NCB

April, 2014
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Saudi Economic Review

NCB Monthly Views on Saudi Economic and Financial Developments

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Executive Summary

- On a fundamental basis, assuming no further escalation in Ukraine situation, Brent prices are set to drift lower over the coming weeks from current levels above USD108/bbl.

- It is expected that the German inflation rate, which currently stands at an annualized 1.24% will prevent the overall rate for the European region from being dragged into deflation.

- In contrast with a stronger dollar, gold slipped on the back of brewing expectations that the Fed might be hiking rates soon. Absence of such revelation in the FOMC meeting, however, helped bringing gold back on a positive trajectory.

- Points of sale (POS) transactions, which is used as a proxy to gauge retail activity, indicates that consumers' confidence remains solid. Growth last year averaged 18.4%, given the buoyant state of the market, sales topped last year by 7.6% in February this year despite the higher baseline.

- The primary market is stagnant this year but is set to witness the largest IPO in Tadawul's history. The National Commercial Bank's (NCB) long awaited listing is underway as they plan to sell 15% to the general public.

- Short-term credit lines still represent the bulk of credit extended by local banks advancing from last year by 8.5%. In retrospect, the rise in longer maturity loans is a result of a more regulated market with reduced risk factors.

- The recent turn of events in China, the largest recipient of exports, led to a decreased manufacturing activity, which weighed heavily on demand for base metals globally, namely copper. Nevertheless, in value terms, non-oil exports to China accounted for 12.5% of the total revenue, advancing by 3.2% Y/Y to SAR2.1 billion.

View of the Month

Investors have been shifting their focus between commodities and, the riskier, equities depending on confidence levels. As stock markets rallied towards the end of 2013, Gold prices recorded their first annual decline in 13 years. The price of Gold was stripped of the risk premiums priced-in by investors and currently has a better reflection of the yellow metal's demand levels.

Macroeconomic Indicators

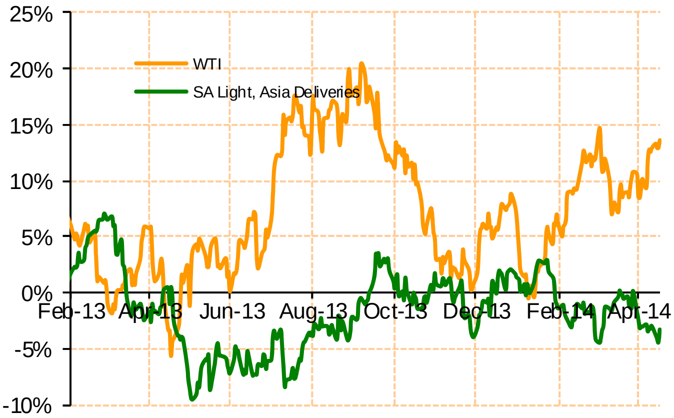
	2008	2009	2010	2011	2012	2013P	2014F
Real Sector							
Average KSA Crude Spot Price, Arab Light, USD/BBL	94.9	59.2	77.6	108.1	110.2	106.4	100.0
Average Daily Crude Oil Production, MMBD	9.2	8.2	8.2	9.3	9.8	9.6	9.4
GDP at Current Market Prices, SAR billion	1,949.2	1,609.1	1,975.5	2,510.7	2,752.3	2,794.8	2,835.0
GDP at Current Market Prices, USD billion	520.5	429.7	526.8	670.4	734.9	746.3	757.0
Real GDP Growth Rate	8.4%	1.8%	7.4%	8.6%	5.8%	3.8%	4.1%
Oil Sector GDP Growth Rate	4.3%	-8.0%	0.3%	11.0%	5.7%	-0.6%	-1.2%
Non-oil Sector GDP Growth Rate	9.8%	5.3%	9.6%	8.0%	5.8%	5.0%	5.4%
Population, million	25.8	26.7	27.6	28.4	29.2	30.1	31.0
Population Growth Rate	3.4%	3.4%	3.4%	2.9%	2.9%	3.0%	3.0%
GDP /Capita, USD	20,184.2	16,116.2	19,112.7	23,625.3	25,172.6	24,816.2	24,440.6
CPI Inflation, Y/Y % Change, Average	6.1%	4.1%	3.8%	3.7%	2.9%	3.6%	3.3%
External Sector							
Merchandise Trade Balance, USD billion	212.0	105.2	153.7	244.7	246.6	214.2	185.5
Oil Exports, USD billion	281.0	163.1	215.2	317.6	357.1	315.3	283.0
Non-oil Exports, USD billion	32.5	29.3	35.9	47.1	51.0	52.2	58.0
Merchandise Imports, USD billion	-100.6	-86.4	-96.7	-119.0	-140.7	-153.3	-155.5
Net Unilateral Transfers, USD billion	-23.0	-27.7	-27.9	-29.4	-30.4	-33.2	-36.2
Current Account Balance, USD billion	132.3	21.0	66.8	158.5	164.8	130.0	105.2
Current Account Balance/GDP	25.4%	4.9%	12.7%	23.6%	22.4%	17.4%	13.9%
Net Foreign Assets with SAMA, USD billion	438.5	405.9	441.0	535.9	648.5	713.3	749.0
Fiscal Sector (Central Government)							
Budgeted Expenditure, SAR billion	410	475	540	580	690	820	855.0
Actual Revenues, SAR billion	1,101.0	509.8	741.6	1,117.8	1,247.4	1,131.0	972.8
Actual Expenditure, SAR billion	520.1	596.4	653.9	826.7	873.3	925.0	952.8
Expenditure Overrun, %	26.8%	25.6%	21.1%	42.5%	26.6%	12.8%	11.4%
Total Revenues/GDP	56.5%	31.7%	37.5%	44.5%	45.3%	40.5%	34.3%
Total Expenditure/GDP	26.7%	37.1%	33.1%	32.9%	31.7%	33.1%	33.6%
Overall Budget Balance, SAR billion	580.9	-86.6	87.7	291.1	374.1	206.0	20.0
Budget Balance/GDP	29.8%	-5.4%	4.4%	11.6%	13.6%	7.4%	0.7%
Break-Even Oil Price	40.2	60.8	64.1	75.3	73.9	81.1	86.8
Financial Sector							
USD/SAR Exchange Rate	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Growth in Broad Money (M3)	17.6%	10.7%	5.0%	13.3%	13.9%	10.9%	10.0%
Growth in Credit to the Private Sector	27.9%	-0.6%	4.8%	11.0%	16.4%	13.5%	13.8%
Average 3M SAR Deposit Rate	3.3%	0.9%	0.7%	0.7%	0.9%	1.0%	1.2%
Average 3M USD Deposit Rate	3.0%	0.7%	0.4%	0.3%	0.4%	0.4%	0.7%
Spread, in Basis Points, SAIBOR-LIBOR	37.4	26.4	39.8	40.9	55.2	60.0	50.0

Oil Market

Looming Downside Risks

Oil prices rallied over last week, with the rapidly escalating political tensions between Russia and Ukraine driving more momentum than the fundamental factors. The return of Libyan oil supplies into the market, following the agreement with the Barqa rebels, has so far failed to create any dent to last week's oil price rally, but has the potential to weaken if the two largest eastern oil terminals, Ras Lanuf and Es Sider, which together have a loading capacity of 0.56mb/d, come on stream. Meanwhile, near term oil outlook will likely be clouded given the support for Brent futures due to the geopolitical concerns surrounding the Russia-Ukraine conflict. On a fundamental basis, assuming no further escalation in Ukraine situation, Brent prices are set to drift lower over the coming weeks from current levels above USD108/bbl.

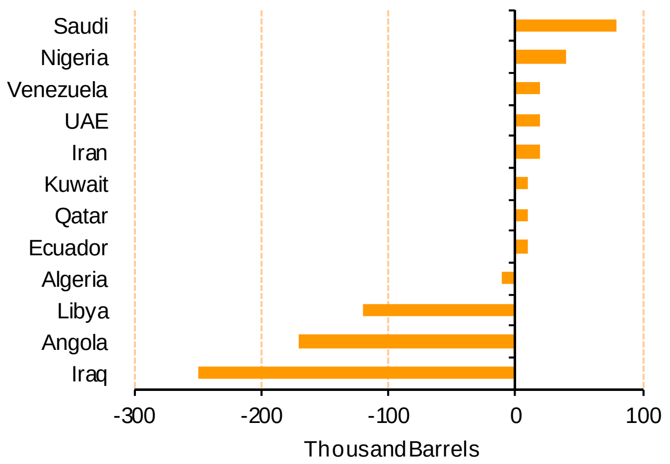
Chart 1: Oil Price Developments, YTD



Source: Thomson Reuters

On the supply side, OPEC's production fell to 29.61mb/d in March versus revised up 30.24mb/d in February. In Iraq, the OPEC's second largest producer, output dropped by 0.321mb/d to 3.09mb/d last month. Saudi Arabian production also declined by 0.284mb/d to reach 9.57mb/d last month. Angolan output declined by 0.167mb/d to 1.52mb/d, the largest decline among OPEC members in March. Libya, which produced only 0.250mb/d last month, has reached an agreement with the eastern rebels on April 6th, as its output has risen to 0.330mb/d last week. Libya's oil exports have slowly started to trickle through, with oil tankers starting to load crude from the eastern port of Hariga for the first time since July 2013. The Barqa rebels also agreed to surrender the other two major ports they currently control, Es Sider and Ras Lanuf, in two to four weeks' time. Accordingly, Libya is capable of boosting its output by as much as 1.0mb/d within a short period of time. Iran raised its production marginally on easing western sanctions to 2.9mb/d in March, but still 1.0mb/d below its current production capacity of 3.85mb/d.

Chart 2: OPEC's Monthly Oil Production Changes



Source: OPEC Survey

On the demand side, the IEA left its forecast for world oil demand largely unchanged at 92.7mb/d for 2014 due to upward revisions to baseline demand in a number of non-OECD Asian countries. The call on OPEC was raised by 0.1mb/d to 29.4mb/d for the second quarter of 2014, and by 0.35mb/d to 30.6mb/d for the second half of the year, according to IEA. Meanwhile, Chinese economic data released last week showed lackluster growth, which suggested that demand for crude could weaken. Moreover, Chinese oil imports were down 8.8% in March from February's average crude intake of 6.03mb/d, which had been a year-on-year surge of 10.9%. Globally, refinery maintenance continues to roll from the Atlantic to the Pacific, and although European refinery maintenance will fall to less than 1.0mb/d in May, more than 2.2mb/d of turnarounds is scheduled in Asia for May and June, limiting the upside potential for prompt demand for crude oil loadings. Overall, this return of supply and moderation of demand would seem to suggest a weakening of oil market balances in the second quarter. Although the aforementioned demand-supply dynamics point to a weakness in the oil market fundamentals, the room for oil prices to move lower is unlikely to extend very far going into May as the summer holidays driving season would start to accelerate the demand on gasoline.

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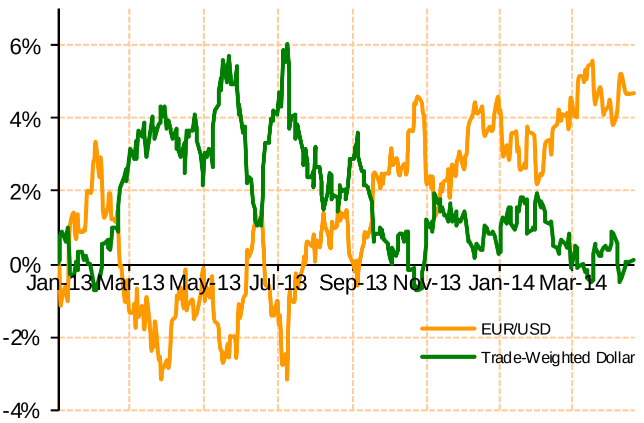
Foreign Exchange

ECB to Strike on Lowflation

In the month of March, the ongoing divergent policies across the world's central banks took on a new shape as the ECB parted ways with the Fed, which is moving forward towards normalization. In a statement from the ECB early March, Mario Draghi, the ECB president, expressed his commitment to use all conventional and unconventional instruments in order to jumpstart the economy, which has been sinking into a deflationary trend since December 2011. The Eurozone's Harmonized Index of Consumer Prices reported a 0.5% Y/Y down from 0.7% a month earlier, shifting even further away from the 2% target. The hazardously low inflation rate which is considered to be the lowest since October 2009 is making the ECB warm up to the idea of Fed-style aggressive asset purchasing in order to stoke inflation.

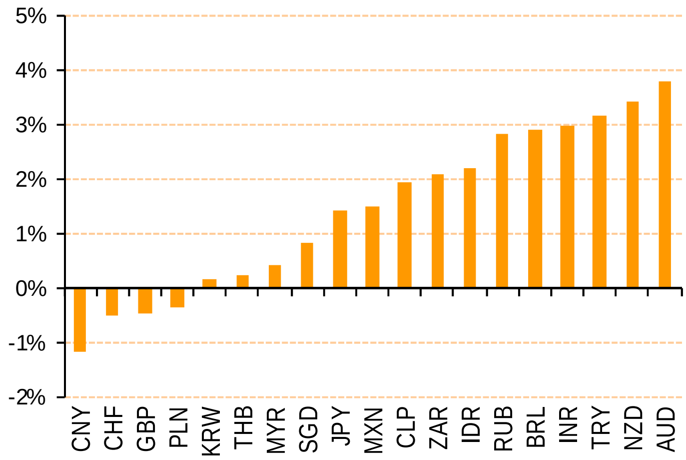
Chart 3: Trade-Weighted Dollar and the Euro



Source: Thomson Reuters

However, we find that the persistently strong EUR had slid by 0.2% in March, closing at USD1.37. The ECB easing rhetoric had a larger impact on long term securities in the Euro area, allowing the 10 year bund yield to lose 6 bps, on a monthly basis, down to 1.6%. Benchmark Spanish bonos yield slipped 27 bps from last month to 3.2% and the Italian BTP also edged lower, dropping 19 bps to 3.3%. It is expected that the German inflation rate, which currently stands at an annualized 1.24% will prevent the overall rate for the European region from being dragged into deflation. Given the stubbornly strong EUR, the geopolitical uncertainties emanating from Russia and Ukraine, and the bullish capital flows; the ECB will have to pull its monetary lever full swing in order to propel the Euro economy out of the grip of deflation. In addition, as the Fed becomes more hawkish, we will likely begin to see the EUR weakening by year-end to 1.30.

Chart 4: Monthly Foreign Exchange Rate Changes



Source: Thomson Reuters

Meanwhile, the US is enjoying an upbeat flow of macroeconomic data, namely from the jobs market. Unemployment stood still at 6.7% in March, while creating 192,000 new jobs. The sticky unemployment figure, however, must not be too stressed upon as it does not take into account discouraged workers who have decided to rejoin the work force. The Bureau of Labor Statistics estimates that the number of discouraged workers has gone down by 13.1% Y/Y to 803,000. Parsing the data from the noise is still a daunting task after the abnormally cold winter capped Q1 GDP growth at 2%; however, the US equity market is running on a 6-year high, reflecting a growing risk appetite. The Dow ended the month gaining 0.8% over the previous month at 16,457.6, while the S&P500 inched up by 0.7%, standing at 1,872.3. As a result, the trade-weighted dollar index rose by 0.5% M/M to 80.1 in March. The US 10-year bond yield gained 6 bps from February to 2.7%. The lesser-than-expected rise in treasury yields indicate that the Fed will likely remain accommodative longer than previously thought, as it's not yet confident enough in the sustainability of the recovery. In our opinion, the Fed will keep its interest rates near 0% until Q1 2016.

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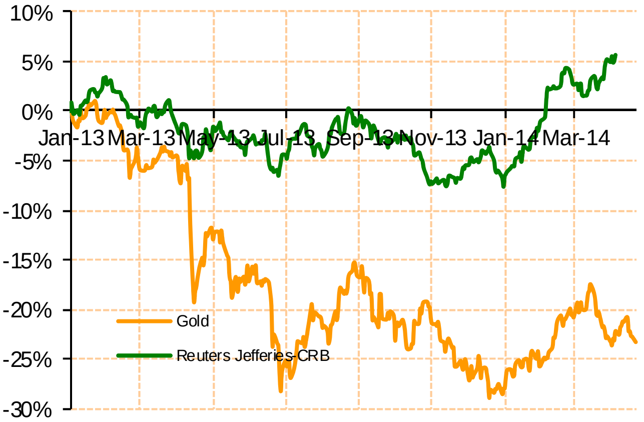
Commodities

Unfavorable Season Boosts Grains Futures

In March, downward price pressures on industrial metals were offset by appreciating agriculture prices, allowing the Thomson-Reuters/Jeffries CRB index to advance by 0.7% M/M, reaching 304.7. Business conditions in China's manufacturing sector deteriorated for the third consecutive month, reflecting contractions in both input and production. According to HSBC China Manufacturing PMI, Chinese firms are cutting their workforce and reducing activities, including purchases of base metals. The PMI posted 48.0 in March, down from 48.5 a month earlier, completing a full quarter of deceleration. The rising fear factor in China hit industrial metals, namely copper, as firms continue to hold some of it as collateral. In addition, concerns over a slowdown in China increased the likelihood for policy measures that include reducing barriers of entry for private investment and loosening of monetary policy. As a result, China posted a fall in average input prices for the third month running. Copper lost 5.2% in the period between February to March, scooping down to a new low of USD6,645/ton. Moreover, the London Metal Exchange (LME) recorded a 3.8% slump in warehouse stock in March, closing at 263.3 thousand tons, indicating a cooling in global demand for the metal. Aluminum prices, on the other hand, inched upwards by 1.8%, standing at USD1,785/ton by the end of March, supported by a solid demand from the auto industry. LME aluminum stock increased by 1.3% to 5.4 million tons at the end of the month as warehouse movements indicate a rise in stock buildup – a proxy for expected future demand. Aluminum delivered into LME warehouses spiked to the second highest levels in the past 12 months, recording 251.1 thousand tons, second only to June 2013.

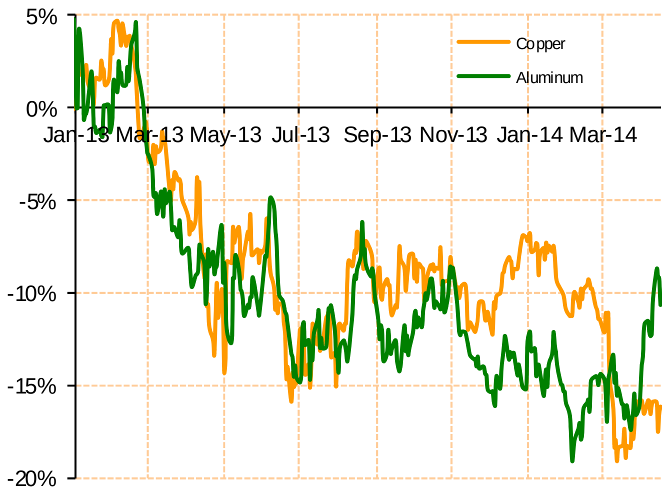
Chart 5: Reuters Jefferies vs. Gold



Source: Thomson Reuters

In contrast with a stronger dollar, gold slipped on the back of brewing expectations that the Fed might be hiking rates soon. Absence of such revelation in the FOMC meeting, however, helped bringing gold back on a positive trajectory. The yellow metal ended the month standing at USD1,285 per troy ounce, inching lower by 3.2% M/M. Since August 2013, spot gold has been ranging between USD1,200/oz to USD1,400/oz and is expected to face resistance beyond these levels. Silver exhibited a similar behavior to its more precious kin. Due to its industrial usage, however, spot silver had a more depressed outlook given the slowdown in the manufacturing activity in China, the second largest importer of the metal after India. Industrial usage of silver spans from catalytic converters for off-road vehicles, corrosion-resistant electrical switches, chemical production, and imaging. Cheaper substitutes, such as aluminum and stainless steel, in addition to technologies such as digital imaging are downward pressuring factors for the metal. Silver tumbled by 6.8% in March to USD19.8/oz.

Chart 6: Base Metals



Source: Thomson Reuters

Soft commodities rallied in March, supported by lower yield prospects following the abnormally cold winter in the US. The S&P/Goldman Sachs Agricultural Commodity index recorded an upsurge of 7.5% at 409.2. While supply of the current 2013-2014 US corn crop remains unchanged, next crop's lower projections provide positive impetus for US corn prices. According to the Chicago Mercantile Exchange (CME), corn futures for the month of May contract was up 8.4% in March to USD5.02/bushel. CME soft red winter wheat futures leaped to 10-month high on US crop outlook. A drought seems to be underway this year for the world's biggest exporter, and the reduced potential yield led the grain to uptrend 15.9% in March, closing at USD7/bushel. Soybeans also gained momentum alongside corn and wheat, advancing by 3.6% M/M, standing at USD14.7/bushel.

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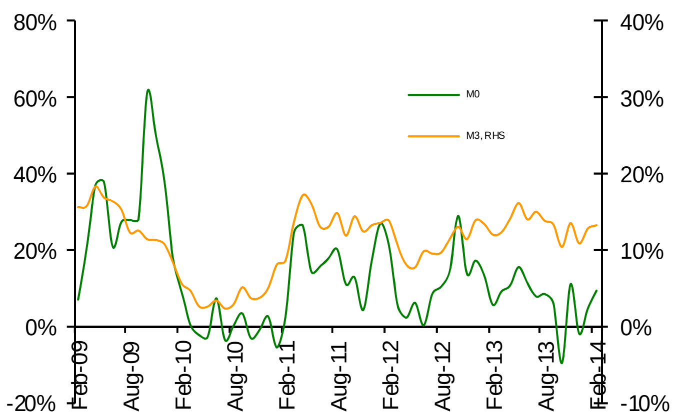
Money & Inflation

Subsiding Inflation As Liquidity Moderates

The 2007-based annualized inflation rate in February recorded 2.8%, well below the past 12-month average of 3.4%. Major categories witnessed some moderation over the past months as food stuff recorded 4.6% compared to the 12-month average of 5.7%. Housing inched down to 4%, below the annual average of 4.2%. Transportation has been trending on the negative side since October 2013, marking the highest deceleration in February at 2.8%. Prices of clothing and footwear, although minor, have also been softening at an average of 0.7% since the beginning of 4Q2013. We expect food stuff to be a catalyst for imported inflation, as soft commodities gained 7.5% in February, according to Goldman Sachs Agricultural Commodity Index which reached 409.2 during the month (see Commodities.) Due to the contractual nature of grains and other essential commodities' imports, however, we expect there to be at around a six month lag before inflationary pressures hit the Saudi consumer. Points of sale (POS) transactions, which is used as a proxy to gauge retail activity, indicates that consumers' confidence remains solid. Growth last year averaged 18.4%, given the buoyant state of the market, sales topped last year by 7.6% in February this year despite the higher baseline.

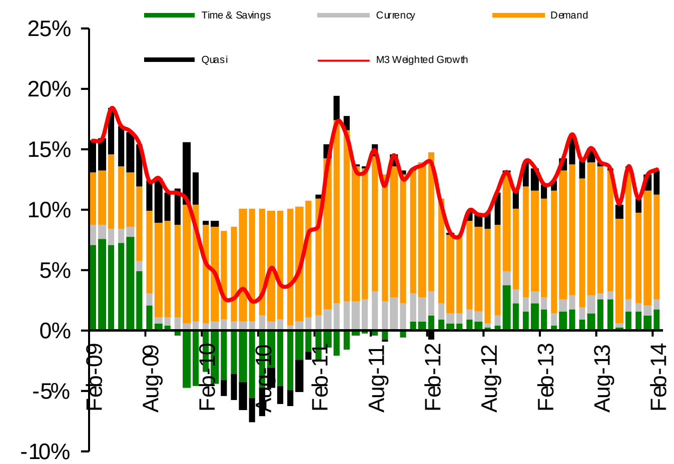
Chart 7: Growth in Monetary Aggregates



Source: SAMA, NCB Estimates

The growth of money supply aggregates in the kingdom continued to pace up in response to the growing demand from consumers and businesses. After a one-month slump in December, annualized growth in monetary base regained traction, recording 9.3%. As bank reserves surged by 10.7%, and currency in circulation was boosted up 7.6% compared to last year, the monetary base (M0) reached SAR338.9 billion. In addition, narrow money aggregate (M1) increased 14.5% Y/Y after demand deposits rose by 15.7% Y/Y, allowing M1 to total SAR1.036 trillion. Time and savings deposits continued their upward trajectory, stacking SAR348.5 billion, leading near money (M2) to leap over last year by 7.3%. Consequently, the broadest measure of money supply (M3) totaled SAR1.58 trillion, denoting a 13.2% Y/Y upturn, which is the average growth rate of money supply in 2013.

Chart 8: Money Supply, Contribution



Source: SAMA, NCB Estimates

SAMA's active monitoring policies ushered away any threats to the steady growth in money demand, allowing for investment-friendly long-term projections in the absence of the damaging effects of price fluctuation. Thus, the relatively stable growth in price levels of goods and services in the Kingdom entices the propensity to consume and invest rather than to save. As a result, 56.2% of money supply consists of demand deposits, followed by time and savings and quasi monetary deposits at 22% and 12.5%, respectively. Moreover, net foreign assets managed by SAMA grew at an annual rate of 10.4%, totaling SAR2.7 trillion, providing adequate cushioning against external shocks, should they occur. Bank reserves upturned by 15% Y/Y to an all-time-high of SAR150.8 billion in a strive to meet the Basel III accord requirements under SAMA's rigorous supervision. Excess reserves grew by 3.9% Y/Y to SAR84.2 billion, in tangent with the banks' move to increase their capital,

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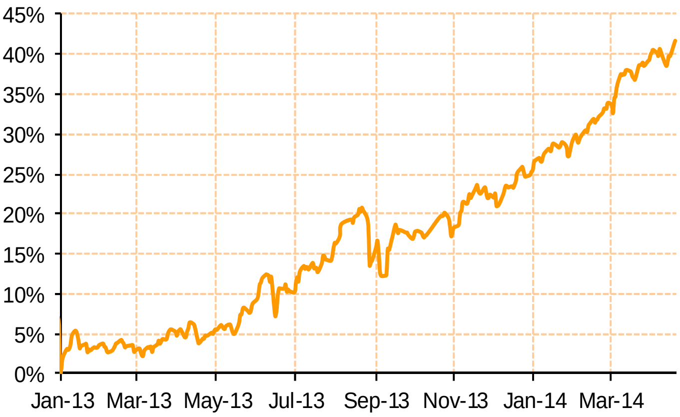
Capital Markets

Tadawul Marching On

The local stock market continues to reach new post-crisis feats as it recorded the seventh consecutive monthly increase during March. Last month, Tadawul gained 4.0% M/M to close at 9'473.71 as the momentum for risky assets maintained a strong foothold in anticipation of corporate profitability. The liquid level of the Saudi market coupled with a healthy economic environment paved the way for stocks to maintain an upward trajectory. During March, the media and publishing sector recorded the highest growth at a staggering 19.9% M/M to reach a YTD gain of 33.9%. The transport and retail sector enjoyed a fruitful month as they climbed by 11.6% and 11.1%, respectively, during last month. The only sector to record a decline was cement, contracting by 1.9% capping its first quarter gains to 4.9%. Towards the end of last month, King Abdullah appointed Prince Muqrin as Deputy Crown Prince, the decision did not hinder the stock market's momentum but rather eased political uncertainty. The index carried over the momentum into April, hovering around the 9'500 level. The technical and psychological barrier of 10'000 will prove to be a key milestone for the market during 2014.

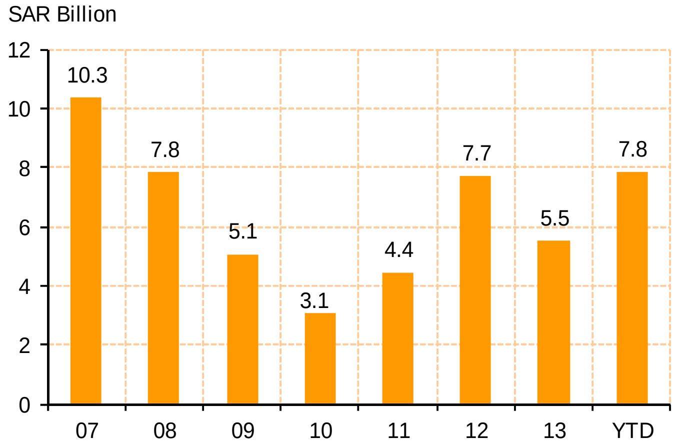
Chart 9: Tadawul All-Share Index



Source: Tadawul

The total number of listed companied has reached 164 and the market is set to add a few more this year. The level of activity dropped markedly during 2013; however, it has gained significantly thus far into 2014. Last month, the average daily traded volumes reached SAR8.8 billion which brings the first quarter average up to SAR7.3 billion, a 32.8% improvement over 2013's average. Furthermore, a total of just over 3 million transactions worth SAR194.0 were conducted last month in comparison to February's 2.2 million transactions with a worth of SAR135.2 billion. Consequently, market capitalization increased to SAR1.925 trillion by the end of the first quarter. The stock rally is expected to ease as the index has already gained 11% by the end of March since the beginning of the year. It will be difficult to sustain the same pace for the remainder of 2014, but we believe ending this year with a range of 15-20% higher is feasible given the supportive fundamentals.

Chart 10: Average Daily Traded Value



Source: Tadawul

As for the primary market, the Saudi Marketing Company was the sole initial public offering (IPO) during the first three months. The primary market is stagnant this year but is set to witness the largest IPO in Tadawul's history. The National Commercial Bank's (NCB) long awaited listing is underway as they plan to sell 15% to the general public. NCB is the largest bank in Saudi Arabia and is the only local bank not listed in Tadawul. NCB generated SAR8.0 billion as net profits for 2013 and the bank accounts for 16.6% of total loans in the market. Gulf International Bank and HSBC have been appointed as advisors and will oversee the process which is expected to conclude towards the end of the year.

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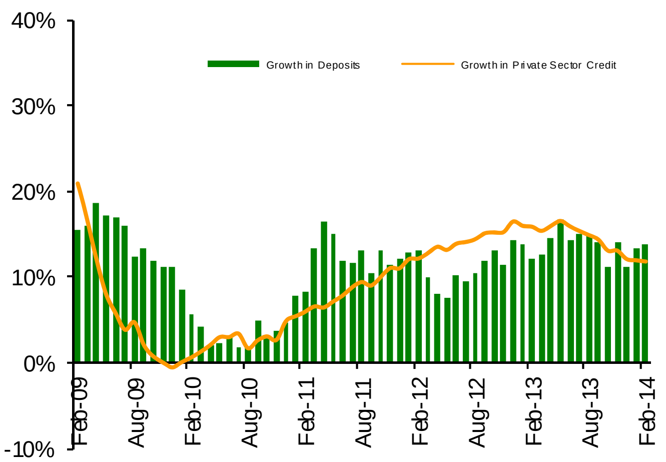
Loans Market
A Plateauing Credit Potential

In the month of February, the asset/liability composition in Saudi banks continued to demonstrate healthy levels of utilization as the economy is awash with liquidity. Credit extended to the private sector advanced over last year by 11.8%, with fresh loans amounting to SAR10.1 billion while deposits grew by 13.9%, leaving the loans/deposit ratio at a comfortable 79.5%. With the kingdom's increasing dependence on the private sector to spring real growth in 2014, lending to the private sector upsurged 11.8% Y/Y, totaling SAR1.1 trillion, accounting for 96% of total bank loans. We expect to see a deceleration in credit activity compared to previous years as the market becomes fully utilized in accordance to SAMA's guidelines. Required reserves are up 15.3% Y/Y, in line with the 27.5% increase in capital by the banking system. Excess reserves in Saudi banks currently stand at 49.6%; a rate that demonstrates confidence while maintaining minimum exposure to high risk credit. Demand deposits surged by 15.7% compared to last year to SAR890.6 billion, while time and deposit rose by 7.3% to SAR348.5 billion. Around 93.5% of demand deposits are made by businesses and individuals due to unattractive interest rates, and positive market sentiments (see Capital Market.) Interest-bearing deposits made by businesses and individuals rebounded after a slump throughout most of 2013 by an annualized 1.7%, whereas time and savings deposits by government entities reached a record SAR153.6 billion by adding 15.4% on an annual basis.

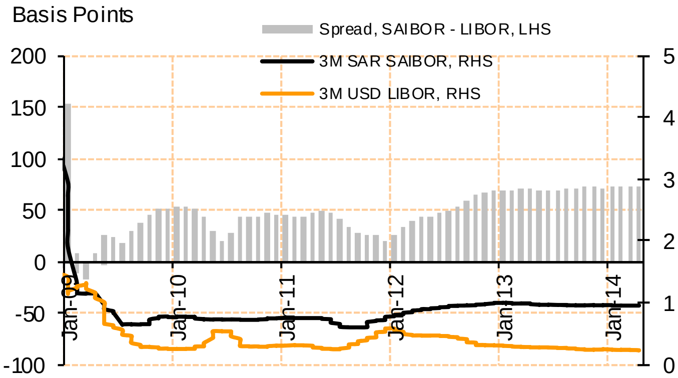
Chart 11: Private Sector Financing



Source: SAMA, NCB Estimates

Bank credit by maturity has been noticeably moving from short term to medium and long term since 2011. Despite the expected lower overall annual increase stemming from the high growth rates in past years, an 11.7% reinforces vibrancy in economic activity and reflects the strong current risk appetite in the market. Short-term credit lines still represent the bulk of credit extended by local banks advancing from last year by 8.5%. In retrospect, the rise in longer maturity loans is a result of a more regulated market with reduced risk factors. Thus, we find that medium-term and long-term loans rose by 8.9% and 20.2%, respectively, relative to the same period of last year. As a measure for liquidity control, the annualized 15.6% upturn in Saudi government securities is indicative that SAMA is actively managing price levels via absorbing excess liquidity to prevent overheating in the economy.

Chart 12: Liquidity and Risk Detector



Source: Thomson Reuters

Analysis of loans by economic activity in the last quarter of 2013 shows that 21% of credit extended by banks were related to commerce, followed by 12.5% for manufacturing, and 6.8% for building and construction. Over the last year, the surge in activity for commerce-related credit has been consistent at 14% Y/Y, measuring the largest increase. Credit for the manufacturing sector grew by an annualized 10.7%, indicating a moderation from the 16.9% year average. Credit for building and construction posted a mediocre 1.6% annual upturn, below the 3.1% yearly average in 2013.

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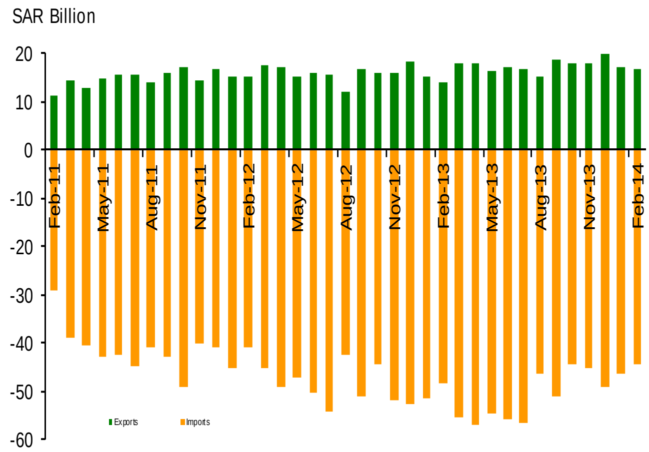
External Trade

An Upward Trajectory for Exports

The state of the kingdom's external trade continues to be marked by strength and resilience as revenues from non-oil exports significantly leaped over last year by 20.5%, reaching SAR16.7 billion. The bill of imports, in contrast, receded by 8% Y/Y, recording SAR44.4 billion. The declines witnessed in imports are mainly associated with moderating construction activities that involves imports of machinery and electrical equipment. Labor crackdowns by the Ministry of Labor are identified as the main culprit for the recently ailing sector, and expected to result in some short term pains. In respect to non-oil exports and imports, we have been noticing a narrowing gap compared to last year which brought the balance of trade less by 19.5%.

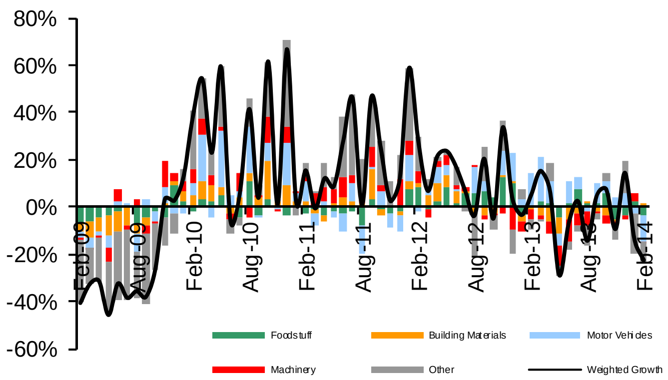
Chart 13: Saudi Non-Oil Trade Balance



Source: CDSI, NCB Estimates

The composition of exports retains plastics and chemical products as the lead revenue generators, both climbing on double-digits. Plastics, which account for 34.4% of February's return from trade, registered an 18.6% upturn from the same period last year, reaching SAR5.7 billion. Chemical products, which sizably contribute to 31.3% of the non-oil exports' bottom line, up surged by 20.3% to SAR5.2 billion , which merits the strong global demand from the kingdom's trade partners. Exports of base metals, on the other hands, inched lower by 7.3% on an annual basis, recording only SAR1 billion of return in February. The recent turn of events in China, the largest recipient of exports, led to a decreased manufacturing activity, which weighed heavily on demand for base metals globally, namely copper (See Commodities.) Nevertheless, in value terms, non-oil exports to China accounted for 12.5% of the total revenue, advancing by 3.2% Y/Y to SAR2.1 billion. Moreover, non-oil exports to the UAE reached SAR1.8 billion, marking an annualized 18.3% upturn. This solid growth in exports allows the UAE to maintain its positions as the second largest destination for Saudi exports, generating 11% of the monthly export return. Exports to Singapore made the largest stride in annual comparison in February, advancing by a staggering 87.8% Y/Y to SAR1.2 billion.

Chart 14: Attribution Analysis of Letters of Credit Opened



Source: SAMA, NCB Estimates

On the imports front, we notice an overall double-digit decline across most categories during the month. Imports of machinery and equipment which account for over a quarter of the import bill tumbled by 15.3% Y/Y, registering SAR11.4 billion. Multiple factors contribute to the weakening prospect for machinery imports, on top of which is the labor reforms, putting deliveries on hold. On the other hand, imports of transport equipment inched higher by 12.4% driven by the strong consumer appetite for big ticket items, namely motor vehicles. Transport equipment make up 19.1% of February's import bill, amounting to SAR8.5 billion. Imports of base metals, which account for 11.4% nosedove by 15.9% compared to the same period last year, affected by a moderation in the construction sector. The bulk of imports to the Kingdom in value terms originates from China (13.4%), the US (12.1%), and Germany (6.7%). When compared annually. imports from all countries recorded a downturn. Chinese imports inched 5.8% lower to SAR5.9 billion. US imports declined by 15.3% Y/Y, settling at SAR5.4 billion. German imports to the kingdom were less by 3.9% from last year, amounting to SAR3 billion.

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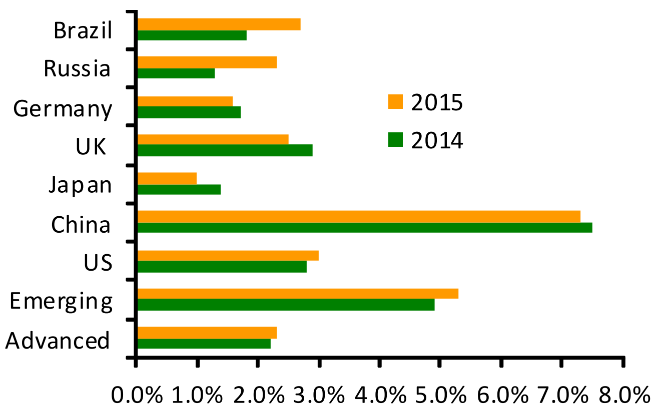
Special Focus:

A Global Perspective

Determining the drivers for global growth has been rather complicated as the inter-linkages between advanced and emerging economies become more entwined over time. Emerging economies were the catalysts post the financial crisis and balancing the macroeconomic stage has set advanced economies towards a slow recovery. Moving forward, the global economy is expected to be spearheaded by advanced economies as growth outlooks are slipping away from emerging economies. In the US, personal consumption expenditure, constituting over two thirds of GDP, has been improving and consumers have been allocating only 4.5% of their disposable income towards savings last year in comparison to 5.7% and 5.6% for 2011 and 2012, respectively. The jobless rate has been steadily improving which has merited the tapering of the quantitative easing program, currently at USD55 billion/month. The European region is less fortunate as it continues to struggle with sluggish growth, with Germany being an exception. Regionally, high unemployment, stubbornly low inflation, and a limited set of tools for the European Central Bank, despite their continuous commitment to ensure support, have been weighing on the region's growth. A similar accommodative program to that of the US is a possibility given the slow economic developments. Meanwhile in Japan, Abenomics will need time to pull the economy from its decade-long deflationary status. The planned fiscal tightening for 2014 represents 1% of GDP, a moderate figure given the magnitude of the task ahead.

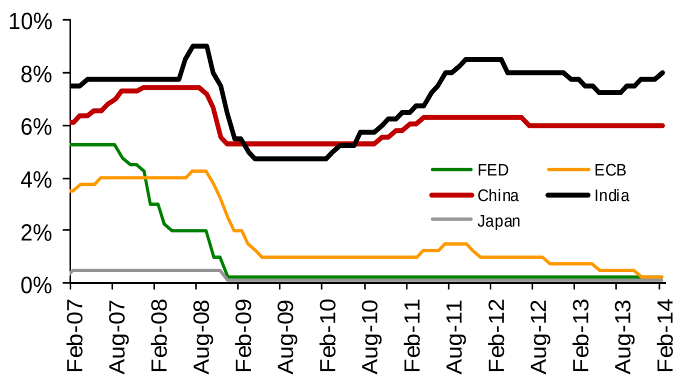
Table 15: Selected GDP Growth Projections



Source: IMF and NCB Estimates

Emerging economies' growth prospects have been recently downgraded by the International Monetary Fund (IMF) to 4.9% from 5.1%. Although their contribution to global growth is more than two thirds, growth balancing pressured economies such as China and Brazil. While others have been engaged in political turmoil, Russia, which triggered a downgrade to their growth projection by 0.6% to 1.3%, according to the IMF. Ukraine represents a gateway to Europe for Russia as it facilitates the transfer of more than half of Russian gas exports. Growth rates in emerging economies which have been recorded post the financial crisis have been a concern with regards to sustainability. The majority have also been hindered by a reversal in capital flows following the recovery of advanced economies. This led to large currency drops against the greenback. The Turkish Lira, Brazilian Real, and Indian Rupee declined during the first quarter of 2014 by 17.8%, 12.4%, and 11.2%, respectively. This resulted in greater complications for policy makers to maintain their growth targets.

Table 16: Key Central Bank Rate Decisions



Source: Central Banks

Investors have been shifting their focus between commodities and, the riskier, equities depending on confidence levels. As stock markets rallied towards the end of 2013, Gold prices recorded their first annual decline in 13 years. The price of Gold was stripped of the risk premiums priced-in by investors and currently has a better reflection of the yellow metal's demand levels. However, the Thompson Reuters/Jefferies CRB index has risen 8.8% during Q1, mainly due to agricultural commodities being hit by worse-than-expected weather conditions which limited crop yields. Moreover, oil prices remain elevated, with the WTI resting above the USD100 level. We expect prices to remain range-bound as political uncertainty and supply disruptions balance out demand downside risks over the short-term at least.

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