



# Saudi Arabian Economy

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## Saudi economy: Consumer spending improves

Central bank data indicated that consumer spending improved in July 2017, as POS transactions and ATM withdrawals, both posted their best annual growth rates in about nine months. However, we would like to see if this improvement can be sustained or not. Meanwhile, credit to the private sector continued to decline, indicating sluggish private sector economic activity. SAMA's reserve assets also resumed the downtrend, slipping 1.2% m-o-m to SAR1,854bn, after a brief monthly rise in June 2017, despite the government raising local debt in July. We believe this might be attributable to the government's foreign investment activities. The government has raised another SAR13bn in August 2017 through a domestic Islamic bond sale to fund its budget deficit, which could limit further foreign reserve drawdown. Meanwhile, the Kingdom's fiscal position improved further in Q2 2017 supported by higher oil revenue and cut in expenditure. The H1 deficit constituted only 37% of the government's deficit projection for the entire year. Moody's stated that the deficit is deemed as 'credit positive' for the Kingdom. The government continues to push for privatization, which will help reduce the burden of the expenditure on government finances, the latest step being floating tenders for greenfield and brownfield expansion projects across a dozen airports.

**Kingdom raised SAR 13bn** from the second monthly sale of domestic Islamic bonds, after raising SAR 17bn in July 2017. The government offered lower yields in the second round owing to higher demand. The 5-year sukuk was priced at 2.7%, the 7-year at 3.2% and the 10-year at 3.5%.

**Saudi Arabia's Q2 2017 fiscal deficit** declined to SAR 46.5bn as against SAR 58bn last year, backed by the 6% yearly rise in revenue and a 1% y-o-y fall in expenses. The H1 2017 deficit is SAR 72.7bn, sharply lower on a pro-rata basis than the government's projection of SAR 198bn for 2017. Revenue increased in Q2 2017 (SAR 163.9bn Vs SAR 144.1bn in Q1 2017), while the expenditure rose to SAR 210.4bn in Q2 2017 compared to SAR 170.3bn in Q1 2017. On a y-o-y basis, 1H revenue increased ~29% to SAR308bn and expenditure decreased ~2% to SAR380.7bn. (Figure 2 & 3)

**Point-of-sale (POS) transaction** pointed to improved consumer spending activity, rising 12.8% y-o-y in July 2017, compared to the annual drop of 0.8% in June. Meanwhile, the ATM transactions rose by 2.4% y-o-y in July 2017 as against the fall of 11.4% y-o-y in June 2017.

**Foreign reserve assets** dropped 1.2% m-o-m in July, despite the government raising funds via domestic Islamic bonds. Meanwhile, the **deposits** rose (+3.3% y-o-y), whereas **credit to the private sector** dropped (-1.3% y-o-y) for the same month thereby pushing the loan-to-deposit ratio below the 90% mark for the tenth consecutive month. Govt reserve and deposits at SAMA declined 2% m-o-m and 32% y-o-y to SAR650bn.

**Banking sector profits** rose in July 2017 at the fastest yearly pace in six months. Cumulative banking sector profits stood at SAR 26,213mn in 2017.

**Inflation** continued to prevail in negative territory in July 2017, owing to the continued drop in food and beverages sector coupled with the fall in transport and clothing/ footwear sectors. Despite the rise in POS transaction value, we believe inflation is being weighed down by benign global commodity prices impacting 'Food and Beverage' sector inflation and weakness in housing and



discretionary sectors (Transport, Restaurants, Clothing and Footwear). We believe inflation does not indicate the actual core inflation in Saudi Arabia as some of the key components that compose inflation index are based on imports or are regulated by Govt.

**Kingdom's foreign trade volume** witnessed a slowdown in 2016 compared to that in 2015. Meanwhile, non-oil exports in June 2017 dropped by 18.9% y-o-y (-9.8% y-o-y in May), while non-oil imports fell by 29.0% y-o-y in June (-11.3% y-o-y in May 2017).

**Crude oil prices** (Brent October futures contract) slipped 0.6% MTD in August 2017 as against the monthly rise of 7.5% in July 2017, owing to concerns over rising output from OPEC countries like Saudi Arabia, Libya and Nigeria. Further, worries over higher production in the US also weighed on the prices.

**Crude price outlook:** The US Energy Information Administration (EIA) in its August 2017 report estimated Brent crude oil prices to average around US\$51/barrel in 2017 and US\$52/barrel in 2018.

**Figure 1 Key macro indicators**

Variable	Aug-17	Jul-17	Jun-17	2016	2015
Inflation Rate (2007=100)	-	-0.3%	-0.4%	3.5%	2.2%
	Aug-17	Jul-17	Jun-17	2016	2015
Average Oil Price (Arab Light) (US\$/Barrel)	48.7	47.1	45.2	41	49.9
	Aug-17	Jul-17	Jun-17	2016	2015
Money Supply (M3)	-	2.7%	2.6%	0.8%	2.5%
Total Banking Sector Claims	-	2.2	1.4	9.1	10.5
Interbank Interest Rate (3 Month)	1.796	1.793	1.750	2.066	0.88
Repo Rate	2.00	2.00	2.00	2.00	2.00
Reverse Repo Rate	1.25	1.25	1.25	0.75	0.5
General Share Price Index (1985=1000)	-	12.6	14.2	4.3	-17.1
		Q1 2017*	Q4 2016	2016*	2015
GDP Rate at Constant Prices (2010=100)	-	-0.5%	2.2%	1.7%	4.1%
		Q1 2017*	Q4 2016*	2016*	2015
Current Account to GDP Ratio (current prices)	-	3.6%	-1.4%	-4.3%	-8.7%
Total Imports (fob) to GDP Ratio (current prices)	-	17.3%	18.0%	19.8%	24.3%
Non-oil Exports to GDP Ratio (current prices)	-	6.7%	7.4%	7.3%	7.7%

Source: SAMA, \* Provisional, Arab light and Interbank interest rate data is as on 25 August and 24 August 2017, respectively.

**Figure 2 Revenue (Budget Performance)- SAR bn**

	Q1 2016	Q2 2016	H1 2016	Q1 2017	Q2 2017	H1 2017
Oil Revenue	52.0	78.9	130.9	112.0	101.0	213.0
Non-oil Revenue	31.7	76.0	108.0	32.1	62.9	95.0
Taxes on income, profit and capital gain	2.0	5.6	7.5	2.0	7.2	9.2
Taxes on goods and services	5.3	8.0	13.3	5.7	8.1	13.8
Commercial transaction tax	3.6	8.8	12.4	4.5	4.9	9.5
Other taxes (including Zakat)	1.1	11.7	12.8	1.6	10.6	12.2
Other revenue (including SAMA and PIF revenue)	19.8	41.9	61.7	18.3	32.1	50.4
<b>Total</b>	<b>83.7</b>	<b>154.9</b>	<b>238.9</b>	<b>144.1</b>	<b>163.9</b>	<b>308.0</b>

Source: MoF, Al Rajhi Capital

**Figure 3 Expenditure -SAR bn**

	Q1 2016	Q2 2016	H1 2016	Q1 2017	Q2 2017	H1 2017
Employee Compensation	99.2	103.2	202.5	94.1	102.8	196.9
Goods and services	21.4	44.9	66.3	16.7	27.2	43.9
Financing charges	0.1	1.2	1.3	1.3	3	4.3
Subsidies	0.6	2.8	3.4	0.1	1.1	1.2
Grants	1.3	0.3	1.6	0.6	0.6	1.2
Social benefits	7.8	11.3	19.1	6.6	16.6	23.2
Other expenditures	20.5	11.5	32.0	21.9	25.8	47.7
Non-financial assets (Capital)	23.8	38.0	61.8	29.1	33.3	62.3
<b>Total</b>	<b>174.7</b>	<b>213.3</b>	<b>388.0</b>	<b>170.3</b>	<b>210.4</b>	<b>380.7</b>

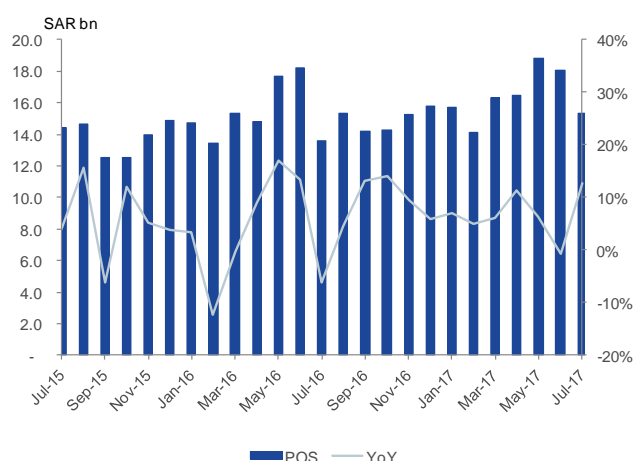
Source: Company data, Al Rajhi Capital



## Consumer spending indicators

POS and ATM data indicated that consumer spending picked up in the month of July. POS transactions jumped 12.8% y-o-y (vs. 0.8% y-o-y decline in previous month), marking the sharpest annual growth in nine months. ATM cash withdrawals grew for the first time in nine months (annual basis), up 2.4% y-o-y in July, versus the fall of 11.4% y-o-y last month. The improvement in consumer spending could be partially attributed to the reinstatement of allowances for public sector employees. Spending growth was primarily seen in the 'Transportation' (+24% y-o-y) and 'Food & Beverages' (+18.2% y-o-y) sectors, while spending in the 'Clothing & Footwear' sector declined (-18.2% y-o-y). Interestingly, on a rolling six month basis, POS transactions on the 'Transportation' and 'Clothing & Footwear' sectors are down 4% and 0.7% y-o-y, respectively, while all other sectors have witnessed an increase in POS transactions.

**Figure 4 Point-of-sale transactions (POS) trend**



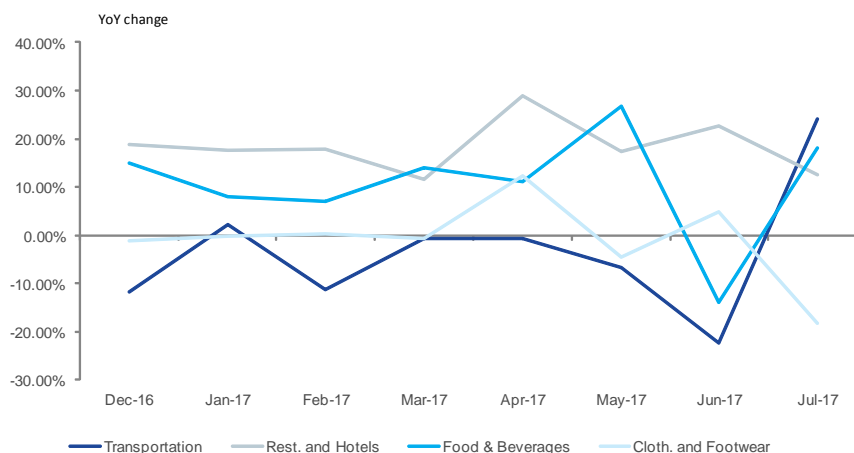
Source: SAMA, Al Rajhi Capital

**Figure 5 ATM cash withdrawals trend**



Source: SAMA, Al Rajhi Capital

**Figure 6 Points-of-sale transactions trend by sectors**



Source: GAS, Al Rajhi Capital



## Reserve assets

Foreign reserve assets in July 2017 declined to its lowest level since May 2011.

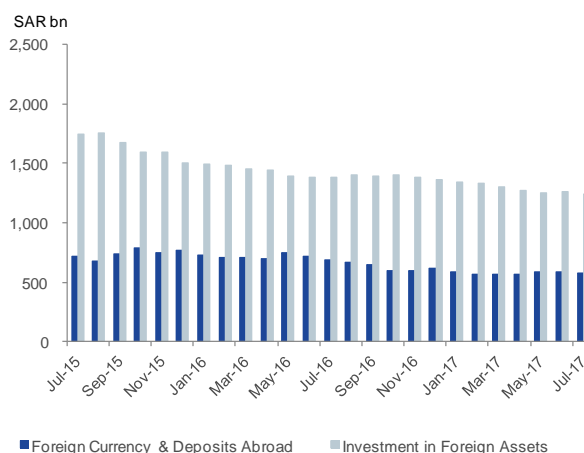
The government continued to drawdown its reserve assets in July, despite raising SAR 17bn via domestic Islamic bonds during the month. After briefly rising in June (+0.3% m-o-m), SAMA's reserve assets slipped by 1.2% m-o-m in July to stand at SAR1,855bn (US\$494.6bn). Govt reserve and deposits at SAMA declined 2% m-o-m and 32% y-o-y to SAR650bn

**Figure 7 Reserves assets**



Source: SAMA, Al Rajhi Capital

**Figure 8 Major components of foreign assets**



Source: SAMA, Al Rajhi Capital

## Credit and deposit growth

Credit growth continued to witness a fall, whereas deposits grew at a faster pace as compared to the previous months

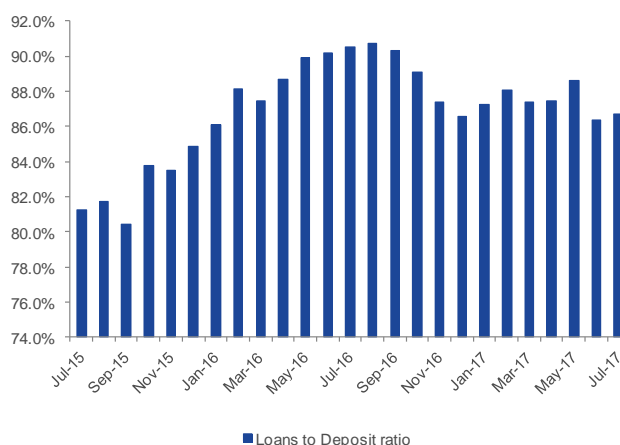
Banking sector credit to the private sector continued to drop for the fifth consecutive month, falling 1.3% y-o-y (compared to 1.4% y-o-y fall in the previous month). On a sequential basis, it was down for the second straight month (-0.1% m-o-m). However, claims on the public sector jumped 25.8% y-o-y, primarily led by increased holding of government bonds. Deposits were up 3.3% y-o-y, though on a sequential basis they declined (-0.3% m-o-m). 'Business and Individual' deposits, which account for over 75% of the total deposit base rose 1.9% y-o-y, while 'Government Entities' deposits jumped 8.8% y-o-y. On a sequential basis, 'Government Deposits' grew 0.9% m-o-m, while 'Business and Individuals' deposits were down 0.5% m-o-m.

**Figure 9 Credit and deposit growth**



Source: SAMA, Al Rajhi Capital

**Figure 10 Loans to Deposits**



Source: SAMA, Al Rajhi Capital



## Money supply

**M3 registered an annual rise for the fourth straight month in July 2017.**

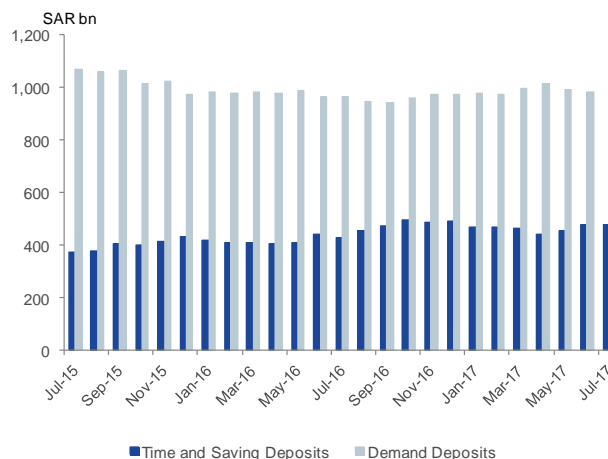
The broader money supply (M3) rose by 2.7% y-o-y in July 2017, its fastest pace since January 2016, to reach SAR 1,802bn, as compared to the 2.6% y-o-y growth witnessed in June 2017. Growth in the M3 indicator picked up due to the rise in demand deposits. On a monthly basis, M3 fell by 1.0% due to other quasi-money deposits, versus a rise of 2.8% last month.

**Figure 11 Money supply growth (y-o-y)**



Source: SAMA, Al Rajhi Capital

**Figure 12 Deposits break-up**



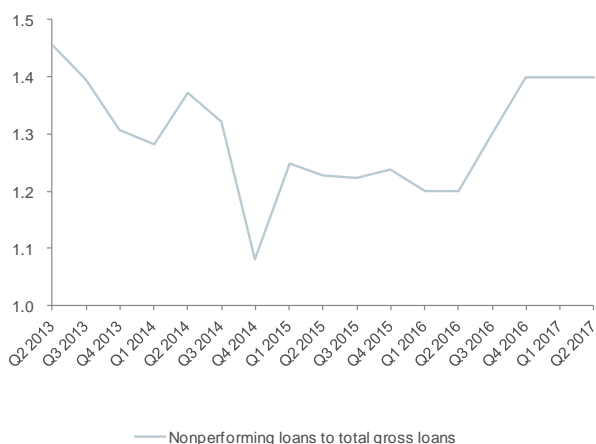
Source: SAMA, Al Rajhi Capital

## Banking Sector

**Banking profits rose in July at the fastest annual pace in six months**

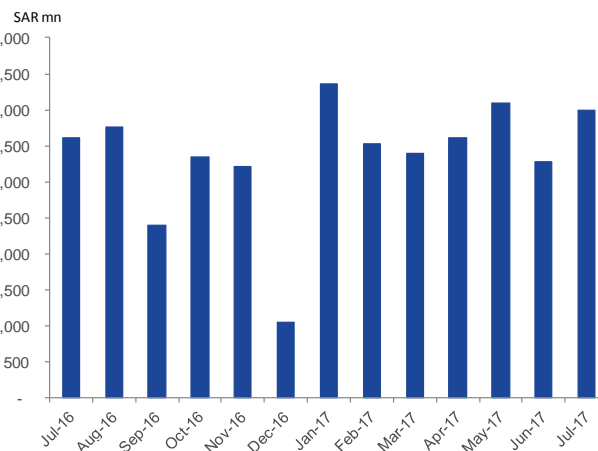
The banking sector profits grew at the fastest rate in six months, up 10.4% y-o-y in July (compared to -13.3% y-o-y in the previous month). The cumulative banking sector profits totaled SAR 26,213mn in 2017, down 1.6% y-o-y. Meanwhile, the non-performing loans to gross loans ratio was stable at 1.4% at the end of Q2 2017, unchanged from Q1 2017.

**Figure 13 Non-performing loans**



Source: SAMA, Al Rajhi Capital

**Figure 14 Net Profit for Banks**



Source: SAMA, Al Rajhi Capital



The index rose on an m-o-m basis, for the second straight month in July 2017

## Inflation dynamics

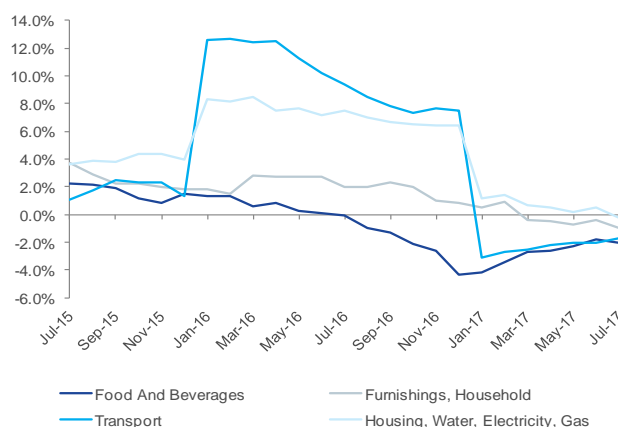
Cost of living index declined 0.3% y-o-y, the seventh consecutive monthly decline on y-o-y basis. All the heavy weight sectors, 'Food & Beverage', 'Transport', and 'Furnishings, Household Equipment & Maintenance' reported a decline in prices on y-o-y basis in July. Despite the rise in POS transaction value, we believe benign global commodity prices are weighing down inflation in the key 'Food and Beverage' sector (21.7% weight). 'Housing, Water, Electricity, Gas, and other fuels' segment (20.5% weight) recorded the first y-o-y decline. Since the utilities segment is regulated (Water, electricity, gas etc), weakness in Housing (real estate and rentals) may be impacting for the sector's inflation. Transport sector (10.4% weight) and Restaurants sector (5.7% weight) inflation may be declining due to cut in discretionary spending by both companies and consumers. Tobacco (0.5% weight) inflation rose 99% y-o-y due to the levy of taxes on harmful products.

**Figure 15 Inflation trend (y-o-y)**



Source: GAS, Al Rajhi Capital

**Figure 16 Inflation drivers (y-o-y)**



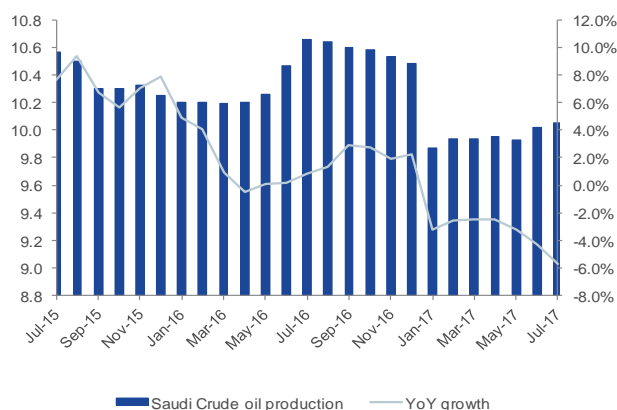
Source: GAS, Al Rajhi Capital

Crude oil production increased on an annual basis in July 2017 to reach 10.05mbpd

## Crude oil dynamics

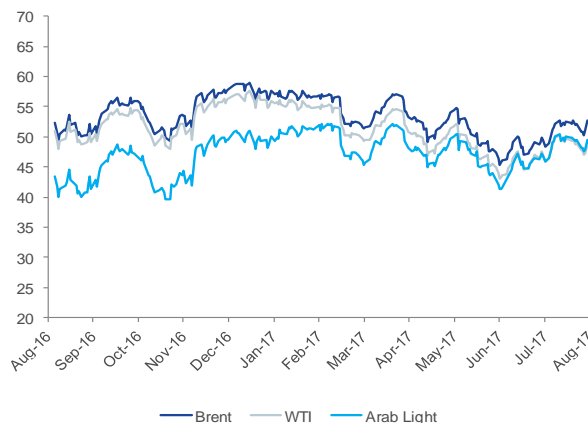
Crude oil production in Saudi Arabia stood at 10.05mbpd in July 2017, indicating a 5.7% y-o-y fall. However, on a monthly basis, crude oil output increased for the second consecutive month in July 2017. Meanwhile, crude oil prices (Brent October futures contract) dropped 0.6% MTD in August 2017, dragged down by concerns over the rise in production from OPEC countries as well as the US. Arab light also declined 3.6% MTD in August 2017.

**Figure 17 Saudi crude oil production trend**



Source: Bloomberg, Al Rajhi Capital

**Figure 18 Crude oil prices trend**



Source: Bloomberg, Al Rajhi Capital



Non-oil exports and imports dropped at a faster yearly pace in June 2017 compared to the previous month

## Non-oil foreign trade

Kingdom's non-oil exports fell 18.9% y-o-y in June. The rate of decline in non-oil exports was faster as compared to the previous month (-9.8% y-o-y). Exports were mainly dragged down by chemical products (-19.4% y-o-y), which contributed 29.9% to the total exports, followed by plastic & rubbers (-3.6% y-o-y), which accounted for 35.3% of the total exports. Further, non-oil imports dropped 29.0% y-o-y in June 2017, as against the fall of 11.3% y-o-y in May. This was mainly because imports of machinery & electrical slipped by 36.9% y-o-y, while that of transport equipments fell by 37.9% y-o-y, which together constituted 40.0% of the total non-oil imports. Meanwhile, as per the latest foreign trade exchange data released by the GASTAT, the Kingdom's total trade volume dropped to SAR 1,214bn in 2016, compared to SAR 1,418bn in 2015. Saudi Arabia's trade volume with the GCC countries recorded a reading of SAR 121.6bn in 2016, as against SAR 127.7bn in 2015.

Figure 19 Non-Oil Exports

Commodities (SAR mn)	Apr-17	May-17	Jun-17	% y-o-y	% m-o-m
Plastics & Rubbers	4,657	4,560	4,259	-3.6%	-6.6%
Chemical Products	3,877	4,215	3,601	-19.4%	-14.6%
Ordinary Metals	1,311	1,362	997	-11.5%	-26.8%
Transport Equipments	1,131	1,125	955	-31.0%	-15.1%
Others	3,488	3,692	2,248	-35.2%	-39.1%
Total	14,464	14,954	12,060	-18.9%	-19.4%

Source: GAS, Al Rajhi Capital

Figure 20 Non-Oil Imports

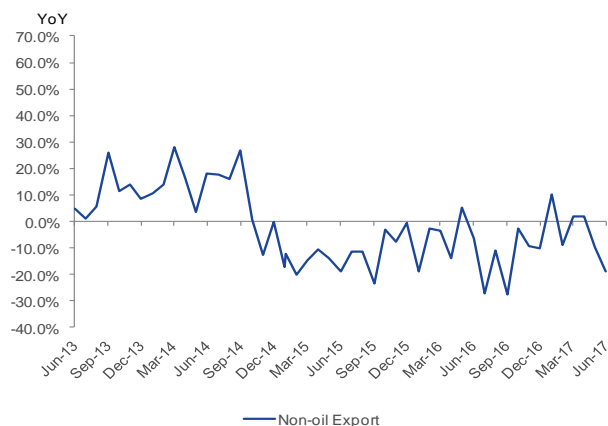
Commodities (SAR mn)	Apr-17	May-17	Jun-17	% y-o-y	% m-o-m
Machinery & Electricals	9,988	10,196	7,188	-36.9%	-29.5%
Transport Equipments	6,207	6,089	5,943	-37.9%	-2.4%
Ordinary Metals	3,935	4,027	3,046	-28.7%	-24.4%
Chemical Products	3,571	3,933	3,077	-23.6%	-21.8%
Others	19,055	19,425	13,538	-20.0%	-30.3%
Total	42,756	43,670	32,792	-29.0%	-24.9%

Source: GAS, Al Rajhi Capital



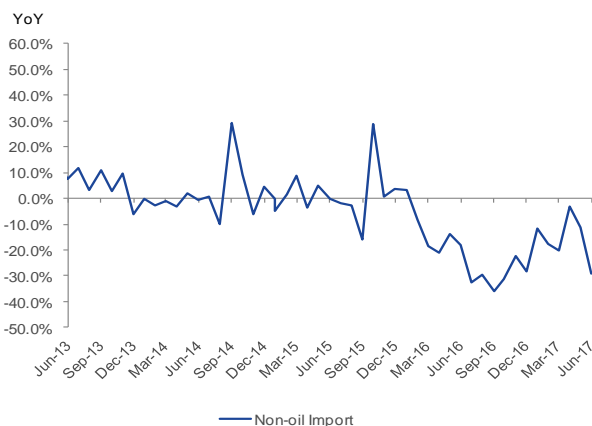


Figure 21 Non-oil export trend (y-o-y)



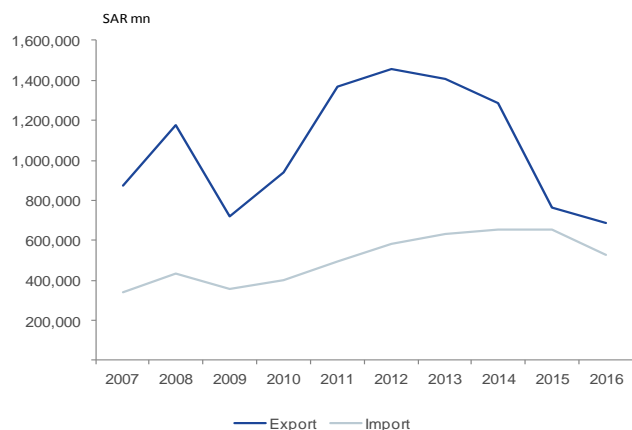
Source: GAS, Al Rajhi Capital

Figure 22 Non-oil import trend (y-o-y)



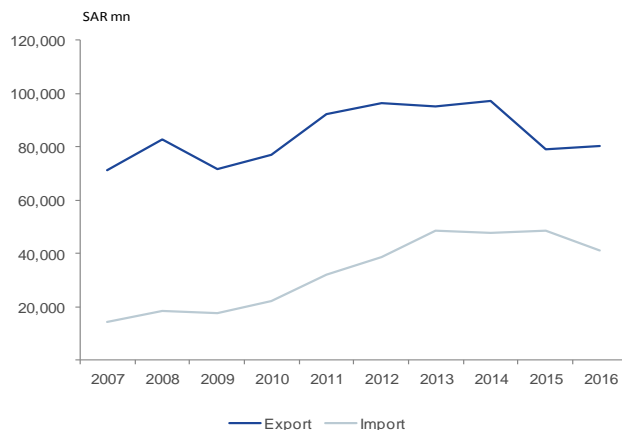
Source: GAS, Al Rajhi Capital

Figure 23 Total Foreign Trade



Source: GAS, Al Rajhi Capital

Figure 24 Trade between KSA and GCC



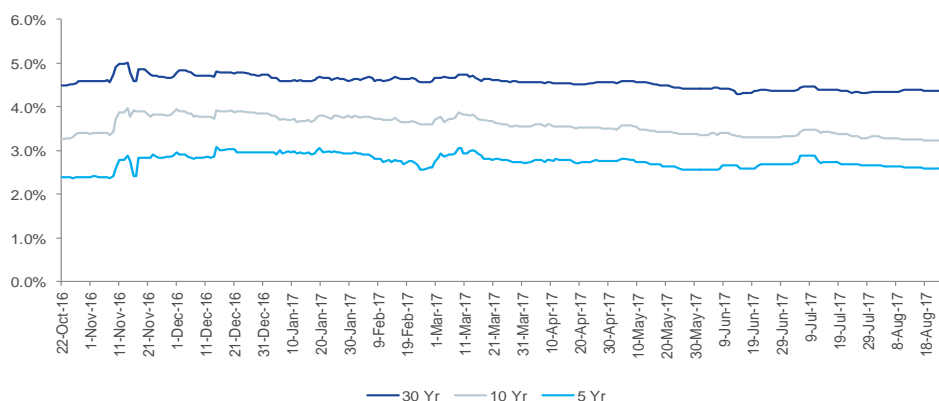
Source: GAS, Al Rajhi Capital

## Saudi International Bond Yields

Saudi International bond yields with lower maturities fell on a MTD

Saudi International bond yields with 30 year maturity rose by 1.5bps MTD, whereas bond yields with 5 and 10 year maturities fell by 11.0bps and 10.8bps.

Figure 25 International Bond Yields



Source: Bloomberg, Al Rajhi Capital





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