. Such consolidation would allow more local banks to participate in the financing of larger investment projects. There are examples of successful mergers in the recent past, and the appetite for mergers is not lacking. Of the primary motives, partial efficiencies of increased profits can be gained with capable bank management decisions and the use of increased capital. The Omani banks' desire to participate in local infrastructure projects raises the need for increased capital and this leads to the need to restructure balance sheets. This last motive has emerged as the strongest stimulus for the recent appetite for mergers.

Socio-economic reasons relating to the necessity to create jobs and maintain domestic employment in Oman dictate that there is little scope for cost reduction from mergers. As long as Omanization requirements for the banking industry remains at ninety percent, human resources rationalization post-merging will remain infeasible, because laying off Omani workers is prohibitively expensive and deterred by the government and by the banking regulator. Oman's competent but conservative central bank is cautiously supportive of mergers to create a more balanced competition and to ensure financial sector stability. However, directors' personal interests in maintaining clout on their bank's board often quash promising merger proposals.

It is clear that the Omani economy needs to diversify in relation to industry sectors in order to ward off its historically high reliance on oil production and the government is providing opportunities for large scale projects. The local banking sector realizes that to participate in meaningful ways in those projects they need to gain additional skills such as advisory and consultancy, and to also gain scale and to recapitalize their balance sheets. By doing so they will be able to participate and to assist with the economic growth and development of the country. The avenue for gaining scale and to address the regulated single borrower limits and capital adequacy requirements for individual banks in Oman is through mergers.

The interviews also revealed knowledge and opinions from the industry experts that larger sized banks can assist with the economic growth of Oman. Some direct quotes from the interviews are shown below,

"In order for us to grow the economy and be able to actually stay in line with the government's desire to, you know, fund large projects and, you know, the banks would have to play that role and that the only way they can do that is to have a larger balance sheet." - stated one of the Islamic banking windows CEO's.

"It is going to be more of a situation which will force a number of banks to really seriously think about the challenges that are coming as a result of this law, the economy, the COVID and the companies that are expected to probably suffer as a result. And how to rescue the market and the economy will require solid banks to work together." - a senior conventional banker.

The example of HSBC merging with Oman International Bank and the resulting change in revenue streams, and the change to higher fee based, income is evidence that in this merger there has been the ability to import financial advisory and consultancy skills to Oman, and these new skills have been used to participate in funding structuring and in that way to contribute in the country's development.

CHAPTER IX
CONCLUSIONS

The objectives of this research were to study the banking sector, and specifically, the important bank management considerations of regulatory reform, transformation and industry related mergers in the Sultanate of Oman, and to answer queries that arose from recent related banking phenomena. Oman was chosen because it is a relatively newly formed modern economy that has experienced rapid development, and it has gained modern banking systems, it also provides varied opportunities for further academic research.

A wide-ranging review of banking and related literature in the global, regional and local arenas set foundations for a framework that concludes regulatory reform, transformation and mergers, within banking systems, all have inter-relations that lead to enhanced country development, and thus economic improvements and social benefit. However, the interview process results and the following analysis could not form firm evidence to confirm the links from the banking sector to country development in the case of Oman, and this area would be an opportunity for further quantitative research once suitable data sets are available in the banking industry for the Omani market, and also a further opportunity for specific qualitative research with an explicit mission to seek out if there are definite linkages.

The present literature assisted in the formulation of “how” and “why” research questions, that by studying phenomena events in Oman, enabled conclusions that complement existing theory, and will be useful to regulators, bankers and educators in Oman, and other banking environments.

The characteristics of the short time-span of business environment in Oman lend themselves to qualitative research methods, and in order to find answers to the research questions, included analysis of information sources from central bank, stock market, bank records and media reports, and these were collaborated by a series of

detailed interviews, as well as the observations of the researcher who has over two decades of Middle East banking experience.

Results of the interview investigations for the three research questions add credence and veracity to the relevant literature and conclude that,

(i) Regulatory Reform - allowing Shariah compliant banking to cohabitate with conventional banking systems, by the use of Islamic windows, is challenging for banking regulators. Separation of Islamic banking has already been instigated in some Muslim majority countries and indications, gained from strong convention in the interviews, are that the Central Bank of Oman is currently assessing present practices in Oman with a view to further regulation review and a similar separation.

(ii) Transformation - urgency and agility are well understood principles in bank management in Oman, and their use has improved stakeholder value through the delivery of transformation strategies. These principles are addressing past practices, and the now changing pace of bureaucracy, and by allowing early mover advantage and speed to market initiatives, the fortunes of at least one bank in Oman have improved in relation to peer-group competition.

(iii) Mergers - traditional motives for mergers in banks in Oman have been set aside by regulatory requirements to reduce systemic risk and government intervention to address social needs, in place of the desire to obtain growth by gaining scale and also by diversifying income streams. There is evidence that managerial self-interest is a reason for mergers to be considered in Oman, however, with the mergers will also come rationalization of prized board and senior executive positions, and the prospect of some individuals losing positions and stature in Oman's banking community has become a reason for merger discussions to be discontinued.

Outputs of the research have also provided materials for contributions to literature by the way of academic case studies, with a focus on each of the sections of regulatory reform, transformation and mergers. These cases are based on live phenomena and market experiences and they give learning opportunities for bankers, regulators, educators and the business community. The case studies address gaps in current knowledge and literature in Oman and the wider banking society.

Limitations of this research were that Oman is a small market and does not lend itself to quantitative research methods, this is also evidenced by the majority of

existing literature that uses qualitative methods and the lack of literature that has been able to answer meaningful investigation using quantitative studies. Using wider data sets which include regional information could be useful in tracking trends in other countries that could be used in forecasting future events for Oman, and this would be an opportunity for future research specifically relative to regulatory reform, transformation and banking mergers. Another limitation of this study is that while a suitable number of interviewees was utilized and the candidates had in-depth knowledge and experiences regarding the topics, a wider audience could have provided additional opinions and views on the topics and future research could address that by using focused questionnaires directed to a wider audience of senior management and completed by a series of surveys, these could be used in tandem with structured or semi-structured interview results. Being able to include interview members from the Central Bank of Oman would also provide conclusions that are balanced with the understanding of the current and future banking landscape from the experiences of bankers, customers, users and also the regulators.

Although the scope of the research is limited to the banking sector in Oman, the context and the conclusions are expected to be useful in varied industries and geographies, and in other emerging and Arabic countries.

Implications for bank management for the Islamic banking situation in Oman is that it has become clear there will be changes coming and bank management is now preparing for a separation from conventional banking. While the central bank completed research on the regulatory landscape in the region and they could see what had happened in Kuwait and Qatar where Islamic windows have been closed, banks in Oman would have been well advised to also gain understandings of the regional trends, and while their reasons for establishing Islamic banking in Oman were reactive to populist pressures and defensive in the changing market, future strategies with a longer term outlook would hold them in good stead. The model established by the Oman Arab Bank and Alizz Islamic Bank merger would have been more efficient to establish and to launch in the wider banking market from the beginning of Islamic banking in Oman rather that at this stage. Other strategic changes in the banking industry would be well considered by studies of other trends and outcomes in more developed geographies, including other GCC countries.

Future transformation will clearly include further digital opportunities and banks in Oman, while they have made key advancements in recent years, are still behind regional and global competition. Evidence from this study and from the interviews show that Oman has a vast young majority and that the youth are looking for digital development. A traditional "bricks and mortar" banking presence with high levels of physical branches and face to face customer interactions are not preferred by the young and well-educated population of Oman, and less reliance on this form of banking will provide better operational and financial efficiencies for the banking system. The implications of this are that bank management needs to continue with speed in driving further into a cash-less, transactions-based ecosystem for Oman, and individual banks that rush to become first movers in this area will hold a strong advantage over the local competition. However, it is well recognized that there is a balance of digitization measures and job creation for Omani youth.

While there has been a recent upturn in global oil prices, the Omani government is still committed to diversifying away from its heavy reliance on oil revenues, and the conservative regulatory framework with regard to single borrower limits and capital requirements are restricting banks in their level of participation in the government's strong push to create large scale infrastructure projects. The central bank has in the past been supportive to local banks in their management of regulations and at times provided temporary relief (their relaxation of requirements at the time of establishing Islamic banking is a most recent example). The CBO could address this on ad hoc assessments to allow local banks to participate more. The other option of industry mergers to obtain scale is a lasting measure, and the many examples of non-completed efforts need to be addressed. The implications here are that bank boards should realize the long-term advantages of mergers versus the short-term desire to maintain current boards and management structures intact.

The conclusions here point to opportunities for bank management to advance business opportunities by further studying regional and global developments, to be swift in answering digital requirements for their customers and by also changing management attitudes to existing bank structures and by adopting mergers.

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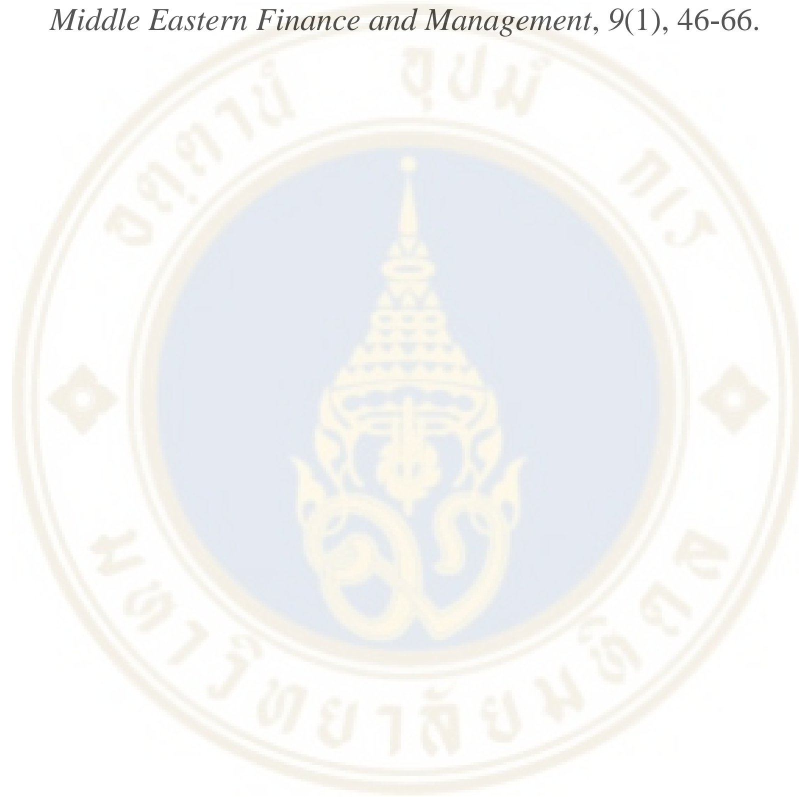

APPENDICES

Case Studies

Case studies have been written describing relative banking phenomena and outcomes in the banking sector in Oman for each of the constructs of Regulatory Reform, Transformation and Mergers. Two of the cases have been published in academic journals and the third has been accepted for publication in principle. Below are details of all the cases, the two that are already published are available through the DOI's (Digital Object Identifier) shown, and a copy of the third (yet to be published) is attached.

Appendix A: Case Study 1: Regulatory Reform

Babicci, K., & Wongsurawat, W. (2020). Islamic Banking in Oman: Laying the Foundations. *Middle East Policy*, *27*(1), 115-124. https://doi.org/10.1111/mepo.12478

Appendix B: Case Study 2: Transformation

Babicci, K., & Wongsurawat, W. (2018). Case study: from an "underperforming 80's bank" to one of Oman's best–the transformation of BankDhofar. *Strategy & Leadership*, *46*(5), 44-49. https://doi.org/10.1108/SL-06-2018-0060

Appendix C: Case Study 3: Mergers

The Myriad Forces Shaping the Future of the Banking Industry in Oman. Note: this case study has been accepted in principal for publication by the Journal of Arabian Studies, and undergoing the review process.

APPENDIX A: Case Study 1: Regulatory Reform

Islamic Banking In Oman: Laying The Foundations

When the Arab Spring erupted in 2011, rulers in the Middle East and North Africa took numerous measures to quell the popular discontent that was boiling over. Shrewd leaders understood that institutions needed to act as valves to release pent up political pressure. In Oman, a country with strong Arab traditions and moderate attitudes, Sultan Qaboos introduced a string of measures to address public grievances, including a minimum-wage hike and stepped-up efforts to create jobs (Al Shaibany, 2013). The sultan also permitted Islamic banking in the country for the first time.

In line with Oman's moderate attitudes, Islamic banking had not previously been allowed in the country. In the view of the recently deceased Qaboos, the father of modern Oman, Sharia-style banking could foster exclusion and extremism. Not allowing Islamic banking at all, nonetheless, is unusual for a country with a majority Muslim population. The Quran explicitly forbids basic practices of conventional banking, such as charging interest.

In 1994 and again in 2005, the Omani government had suppressed rebellious plots, arresting 430 members of fundamentalist parties and seizing caches of illegal weapons. A major motivation for these parties was to promote Islamist ideals and, among other things, demand Islamic banking (Worrall, 2012). At the time, Oman was the only country in the Gulf Cooperation Council (GCC), and the only country in the world with a Muslim majority, that did not allow Islamic banking.

However, the disruptions of 1994 and 2005 were relatively small and thus rapidly quashed. It was not until the much larger and more widespread Arab Spring uprisings in 2011 that the sultan was forced to take notice. As an immediate response to the protests, he asked for a list of concerns to be presented to the government. The demands of the protesters centered on concerns that particularly troubled the large youth population of Oman: educational development and job creation. The sultan also addressed the social/religious discontent caused by the ban on Islamic banking. By the end of 2012, there was a royal decree allowing Islamic banking, and the Central Bank consequently introduced a new regulatory framework.

Oil Reliance and Unemployment

Located at the mouth of the Persian Gulf and sharing borders with the United Arab Emirates (UAE), Saudi Arabia and Yemen, Oman is known for solid relationships with the West and for "neutral" foreign policies. With a rapidly growing population of 4.6 million, the country is made up of about 43 percent expats employed at all levels of private and public enterprise (National Center for Statistics and Information, Population Clock). Qaboos came to power in 1970 amid a longstanding civil war. Under his leadership, social and political order was re-established, and Oman was transformed from a simple fishing and trading backwater into a prosperous modern nation. Economic development has been strong - Oman's GDP has more than doubled in the last decade.

After finding oil in the 1960s and, more recently, natural gas, Oman has progressed into a significant energy supplier, especially to Asia. Revenues have been used to build modern infrastructure and improve living standards. Government spending has ensured quality in health and social services for both citizens and expats. However, rapid population growth and the recent fluctuating oil prices have caused growing concerns. About half of Omanis are under the age of 24, and providing access to education and careers are the primary challenges for the government (National Center for Statistics and information). Youth unemployment in 2016 was worryingly high and has been steadily growing for at least a decade. The government is relied on heavily for social assistance, especially with strategies to boost job creation. Fulfilling expectations within fiscal constraints is a constant struggle, when state revenues and GDP are so dependent on elevated oil prices.

"Omanization" in employment is taken very seriously. For example, the Central Bank of Oman requires that 90 percent of bank staff be Omanis; infractions are met with stiff financial penalties. In Qatar and the UAE, targets are much lower, at 50 percent and 25 percent respectively, and neither as stringently regulated nor penalized. Qatar and the UAE also have financial centers that are not regulated by their central banks and allow commercial banks to open subsidiaries and employ staff as they wish.

Oman does not have a financial center, preferring close and robust regulation from the Central Bank. This ensures that banks cannot escape Omanization requirements through the backdoor. The stringent localization policy, nevertheless, causes strains on recruitment, education and efficiency. The balance between well-

educated, experienced and qualified local staff and the needs of the business is always fraught. The private sector is regularly called upon by the government to provide jobs for new Omani graduates.

Policies still provide for substantial public-sector employment of those leaving school. Currently 45 percent of employed Omanis work for the government (National Center for Statistics and Information, July 2019). Such a high level of public employment is not sustainable and creates a significant burden on the state. It is feared that future capacity cannot keep pace with the numbers of youth entering the workforce. Many young Omanis considered the government's efforts inadequate, and tensions in this traditionally very moderate and calm nation have been felt (Worrall, 2012).

There are some positives, however. Oil-price increases since 2017 are improving government resources. Oman also has strong initiatives in place to expand non-oil sectors through new enterprises and policies. Strategies ensure that as part of their 2030 vision, the government and the private sector work together to address development and economic diversification, including job creation. There are also new opportunities to attract foreign investment and large infrastructure initiatives such as the Duqm port-refinery and super-city project, which will create at least 32,000 new jobs, including 20,000 for young Omanis (Times of Oman, 21/3/2017). Additionally, the government has pledged to create 40,000 to 50,000 new jobs per year until 2022, 60 percent of them in the public sector (Al Shaibany, 2017).

Islamic Banking, Theory and Reality

The following are the "five pillars" that differentiate Islamic from conventional banking:

(i) The ban on charging or paying for any financial transaction. Money has no intrinsic value and consequently cannot produce returns on its own. Rather, it is a vehicle to facilitate transactions.

(ii) The ban on uncertainty and speculation. This generally rules out derivatives, options and future contracts. However, risk taking is allowed when the terms and conditions are clear and known to all parties.

(iii) The ban on financing enterprises deemed unlawful by Sharia, such as weapons, pork and gambling.

(iv) The profit- and loss-sharing principle: parties to a financial transaction must share in the risks and rewards attached to it.

(v) The asset-backing principle: every financial transaction must refer to a tangible, identifiable underlying asset.

The six GCC countries control 42 percent of the world's Islamic-banking assets, the next-largest markets are the Middle East and North Africa (MENA) region, with 29 percent, and Asia, with 24 percent. The GCC, as a major player worldwide, is looked upon for innovations as well as regulation and control. The growth of Islamic assets in the GCC has also been the fastest globally, at 8.8 percent (Islamic Financial Services Industry Stability Report, 2018*)*.

When Islamic banking was first introduced in the 1960s, there were only dedicated Islamic banks. Conventional banks chose not to participate, as they did not realize the size of the market. They felt that Islamic finance was founded only upon religious enthusiasm and destined to fail, as it was not a commercial substitute for conventional banking.

However, Islamic banking won a large part of the conventional market, causing bankers to reevaluate their thinking. Conventional banks needed to convince Islamic-banking clients to trust them and their ability to properly implement Sharia principles. As a result, conventional banks established "Islamic windows" as independent departments and appointed religious bodies (Sharia Supervisory Boards) to supervise their operations. While an Islamic bank is based on Islamic principles and does not offer any conventional banking products, Islamic windows are services provided by conventional banks based on Islamic principles. It is essential for Islamic windows to ensure that there is no cross-contamination of funds, and no comingling of Islamic and conventional products. All aspects of Islamic windows and conventional banks are to be kept separate.

At a time when Oman had recently opened to Islamic banking, some Muslim countries were considering controversial reforms to their own procedures. In the GCC and other Muslim countries, there are examples where compliance with Islamic banking has been questioned and regulators have acted.

Bangladesh

The third-largest Muslim country in the world, Bangladesh has an Islamic-banking sector employing over 30,000 people in eight fully fledged Islamic banks and 25 Islamic-banking windows. However, religious academics and policy makers argue that Islamic banks are generally too unregulated. There is still no separate, relevant law and no Islamic banking framework that can be used as a guide for governance. In response to growing concerns that Sharia principles were not being followed, the Bangladesh Central Bank has stopped issuing new Islamic banking licenses and is planning major regulatory reviews and changes (Islam, 2018).

Qatar and Kuwait

In the GCC countries as well, the ability of banks to adhere to Sharia requirements has been examined. The Central Banks of Qatar and Kuwait have withdrawn Islamic windows altogether for fear of Islamic funds becoming "tainted" with those of conventional banking. A major concern is "leakage," a situation that obtains when Islamic banks use interbank placements with conventional banks. To help combat these concerns and ensure adherence to Sharia principles, there is a need to develop strong Islamic regulatory frameworks.

The ruling law on Islamic-banking governance in Qatar is a Royal Decree of 1993 covering both conventional and Islamic banking. It is not fit for its dual purpose and is now outdated. There is no separate Islamic regulatory framework (Perumal, 2018). In 2011, the Qatar Central Bank ordered all Islamic windows to be closed. Similarly, Kuwait does not have an Islamic-banking framework and has also decided to close Islamic-banking windows. The Central Bank of Kuwait does have instructions for Islamic banks, but they are almost identical to the instructions for conventional banks and are not considered a framework for Islamic banking.

A major regulator of Islamic banking is the Sharia Supervisory Board of each bank. In Kuwait, the Sharia board is to preserve the reputation of Islamic banks, uphold Sharia principles and protect the confidence of their customers. While the boards of conventional banks are highly regulated, Islamic banks are allowed to select their own Sharia Supervisory Boards and have these appointments approved by shareholders. The only requirement the central bank stipulates is that "members should be Islamic

Sharia scholars of recognized efficiency and experience" (Central Bank of Kuwait, Instructions for Islamic Banks, 2003).

In early 2019, the Central Bank of Kuwait recognized the need for regulatory change. It has announced the proposed drafting of new banking laws to appoint an independent Higher Sharia Supervisory Board that will be part of the Central Bank. This board will be responsible for standard approaches to governance and control of Islamic banking (Muzoriwa, 2019).

Qatar and Kuwait have both taken radical decisions to ensure the efficacy of Sharia-compliant banking by separating Islamic and conventional bank activities entirely.

Bahrain

There is an Islamic-banking framework in place in Bahrain, and the Central Bank has tightened its rules by requiring Islamic banks to be subject to external audits. Currently, however, the whole Islamic-finance industry is under review. Bahraini laws do not encompass Islamic windows. Accordingly, windows are outside the Central Bank governance to which conventional banks and fully fledged Islamic banks are subject. The Central Bank recognizes this as a major deficiency and is currently looking at ways to change the laws. It is also concerned with the potential contamination of Islamic funds, which can lead to non-adherence with Sharia law. Currently, however, there is no mechanism for governance of Islamic windows in Bahrain (Vizcaino, 2018). There is a Higher Sharia Supervisory Board within the Central Bank, but, again, this does not extend to Islamic windows.

The United Arab Emirates

The banking system of the UAE was hit hard during the global financial crisis of 2008, and the government pushed for stronger governance and regulatory reform. However, change through the Central Bank has been slow; it was only in 2018 that a federal law was passed. This law does not refer to any Islamic-banking framework, but it does stipulate that a Higher Sharia Authority be formed. The board will regulate both full Islamic banks and Islamic windows. The Higher Authority will be responsible for Sharia compliance as well as the approval of all products for Islamic banking, including windows (UAE Decretal Federal Law No. 14 of 2018).

Saudi Arabia

Saudi Arabia is the only GCC country that relies purely on Sharia law as the mainstay of its legal system. Scholars have concluded that countries ruled fundamentally by Sharia law have no need for separate or more specific banking regulations or a Higher Sharia Supervisory Board at the national level (Alam et al., 2019). Thus, while Islamic assets make up almost two-thirds of the total banking system of Saudi Arabia, there is neither a separate Islamic-banking framework nor a distinct higher supervisory authority. This absence blurs the regulatory field between conventional and Islamic banking. However, the Central Bank of Saudi Arabia is clear that the law of the land is Sharia, and hence there is no need to differentiate Islamic banking.

In the GCC countries of Kuwait, Qatar, Bahrain and the United Arab Emirates, which are not governed by Sharia, there have been doubts about the competency of Islamic governance and regulation. There have been reviews in every case. The UAE has implemented laws to allow for a Higher Sharia Supervisory Board but does not mandate a dedicated Islamic-banking framework. Bahrain does have a framework and a Higher Sharia Board, but these do not pertain to Islamic windows. In fact, the Central Bank does not supervise Islamic windows at all. Of greatest concern to Central Banks is the ability to ensure Sharia compliance. In Qatar and Kuwait, actions were taken to stop Islamic banking via windows altogether. In the cases of Bahrain and the UAE, the banking laws have been reconsidered and are under review.

Oman's Approach

Until 1968, the British Bank of the Middle East was the only bank in Oman. Since then, the industry has expanded to 20 licensed banks and ultra-modern services. The first local bank was formed in 1973, and the Central Bank of Oman was established in 1974. During the 1970s and 1980s, there was rapid growth of the banking sector with foreign and specialist banks also entering the market. The 1990s saw a period of consolidation involving several takeovers and mergers, and during the 2000s there was strong advancement in the industry powered by increased trade and the growing oil industry. The Omani banks are subject to uncertainties when oil prices fluctuate. Bank assets and GDP are closely associated with oil prices.

Only about 56 percent of Oman's population hold bank accounts (National Center for Statistics and Information, May 2017), suggesting great opportunity for banks to grow. The large number of nonparticipants is due to the fact that Islamic banking was traditionally not allowed; Muslims that closely adhere to the teachings of the Quran prefer not to use conventional banks.

There were clear business reasons for introducing Sharia-style banking. Increasing research indicates that Islamic banking has a favorable effect on banking and financial development as well as on economic growth (Boukhatem & Moussa, 2018; Gheeraert, 2014; Gheeraert & Weill, 2015). Yet the supervision and governance of Islamic financial institutions continue to lack standardization (Garas & Pierce, 2010).

Oman is no different than other countries that have introduced Islamic banking, in that it has encountered certain barriers and obstacles. First, there is strong competition with the already established conventional banks, and the efforts required to woo customers away from existing relationships can be tough. Second, the availability of staff with relevant knowledge and experience is a challenge, as there are few education opportunities specific to Islamic banking. As the industry is young globally, experience levels are shallow.

In Oman, where 90 percent of bank employees must be Omani, and Islamic banking has not been previously allowed, how can the new banks find or quickly grow experience? To this point, the College of Banking and Financial Studies has been hugely supportive, providing Islamic-banking courses as well as a fully recognized bachelor's degree in Islamic banking.

The third challenge concerns products: they must be specific to Islamic banking and acceptable to Sharia law. This challenge has been easier to address, as many products have been tested in other markets. The main requirement is to ensure that the Sharia board of each bank guarantees the proposed products are Sharia-compliant. Solutions to the barriers were well addressed, partly because, being late to the market, Oman was able to learn from other countries experiences Magd & McCoy, 2014).

While conventional banking is still predominant in Oman, the market now also includes an increasingly vibrant Islamic-banking segment that was immediately accepted and has grown rapidly. In the first nine months of 2017, it expanded by 29 percent, the fastest rate globally (Oxford Business Group, 2019). There are now two dedicated Islamic banks, and of the seven local commercial banks, six have Islamic windows.

With all this happening and the laws of the sultanate not being Sharia-based, the Central Bank was fortunate to be able to consider the examples of other GCC countries to build strong governance criteria.

The soundness of the Omani financial sector through the 2008 global financial crisis is largely due to the conservative stance taken by its Central Bank, well known in the region for its strong regulation and governance. With the changes in 2012 to allow Islamic banking, the Central Bank was tasked to make sure that it not only set in place strong governance, but also supported the new banking system and upheld Sharia principles. It learned from the experiences of other GCC countries that both a comprehensive Islamic banking regulatory framework and a higher Sharia supervisory authority are needed to ensure compliance.

The Islamic Banking Regulatory Framework introduced in December 2012 included the immediate establishment of a Higher Sharia Supervisory Authority. The Central Bank of Oman also wanted to ensure correct financial reporting in this new sector and worked closely within the standards of the Accounting and Auditing Organization for Islamic Financial Institutions. The result was the Islamic Banking Regulatory Framework, which extends to 591 pages.

After the regulatory structure was set in place, one of the early considerations concerned whether Oman should have a dual Islamic-banking system that includes windows. The Central Bank was well aware that allowing conventional

banks to begin Islamic-window operations would promote diversity and inclusion. However, allowing windows could also be perceived as promoting uneven opportunities, because conventional banks have the ability to draw from their parent banks' resources.

Prohibiting windows, nonetheless, would mean denying conventional banks the opportunity to set up outlets to serve existing customers. It would also deny the general public access to Islamic banking until fully fledged Islamic banks became established. In taking the decision to also allow Islamic operations through Islamic windows, the Central Bank of Oman fulfilled its critical responsibility to mitigate the risks of non-adherence to Sharia principles (Islamic Financial Services Industry Stability Report, 2018, box 1.1: Development of Islamic Banking Sector in Oman, 17-24)). Drawing lessons from the experiences of Qatar and Kuwait, the Central Bank of Oman knew that regulations for windows would need to be comprehensive and clear.

The Oman Islamic Banking Regulatory Framework is inclusive in its management of windows. Among other things, it stipulates that they can offer only Islamic banking products and services. Conventional-bank branches cannot carry Islamic-banking business, and there is to be no comingling of funds. Windows are to have independent and compliant IT systems as well as a dedicated treasury to manage Sharia-compliant instruments. The windows also need to have a clear vision and business plan that the Central Bank will approve, regularly review and monitor. All senior management must be properly qualified, with appointments approved by the Central Bank. Windows are constrained in relation to their net worth for prudential limitations. Their single borrowing limits would be reliant on the banks' net worth. All these rules are set to guarantee that Sharia principles are strictly adhered to, and that the operations of conventional banks' windows are on a level playing field with the newly established Islamic banks.

Banks are also to install their own Sharia supervisory boards to oversee and monitor all aspects of Islamic banking. The appointment of appropriately qualified scholars to these boards also must be approved and monitored by the Central Bank. Penalties for noncompliance with Sharia principles in Oman are tough. If violations occur, transactions will be canceled and income attributable to the bank or window

donated to Muslim charities. These rules place the reputation and sustainability of the banks at stake (Alam et al., 2019).

To ensure that there is a continuing supply of qualified staff, the Central Bank and the commercial banks in Oman worked with the College of Banking and Financial Studies to establish a dedicated bachelor's degree in Islamic banking. Staff can enroll in specialist subjects to enhance their Islamic-banking knowledge. This setup provides a distinct incentive to assist with ensuring knowledgeable operations and compliance.

The Central Bank also recognized the need for some initial regulatory support. For a limited time, it relaxed some of its rules to give the new operations a fighting chance against the already established conventional banks. A case in point: banks in Oman are limited to 15 percent of a total loan portfolio for housing finance and 35 percent for other personal finance. With consideration of the large number of nonparticipants in banking, Islamic banking entities were permitted for two years to exceed these limits up to a combined maximum of 75 percent for personal finance. This relaxation was gradually reduced by December 2017 (Alam et al., 2019).

The Central Bank of Oman set good guidance in place from the beginning and supported the sector, working in consultation with external associations, existing banks and educators. The market was ready and enthusiastic about the new Islamic offerings.

The difference made by having a strong regulatory framework is very clear. Within five years, Islamic assets had grown to 12.4 percent of total bank assets. Growth in 2017 was 23.8 percent, against the 5.3 percent growth of conventional banking assets, outperforming GDP growth of 8.7 percent.

The quality of assets has also been maintained, with nonperforming loans of Islamic-banking entities at 0.35 percent, compared to the total banking sector’s 2.8 percent — 6.4 percent in Bahrain and 5.9 percent in the UAE (Annual reports from Central Banks of Oman, Bahrain and the UAE).

Concluding Remarks

Oman was forced by the outcome of the Arab Spring and earlier Islamist activities to introduce Islamic banking. The results of regulatory reform by the Central

Bank of Oman ensured that their citizens now have the ability to adhere to both bank regulations and the teachings of the Quran in accordance with Sharia principles. The Central Bank supported the industry with some initial relaxation of its rules to enable competition. The results have been impressive growth outperforming both GDP and conventional banking returns and highly profitable with minimal nonperforming assets.

Oman drew on the experiences of other countries in designing its own Islamic banking system. An astute observer, it installed a strong governance structure ensured by the Islamic Banking Regulatory Framework and the Higher Sharia Supervisory Authority. Oman is the only GCC country to have both of these governance tools for Islamic banks and Islamic-banking windows.

The lessons are very clear. Islamic banks and Islamic-banking windows can cohabit, under strong regulation to allow competition. Windows also encourage the offering of Islamic products to all customers with minimal disruption to the existing banking sector.

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APPENDIX B: Case Study 2: Transformation

Case Study: From an "*Underperforming 80's Bank*" to One of Oman's Best – the Transformation of Bank Dhofar

In 2009, one year after the subprime crisis rocked the global financial system, Bank Dhofar won the "Number One Bank in Oman" prize from *Business Today* and Ernst and Young. In 2010, after becoming the country's second largest bank, it was the *Oman Economic Review* and *Euromoney*'s Best Bank in Oman, a nation on the Arabian Peninsula. These accomplishments were remarkable, considering that only two years earlier, Bank Dhofar was rapidly losing ground, slipping to number five in market share. A detailed analysis by outside consultants at the time had concluded that Bank Dhofar was an "underperforming 80s bank," facing a real risk of sliding further behind competitors.

A set of strategic initiatives set a foundation for this notable turnaround, which took place in one of the Gulf States rapidly growing economies. Similar to many other successful stories of corporate renewal, the transformation required bold leadership that enlisted the hearts and minds of the people in the organization. Importantly, the momentum for change was sustained through the leadership's willingness to take big risks and see the daunting challenges that confronted them as opportunities to kindle team spirit and solidify a new, winning attitude.

Background

Until the late 1960's the financial markets of The Sultanate of Oman were underdeveloped. There were just three banks in the country, with few branches, and very little banking activity or formalized trade. With the discovery of oil in 1967, economic development surged and fostered the need for a more sophisticated financial market that could cater to growing domestic requirements as well as international investment. This growth in demand led to the establishment of The Central Bank of Oman in 1974, and the introduction of more local banks, and opened the way for international banks to enter the market. Over the next three decades Oman's growth was steady and so was its

banking sector development. By 2007 Oman was served by 17 commercial banks with over 360 branches.

Bank Dhofar was established in 1990 with just two branches, one in the capital, Muscat, and the other in the southern region of Dhofar, the home area of its founding investors and promoters. In 1992 it purchased the local assets and liabilities of Bank of Credit and Commerce International and in 2002 it merged with a local institution, Majan International Bank. These acquisitions made Bank Dhofar much larger, and a contender with other major banks in the country. Over the next few years the economic expansion of Oman, and the organic growth and development at Bank Dhofar were steady. Nevertheless, Bank Dhofar's growth did not keep up with the pace of other major players (see Figure B).

At the beginning of 2007 Bank Dhofar had 48 branches and assets of USD 1.8 billion. On the face of it, Bank Dhofar was growing quickly and doing well. However, the banking market had become increasingly competitive. Bank Sohar was an aggressive new player in town, and it was buying up market share and recruiting talent from Bank Dhofar's staff.

On the back of the rapidly developing oil and gas industry, Oman's annual GDP growth reached 19 percent, and the banking system was expanding rapidly. The Board members at Bank Dhofar, however, had become concerned that their bank was not only failing to achieve its potential in a growing market but was also losing ground to its peers. In addition to its formidable rival Bank Sohar, there were now seven local banks and by most measures Bank Dhofar was sitting in fifth place, and dropping. As it lost market share its staff was being enticed to join other banks. Morale and motivation levels of the remaining staff were falling fast.

Bank Dhofar needed a strategic initiative to vault itself back into contention with its rivals. A new CEO, a veteran banker who held senior positions in Australia and New Zealand Banking Group, and at Standard Chartered Bank, was appointed to lead the change. Together with a team of external consultants, the management was tasked with drawing up a growth strategy for the next five years. Oman can pose unnerving challenges for strategy teams accustomed Western business practices.

How the Middle East can be Hazardous to Western Bankers

In their quest to modernize and gain international recognition, Middle Eastern banks frequently recruit veteran banking executives – Westerners – to fill their top management positions. Strong internal politics, family influences, ambiguous rules and regulations and unreliable legal systems, can nevertheless make such professional opportunities a gamble. Circumstances can flip quickly and drastically, as the example below illustrates, that it is not uncommon for expat CEOs working in the Gulf region to hold multiple passports and a ready stash of cash just in case an emergency exit is called for.

In 2007, David Proctor, a seasoned British banker, was tapped to become the CEO of Al Khaliji, a well-connected start-up bank in Qatar. The ensuing Global Financial Crisis in 2008 sparked a political shift in the control of the country's banking sector. When Proctor's position became untenable and he attempted to negotiate exit terms, his exit visa was denied. The veteran banker ended up spending fourteen months in legal limbo, unable to leave the country for any clear reason, a situation euphemistically known among local expats as getting "sent to China". Having survived the ordeal, Mr. Proctor says he has no intention of returning to Qatar (Dawber, 2010; Ellis, 2010).

The Strategy

The taskforce's findings, released in mid-2007, confirmed the Board's concerns that while Bank Dhofar was showing good internal growth, it was underperforming against its peers. Unless there were some essential changes, Bank Dhofar would drop even further in the rankings. This was a major alarm for Board members, especially as they had spent significant resources in the recent Majan International Bank merger.

The taskforce identified the following three areas of weakness:

1. *There were people and performance gaps: staff motivation was low, attrition rates were high and Bank Dhofar was not in a position to attract high caliber talent from the market.*

2. Market research identified capability issues: including limited market visibility, inconsistent branding, ineffective product development and slow response to the competition. Bank Dhofar had legacy computer systems and limited access to the market and customers. In short, it was an old fashioned bank with a concentration on branches and ATM's as avenues to access customers. There was no internet or electronic banking.

3. Bank Dhofar was seen as having a lack of customer focus, no service differentiation, no retail segments, no SME or Government business products and the different business units (Retail Banking and Corporate Banking) were operating independently. Traditional products were undifferentiated from the competitions'. In other words, the bank's offering were "very vanilla."

Adding to these concerns, share value was low and the company valuation was flagging. The consultants described Bank Dhofar in 2007, as an "underperforming 80's bank". They worked closely with the management and the Board during the process of forming a new strategy. Decisions were made based on the consultant's recommendations in conjunction with the management and the Board. Then implementation of the strategic initiatives were completed based on those decisions. The Board pledged full support for the resulting plan. The main focus of the strategic intent would play out in three areas of the business – people, processes and products. All three needed to be addressed in concert as each would need to mount initiatives that were reliant on the success of the others.

People

During 2007 a large number of staff were recruited by other banks. The attrition rate was almost 24 percent, leaving Bank Dhofar with significant personnel gaps. Turnover was expensive to manage and also gave Bank Dhofar a poor name as a place to work. Many of the staff members that remained weren't motivated.

It was important to fix the people issues quickly. The consultants had already discovered that salaries, bonuses and other benefits were generally lower than other banks offered. These were easy to fix and the Board agreed immediately to revised salary scales. The formula for paying bonuses was also rethought and set in place based on measured performance, so that all staff could participate; individual bonuses were

based on achievements. Management was also empowered to make some on-the-spot bonuses to staff that made significant contributions. These rewards were a powerful way to show that Bank Dhofar was serious about paying for exceptional performance.

The management also improved communications with the staff. This was done by instituting regular "town hall" meetings and visits to departments and branches. The purpose of these meetings was to show that the top management was committed to the staff and also to make sure that all messages were consistent and timely. A new communications department was set up to oversee formal gatherings, internal newsletters and routine external press releases. The outcome of all this was a reinvigorated staff and an increased ability to attract good people from the job market. A "buzz" about Bank Dhofar as a good place to work had been created and very quickly results started to show.

The Local Context

The Omani economy is dominated by a handful of powerful families, and the banking industry is no exception. Certain practices will inevitably raise some eyebrows among those who are used to standard corporate governance. For instance, the local banks seem to always pay handsome dividends to their shareholders, even in years when performance has been lackluster.

Family affairs are ever present in board politics, to the extent that key positions like the CEO may be left vacant for years. Hiring at the lower level can sometimes fall outside of the control of management. With a youthful population in dire need of employment, the Omani government will often stipulate local job quotas for each bank, known as "Omanization." Such quotas are set entirely independent of each bank's needs. Furthermore, the positions must be filled by Omani citizens, most of whom lack experience or required skills. Several key departments, however, are routinely dominated by foreign workers. The risk management and information technology departments, for example, are heavily populated by engineers trained at prestigious Indian IT schools.

Processes

Bank Dhofar's existing computer systems were outdated and holding back progress. A new system was needed to provide better and wider range of products, cheaper and quicker. A company-wide, two-year changeover project was put in place. Management decided that there should be a one-time system switch. This was a large risk and required extensive training for all staff over the full two years. This "big bang" approach necessitated a prior, full clean-up of all customer files and information. The transition would, in theory, remain invisible to customers.

The changeover proved to be immensely stressful and exhausting. The grueling experience, nevertheless, proved to be a great opportunity for building camaraderie. Over the two years of the project there was a lot of teamwork interaction that provided opportunities to get staff together for a common task. Bank Dhofar's leadership used those opportunities to talk about what was happening and to seek feedback and suggestions for improvements from all levels.

The final weeks of the project required precision execution. Key staff members were sleeping at the bank in makeshift quarters.

In the end, the changeover was a great success. Celebrations through all the offices fostered the sense of a new beginning. Morale was boosted, reinforcing the earlier strategic intent to focus on people. In contrast to this fortuitous outcome, Bank Muscat, the number one rival, had opted for a phased approach when it changed IT systems several years earlier. Bank Dhofar ended up completing the upgrade before their rival. The new system proved to be a great competitive advantage for Bank Dhofar and was used to provide better products and quicker service to customers.

Products

Armed with a faster and more efficient computer system, Bank Dhofar was ready to use the new resource to its advantage. Product development had not been a strength of Bank Dhofar in the past. However, with a new computer system, management felt that it was time to break the mold. The first new product to be brought out was a revised credit card, an offering Bank Dhofar also offered to non-customers and to different market segments. Government workers and teachers, who earned stable salaries, were especially a good source of new business.

The no-frills new credit card was marketed as a fast-to-approve and easy-to-use alternative. Importantly, it was enthusiastically promoted by a well-incentivized and invigorated sales force. In the end, the innovation experiment proved to be an important lesson for Bank Dhofar. The card turned out to be such a big hit the sheer volume of new applications almost broke the bank's under-resourced back office! Riding the high morale from its earlier wins, the bank's staff rallied to the challenge and eventually came out of the crisis both stronger and wiser.

Housing loans were the second product area to be revived. Here again, the differentiator there was to be fast in providing approvals. Customers were eager to have a product with a rapid and transparent approval process that would allow them to put a deposit on a new home. The energetic staff and modernized computer system enabled the new housing loans to become successful. Bank Dhofar also used its new system to develop a modern internet banking product. Until 2010 there was no internet banking product at Bank Dhofar. The upgrade meant the bank could compete in this important service area.

The Results

In the first half of 2008, the efforts produced remarkable results. The exodus of talent had just about stopped and management now had space to address the poorer performers. There was a noticeable jump in staff motivation, which was reflected in improved customer satisfaction levels.

When the half-year results came in, assets had grown by 44 percent, mostly helped by growth in customer loans. Revenues grew 54 percent, and on the back of that, profits grew by 63 percent after accounting for the additional USD 5.6 million investment in strategy initiatives during first six months – mainly the implementation of a new salary structure, recruiting new staff, and paying for the bonus scheme. The market also took notice of the changes as share prices increased by 32 percent.

During 2009 and 2010 Bank Dhofar won a number of industry awards. It was named the Number One Bank in Oman in 2009 by *Business Today* and Ernst and Young. It was one of *Oman Economic Review*'s "Top 20 Companies" in both 2009 and 2010, and the Best Bank in Oman in 2010. *Euromoney* also named Bank Dhofar the "Best Bank in Oman" in 2010.

During the next two years the delayed effects of the Global Financial Crisis hit Oman's economy. Bank Dhofar could not fully meet the financial objectives of the strategic plan period. However, because of the capabilities put in place by the plan, over the five-year period from 2007 to 2012, the bank's assets grew by 124 percent, revenues by 90 percent and profits by 64 percent, all in a time of great financial turmoil and uncertainty. It had also climbed from number five position to become the second largest bank in Oman. An independent study by Omani academic researchers concluded that between 2009 and 2013, Bank Dhofar was, based on observed inputs and outputs, Oman's most efficiently-run bank (Singh & Fida, 2015). As of 2016, the total assets of the bank were US$9.4 billion and net income was US$121 million (CPI, 2015).

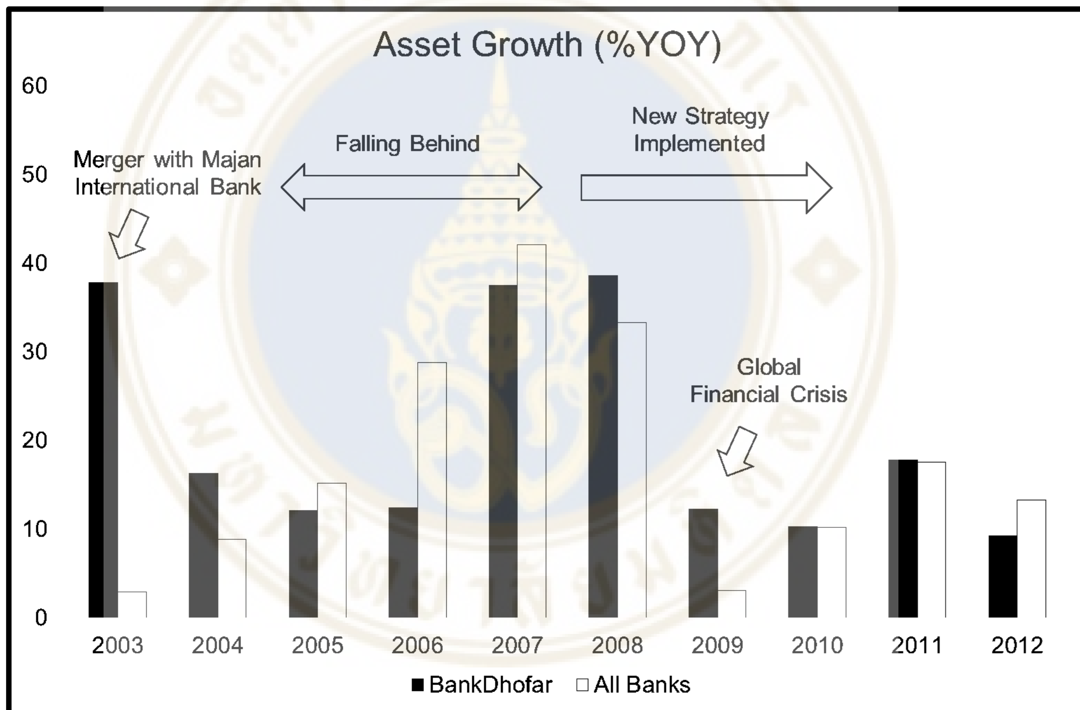

Figure B Asset growth – BankDhofar compared with all banks in Oman

Source: Omani Bank Annual Reports and Central Bank of Oman Annual Reports

In the first half of 2008 BankDhofar's assets increased by 44% Year on Year (YoY), but the loans to customers was the main driver which increased by 48%.

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APPENDIX C: Case Study 3: Mergers

The Myriad Forces Shaping the Future of the Banking Industry in Oman

Abstract

In the past decade there have been two bank mergers in Oman. There have also been a number of unsuccessful negotiations among others in the banking sector showing a large appetite for bank mergers. This study explores, through in-depth interviews with key stakeholders, the motivations for mergers in the banking sector in Oman, and reasons for the recent phenomena of non-completion of others. The results show the Omani banking sector could benefit from more consolidation activities. Such consolidation would allow more local banks to participate in the financing of larger investment projects. Socio-political reasons relating to the necessity to create jobs and maintain domestic employment dictate that there is little scope for cost reduction from mergers. Directors' personal interests often quash promising merger propositions from going through.

Keywords: Mergers, Banking, Oman, Omanisation

When Sultan Qaboos passed away in 2020, Oman had transformed into a country completely different from the one he took rein five decades earlier. Until the 1970's, Oman was very much an underdeveloped country. However, when oil was discovered in the late 1960's and extraction commenced, economic development began in earnest. Having quelled a chronic civil war known as the Dhofar Rebellion, Qaboos initiated a program of economic liberalization and lead the effort to modernize government administration. In 2010 the UNDP rated Oman as the fastest developing country since 1970 (United Nations Development Program, Human Development Report, 2010), although the rate of GDP growth has slowed dramatically since with the vast reduction of world oil prices.

The rapid progress of infrastructure, healthcare and education facilities brought serious, new socio-economic challenges. Among the biggest tasks facing the government is to create employment opportunities for the large numbers of school leavers and graduates. While the population of Oman is small (approximately 4.5 million with 2.8 million being Omanis and 1.7 million being expatriate workers), Omani families are traditionally large. With the much-improved medical facilities, infant mortality has reduced dramatically from 15.3% in 1970 to 1% in 2019 (UNICEF, 2020). As a consequence, Oman has a very young population, with a share of Omani's below the age of 25 at 55.5%. (Electronic Census of Population, Housing and Establishments, 2021).

Oman's path ahead is complicated by fluctuating energy prices and the country's depleting oil reserves, which are expected to run out in less than two decades (Abouzzohour, 2021). To counteract the heavy reliance on the oil industry (85% of government income is from oil) and to create jobs for the large numbers of young job seekers, the government has embarked on a program of creating *In-Country Value (ICV)*[1] by diversifying revenue streams and investing in new ventures and infrastructure projects. The current budget for new projects is US$160 billion. The Duqm Special Economic Zone and super city project is projected to generate 40,000 to 50,000 jobs per year for five years beginning in 2018 (Al Shaibany, 2017).

Extensive public spending coupled with declining oil revenue has resulted in public finance woes for Oman, as Moody's, Fitch and Standard & Poor's have all downgraded the government's credit ratings to junk status in 2019 and 2020 (Abouzzohour, 2021). The government's rising cost of borrowing coincides with a period when new investments are most critically needed to diversify the economy. This study looks at an alternative vehicle for financing investment projects, namely the commercial banking system. Assuming an important role in linking borrowers and savers (financial intermediation), the commercial banking system in well-functioning, successful economies help ensure that worthy investment projects receive funding at acceptable levels of risk to the lenders (Cowen and Tabarrok, 2014). A competitive,

[1] See http://www.incountryvalueoman.net/FAQ

well-run and judiciously regulated banking system is thus likely a key ingredient for the future health of the Omani economy.

Oman's Banking Sector

Oman's economic development has been intertwined with the development of banking and regulation in the country. The National Bank of Oman and Oman Arab Bank were established in 1972, and the Central Bank of Oman in 1974. Bank Muscat was incorporated in 1984 and Bank Dhofar in 1992. It wasn't until 2012 that Oman allowed Islamic Banking, and Alizz Islamic Bank and Bank Nizwa were formed.

There are now 20 licensed banks in Oman. This includes seven domestic commercial banks, two dedicated Islamic banks, nine branches of foreign banks and two specialty banks, Oman Housing Bank and Oman Development Bank. Twenty is a large number of banks for a country with a total population of barely five million people. The Oman National Centre for Statistics and Information published a survey in 2017 that found only 56% of Oman's inhabitants have bank accounts. The proportion increases to 68% when only Omani national are included. Omanis benefit from good access to financial infrastructure but it is evident that the Omani economy is over banked. In per capita terms, Oman has 16.3 bank branches per 100,000 people in 2016, above the international average of 12.5 and also above other countries in the Gulf Cooperation Council (GCC), which average 12.8 branches per 100,000 people.

Oman's banking system has become modern and sophisticated in recent years. Foreign bank executives have played important roles in modernizing and transforming Omani banks (Babicci and Wongsurawat, 2018). As a robust regulator, the Central Bank of Oman (CBO) has ensured that the rapid development of the financial system has not destabilized the country's macroeconomy. However, with the situation of surplus banking services, there are regular negotiations between bank boards for merger and consolidation, and the Central Bank is supportive, for the right merger.

The current banking landscape in Oman follows a history of mergers. Bank Muscat, which holds about 35% of the market share (by total assets), grew to be the dominant bank by a series of acquisitions in the 1990's. Its merger with the Commercial Bank of Oman in 2000 was the largest bank merger in the country at the time, and immediately created a giant in Oman's banking system. Bank Dhofar is the number two

bank, but its market share follows a long way behind Bank Muscat with 12%. National Bank of Oman and Bank Sohar currently hold 10% each. These are the largest four banks and they are often compared amongst each other for services and performance. Bank Muscat is the largest bank by a significant lead (about three times larger than its closest competition) and the CBO is keen to see this margin reduced, which again calls for mergers and rationalisation. Market shares in 2019 by bank assets are shown in Figure C.

Searching for a Merger – Bank Dhofar's Experience

In the past decade there has been much merger talk among the larger banks and the Central Bank (with the exclusion of Bank Muscat). Although the CBO has been supportive, there have only been two mergers eventuate among smaller banks. In 2010, after Bank Dhofar had implemented a significant growth strategy, the then-CEO and Chairman went on the hunt for significant mergers. They first approached Oman International Bank and initial discussions were positively received. At Bank Dhofar's end some significant internal analysis had been conducted. Bank Dhofar was strong in the corporate banking sector and Oman International Bank had a larger retail base. The thinking was that the two businesses were complementary and a merger would be seen as a first step to set a firm foundation for rapid growth. The talks with Oman International Bank were soon stopped after the Chairman of both banks could not find agreement of the general terms. Oman International Bank, however, was clearly agreeable to a union (just not with Bank Dhofar), and they did merge with the Hong Kong and Shanghai Banking Corporation's (HSBC) Oman office in 2012.

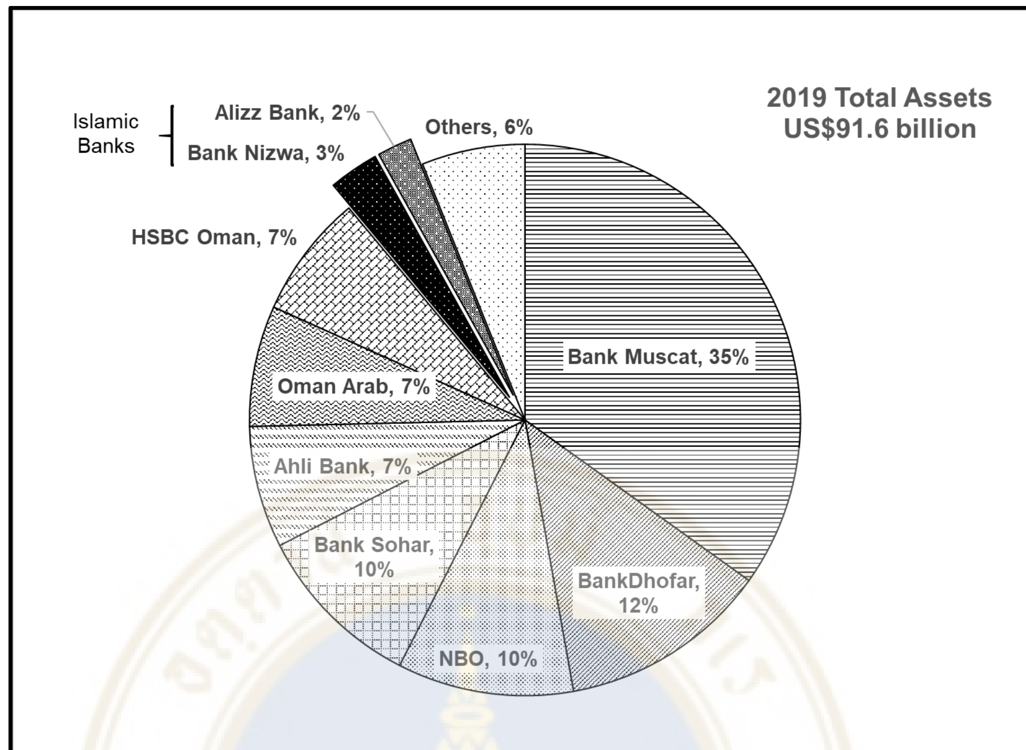

Figure C Banking market share by assets.

Source: Assembled from bank annual reports.

The next target that Bank Dhofar approached was the National Bank of Oman (NBO), which was 35% owned by The Commercial Bank of Qatar. In late 2010 there was a high-level meeting at the Grand Hyatt hotel in Muscat with the CEO and Chairman of Bank Dhofar along with an external banking consultant and The Commercial Bank of Qatar's CEO and owner's representative from the Al Fardan group in Qatar. Everybody left that meeting in agreement that a merger in Oman was the right strategy and that both parties would further discussions with their respective boards. The Bank Dhofar team had again done a lot of analysis and already had agreement from their Board. After the meeting in Muscat, they were quietly confident that this time a merger would go ahead. However, within 48 hours the news came back through NBO's top management that the possibility of a merger would not progress because the Commercial Bank of Qatar did not support the deal.

The next series of merger negotiations began in mid-2013 between Bank Dhofar and Bank Sohar. The market sentiment was that this merger would happen and propel the joint bank solidly into number two position with about 22% of the market.

Talks continued in earnest and both banks entered into a non-binding Memorandum of Understanding in 2015. Legal and financial consultants were appointed for the due diligence process. In 2016 when both boards agreed on a Share Swap Ratio, subject to regulatory approvals, it appeared that after a long gap this merger would go ahead. However, in October 2016, after three years of negotiations, Bank Dhofar advised its shareholders that due to the banks being unable to agree on certain key issues, negotiations were discontinued.

In June 2018, The Commercial Bank of Qatar announced on their stock exchange (in Qatar) that it would commence discussions for a possible merger between Bank Dhofar and NBO. Bank Dhofar responded a month later with an announcement that the Board of directors had resolved to also enter discussions. However, by December the Commercial Bank of Qatar made a further announcement that they do not support the merger, similar to their decision in 2010.

It is shown that over the past ten years there has been a desire for bank mergers in Oman to address the over banked situation with relation to the small population, and to rebalance the market in relation to Bank Muscat's strong foothold. Whilst earnest negotiations had been set in motion, none of the larger banks have been able to agree on a format to merge. There have been six documented attempts for amalgamations, but only at the lower end of the market have Boards and management been able to fully agree terms.

The questions that arise from the study of this ten-year background are; why is there a consistent undertone of merger discussion in Oman and how will any mergers of banks in Oman benefit the market and other stakeholders specifically?

The Economics of Bank Mergers

Despite mergers being complex in nature, increasingly corporate executives consider mergers as a method to fast-track business development and to respond to the changing business environment and competitive pressures (Borodin et al., 2020). Mergers can be multi-faceted, and there are many motives for companies to consider them as a strategic tool to drive advantage (Marks & Mirvis, 2011).

Mergers are commonly approached as a structural procedure that allows companies to combine competencies and realize strategic and operational goals. They

also serve to fill gaps in business lines; and by doing so they combine the resources of two or more businesses into a single entity (Sawler, 2005). Mergers are designed to be permanent and the expectation of successful integration of the combining businesses is for long term positive gains.

Motivations for Mergers

Recent research (Rabier, 2017; Hassan et al., 2018) indicates that internal motivations for mergers consistently include (i) efficiencies resulting from costs savings, (ii) internal structural benefits (for reasons of tax, wealth transfer, or capitalizing on merged business strengths), often called synergies, and (iii) enhanced market power from becoming a bigger player. Cost savings occur when the merged entity can share human and physical resources, thus enjoying greater economies of scale. An example of a synergy (or economies of scope) is when client data from one line of business (e.g., retail banking) of the first bank can be productively employed in a second line of business (e.g., life insurance) of a second bank. Finally, becoming a big player comes with privileges such as the ability to become a price leader[2].

A controversial consideration that is not always readily identified in board room discussions, is managerial self-interest. In agency theory research, Eisenhardt (1989) shows that mergers are an arena in which principal and agent (owner and manager) interests can deviate. Gupta and Misra (2007) confirm that managers can use mergers to build their own objectives and personal interests, and as a way to boost or to defend their authoritative positions. Managers could go on an acquisition spree to boost their compensation, avoid the possibility of being acquired themselves, or in the case of banks enjoy the perks of becoming “too big to fail”[3].

Timing of Mergers

History has shown that mergers in the banking sector occur in waves (De Young et al., 2009). More than ever, in recent times banking mergers follow the waves

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[2] Price leadership occurs when a preeminent firm announces a price change, and all other players follow in the same direction. Economist consider such behavior to be tacit collusion between players in an oligopolistic market (Besanko, et al. 2010).

[3] A company becomes too big to fail if its bankruptcy would result in a catastrophe to the economy as a whole (due to some domino-effect or massive job loss). The government is therefore implicitly guaranteed to bail the company out if it ever falls into serious trouble.

of financial crises. Since the Asian Financial Crisis of 1997 and the Global Financial Crisis of 2008, banking industry mergers are perceived to promote financial sector stability, as there is a general expectation that mergers will lead to better bank performances (Du & Sim, 2016). Mergers are also more likely after financial upheaval because share prices tend to be cheap.

Financial crises are always followed by regulatory reforms. Mergers can also occur as a response to changes in compliance and regulations (Karolyi & Taboada, 2015). Stricter regulation can force banks to merge in order to comply with new rules. Alternatively, deregulation can also encourage mergers to exploit arising new opportunities. In short, waves of mergers are expected following significant changes in the regulatory environment.

Outcomes

The art of bank management has been ever changing. It is complex in its nature and often the inner workings of merger motivations and outcomes are opaque, at best, to the outside community, and less transparent than other types of firms (Jiang et al., 2016; Blau et al., 2017).

While most mergers are negotiated and implemented to favor the acquiring company, many merger efforts fail to result in intended performance enhancements. McKinsey and Company (2010) report that merger activity is critical for long term survival. Yet, their study finds that as low as 23% of mergers are fully successful. Many of the failures begin with poor due diligence, through to lax consideration for pre-merger and post-merger capabilities. There are examples of merger failures from a lack of understanding of the tasks involved, inadequate assessment of the target, lack of leadership and strategic supervision, and human resources issues such as fundamental cultural differences, and managerial hubris (Brouthers et al., 1998; Banal-Estañol & Seldeslachts, 2011; Vazirani, 2012).

In spite of the rapid changing technology and regulatory environment, the poor record of merger successes should serve as a reality check for managers looking to improve efficiency and enhance stockholder value through mergers and acquisitions.

In-depth Interviews

To investigate the motives for bank mergers in Oman, a qualitative research approach was chosen. We conducted in-depth interviews, sourcing the opinions from a selection of the highest levels of the banking and business community in Oman. Interviewees selected were expected to have been in their respective industries in Oman for ten years or more, and in their current role for at least four years. Interviews were conducted on an individual, one-on-one basis. The affiliations and positions of interviewees are summarized in Table C.

The interviews were conducted in a series of discussions with an outline of relevant questions to set the general course. There was a balanced mix of Omani and expatriates (7 Omanis and 5 expatriates). Conducted during the second half of 2020, the total interview time ran for 14 hours and thirteen minutes (with average time per interview of one hour and twelve minutes).

The reason for specifying ten years in the industry is that this period is approximately 25% of a projected career life. The selected interviewees will have built up substantial knowledge and experience in their field. This observation also runs true for working in Oman for at least ten years, where employees are able to build knowledge and experience specifically about the Omani markets. The reason for selecting four years in their current roles is that the interviewee would be on their second or even third contract cycle with the one employer. Generally, employment contracts for expatriates in the Oman are for two to three years. Therefore, the respondent selection will be well regarded and have continuity of employment with one employer. All prospective respondents were at the very senior CEO or business head level.

Table C Affiliations and positions of interviewees.

Affiliation	Position
Local Banks	Chief Executive Officer Business Head
Local Bank Islamic Windows	Board Member Chief Executive Officer
Islamic Banks	Chief Executive Officer Business Head
International Banks	Business Head
Large Businesses	Chief Executive Officer
SME's	Chief Executive Officer
Accounting Firms	Partner
Legal Firms	Partner
College of Banking and Finance, Oman	Former Dean

The Central Bank of Oman declined to be interviewed and responded that internal approvals were unavailable due to the market sensitive nature of the proposed discussions.

Qualitative enquiry is a complex process that requires considerable patience. Much effort is needed to disentangle multifaceted issues and to piece together explanations worthy of thoughtful and reflective academic findings that explain research phenomena (Yin, 1981, 2013). The questions employed for this study were small in number and open in content so as not to cloud the outcome or to signal any direction. They were sent to prospective interviewees in advance so that they could contemplate and prepare for earnest and open discussion. The questions, designed simply as a kickoff to stimulate discussion, are listed below.

(1) The Central Bank of Oman has been supportive of bank mergers and recently there has been discussion about possible mergers (for example, Bank Dhofar/Bank Sohar, Bank Dhofar/National Bank of Oman, Oman Arab Bank/Alizz Bank). Is Oman currently overbanked, and is this the right time for more mergers?

(2) Oman's Council of Ministers has also committed to provide jobs for new Omani graduates, and many of these will be expected to be in the banking industry. In addition, to ensure job creation for Omani's, The Central Bank of Oman maintains strict

Omanisation requirements in banks, which is currently 90%. How can banks ensure that Omani employment and Omanisation requirements are met, and also deliver efficiencies and cost containments?

(3) There are many motives for bank mergers including increasing revenues, cost savings, synergies and rationalization. Staff costs in Oman banks are high at 65% of operating costs, and mergers can create higher staff costs. Oman has the desire for bank mergers, but with Omanisation, job creation expectations and high staff costs; what are the likely motivations for these mergers?

In the normal course of utilizing semi-structured interview techniques for data collection, the researcher would preferably meet with the respondents to conduct interviews in person and face-to-face, to enable a depth of interaction and to ensure the best quality of responses. During the research period for this study the global pandemic of COVID – 19 closed airlines and inhibited all travel to Oman.

The Sultanate of Oman is peculiar, especially in a first world environment, in that the Telecommunications Regulatory Act (2002) prohibits the use of social media applications, including video conferencing. With the inability to travel to Oman and these restrictions it was a concern that this research would be jeopardized and need to be abandoned, at least until COVID – 19 restrictions are lifted. With climbing cases of COVID – 19 and prospects of second, and even third waves, the delays could be substantial.

Fortuitously in response to the COVID – 19 situation the Omani government partially lifted their restrictions and during 2020 allowed the temporarily use of VoIP applications to accommodate companies and educational institutions to conduct remote meetings. The interviews for this research project were therefore held using Zoom video conferencing.

Once the interviews were completed, qualitative data analysis was conducted to produce findings by coding and organizing themes using the software application NVivo. NVivo was able to transcribe the video evidence to reveal repeated ideas and concepts leading to relevant codes, nodules and theme categories.

Validation of data was conducted using triangulation method to collaborate the efficacy of data collected by secondary research (analysis of academic publications, media reports company reports and Central Bank and stock markets information). The

third part of triangulation was by observations of the researcher and other experts who also have in-depth knowledge of the banking industry, and of Oman.

Findings and Discussion

The literature is expressive in that the reasons companies consider merger activity is for efficiency gains, structural benefits, enhanced market power, and in some cases managerial interests. Specifically relevant to banking sector mergers, motives also include technology enhancements, better risk management, portfolio quality enrichment, promoting stability in the wider financial sector, regulatory influence, and regulation or de-regulation changes. We explore whether such motivations are pertinent in the banking sector of Oman, and whether other motives, if any, are also present.

Efficiency – The Practitioners' Perspective

In 2012, HSBC and Oman International Bank merged to control a 7% share of the Omani banking industry. Seven years after the merger, HSBC's total assets in Oman had expanded by a mere six and a half percent (from USD 6.2 billion in 2012 to USD 6.6 billion in 2019). Annual profits, however, had grown by almost four-fold (from US 18.6 million to USD 90.1 million) while capital shrank by more than half (from USD 748.8 million to USD 344.8 million). These numbers suggest that, operating in a small and developing market such as Oman, mergers may allow banks to take on more desirable risk and operate more profitably.

An often-cited benefit of mergers is to create healthier industry competition. Competitive pressure, in theory, will push banks to operate more efficiently. A market composed of a handful of players of similar sizes is believed to produce more intense competition than one with a single dominant firm and a bunch of small players[4]. In Oman, Bank Muscat has always been the biggest player by a wide margin. While there is evidence that the industry would benefit by leveling the competitive playing field and reducing the "lopsided" banking landscape, the reality is that only a merger of the three largest banks (behind the market leader) would be enough to give size to challenge Bank

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[4] Regulators often use the *Herfindahl index* to measure the degree of competition (Besanko et al., 2010). The Herfindahl index equals the sum of the squared market shares of all the firms in the market. The US Department of Justice considers a Herfindahl index of greater than 0.25 to signify high market concentration.

Muscat. Such a merger, nevertheless, would be both unlikely and impractical. Even if the boards could arrive at acceptable terms, such a merger would end up creating a market with two large players without a credible third challenger. Merger benefits from a more balanced competition in the Omani banking section is therefore unlikely to be realized in the near future.

Could mergers allow banks to create a more balanced portfolio of products and services? As it turns out, the make-up of banks in Oman is very similar. They all have retail banking businesses, corporate banking and treasury services. They are all at the same level of technological advancement with good computerization, digital and mobile banking offerings, and they all operate in the same risk environment. Experts we interviewed agreed that there would be no advantage to balancing individual portfolios (retail banking or corporate banking portfolios) with mergers, other than to increase portfolio sizes.

A unique merger case between a conventional and an Islamic bank occurred in 2020. Oman Arab Bank, a subsidiary of the Jordanian Arab Bank Group, merged with Alizz Islamic Bank. The merger was a consolidation of two small banks in Oman. The combined market share was 9%. The key reasons for the merge were (1) to provide Oman Arab Bank with a vehicle that would list it on the Muscat stock exchange and (2) to open up broader markets for Alizz bank's products and services. It is still too early to assess whether benefits from the merger will be fully realized.

Mergers driven by managers and directors' self-interests, the literature indicates, can create *inefficient* deals. Many of the banks have longstanding board members that are well known in the Omani market. Some of the recent discussions with Bank Dhofar in particular and its negotiations with National Bank of Oman and also Bank Sohar could have been justified as being the basis for managers and Board members growing their own interests by creating a larger entity. However, evidence through stock market reports in both Oman and Qatar show these mergers did not go through because the management and the Boards of the respective banks could not come to agreement on terms. Through discussion with the interview participants and through the stock market releases, it is evident that managerial self-interests worked as a de-motivator for mergers. The reason is many Board members would not want to risk losing a Board position in any amalgamation.

The Socio-political Factor

Social and political considerations, while not often considered in the economics and finance literature, are potentially eminent factors in explaining the competitive configuration of an industry, especially one as important as commercial banking. While Oman is an absolute monarchy, its rulers must nonetheless contend with the possibility of popular discontent. When oil prices are high, state oil revenues create flexibility in financing programs to keep the majority of the populace happy. When oil prices drop, such as during the Global Financial Crisis in 2008, government coffers quickly run dry and rulers can feel pressure from the disgruntled masses. The Omani government's recent policy changes (Oman Observer, 2020a/b) aimed at expediting early retirement to make more jobs available for new graduates can be seen as a symptom of rising stress in the labor market.

While Oman did not face severe political upheaval, compared to its neighbors, during the Arab Spring of 2011, the country's leaders were keenly aware of the political risks posed by the economic challenges. A strategic concession made by the Omani government in the aftermath of the Arab Spring was to allow the previously banned Islamic banking in Oman for the first time (Babicci and Wongsurawat, 2020). Sultan Qaboos, the father of modern Oman, previously viewed Islamic banking as a threat to the country's moderate Islam. The sultan, however, was willing to yield to previous popular demand and allow Sharia-style banking for the first time in 2011. As new Islamic banks were set up and conventional banks scurried to open Islamic windows, the banking industry quickly adapted to a new parallel banking system.

To guard against the risk of an uprising, unemployment especially among the youth needed to be earnestly managed. Enough new jobs for the country's young and growing workforce were required. The commercial banking sector was called upon to assist in this key task. "Omanisation", the setting of quotas for Omani workers in different industries, is one policy instrument the government uses to boost domestic job creation. As political pressure rose, so did the government's demands on the commercial banks to step up their hiring of new graduates.

Most interviewees expressed understanding for the need of the Omanisation program, which currently requires 90% of bank employees to be Omani citizens. This lofty requirement, higher than any other GCC country, does pose a challenge for bank

management in terms of career-path and cost management. Some comments were that Omanisation is fully supported by all but could be seen as "overly successful", "solving a temporary problem" and that there is a "tradeoff between the desire to create employment and enhancing profits".

All interview respondents were cognizant of roots of the socio-political configurations of Oman, and their current legacies. Historically, Omani's had large families, for continuity and succession reasons. When medical facilities were scarce and life expectancy was much shorter than today, such traditions were sustainable. However, family sizes have not fallen with the country's growing life expectancy. In Oman's first census in 1993, women between the ages of forty and forty-four had an average of 8.13 children. Qaboos, the sultan at the time, voiced his concerns stating "a big family is a burden on us all" (Drysdale, 2010). A rapidly growing population continues to pose challenges in terms of employment opportunities for the large numbers of Omani youth.

An offshoot of this vigorous employment creation program is that when it came to bank mergers, significant cost reductions would *not* be realized from mergers of the local banks in Oman. The prospect of synergies from branch consolidations are very limited as the central bank and also the government deter actions that would reduce employment numbers. With staff costs at about 65% of all bank expenses and high Omanisation requirements, synergies from human resource rationalization will not be significant and will not provide meaningful cost savings.

There is no doubt that the Central Bank of Oman (CBO) maintains tight control over banking regulation – and at times this control extends into areas of human resources practices. The College of Banking and Financial Studies in Oman comes under the organizational umbrella of the central bank. One interesting story that was conveyed during the interviews was that the college recently contracted an industry expert to come to Oman to conduct a seminar for students on technological advancements in banking, the success of digital banking and experiences of branchless banks. The CBO advised that the seminar should be cancelled as the banking industry in Oman was seen as a major employer for school leavers and graduates, and innovations such as branchless banking could lead to less opportunities and obstruct those efforts.

The Regulatory Requisite – Financial Stability

One of the most consistent threads brought out of the discussions, both with bankers and non-bankers, was confirmation of the complexity of bank management. In addition to stock market authority regulations, bank governance is directed and regulated by the central bank, a body concerned with banking sector stability, loan portfolio quality and depositor protection. Most of the interviewees regarded bank regulation in Oman as well managed but conservative. The CBO guidelines are more restrictive than international norms, including other GCC countries. In the interviews, all the bankers were unanimous and three of the five non-bankers confirmed this conservative stance. Specifically, Oman-based banks cannot lend outside Oman, they cannot operate internationally, and they are restricted in lending to non-resident individuals or companies in Omani Rials. Capital adequacy[5] requirements are high at 12% and single borrower limits[6] are restricted to 15% of the banks net worth.

Before arriving in Oman in 2007, the first author had worked for many years as Country Head and Senior Executive levels in Asia, the Indian Sub-Continent and Qatar. The Omani regulatory system was the most conservative among all these countries. Banking professionals often viewed the restrictions as bothersome impediments to business growth. When the Global Financial Crisis hit the banking industry hard in 2008, however, Oman was less affected than other GCC countries. Bank executives often look back on those days thankful for the strong stance that the CBO had taken.

An outcome of the regulations on the capital adequacy and single borrower limits is that banks are restricted in the amount of free capital that they have to lend. Large local projects cannot always be catered to in meaningful loan quantities, depending on the size of lending requirements. Foreign developers are also restricted in borrowing through Omani banks. In the past the Omani government was able to support projects with funding, but now due to reduced oil revenues, those options have also been

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[5] Capital adequacy is the amount of capital a bank must retain in relation to its risk portfolio, so that in case of need, the bank can sustain a reasonable amount of bad debts. It is a measure of the financial soundness of a bank and in practice a higher ratio means the bank will have less capital available to employ for business purposes, or to lend to its customers. International standards set by the Basel III Accord are 8%.

[6] This is the total amount that a bank can lend to any one customer or any one related group of customers and is measured in relation to a bank's net worth. In developing countries where financing of infrastructure requires high levels banks need the ability to provide significant loans. In Oman this is restricted by the relatively small size of the Banks' balance sheets and also the Central Bank regulations. The Basel III Accord guidelines is 25%.

restricted. In order to compete for business, bank management is consistently looking for ways to increase their capital holdings. Mergers are a tool to right-size capital.

A key theme that emerged from the interviews is that banking in Oman is a "game of scale". The observation is important when considering the country's current economic condition, which has been subdued by reduced oil revenues, and Oman's plan to promote large-scale infrastructure and manufacturing projects. Oman's modest population and small economy restrict market growth. For a bank to thrive "size and scale are necessary". The importance of increasing bank capital and size was a feature of almost all the interviews and emerged in analysis as a major part of bank management concerns for future growth.

Concluding Remarks

Results from a series of in-depth interviews with experts at the highest level in the industry reveal that the Omani banking sector could clearly benefit from more consolidation activities. Such consolidation would allow more local banks to participate in the financing of larger investment projects. There are examples of successful mergers in the recent past, and the appetite for mergers is not lacking. Of the primary motives, partial efficiencies of increased profits can be gained with capable bank management decisions and the use of increased capital. The Omani banks' desire to participate in local infrastructure projects raises the need for increased capital and this leads to the need to restructure balance sheets. This last motive appears to be the strongest stimulus for the recent appetite for mergers.

Political economy reasons relating to the necessity to create jobs and maintain domestic employment dictate that there is little scope for cost reduction from mergers. As long as Omanization requirements for the banking industry remains at ninety percent, human resources rationalization post-merging will remain infeasible, because laying off Omani workers is prohibitively expensive. A competent but conservative central bank is cautiously supportive of mergers to create a more balanced competition and ensure financial sector stability. However, directors' personal interests in maintaining clout on their bank's board often quash promising merger propositions from going through.

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