May 2016

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Saudi Economic Review

NCB Monthly Views on Saudi Economic and Financial Developments

Contents

Executive Summary

- OPEC organization, led by Saudi Arabia, had already altered its traditional role of managing output to defend price, instead choosing to boost output to defend market share from high cost producers, particularly, US shale producers, thus crushing prices in the process.

- The Japanese yen appreciated the most among the G10, marking a 13.1% YTD upturn, standing at JPY106.4/USD by the end of April.

- Industrial and precious metals rebounded on improving sentiments and a weakening USD. In addition, the demand boost received by copper can also be traced to China's record stockpiling.

- Low oil prices hit the balance sheets of Saudi lenders, bringing the loan-to-deposit (L/D) ratio to its highest levels since 2008 at 87.5%. The range of allowable L/D ratio was extended by SAMA to accommodate for the current liquidity shortage emanating from lower oil revenue and heavy government withdrawals.

- By the end of April, QFIs held less than 0.1% of shares in Tadawul which prompted the CMA to review the acceptance criteria. Accordingly, the CMA widened the scope of institutions under the QFI definition to include sovereign wealth funds, university endowments among others.

- Despite the ambitious economic and social reforms announcement in the Kingdom's vision for the year 2030, Moody's credit rating agency joined S&P and Fitch in downgrading Saudi Arabia's long-term credit rating from Aa3 to A1. This reflects concerns over the country's ability to diversify away from oil, and carry out promised reforms.

- As more resources are geared toward servicing the non-oil sector, we expect to see more diversification in non-oil exports which in turn should reduce the susceptibility of non-oil trade to oil downturns.

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View of the Month

Over the coming weeks, the finalized National Transformation Plan figures will be released which will provide further subsidy reforms, fees on exceeding foreign labor limits, greencard-like program, value-added tax, and "white land" tax among other measures totaling an estimated USD100 billion of additional non-oil revenues by 2020. The vision also includes an increased role for the private sector to drive the economy forward as its contribution to GDP is planned to increase to 65% of GDP.

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Macroeconomic Indicators

	2011	2012	2013	2014P	2015F	2016F
Real Sector						
Average KSA Crude Spot Price, Arab Light, USD/BBL	108.1	110.2	106.4	97.2	50.2	50.0
Average Daily Crude Oil Production, MMBD	9.3	9.8	9.6	9.7	10.2	10.2
GDP at Current Market Prices, SAR billion	2,510.7	2,752.3	2,791.3	2,826.9	2,449.6	2,346.6
GDP at Current Market Prices, USD billion	670.4	734.9	745.3	754.8	654.1	626.6
Real GDP Growth Rate*	10.0%	5.4%	2.7%	3.6%	3.4%	2.1%
CPI Inflation, Y/Y % Change, Average	3.7%	2.9%	3.5%	2.7%	2.2%	2.7%
External Sector						
Current Account Balance, USD billion	158.5	164.8	135.5	76.9	-41.3	-47.4
Current Account Balance/GDP	23.6%	22.4%	18.2%	10.2%	-6.3%	-7.6%
Net Foreign Assets with SAMA, USD billion	535.9	648.5	717.7	725.2	640.2	580.4
Fiscal Sector (Central Government)						
Actual Revenues, SAR billion	1,117.8	1,247.4	1,156.4	1044.4	608.0	629.1
Actual Expenditure, SAR billion	826.7	873.3	976.0	1140.0	975.0	897.0
Expenditure Overrun, %	42.5%	26.6%	19.0%	33.3%	13.4%	6.8%
Overall Budget Balance, SAR billion	291.1	374.1	180.3	-95.6	-367.0	-267.9
Budget Balance/GDP	11.6%	13.6%	6.5%	-3.4%	-15.0%	-11.4%
Break-Even Oil Price	75.3	73.9	82.6	103.6	79.2	69.2
Financial Sector						
USD/SAR Exchange Rate	3.75	3.75	3.75	3.75	3.75	3.75
Growth in Broad Money (M3)	13.3%	13.9%	10.9%	11.9%	6.8%	6.6%
Growth in Credit to the Private Sector	11.0%	16.4%	12.1%	11.9%	6.8%	5.2%
Average 3M SAR Deposit Rate	0.7%	0.9%	1.0%	0.9%	1.0%	1.4%
Average 3M USD Deposit Rate	0.3%	0.4%	0.3%	0.3%	0.4%	0.7%
Spread, in Basis Points, SAIBOR-LIBOR	40.9	55.2	68.7	69.5	60.0	70.0

Sources: Thomson Reuters, SAMA, and NCB

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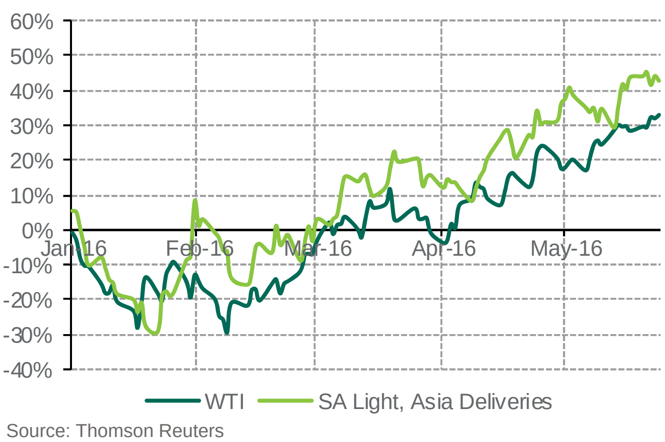
Oil Market

Crude Prices Flirt with 50s

Brent crude already tested the USD50 a barrel level, and WTI crude reached USD49 a barrel last week, boosted mainly by supply concerns, marking the highest levels since October 2015. As the oil market is rebalancing with prices likely to move in the USD50-60 a barrel range, it is not expected to return to the USD100 a barrel level again in the medium term. Oil supply disruptions have risen to unprecedented levels in May and just as outages appeared to be abating, new concerns emerged, keeping prices elevated. While Canadian oil sand producers were set to operate, the wildfires changed course, creating evacuations and preventing workers from returning to certain facilities. In Nigeria, Exxon restarted Qua Iboe production, only to have access to the export terminal temporarily blocked by locals. Although disruptions are not easy to predict, outages are expected to decline in the coming months assuming wildfires in Canada subside and oil sands producers resume operations. In turn, disruptions will likely fall from the current levels and accordingly will put downward pressure on prices over the near term.

Chart 1: Oil Price Developments, YTD

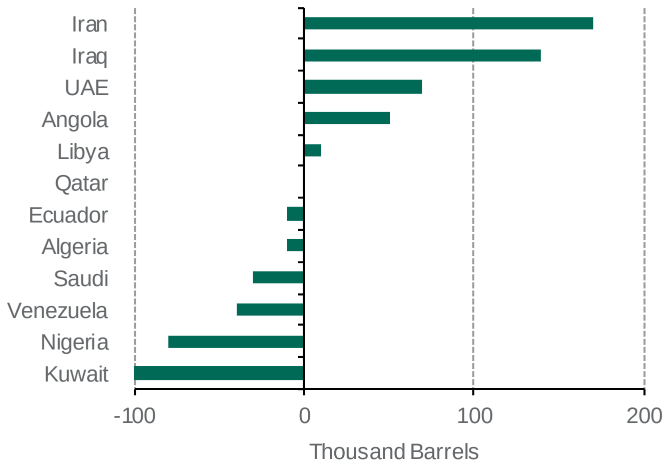


Source: Thomson Reuters

OPEC organization, led by Saudi Arabia, had already altered its traditional role of managing output to defend price, instead choosing to boost output to defend market share from high cost producers, particularly, US shale producers, thus crushing prices in the process. This new policy seems to be working, as prices have rallied by 80% from a 12-year low in January, but still very early to assume complete success. While oil price is recovering from its steep decline since OPEC's November 2014 meeting, it is trading far below a fair price that is necessary to make investment in oil exploration and expansion feasible. Meanwhile, the group, which contributes nearly 40% share of world's oil supply, will meet in Vienna on June 2nd, but it is not expected that there will be any shift in its policy.

On the supply side, OPEC crude output rose by 0.33mb/d in April to 32.76 mb/d, as a jump in Iranian output and a boost in supply from Iraq and UAE more than offset outages in Kuwait and Nigeria. Saudi production remained steady at 10.2mb/d. Iranian supply rose to 3.56mb/d, a level last seen in November 2011, before sanctions were introduced. Moreover, Iran's oil exports recovered strongly, touching 1.9mb/d, just 0.3mb/d short of the 2.2mb/d pre sanction level in 2011. Iran targets oil exports to reach 2.2mb/d by the end of summer. In Iraq, crude output has jumped, reaching 4.36mb/d in April, up 0.17mb/d m/m, according to IEA. Its exports also reached near-record levels at 3.87mb/d last month including output from the Kurdish region. While Iran and Iraq boost their exports, Nigerian oil exports fell sharply. The Niger Delta Avengers (NDA) have carried out a number of attacks already this year, causing major supply disruptions, which recently brought output to its lowest level in a long time at 1.4mb/d from 1.9mb/d at the beginning of the year. Elsewhere, rebel attacks in Colombia and an earthquake in Ecuador led to pipeline disruptions, while an agreement was reached in Libya, allowing the restart of oil exports from the eastern port of Hariga. On the demand side, the IEA revised global oil demand growth for the 1Q' 2016 upwards to 1.4mb/d, led by strong gains in India, China and Russia. For the year as a whole, demand growth is forecast at 1.2mb/d, with demand reaching 95.9mb/d.

Chart 2: OPEC's Monthly Oil Production Changes



Source: OPEC Survey

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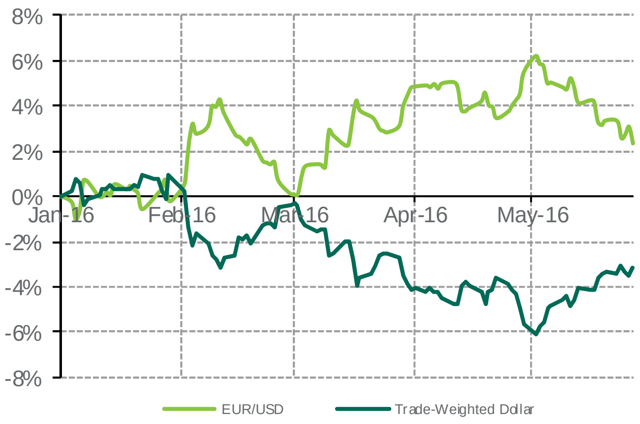
Foreign Exchange

Greenback to Resume Strengthening

A growing concerned tone at the Fed echoed through financial markets in April, notably after skipping one of the four rate hikes originally planned for this year. On the other hand, a more aggressive QE program at the ECB is reshaping the outlook on the EUR/USD pair. Weaker year-to-date performance for global equity markets allowed the JPY to appreciate on safe-haven seeking. Despite sharp sell-off in emerging and developing market currencies in January, we see a noticeable recovery contemporizing with oil prices gaining a footing into the high forties.

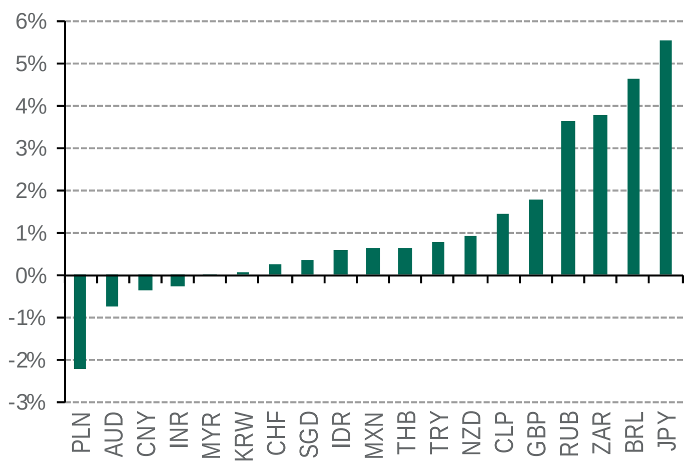
Chart 3: Trade-Weighted Dollar and the Euro



Source: Thomson Reuters

The US economy has let off some steam at the turn of the year as the 2016 GDP forecast by the IMF rests at 1.9%. Despite the most impressive US job growth in a decade, larger disposable income from cheaper energy and commodity prices, and global spillover had capped gains for the greenback. The slowdown in China and other emerging countries would affect the external balance for the US economy amid a stronger dollar. Therefore, trade and financial linkages may impede the acceleration of the Fed monetary normalization process. The Fed rate hike postponing alleviated pressure off the USD and offered its currency peers a respite. The retrenchment of oil drilling activity in the US is encouraging lesser investment in the shale industry, contributing to the slowdown of capital repatriation. The trade-weighted USD ended the month of April 1.6% lower than March. Our view remains constructive on the dollar due to strong economic fundamentals, and we expect the currency to resume strengthening as the rate hike rhetoric intensifies during the second half of the year. The EUR strengthened on the back of increased ECB stimulus which went up to EUR80 billion/month from EUR60 billion/month. Divergent monetary policy dynamics between the Fed and the ECB are yet to materialize as the Fed remains fairly accommodative at a funds rate of 0.5%. The ECB maintained negative rates on deposits as it attempts to fix the transmission mechanism for European banks, penalizing excess reserves and encouraging lending. In April, the EUR appreciated by 5.5% YTD, standing at USD1.15. The EUR/USD rally throughout March and April was driven by assessment of relative central bank policy, reflecting investor sentiments and their positioning. Despite strong buying of the single currency, we maintain a fundamentally bearish driven outlook emanating from the challenges facing the European union. The British exit scenario is seen to have a negative overall impact on the currency as a British precedence might lead to a union-wide domino effect. The Inflationary prospect remains negative due to lack of price pressures from commodities and energy, although we expect inflation to edge higher to 1.1% in 2017 due to base effect and improving oil outlook.

Chart 4: Monthly Foreign Exchange Rate Changes



Source: Thomson Reuters

The Japanese yen appreciated the most among the G10, marking a 13.1% YTD upturn, standing at JPY106.4/USD by the end of April. The Bank of Japan (BoJ) is preparing an additional round of quantitative and qualitative easing with negative interest rates if the country's inflation level fails to move towards the bank's target of 2%. The consumption tax currently slated for April 2017 will temporarily push inflation above target but underlying inflationary pressures will remain muted. Battling the deflationary mindset in Japan, Mr Kuroda might push policy rate deeper into negative territory in order to entice more lending.

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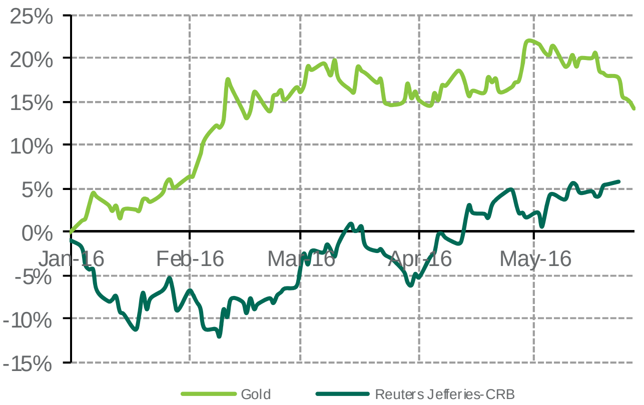
Commodities

Second Fed Hike May Derail Recovery

Commodities extended March's bull run into April reaching YTD highs. A more dovish tone at the Fed and constructive views on oil softened the outlook on commodities, allowing them to bounce back to positive territory. Despite abundant supply and slowing global industrial demand, by the end of April, the Reuters/Jeffries CRB index climbed 4.8% YTD, standing at 184.6. Industrial and precious metals rebounded on improving sentiments and a weakening USD. In addition, the demand boost received by copper can also be traced to China's record stockpiling. According to China's general Administration of Customs, a surge in China's copper stockpiling in March of which cargoes weighed 570,000 tons helped bid up the red metal's prices. China's share of global metal consumption rose above 50% in 2015, and although the country is rebalancing its economy, we continue to view China's economic performance as a main driver for metal base prices. The difference between domestic and foreign prices encouraged arbitrage, and as a result, inventories of the Shanghai Futures Exchange are higher than the London Metal Exchange for the first time in over a decade. On the supply side, high cost producers are halting aluminum production due to squeezed margins despite support from low energy prices. Copper prices stood at USD5,050/ton by the end of April, upturning by 7.3% YTD, while aluminum prices surged 11.4% in the same period, standing at USD1,679/ton. Downside risks include slowing Chinese end-use consumption and the Fed's second rate hike, possibly in June.

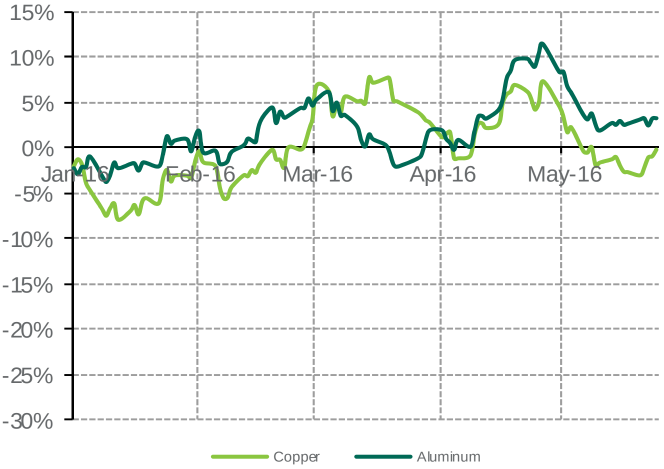
Chart 5: Reuters Jefferies vs. Gold



Source: Thomson Reuters

Gold prices breached the USD 1,200 level in February on the back of postponed Fed action. Intensified financial speculation largely attributed to the British Euro exit referendum also provided support for the yellow metal which ended April 21.9% higher YTD, standing at USD1,294.1/oz. Support above the USD1,200 level should remain throughout the year as the adoption of negative interest rates by many central banks, namely the BoJ and the ECB, should increase the attractiveness of gold as a hedge against the depreciation of financial assets. On the other hand, rising interest rates in the US during the second half of the year hold negative implications for gold as investors will seek to hold yield-bearing assets. Physical demand on gold remains weak in the largest gold markets in the world; India and China. Government restrains on gold imports including the levy of a 1% tax on jewels is a drag on local Indian demand. In China, slower economic activity is trickling down to demand which was exacerbated by the New Year holidays.

Chart 6: Base Metals



Source: Thomson Reuters

Agricultural commodities are expected to see a modest price recovery from last year as global demand strengthens. The Goldman Sachs Agricultural index stood at 305 by the end of April, an upturn of 7.6% YTD. El-Nino affected areas such as Southeast Asia will likely see price pressures, mainly in rice and wheat. However, due to the geographic limitation of the event, we do not expect to see a lasting global impact on prices. By the end of April, the Chicago Board of Trade wheat futures maintained prices unchanged at 478 cents/bushel, while corn futures prices rose 7.1% to 390.3 cents/bushel.

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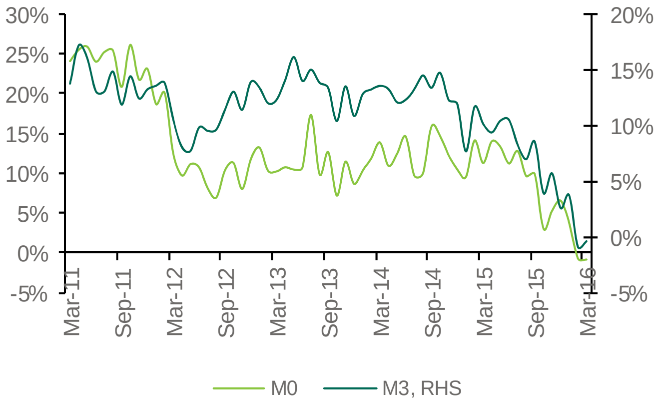
Money & Inflation
Liquidity Concerns as Deposits Fall

The monetary situation in the Kingdom continues to decline as both the monetary base (M0) and broad money (M3) shrink on an annualized basis. By the end of the first quarter of 2016, the monetary base recorded a negative Y/Y growth of 0.8% at SAR298.2 billion, and broad money supply inched down by 0.4% Y/Y standing at SAR1.78 trillion. Looking at the components of the monetary base, we find that the largest decline came from heavy withdrawals from public financial institutions where deposits with SAMA shrank to almost a quarter over the past twelve months. Deposits of public financial institutions stood at SAR2.4 billion, down by 73.8% Y/Y while local bank deposits inched down for the first time in over a decade. Low oil prices hit the balance sheets of Saudi lenders, bringing the loan-to-deposit (L/D) ratio to its highest levels since 2008 at 87.5%. The range of allowable L/D ratio was extended by SAMA to accommodate for the current liquidity shortage emanating from lower oil revenue and heavy government withdrawals. The depositary base on which Saudi banks' lending capacity relies comprises mainly of demand deposits by around 55.4%. Demand deposits fell below SAR 1 trillion in November last year, standing at SAR985.4 billion by the end of 1Q2016. By annual comparison, demand deposits declined 6.2%, notably pulling M1 money supply down by 5.2%. In contrast, time and saving deposits displayed an annualized growth of 7.2% to SAR412.4 billion, softening the blow for M2 money supply, declining by 2.2% Y/Y.

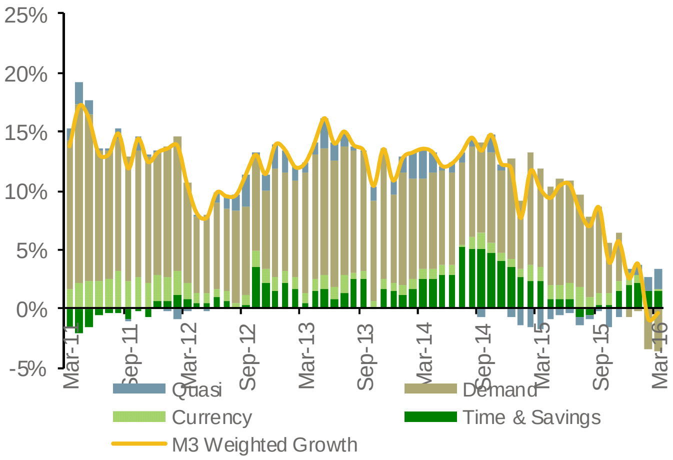
Chart 7: Growth in Monetary Aggregates



Sources: SAMA and NCB Estimates

Quasi monetary deposits were the only component in the Saudi money supply that registered a double-digit surge in Q1, rising by 15.4% Y/Y. Standing at SAR 211.3 billion, quasi monetary deposits consist of deposits of foreign currency at 85.8%, letters of credit at 8.4%, outstanding remittances at 5.7% and repo transactions at 0.1%. The largest contribution to quasi monetary deposits came from deposits of foreign currency which rose by a staggering 17.3%, the highest rate since May 2013 to reach SAR 181.3 billion. By the end of 1Q2016, local banks' holdings of SAMA bills fell by a record low of 64.1% Y/Y to SAR 80.9 billion, contrasting with an annualized 120.5% surge in government bonds to SAR120.6 billion.

Chart 8: Money Supply, Contribution



Sources: SAMA and NCB Estimates

Inflation levels in the Kingdom are trending higher since January after much of the energy and utility subsidies were revised. In March, the Cost of Living index recorded the highest annualized surge since the index was rebased to 2007 prices. Food and beverages which account for 21.7% of the consumer basket posed low inflationary pressures as they edged up 0.6% from last year. On the other hand, utilities, and transportation surged by triple digits, contributing to most of the gain in the index. Average water supply prices surged by 189.6%, and electricity bills were up 14.3%. The transport category surged by 12.4% Y/Y affected by a 61.7% Y/Y rise in fuel prices. It is also worth-noting that insurance prices surged 16.4%on the back of auto vehicle insurance rising 24.2%. On the other hand, the hospitality sector was under downward price pressures emanating from cheaper commodities. Prices at restaurants, cafés and their likes slid 4.4% Y/Y while accommodation services fell 4.7% Y/Y.

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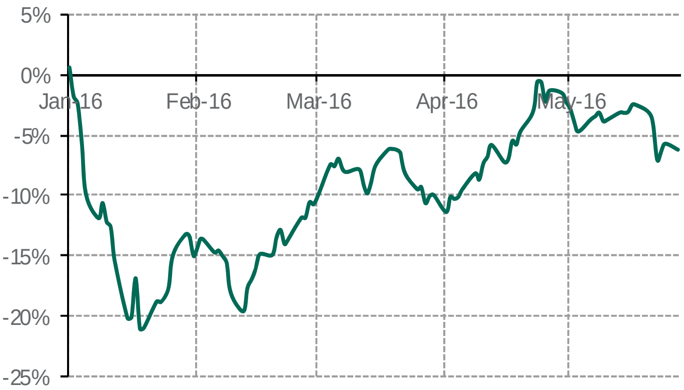
Capital Markets
Continuous Development

The Saudi economy has been anticipating the announcements of transitional programs to overhaul the Kingdom and break its reliance on oil. Since the budget announcement in December, the government's intent on creating the building blocks for a sustainable future was evident by swift decisions to contain the economy's deficit. During early April, it was announced that Saudi Vision 2030 will be revealed later during the same month, see Special Focus. By the same token, the Capital Market Authority (CMA) has been actively seeking to develop the local stock market to attract local and international investors. Under the strategy, Tadawul's market capitalization is projected to double within seven year to match the size of the domestic economy. Additionally, Tadawul is aiming to be the most active primary market by increasing listed companies to 250 from the current 170, including the listing of oil giant Saudi Aramco. Furthermore, trading hours have been extended by 30 minutes to increase daily trading volumes which have subdued to a YTD average of SAR5.7 billion, down from an average of SAR6.6 million last year. Tadawul is also aiming to establish an equity market for small-to-medium enterprises early 2017 to deepen and develop Saudi equity markets and provide an alternative financing route for local businesses.

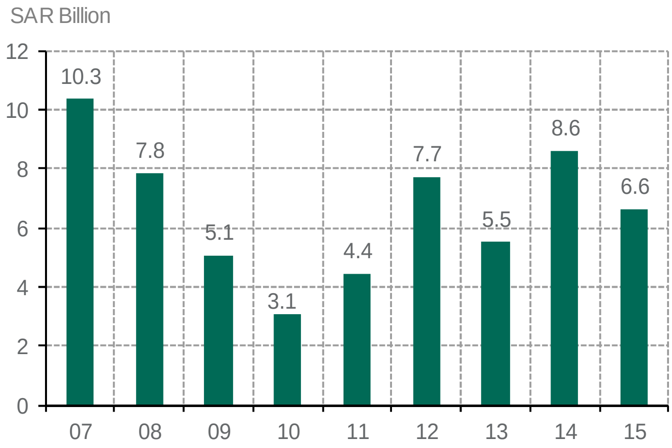
Chart 9: Tadawul All-Share Index



Source: Tadawul

Opening the market for qualified financial institutions (QFI) in June 2015 was intended to attract foreign capital and provide much needed stability while targeting an inclusion into MSCI indices. By the end of April, QFIs held less than 0.1% of shares in Tadawul which prompted the CMA to review the acceptance criteria. Accordingly, the CMA widened the scope of institutions under the QFI definition to include sovereign wealth funds, university endowments among others. Additionally, the minimum value of assets under management has been lowered to USD1 billion from USD5 billion. Also, the previous limitations on trading have been unified under one constraint which is that one QFI investor may not reach 10% ownership of a single listed company. Meanwhile, the limitation on all foreign ownership (resident and non-resident) will remain at 49%. In order to mirror international practices, Tadawul will implement a (T+2) settlement cycle for stock transactions which is widely used in Europe and is under consideration for US markets. Moreover, an introduction of securities lending and covered short selling has been approved by the CMA. The new decisions will be implemented within the first half of 2017.

Chart 10: Average Daily Traded Value



Source: Tadawul

Driven mainly by the announcement of Saudi Vision 2030, Tadawul posted a rise of 9.4% to reach 6'805.84 during the month of April. On a sectoral level, the industrial investment sub-index registered the highest gain at 19.8% followed by the hotel sub-index at 18.9% during April. The least performing sector was telecommunication which edged higher at 0.5% M/M. The bull oil market underpinned a rise in petrochemical stocks, gaining 14.2% as oil prices hovered near USD50/bbl. Going forward, the market will remain volatile despite the recent fiscal and budgetary measures, Moody's was the latest rating agency to downgrade the Saudi economy by one notch to A1 from Aa3. Stock investors' sentiments are more inclined to be affected by the short-term pain of current low oil prices. However, we believe that the Saudi equity market holds attractive entry points for long term investors to benefit from government reforms.

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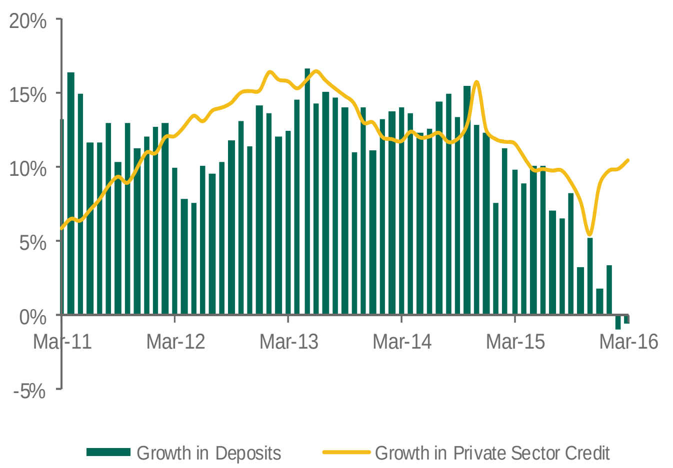
Loans Market

Strong Growth Despite Shrinking Deposits

As the depositary base in Saudi banks shrinks due to lower oil revenues, the credit market adequately reflects tighter conditions. Due to the conventional nature of credit in the Kingdom which is deposit based, the decline in deposits led to a surge in the loan-to-deposit ratio (L/D), raising concerns over an underlying liquidity squeeze. Despite the ambitious economic and social reforms announcement in the Kingdom's vision for the year 2030, Moody's credit rating agency joined S&P and Fitch in downgrading Saudi Arabia's long-term credit rating from Aa3 to A1. The attitude of these credit rating agencies reflect their concerns over the country's ability to diversify away from oil, and carry out promised reforms. Lower growth rate, higher debt, and less capital buffers could mean less shock absorption for the Saudi financial system than previous years. SAMA's policy response has so far included more relaxed macro prudential policies manifesting in raising the allowed L/D ratio from 85% to 90%. By the end of 1Q2016, the L/D ratio stood at 87.5% as banks continued to expand their credit portfolio holdings in order to maintain credit growth amid dwindling deposits.

Chart 11: Private Sector Financing



Sources: SAMA and NCB Estimates

The consolidated balance sheet of all Saudi banks compiled by SAMA indicates that total deposits ticked down by 0.6% Y/Y by the end of March, standing at SAR1.6 trillion. Demand deposits constitute the bulk of deposit types at 61.2%, highlighting depositors' preference amid very low interest rates on deposits. March figures of demand deposits saw an annualized downturn of 6.2% to SAR985.4 billion. The decline can be traced to deposits made by businesses and individuals falling by 7.1% Y/Y. On the other hand, time and savings deposits grew by 7.2% Y/Y, totaling SAR412.4 billion. The surge in this type of deposits also is due to a 26% Y/Y surge by businesses and individuals; in a response to the slowing momentum of economic activity in the Kingdom. Quasi monetary deposits notably rose 15.4% Y/Y to SAR211.3 billion on the back of increased foreign currency deposits by 17.3% Y/Y.

Chart 12: Liquidity and Risk Detector

Source: Thomson Reuters

On the asset side, total bank credit was up by 9.8% Y/Y, totaling SAR1.4 trillion. Discounting credit to public sector enterprises, total credit to the private sector continued to display a strong growth of 10.5% Y/Y, standing at SAR1.37 trillion. The rising disparity between strong credit growth and shrinking deposits puts a lot of pressure on SAMA as a banking regulator that has an inherent limitation on its monetary policy given the currently fixed peg of the SAR to the USD. Possible scenarios in the second half of the year could include either or all of these actions: 1) Further relaxing the L/D ceiling imposed by SAMA to reach or surpass 100%, on par with other Gulf states. 2)Repatriating some of Saudi banks' investments abroad which are currently valued around SAR159.6 billion, and 3)relaxing statutory deposits currently standing at SAR94.8 billion. The Saudi interbank rate captures the level of stress in liquidity as the 3-month Saudi Interbank Offered Rate (SAIBOR) stood at 2.1% by the 19th of May, the highest rate since January 2009. The spread between the LIBOR and SAIBOR widened to 149 bps in May, the highest since November of 2008. The divergence fundamentally goes back to the Fed's continued accommodative stance as no Fed rate hike took place since December, leaving LIBOR relatively flat. In contrast, concerns over a liquidity squeeze among Saudi banks prompted SAIBOR to rise abruptly.

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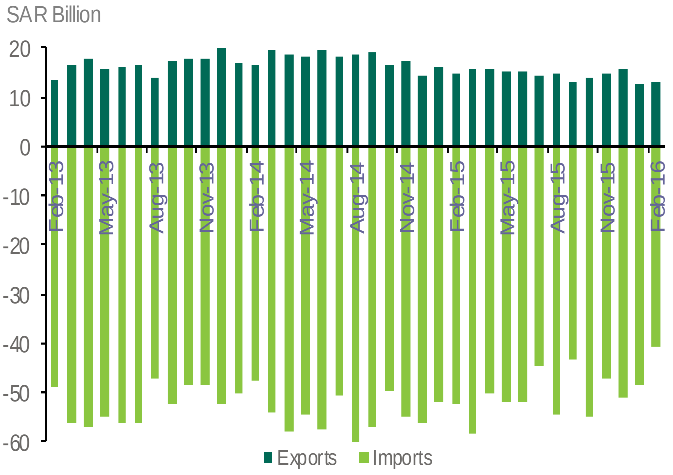
External Trade

Consolidation Measures Hit Non-Oil Trade

Increased government reliance on non-oil GDP comes at a time of declining returns from oil. The new paradigm shift the Kingdom aims to achieve by the year 2030 has a major impact on non-oil trade. As more resources are geared toward servicing the non-oil sector, we expect to see more diversification in non-oil exports which in turn should reduce the susceptibility of non-oil trade to oil downturns. In the month of February, sales from plastic and petrochemical exports accounted for 55.7% of non-oil exports which are largely correlated with oil markets. In addition to the oil story which began its downhill journey in the second half of 2014, the slowdown in China weighed on demand for the Kingdom's non-oil exports which are used as raw or intermediate material in Chinese manufacturing. According to the General Authority of Statistics' monthly bulletin, non-oil exports slid 11.2% Y/Y in February, to SAR13.1 billion. Imports-wise, the Kingdom's deficit reduction efforts have hit the import bill, leading it to fall by 22.4% Y/Y at SAR40.7 billion.

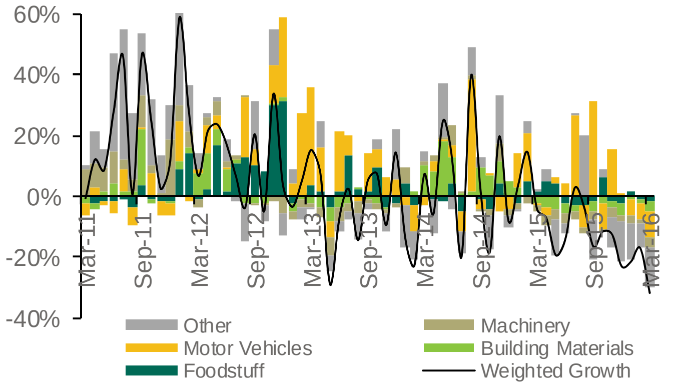
Chart 13: Saudi Non-Oil Trade Balance



Sources: SAMA and NCB

By composition, exports of plastics accounted for 30.3% of the monthly total, valued at SAR3.97 billion. Compared to the same period last year, we notice a significant 18.2% decline in value which is in line with falling energy prices as well as global industrial demand. Exports of petrochemicals, which make up 25.4% of the monthly total value, slid 9.2% Y/Y to SAR3.3 billion. Moreover, base metal exports tumbled 13.5% Y/Y to SAR 1.1 billion. By destination, the UAE ranked at the top accounting for 16.5%, followed by China accounting 8.6%, and Bahrain accounting for 5.5%. The value non-oil exports to the UAE reached SAR 2.2 billion upturning by 6.7% Y/Y contrasting which exports to china tumbling by 33% to SAR 1.1 billion. Exports to Bahrain overtook Singapore and India in February as the third largest export destination with a value of SAR727 million, rising by 8% Y/Y.

Chart 14: Attribution Analysis of Letters of Credit Opened



Sources: SAMA and NCB

On the import side, the value of imports of machinery and electrical equipment slid by an annualized 24%, reflecting the state of moderation in economic activity in the Kingdom. The sizeable chunk this category represents at SAR11.2 billion accounts for 27.5% of the monthly bill pushing imports to the lowest levels YTD. Imports of transport equipment tumbled 26.8% Y/Y to SAR7.1 billion while imports of chemical products slid 10.4% to SAR4.1 billion. Imports by source country show that China still dominates by accounting for 15.7% of the imports share at SAR6.4 billion. Compared to same period last year, however, imports from China tumbled 24.4% on the back of weaker demand. Imports from the US which account for 12.4% of the monthly import bill totaled SAR5 billion, falling by 27.5% Y/Y. Furthermore, imports from Germany were valued around SAR2.8 billion, declining by 13.9% from last year. In March, settled letters of Credit (LCs) for imports financed through banks marked the largest decline since August 2013 totaling SAR16.6 billion. Drastic declines among the largest categories, motor vehicles, machinery, and building materials were the main culprits in the downturn. LCs for motor vehicles dwindled 40.8% Y/Y to SAR3.2 billion while LCs for machinery halved from a year ago to just SAR944 million. LCs for building materials fell 24.5% to SAR1.7 billion.

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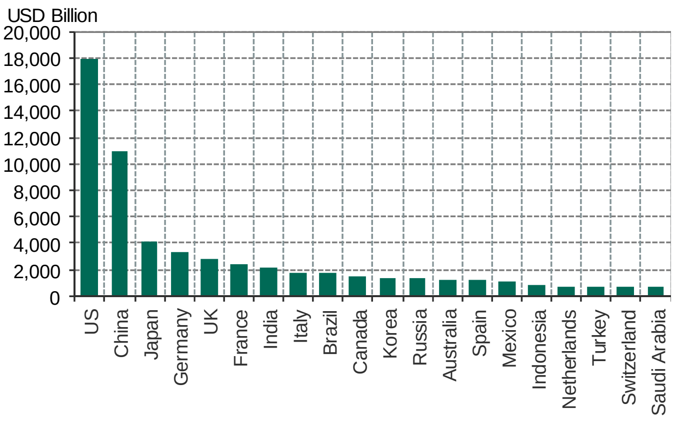
NCB الأهلي

Special Focus:
Saudi Vision 2030

Over the course of the nation's history, inflation adjusted oil prices are experiencing the second collapse which prompted the Saudi government to devise the means to end the dependence on this inherently volatile commodity. Recently, there has been an acceleration in reforms to contain the country's deficit amidst the decline in oil prices. Saudi Vision 2030 provides the blueprint to move away from an oil-centric economy and vital to that is diversifying the economy in every sphere: economic, human and social. The vision is targeting sustainable economic development for the Kingdom with multiple social and economic programs depending on three pillars, being the heart of the Islamic world, being identified as an investment powerhouse, and exploiting the strategic geographical location of the country. The cumulative outcome of these programs is expected to increase Saudi's size by almost twofold to overcome the likes of Switzerland, Turkey, and Mexico to achieve the target of being the 15th largest economy. This will largely be realized by raising non-oil revenues from SAR163 billion in 2015 to over SAR500 billion in 2020, the first milestone towards 2030's SAR1 trillion target, to serve as the main economic driver for the future of Saudi.

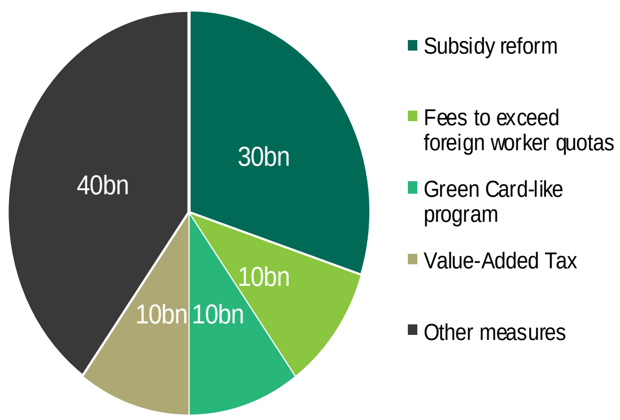
Chart 15: Top 20 Economies, 2015



Source: IMF

Over the coming weeks, the finalized National Transformation Plan figures will be released which will provide further subsidy reforms, fees on exceeding foreign labor limits, greencard-like program, value-added tax, and "white land" tax among other measures totaling an estimated USD100 billion of additional non-oil revenues by 2020. The vision also includes an increased role for the private sector to drive the economy forward as its contribution to GDP is planned to increase to 65% of GDP. SMEs will continue to receive the much needed support through easing regulations and greater access to funding as their contribution to GDP is planned to increase from 20% to 35%. In addition, the social aspect of the vision is targeting a decrease in the unemployment rate to 7% as well as increasing the female participation rate to 30% through providing jobs for Saudis, namely 1 million jobs in the retail sector and 90'000 jobs in the mining sector. The government target of increasing home ownership from 47% to 52% by 2020 implies adamancy to mitigate the housing shortage that had constituted a challenge over the last two decades. The government is also aiming to improve the quality of life by implementing various social programs which will target having three Saudi cities in the top 100 global ranking.

Chart 16: Additional Non-oil Revenues by 2020



Sources: Bloomberg

Furthermore, the investment focus going forward will result in building the largest sovereign wealth fund with a value of SAR7 trillion, the backbone to raise investment income higher than oil revenues by 2030. The privatization programs will offload government entities to the public to increase transparency and efficiency, such as Aramco, the crown jewel of government assets. However, the fund will allocate 50% of its portfolio in international investments to reach the colossal target. The spillover effects will aid local and international businesses to contribute and prosper in a more welcoming environment as foreign direct investment is expected to reach 5.7% of GDP in 2030, up from the current 3.8%. Saudi Vision 2030 is a grand attempt at overhauling an aging economy that has been struggling to break the reliance on oil. The ambitious plan would benefit from higher oil prices to speed up the decoupling process, rather than impede it, with Saudi targeting a far more sustainable economic direction.

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