جدوى للإستثمار
Jadwa Investment

23 December 2013

Saudi Arabia's 2014 budget

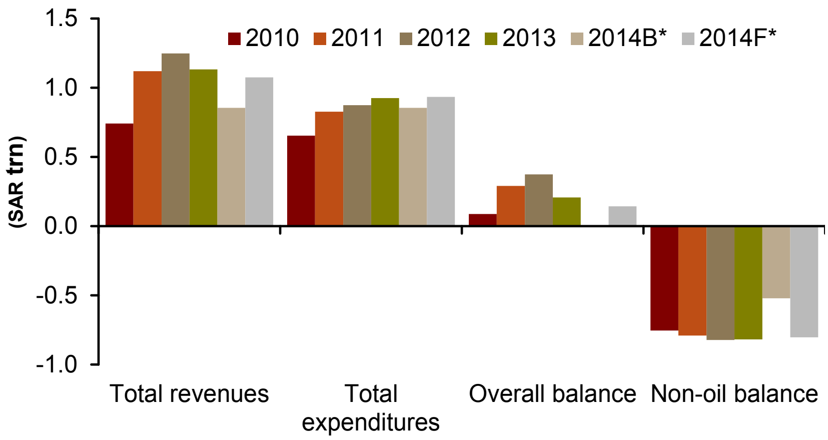
The government's budget for the 2014 fiscal year (31 December 2013 to 30 December 2014) was endorsed by the Council of Ministers on December 23. It was another expansionary budget with a record spending which will play a vital role in supporting the economy. The highlights are:

- For the first time since 2005, a balanced budget is projected, based on revenues and expenditure of SR855 billion. Education and healthcare remain the focus of government spending, accounting for 38 percent of total spending.

- The budget highlights again the government's intention to continue to stimulate the economy. Elevated budgeted investment spending of SR248 billion, will support healthy economic growth and provide encouragement and opportunities for the private sector at a time of global and regional uncertainty. While revenue projection is less conservative than in previous years, but in the event of a shortfall in revenues, any deficit can be financed comfortably by drawing from SAMA's huge stock of foreign assets, which stood at $712 billion at the end of October.

- A budget surplus of SR206 billion was recorded in 2013 (Jadwa: SR201 billion), compared to a budgeted surplus of SR8 billion. Recorded surplus was 44.8 percent lower than that realized in 2012 owing to both lower total revenues and higher expenditures. Total revenues recorded SR1.131 trillion (Jadwa: SR1.096 trillion) while total spending was at an all-time high of SR925 billion (Jadwa: SR895 billion). Spending grew at 5.9 percent year-on-year, a moderate rate compared to the previous five years. This was expected as the government tries to

Figure 1: Saudi Arabia's fiscal stance remains expansionary



Note: *2014B refers to the budget projections, while 2014F refers to Jadwa Investment's forecasts.

For comments and queries please contact:
Fahad Alturki
Head of Research
falturki@jadwa.com

Head office:
Phone +966 11 279-1111
Fax +966 11 279-1571
P.O. Box 60677, Riyadh 11555
Kingdom of Saudi Arabia
www.jadwa.com

maintain and control the growth of its spending.

- Preliminary economic data show that 2013 was a healthy year for the economy with real GDP growth of 3.8 percent (Jadwa: 4 percent). Non-oil private growth maintained a strong growth of 5.5 percent year-on-year, with growth of construction, retail transport and communications and non-oil manufacturing sectors above 5 percent year-on-year. Elevated oil export revenues maintained a double digit current account balance at 17.4 percent of GDP or $129.8 billion.

We estimate that a price of $67 per barrel for Saudi export crude (around $71 per barrel for Brent) and production of 9.4 million barrels per day are consistent with the revenue projection contained in the budget. We expect both revenues and expenditures to be above the budgeted level and forecast a budget surplus of SR140.8 billion (4.8 percent of GDP) based on oil price of $104 per barrel for Brent.

The 2014 budget

Budgeted spending is at another all-time high…

...with an expected balanced budget in 2014.

Budgeted spending is at another all-time high in 2014, as the government continues with its program to upgrade the human and physical infrastructure, spurring economic growth and meet the demand of a rapidly growing population. For the first time since 2005, the Kingdom has budgeted for a balance budget this year compared with small surpluses in the last two years. The budget foresees a moderate annual growth in both expenditures (4.1 percent) and revenues (3.1 percent) compared to last year's budget. In the US and across Europe, countries are cutting spending and/or rising taxes to bring budget deficits under control and reduce their debt. This is not a concern for the Kingdom. While the budget is expected to be balance in 2014, debt is very low and should a deficit occur it can be financed comfortably by drawing on the vast stock of foreign assets rather than issuing new debt, we think.

Expenditure

Growth in budgeted expenditure is the lowest since 2002...

Total expenditure is budgeted at SR855 billion in 2014 (Figure 2). This is 4 percent above the amount budgeted for 2013 and is the lowest growth in spending since 2002 (Figure 3). In nominal terms this is a SR34 billion increase on the figure budgeted for 2013 which

Figure 2: Budgeted expenditure

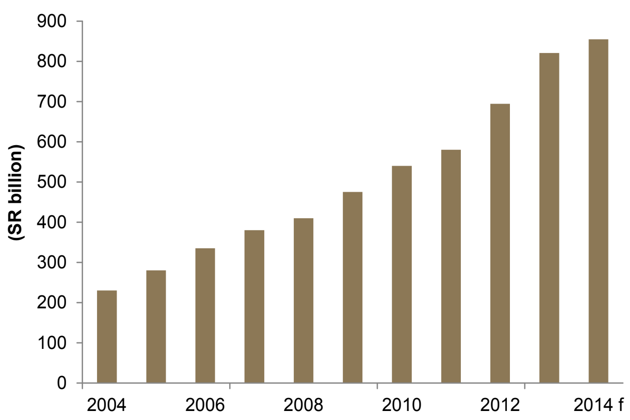
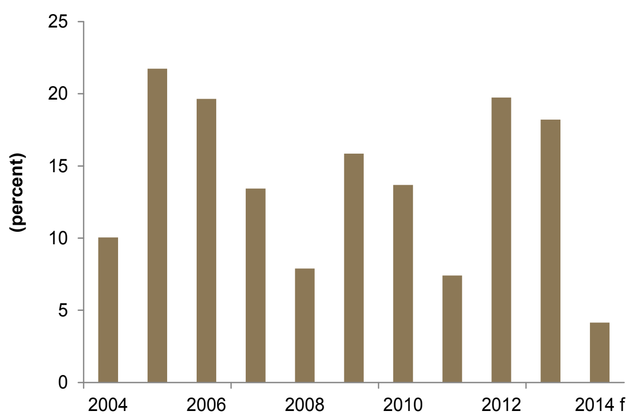


Figure 3: Growth in budgeted expenditure



is the lowest nominal increase in budgeted spending since 2007.

….but expenditures remains high relative to non-oil GDP.

Budgeted spending is someway below the actual level in 2013 of SR925 billion. We don't view this as withdrawal of the stimulus or a rethinking of the ongoing expansionary fiscal stance. The last year that budgeted spending was greater than actual spending in the previous year was 2000. In addition, budgeted spending as a share of non-oil GDP remains on the high side of historical standards (at 52 percent), compared with 49 percent of non-oil GDP in the last ten years. In addition, the government has consistently overrun its budgeted spending by an average of 24 percent over the past decade (Figure 4). The narrowing difference between the level of expenditure budgeted for 2014 and the actual level of spending in 2013 at 8 percent was, however, in line with previous year.

Current spending is set to increase while investment spending are reduced for the first time since 2002.

The SR34 billion increases in overall budgeted spending was entirely due to higher current spending while investment spending was reduced. Budgeted current spending has been raised to SR607 billion or by 13 percent compared to the level budged last year. This is in line with the growth for the previous year. Wages and salaries are the largest component of this and are certain to be a major contributor to the higher spending. Operations and maintenance costs are also likely to be a growing source of current spending in future years as major projects become operational. At the same time, investment spending was cut by 13 percent to SR248 billion. While this is the first time since 2002 that we see the government reduces its budgeted investment spending, this was anticipated given the rapid growth in this type of spending over the last ten years which averaged 14.8 percent per year. That said, the current budgeted investment spending are 81 percent higher than its level five years ago.

Spending priorities are consistent with recent years.

While budget expenditures in the 2014 budget spans all sectors the priorities are consistent with recent years (Figure 5). Education is allocated the biggest share of those departments disclosed in the budget, at 25 percent of total spending followed by the health and social affairs with 12.9 percent. Municipal services and health and social development received the largest increase in their allocations, at 9 and 8 percent, respectively.

Figure 4: Budgeted versus actual spending

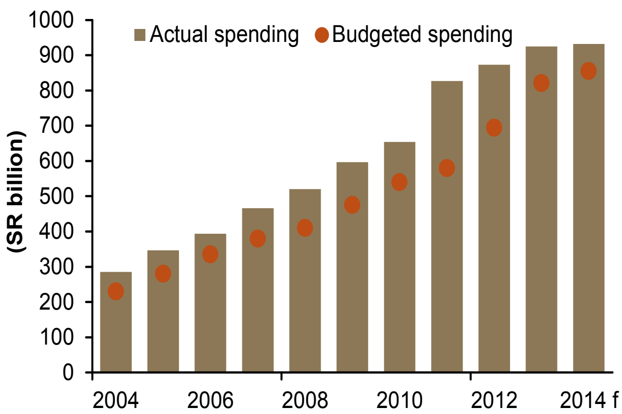
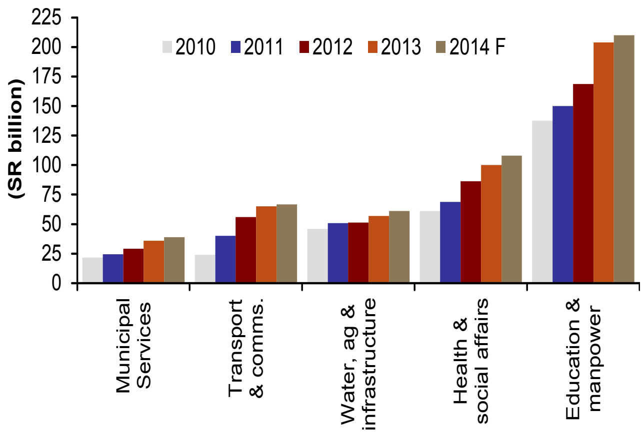


Figure 5: Spending by sector



Spending plans for key public sector areas outlined in the budget include:

Education and manpower accounts for 25 percent of total spending.

Education and training was allocated SR210 billion, a moderate 3 percent increase on 2013 allocation compared with an all-time high of 21 percent last year. This will be used to finance work on 465 new schools and 1,544 existing school-construction projects as well as the necessary funds to refurbish 1,500 schools. The allocation also included 8 new colleges and further work to refurbish female colleges in a number of universities. SR16.3 billion has been appropriated for new and expansion of existing projects for the Ministry of Higher Education. Finally, SR22 billion has been allocated for the over 185,000 Saudi students studying abroad and their families.

Health and social affairs accounts for 12.9 percent of total spending.

Health and social affairs was awarded an 8 percent rise in its budget, to SR108 billion, accounting for 12.9 percent of total spending. New projects in this area will include construction on a total of 34 healthcare facilities including 11 new hospitals, 11 medical centers, and two medical complexes. This is in addition to the 132 already in progress. Social projects will include construction of 20 new sport club centers and 16 social and rehabilitation centers and social security offices at a cost of SR29 billion.

Transport and infrastructure accounts for 7.9 percent of total spending.

Transport and infrastructure received the third largest allocation of SR66.6 billion. Spending in this category is budgeted to rise by 2.5 percent compared to the 2013 budget. New projects in the transport sector include finishing work on existing road projects, finishing industrial cities' and Ras Al-Khair's infrastructure projects, in addition to new sea ports and construction of railways. These projects are expected to account for SR40.2 billion of the total allocation to this area. Work will begin on 3,500 kilometers of roads and finishing the planning and designing phases of another 1,360 kilometers of roads.

Water, agriculture and (related) infrastructure accounts for 7.3 percent of total spending.

Water, agriculture and (related) infrastructure spending is budgeted at SR61 billion, an increase of 5.7 percent compared to 2013 budget. Funds have been set aside for new and expansion of existing projects including new silos projects, new desalination stations, in addition to enhancing water and related utility services supply and improving the water and water treatment networks.

Municipality services accounts for 4.6 percent of total spending.

Municipality services were given a 9 percent increase in budget, the highest increase of any of the area announced. The total allocation thus increased to SR39 billion of which SR4.4 billion will be financed from municipality services. The spending retains the same focus as previous years.

While not disclosed, defense and security spending is likely to account for the largest share of total spending.

Although not disclosed in the budget announcement, it is likely that defense and security accounted for the largest component of government spending. According to Saudi Arabian Monetary Agency, defense and security spending accounted for 31 percent of the budgeted total in 2013. Several multi-billion dollar defense contracts have been signed in last few years and media reports of new agreements appear sporadically. These payments tend to be spread over many years, so the additional impact on spending in 2014 should not be too great.

Revenue

Total revenue is budgeted at SR855 billion.

Total revenue is budgeted at SR855 billion. We anticipate that around 90 percent of total revenue will come from oil; an official revenue breakdown was not published. As is the norm, the oil price and production projections used to derive the revenue figure were not disclosed. We calculate that oil production of 9.4 million barrels per day (mbpd) at a price for Saudi export crude of $67 per barrel (equivalent to around $71pb for Brent) and an oil export/revenue transfer ratio of 88 percent is consistent with the oil revenue projection in the current budget.

We calculate that oil production of 9.4mbpd at a price $71pb for Brent is consistent with the oil revenue projection in the current budget.

The government has consistently based its budget on a conservative oil price assumption. Over the last decade the actual oil price has averaged over 70 percent higher than the one used for the budget. The last year where actual oil prices averaged below the budgeted level was 1998. Year-to-date Brent is trading at $109.6pb, 54 percent above the level we estimate is used for the budget. Nonetheless, considering that oil prices are likely to fall gradually next year, we think price assumption in the current budget remains less conservative than last year.

Actual oil price has averaged over 70 percent higher than the one used for the budget in the last 10 years…

With these assumptions in the background, the announced revenues are projected to rise by 4 percent above the previous year's budget. Even though we anticipate that both production and prices will be lower than in 2013 (see box), we think that revenues will be comfortably above the government's assumption. Revenues generally provide the base from which expenditure is calculated; unrealistically low oil revenue and spending assumptions have contributed to high levels of overspending in recent years.

...which we view as one of the reasons behind consecutive years of substantial overspending.

Projections for non-oil revenues were not published. Fees and charges for government services and customs tariffs are the main sources of non-oil revenues. We anticipate receipts from both of these sources to increase as a result of solid economic performance as well as higher demand on government services particularly those related to labor registration. Although government foreign assets are at an all-time high, revenues earned from investment income are unlikely to rise too much because of the exceptionally low interest rates on US government bonds, which we think constitute the bulk of Saudi government foreign assets. No new policies to raise non-oil revenues were contained in the budget.

Higher demand on government services will improve non-oil revenues.

Jadwa's budget forecast

We forecast a budget surplus of SR140.8 billion in 2014, equivalent to 4.8 percent of expected GDP. This is because we expect the oil price to be higher than that used in the budget and therefore that oil revenues will exceed the budgeted total (see box). We forecast total oil revenues to the budget at SR957.8 billion and non-oil revenues at SR116.6 billion.

We forecast a budget surplus of SR140.8 billion in 2014 (4.8 percent of GDP).

Spending will be above the budgeted level. Over the last ten years, actual government spending has averaged 24 percent higher than the budgeted amount. The extent of overspending eased in 2013, when it was 12.7 percent, the lowest level since 1999. Given that spending has already reached a very high level particularly on the investment side and Given the more prudent expenditure control together with the low rise in spending budgeted for 2014, we expect that the actual spending in 2014 will be relatively close to the

We expect actual spending to be 9 percent higher than budgeted budget projection leading to a total expenditure of SR932 billion.

The fiscal breakeven oil price is expected to average the $81pb.

The oil price level necessary for revenues to balance our forecast level of government spending, known as the fiscal breakeven oil price, is $81pb for Saudi export crude (equivalent to around $85pb for Brent). This is based on our production assumption of 9.4 million barrels per day, domestic consumption of 2 million barrels per day and an oil export/revenue transfer ratio of 88 percent. Rising domestic gas production should take some of the burden from oil as the fuel for domestic energy consumption next year. According to JODI, domestic crude consumption for the first nine months fell by 9 percent year-on-year.

Jadwa's oil market outlook for 2014

We forecast that Saudi export crude will average $100 per barrel in 2014.

Our macroeconomic forecasts for the Kingdom are based a moderate decline in oil prices compared to their level this year. We forecast that Saudi export crude will average $100 per barrel (equivalent to $104pb for Brent) in 2014 compared with a year-to-date average of $104pb (equivalent to $109.6bp for Brent). With output from Iraq, Iran, Libya and non-OPEC countries expected to steadily rise over the course of next year, we maintain our view that the Kingdom's oil production will gradually fall in 2014 to an annual average of 9.4 million barrel per day (mbpd).

Global oil demand is expected to increase to 92.1mbpd…

...most of which will be generated by non-OECD countries.

- Overall global oil demand is expected to rise by 1.3 percent year on year to 92.1mbpd. According to the International Energy Agency (IEA), global oil demand will grow by 1.1mbpd next year compared with a growth of 1.04mbpd in 2013 (Figure 8). Demand by OECD countries is expected to decline for the fourth consecutive year (by -0.19 mbpd in 2014), while that of the non-OECD countries will increase by 1.32mbpd in 2014. China, India and other non-OECD Asia Pacific countries will account for the bulk of this increase in demand (55 percent) followed by Middle Eastern countries (19 percent). This will in turn maintain a robust demand on Saudi crude exports particularly considering that the Saudi oil exports to these two regions account for 69 percent of total crude oil exported by the Kingdom in the last five years.

- Total world oil output should also rise in 2014 owing mostly to a

Figure 6: Budgeted versus actual revenues

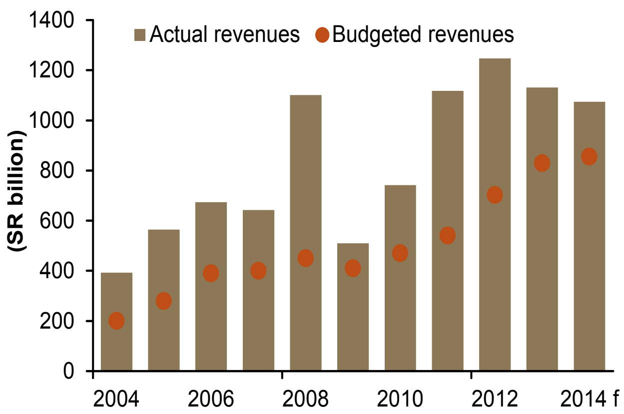
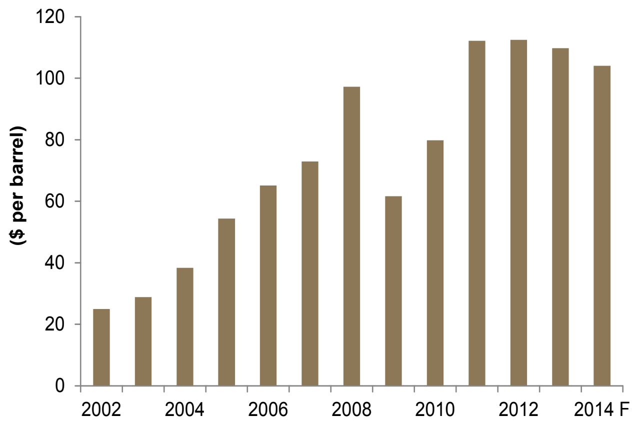


Figure 7: Oil prices
(Brent crude, period average)



Non-OPEC oil supply is expected to exceed global oil demand growth for the second consecutive year.

rapid increase in non-OPEC supply. In fact, the growth of the non-OPEC oil supply is expected to exceed global oil demand growth for the second consecutive year (Figure 9). According to the IEA, non-OPEC oil supply is expected to grow by 1.79mbpd in 2014 compared with a growth of 1.3mbpd estimated for this year. North America crude oil output growth is forecast to slow slightly from this year's rapid pace, but that will be more than made up for by better performance elsewhere in non-OPEC. This will create a pressure on OPEC countries to reduce their output in order for the market to be able accommodate additional non-OPEC supply growth. We thus expect Saudi Arabia to slightly cut production to 9.4mbpd next year compared with 9.6mbpd in 2013.

Balanced market and high commercial oil stocks will also contribute to the downward pressure on oil prices.

- The current high commercial oil stocks shows the market is well supplied. This should also pose negative element for oil prices. OECD crude stock levels remains at a comfortable level when measured in days of forward cover as well as relative to their five-year average. This reflects both weaker demand by non-OECD countries as well as higher production from non-OPEC countries.

Political instability in some Middle Eastern countries will keep the geopolitical risk premium built into oil prices.

Geopolitical risks and increased liquidity poured into the system from central banks also need to be considered when forecasting prices. The turbulence in the Middle East and North Africa added a risk premium to prices in the last few years and this will likely remain the case for most of next year as uncertainty is likely to linger. While the historic nuclear pact between Iran and the P5+1 should in principle reduce the geopolitical risk premium in the oil markets, the progress toward a full removal of economic sanctions is likely to remain gradual. At the same time, political instability in Syria, Iraq, Libya and Sudan will all maintain the geopolitical risk premium built into oil prices.

Less accommodative monetary policies in advanced economies will have a temporary impact on oil prices

Financial flows have also influenced oil prices in recent years. The US, Japan, and EU monetary easing measures have, among other factors, maintained elevated oil prices despite subdued global economic fundamentals in the last three years. Policy adjustments toward less accommodative monetary stance especially in the US would, in our view, have a temporary negative impact on crude prices. This is because monetary policy would be tightened only if economic outlook substantially improves which should offset any negative impact of a less simulative monetary policy on oil prices.

Figure 8: Change in global oil demand

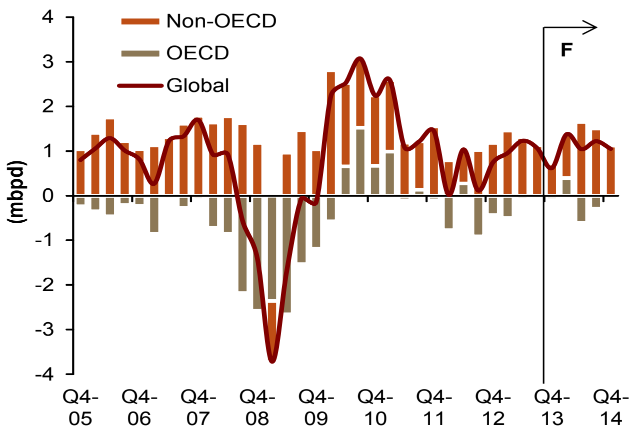
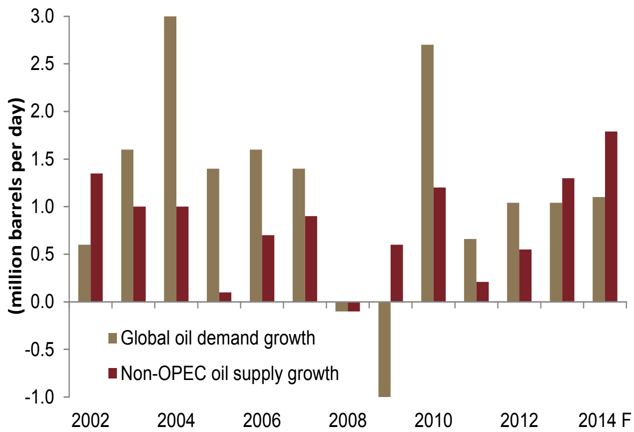


Figure 9: Global demand and non-OECD supply
(year-on-year change)



Budgetary performance in 2013

As expected, the 2013 fiscal outturns were better than the 2013 budget's projections…

The recent announcement by the Ministry of Finance also reveals that 2013 fiscal outturns were better than the 2013 budget's projections and slightly exceeded Jadwa's forecasts. At SR206 billion, the surplus was slightly above our SR201 billion forecasts. It was the equivalent of 7.4 percent of GDP. Higher oil revenues, the result of elevated oil prices ($109.6pb for Brent) and production (9.6mbpd), were the reason for the larger surplus. Spending was well in excess of the budgeted projection, but this was outweighed by the increase in oil revenues.

Total revenues is estimated at 1,131 billion in 2013, the second highest on record.

Revenue totaled SR1,131 billion (Jadwa: SR1,096 billion), the second highest revenues on record. It was 36 percent above the budgeted level, but 9.3 percent lower than their 2012 level as oil production fell by 2.3 percent in 2013. We estimated that the 2013 budget was based on a price for Saudi oil of $66 per barrel and production of 9.6 million barrels per day. With a few days of the year left, it seems likely that the actual price of Saudi oil will average $104pb. Actual level of oil production was in line with our forecasts. Non-oil revenues were SR113 billion, up around 11 percent on the 2012 total.

2013 Budget data
(SR billion)

	Budget	Actual	Difference
Revenues	829	1,131	302
Expenditures	821	925	104
Balance	8	206	198

Expenditure amounted to SR925 billion in 2013…

...5.9 percent higher than in 2012.

Expenditure amounted to SR925 billion (Jadwa: SR895 billion), 12.6 percent above the budgeted level and 5.9 percent higher than in 2012. The annual increase in 2013 was, however, lower than the average of the last five years (14 percent) as the effect of the 2008's and 2011's fiscal stimuli wane. Despite such moderate increase, the permanent measures of these two packages particularly on wages and other allowances kept spending elevated in 2013. The actual spending is 78 percent higher than its level five years ago. A breakdown of spending into capital and current expenditure was not published. It is important to note that the initial estimates of

Figure 10: Budgetary performance

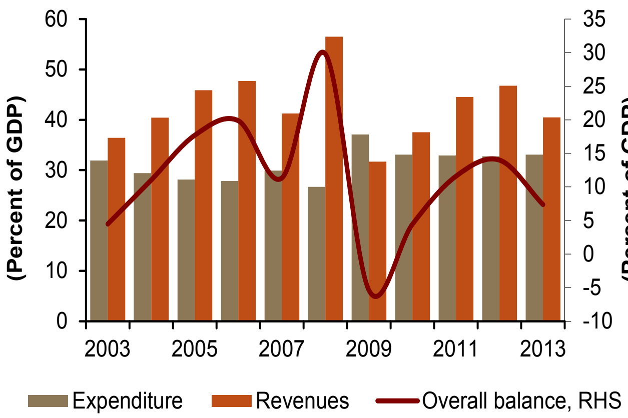
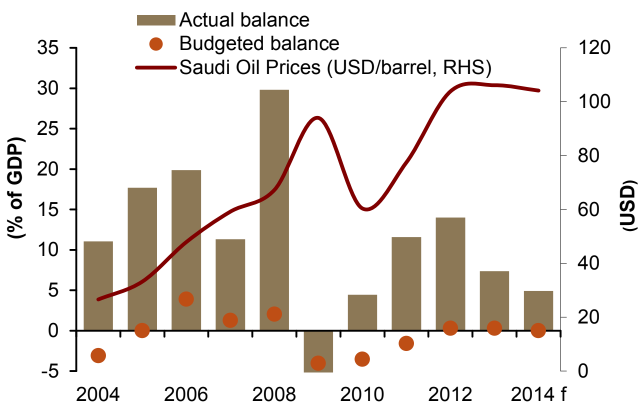


Figure 11: budgeted versus actual balance and oil prices



government spending and revenues contained in the budget statement tend to be revised. Generally, both are increased, with the rise in spending usually larger than that for revenue.

Public debt was reduced by SR23.7 billion to SR75.1 billion or 2.7 percent of GDP

Total outstanding government debt was projected to fall to SR75.1 billion by the end of 2013, equivalent to just 2.7 percent of GDP (Figure 12). It is worth noting that commercial bank holdings of government and quasi-government debt securities have increased by SR39 billion over the first 10 months of this year. Bank holdings of longer-term government bonds were up by SR5 billion to SR47.7 billion despite the fall in public debt. While a breakdown of such holdings is not available, we think this increase is mostly due to banks investment in quasi-sovereign sukuks including those issued by the General Authority of Civil Aviation. The remaining government debt is held by the two government pension funds, the General Organization for Social Insurance and the Public Pension Agency.

Economic performance in 2013

Overall growth slowed to 3.8 percent in 2013...

...owing to negative growth in the oil sector…

The Ministry of Finance budget announcement included preliminary macroeconomic data, which provide some insight into the government's view on economic performance this year and prospects for next year. This showed that overall economic growth slowed to 3.8 percent year-on-year due to negative growth in the oil sector. Non-oil economic growth was at 5 percent year-on-year 0.6 percentage point lower than our forecast. Non-oil private sector expanded by 5.5 percent compared with our forecasts of 6 percent. Lower oil prices this year compared with 2012 caused the nominal economic growth to slightly slow (1.5 percent year-on-year), but elevated oil revenues maintained a strong current account surplus. Inflation increased.

...as the Kingdom cut its oil production.

The performance of the non-oil private sector remains robust, expanding by 5.5 percent.

Real GDP growth slipped to 3.8 percent year-on-year (Jadwa: 4 percent). We had anticipated a slower economic growth compared to last year due to lower oil production. The Kingdom produced an average of 9.6mbpd so far this year compared with 9.8mbpd in 2012. As a result the oil sector contracted by 0.5 percent year-on-year. Instead, the growth stemmed from the non-oil economy particularly the private sector which expanded by 5.5 percent compared with 4.9 percent last year. The growth of government services, however, slowed to 3.7 percent year-on-year, its lowest growth since 2006.

Figure 12: Government debt

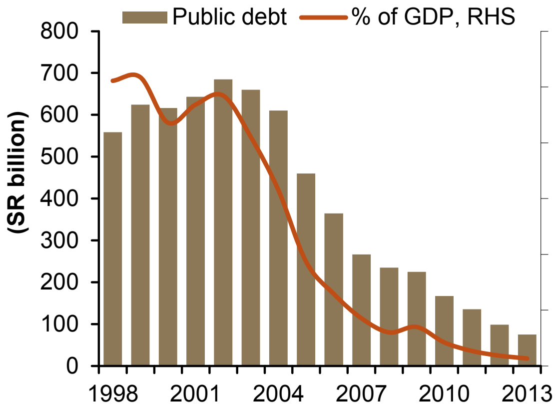
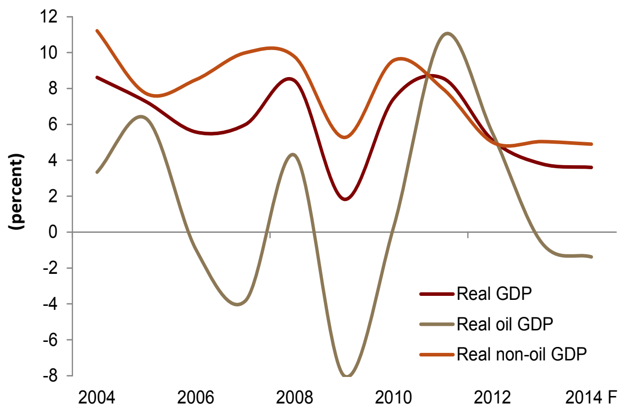


Figure 13: Real GDP growth
(year-on-year change)



The budget announcement seems to also include yet another revision to 2012's growth rate which is now revised upward to 5.8 percent compared to 5.1 percent previously. The announcement, however, did not include the revised breakdown for the GDP components in 2012.

Construction, transport and communication and retail sectors were the fastest growing sectors in 2013.

The **non-oil private sector** grew by 5.5 percent. We had anticipated an improvement in 2013 as consecutive years of elevated government spending lifted business and consumer confidence and banks' comfort in the lending environment despite another year of regional turbulence and slow global economic recovery. Some of the sectoral growth rates were slightly above what we had forecast, though the budget announcement confirms our expectations that construction, transport and communication and retail sectors would be the fastest growing sectors in 2013. These three sectors expanded by 8.1, 7.2, and 6.1 percent year-on-year in 2013 respectively. Growth in other sectors was also in line with expectations, with finance at 4.9 percent and non-oil manufacturing at 4.7 percent.

Inflation picked up in 2013 owing to higher food prices…

...though international food inflation remains subdued.

Inflation was put at an average of 3.35 percent, compared to 2.9 percent in 2012. This is slightly different than the inflation data produced on a monthly basis by the Central Department of Statistics. According to the Central Department of Statistics inflation averaged 3.6 percent over the first eleven months of 2013 compared with 3.5 percent for the same period last year. Based on this, inflation in December must fall to 0.9 percent year-on-year compared with 3 percent in November for the annual average to be in line with MoF estimate, an unlikely scenario in our view. The surge in consumer spending resulting from higher public sector wages and other labor market reform initiatives have fed into inflation, but given the extent of the spending, the rise in inflation from areas such as education and entertainment and transport and telecoms has been fairly modest. In fact, our measure of core inflation which excludes food and housing and related services has slowed to 2.6 percent in the first eleven months of this year compared with 2.9 percent for the same period of last year (Figure 15). Food inflation, however, rose from 4.4 percent in the first eleven month of 2012 to 5.9 percent for the same period this year. Another measure of inflation, the non-oil GDP deflator slowed to 1.85 percent from 3.8 percent in 2012. The non-oil GDP deflator is only available on an annual basis; it is the difference between nominal and real GDP, and measures the prices

Figure 14: Inflation
(year-on-year change)

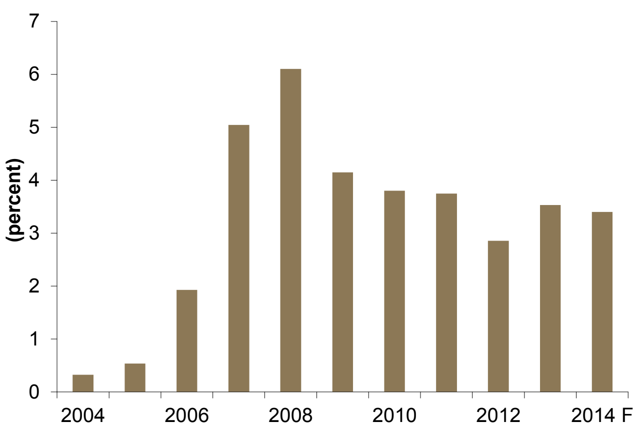
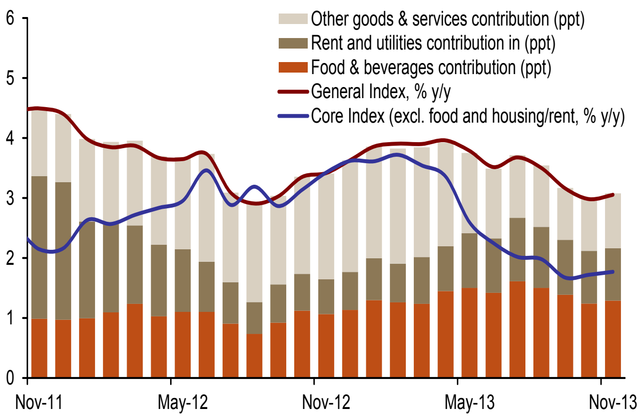


Figure 15: Food, rental and core inflation



Current account surplus recorded a surplus of $129.8 billion in 2013 down form $164.8 billion in 2012.

of all non-oil goods consumed in the economy.

The **current account surplus** recorded a surplus of $129.8 billion (SR486.7 billion), down from an all-time high of $164.8 billion in 2012 (Figure 17). Although a detailed breakdown of the current account is not published, it is clear that this surplus is mostly due to elevated oil revenues (oil revenues account for around 85 percent of total current account receipts). Elevated oil prices and production raised oil export revenues to SR1,180.6 billion, 86 percent of total export revenues. Non-oil exports rose by 3.9 percent, in line with our expectations as global demand for petrochemical product slowed during the year. Imports were up by 13.3 percent, broadly in line with the monthly trade data. Data for the first ten months of 2013 show that imports of transport equipment are well up on 2012. Data on the other components of the current account was not published.

The economic outlook for 2014

We expect 2014 to maintain the solid growth momentum particularly for the non-oil sector.

We expect 2014 to maintain the solid growth momentum albeit at slower pace. While overall economic growth will slow, this will be due to lower oil production. Greater execution of government investment projects, especially in the infrastructure sector, means that non-oil growth should maintain the current solid performance. Bank lending will remain supportive and regional unrest will be less of a drag on domestic performance. Inflation should be down a little as domestic spending pressures recede and external pressures stay subdued, though the risks are on the upside given the large liquidity in the market. Oil prices are expected to slightly fall as the market accommodate higher crude from North America, though the regional geopolitical risk in the Middle East will keep a floor on prices.

We expect overall growth to slightly fall to 3.6 percent in 2014…

...but the private non-oil sector Growth is likely to remain above 5 percent.

Economic growth in Saudi Arabia is forecast to ease to 3.6 percent in 2014, owing to lower oil production and large base-effect for the non-oil sector. High government spending will continue to be the engine of the non-oil economy, supported by greater bank lending and healthy domestic consumption demand. Within the non-oil sector, we expect the government's real GDP to expand 4 percent year-on-year due to higher capital spending and increased demand on government services, while the non-oil private sector is expected to expand by 5.2 percent. In particular, we expect construction,

Figure 16: International food prices
(year-on-year change)

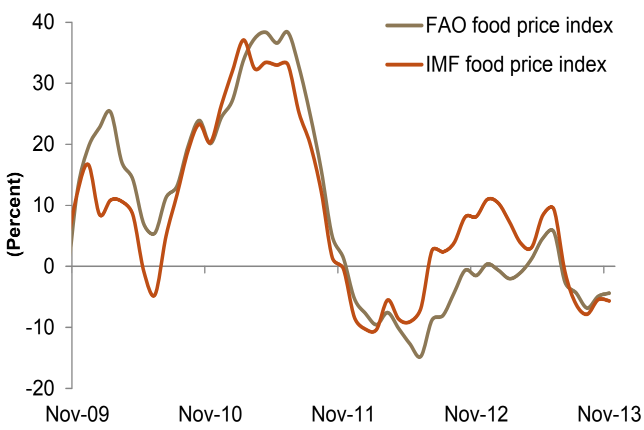
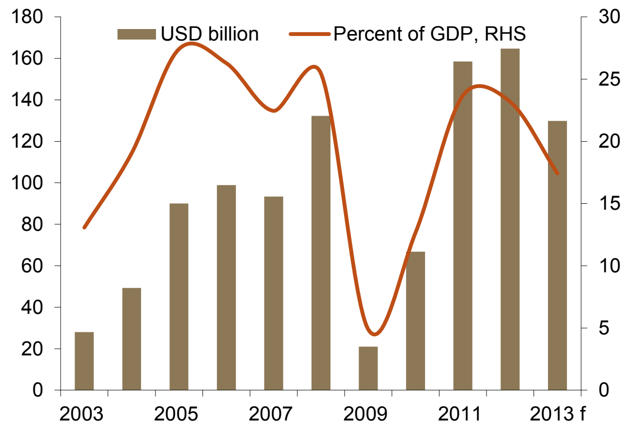


Figure 17: Current account



Inflation is expected to slightly fall to an average of 3.4 percent next year.

Lower oil revenues will cause the current account surplus to slip to 11.6 percent of GDP.

transportation, retail and utilities the main beneficiaries of government spending, to be the fastest growing sectors of the economy.

Inflation is expected to slightly fall to an average of 3.4 percent with rent and food prices the main contributors. External pressure on domestic prices is likely to remain weak particularly as international food inflation remained subdued (Figure 16). Rental inflation should decline as more properties enter the market, but it has been rising in the second half this year owing to higher consumer disposable income, which should mean any drop here will not be large. We also maintain our view that there will be some local inflationary pressure as a result of the high level of consumer and government spending. We do not foresee any changes to the riyal's peg to the dollar. Lower oil revenues will cause the current account surplus to slip to 11.6 percent of GDP.

2013 results and 2014 Jadwa forecasts

	2013 Actual	2014 Jadwa Forecast
Real GDP (% change)	3.8	3.6
Nominal GDP (% change)	4.8	3.5
Inflation (1999 =100, %)	3.5	3.4
Current account balance (SR billion)	486.7	335.4

Overall economic performance in 2014 will still be very heavily dependent on the government...

….with downside risks stemming mainly from external uncertainties.

While the economic picture will improve, performance in 2014 will still be very heavily dependent on the government. Elevated government spending remains affordable, but rising current spending increases budget rigidities further. The downside risks to our growth forecast stem from external uncertainties related to the balance of international oil market, the path of the US fiscal policy and the performance of emerging market economies.