جدوى للإستثمار
Jadwa Investment

November 2020

Macroeconomic Update

Not bad, all things considered

- A less steeper decline than expected in Q2, and a stronger recovery in Q3 has led us to revise our non-oil GDP forecast for the Kingdom in 2020. All in all, we expect non-oil GDP to decline by 2.7 percent (compared to -3 percent previously).

- At the same time, with no revisions to our oil GDP forecast (-4.8 percent), and a downward revision to government sector GDP, overall GDP in 2020 is expected to decline by 3.6 percent, marginally better than -3.7 percent previously.

- Looking out into 2021, despite there still being a considerable degree of uncertainty as a result of the prevalence of COVID-19, and its potential impact on the non-oil economy, we do nevertheless expect a broad-based recovery next year.

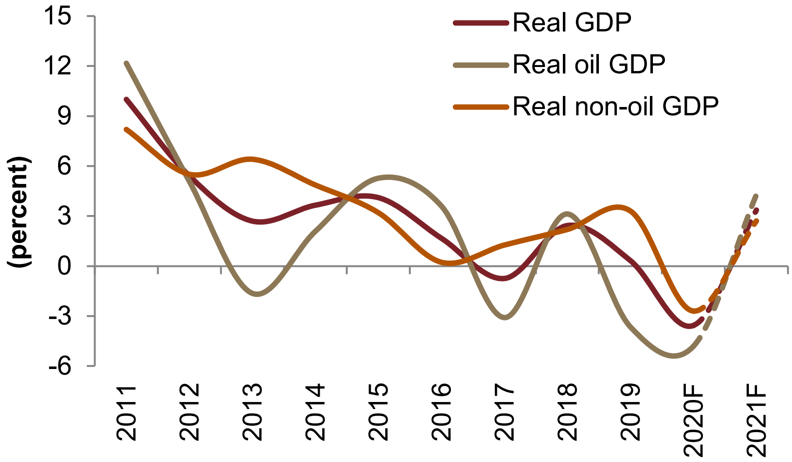
- The current time-line embedded in our forecast assumes a sizable roll-out of a vaccine by mid-2021 (with news of major breakthroughs by a number of vaccine developers announced recently). As such, we expect to see a more vigorous economic recovery in the second half of 2021.

- On the oil side, whilst our current forecast for Saudi crude oil production assumes OPEC+ adding an additional 1.9 million barrels per day (mbpd) to total output in January 2021, oil output could well be lower than forecasted if the alliance tapers back part of the planned rise at an OPEC+ meeting next week.

- On the fiscal side, we now expect the deficit to total SR298 billion (-10.9 percent of GDP) in 2020, down from our previous forecast of -SR363 billion (-13.4 percent of GDP). In 2021, a combination of higher yearly oil revenue and lower expenditure will result in the fiscal deficit narrowing to -SR171 billion (-5.6 percent of GDP).

- Overall, the main risk to our forecast relates to a second wave of COVID-19 occurring in the Kingdom before the roll-out of a vaccine, or indeed a delay in the current assumed timeline related to the roll-out of an effective vaccine.

Figure 1: Saudi Arabia's real GDP forecast



For comments and queries please contact:

Asad Khan
Head of Research
rkhan@jadwa.com

Nouf N. Alsharif
Senior Economist
nalsharif@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

Released: November-25-2020, 17:00 UTC+3

A less steeper decline than expected in Q2, and a stronger recovery in Q3 has led us to revise our non-oil GDP forecast for the Kingdom in 2020.

We expect non-oil GDP to decline by 2.7 percent (compared to -3 percent previously)…

...with this improvement being driven by better than expected non -oil private sector performance…

...at -3.6 percent (versus -4.5 percent previously)…

... with our non-oil private sector composite index showing economic activity rebounding sharply in Q3.

Overall GDP is expected to decline by 3.6 percent, marginally better than -3.7 percent previously.

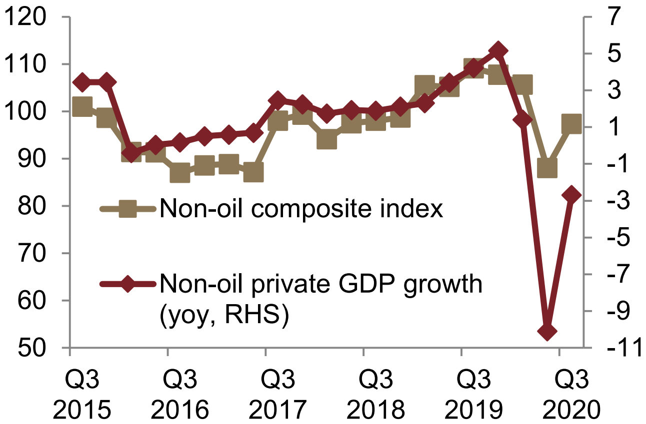
Non-oil GDP faring better than expected:

A less steeper decline than expected in Q2, and a stronger recovery in Q3 has led us to revise our non-oil GDP forecast for the Kingdom in 2020. In particular, we have upgraded a number of sectors' performances for the year. This includes the "Wholesale & Retail Trade, Restaurants & Hotels" and "Construction" sectors, both of which are still expected to see yearly declines, but at an improved rate compared to our previous forecast. Additionally, we now see the "Finance, Insurance & Business Services" sector registering growth during the year, albeit marginally (Box 1). All in all, we expect non-oil GDP to decline by 2.7 percent (compared to -3 percent previously) with this improvement being driven by better than expected non-oil private sector performance, at -3.6 percent (versus -4.5 percent previously) with our non-oil private sector composite index showing economic activity rebounding sharply in Q3 (Figure 2). At the same time, with no revisions to our oil GDP forecast (-4.8 percent), and a downward revision for government sector GDP (-0.5 percent versus 0.5 percent previously), overall GDP is expected to decline by 3.6 percent, marginally better than -3.7 percent previously.

Box 1. Non-Oil GDP Revision

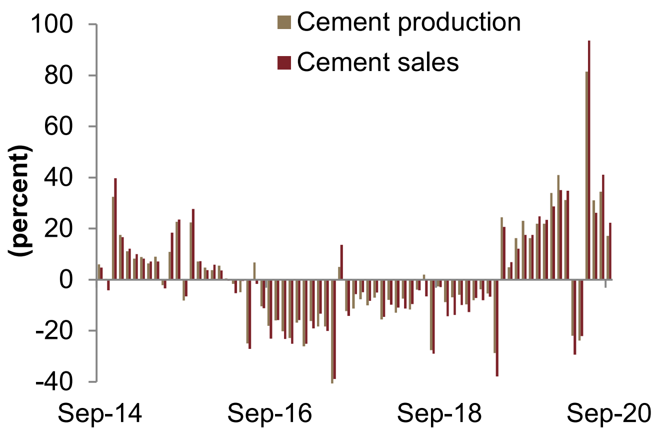
We scaled back the level of contraction in the "Wholesale & Retail Trade, Restaurants & Hotels" for 2020, due to better than expected consumer spending figures. In fact, POS transactions in the year-to-October were 22 percent higher year-on-year, primarily as a result of huge rises at 'gas stations' (up 275 percent), and 'food and beverages' (up 69 percent), versus the same period last year. These rises came about despite lower POS transactions being observed immediately after a hike in VAT in July. Meanwhile, proxy measures for the "Construction" sector also suggest better performance. Whilst cement sales and production dropped sharply during Q2, when strict lockdown measures were in place, a strong recovery was observed immediately after (Figure 3). We see this recovery primarily as a result of progress on mega-projects by the Public Investment Fund (PIF). Lastly, we now expect "Finance, Insurance & Business Services" to register a modest level of growth this year, as a result of higher yearly bank credit (see "Interest rates, liquidity and credit" section below) and a continued rise in ownership of homes. As outlined in our recent *Inflation* update, ownership of homes will be aided by i) a recent royal decree allowing government to bear the cost of a newly introduced property transaction tax for first time buyers, and ii) higher supply of affordable housing under the Ministry of Housing (MOH)'s Sakani program.

Figure 2: Jadwa's non-oil private sector composite index



*Jadwa estimates for Q3 2020 non-oil private GDP growth

Figure 3: Cement sales and production has rebounded strongly



Looking out into 2021, whilst there is still a considerable degree of uncertainty as a result of the prevalence of COVID-19…

...we do nevertheless expect a broad-based recovery next year.

The current time-line embedded in our forecast assumes a sizable roll-out of a vaccine by mid-2021…

...as such, we expect a more vigorous recovery in the second half of 2021.

Full year government oil revenue is expected to total around SR410 billion in 2020.

Looking further ahead into 2021, we see oil revenue rising 9 percent year-on-year.

Non-oil revenue is expected to rise by 13 percent over budgeted levels in 2020 as a whole.

Looking out into 2021, whilst there is still a considerable degree of uncertainty as a result of the prevalence of COVID-19, and its potential impact on the non-oil economy, we do nevertheless expect a broad-based recovery next year. The current time-line embedded in our forecast assumes a sizable roll-out of a vaccine by mid-2021 (with news of major breakthroughs by a number of vaccine developers announced recently). As such, we see a sequential quarter-on-quarter improvement in the Saudi economy over the remainder of the Q4 2020 and next year, with this recovery being more vigorous in the second half of 2021. On the oil side, whilst our current forecast for Saudi crude oil production (Figure 4) assumes OPEC+ adding 1.9 million barrels per day (mbpd) to total output in January 2021 (please see our recent *Oil Update* for more details), there is a risk that output could well be lower than forecasted if the alliance tapers back part of the planned rise at an OPEC+ meeting next week.

Unsurprisingly, the main risk to our forecast relates to a second wave of COVID-19 occurring in the Kingdom before the roll-out of a vaccine, or indeed a delay in the current assumed timeline related to the roll-out of an effective vaccine.

Fiscal deficit gradually decreasing:

Brent oil is currently trading around $48 per barrel (pb), with the year-to-date average at $41 pb, down 37 percent compared to the same period last year. Despite this, government oil revenue (at SR317 billion in the year-to-Q3) has been lifted by sizable dividends from Aramco, with full year government oil revenue is expected to total around SR410 billion in 2020. Looking further ahead, based on our full year 2021 Brent oil price forecast of $55 pb and oil production of 9.6 mbpd, we see oil revenue rising 9 percent year-on-year. That said, if Aramco were to continue paying dividend at levels similar to this year, we would expect to see a reasonably higher oil revenue than currently projected.

In the year-to-Q3, non-oil revenue was down 5 percent year-on-year (*for more on this please refer to our Q3 Budget Statement update*), but we expect to see a large rise in 'Other Revenue' receipts in Q4, helping push up non-oil revenue by 13 percent over budgeted levels in 2020 as a whole, to SR360 billion. Looking into 2021, we expect non-oil revenue to continue rising on a yearly basis on the back of higher tax receipts as the economy recovers. More specifically, we expect the full year effects of higher VAT levels to push overall non-oil revenue up 4 percent year-on-year, to SR373 billion (Figure 5).

Figure 4: We expect Saudi crude oil output to average 9.2 and 9.6 mbpd in 2020 and 2021

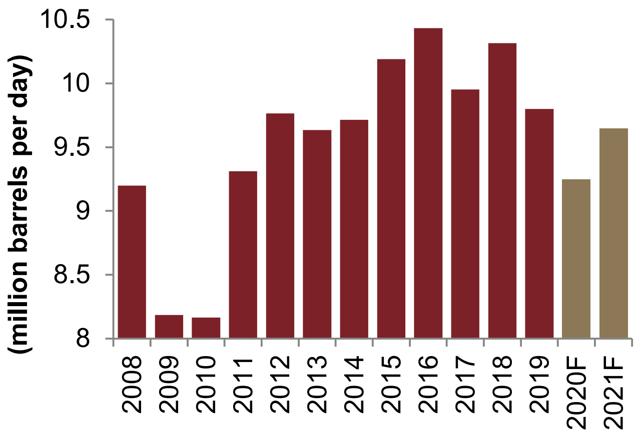
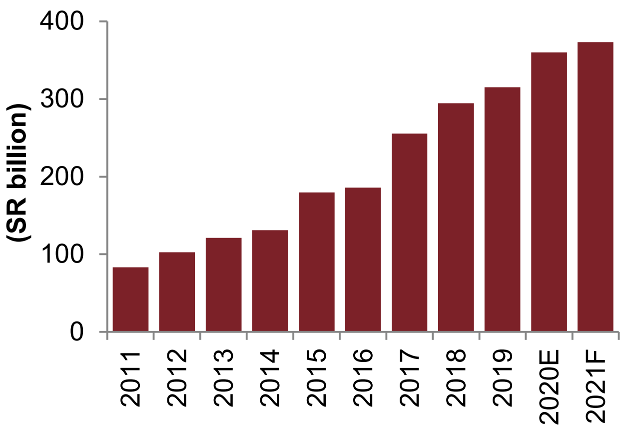


Figure 5: Non-oil revenue expected to be boosted by tax revenue in 2021



Meanwhile, capital expenditure will be squeezed in 2020 as a whole, with this segment expected to decline by 21 percent over both budgeted and year-on-year levels.

The recent preliminary budget report highlighted that 2020's expenditure is expected to be SR48 billion (or 5 percent) higher than previously projected, at SR1.068 trillion. The statement highlighted that whilst some reductions have taken place within certain segments of the budget, these have been subsequently re-allocated to other segments such as healthcare. In this context, capital expenditure will be squeezed in 2020 as a whole, with this segment expected to decline to SR137 billion, down 21 percent over both budgeted and year-on-year levels.

Next year's expenditure is expected to total SR990 billion, down 7 percent year-on-year…

Meanwhile, next year's expenditure is expected to total SR990 billion, down 7 percent year-on-year. That said, as has been the case in the last few years, capital expenditure will be boosted by the Public Investment Fund (PIF). As a part of its continued efforts in strengthening and diversifying the economy, the PIF is expected to inject around SR150 billion per year into the local economy in both 2021 and 2022, resulting in SR611 billion worth of cumulative investments into local economy between 2017-22 (Figure 6).

...although the PIF is expected to inject around SR150 billion per year into the local economy in both 2021 and 2022.

Taking into account adjustments in government revenue and expenditure, we now expect the fiscal deficit to total SR298 billion (-10.9 percent of GDP) in 2020, down from our previous forecast of -SR363 billion (-13.4 percent of GDP). In 2021, a combination of higher yearly oil revenue and lower expenditure will result in the fiscal deficit narrowing to -SR171 billion (-5.6 percent of GDP) (Figure 7).

Debt-to-GDP stabilizing:

In 2021, an additional SR87 billion in debt is expected to be issued during the year…

Public debt totaled SR848 billion at the end of Q3 2020, versus SR678 billion at the end of 2019. Looking ahead, we expect a further SR6 billion in new debt, plus circa SR9 billion in refinancing during Q4, thereby pushing total debt issuance and refinancing to SR220 billion during 2020. In 2021, an additional SR87 billion in debt is expected to be issued during the year, resulting in total debt reaching SR941 billion, with debt-to-GDP remaining unchanged at circa 31 percent, according to our forecasts.

...resulting in total debt reaching SR941 billion, with debt-to-GDP at circa 31 percent.

External sector:

Monthly trade data shows that the Kingdom's trade balance moved back into a thin surplus recently.

Monthly trade data shows that the Kingdom's trade balance moved back into a thin surplus recently, having dropped into deficit earlier this year, with the improvement being brought about by a recovery in oil exports (Figure 8). Meanwhile, latest available data shows that non-oil exports were still down 15 percent year-on-year in the year-to

Figure 6: PIF's investment into local economy expected to total SR611 billion between 2017-22

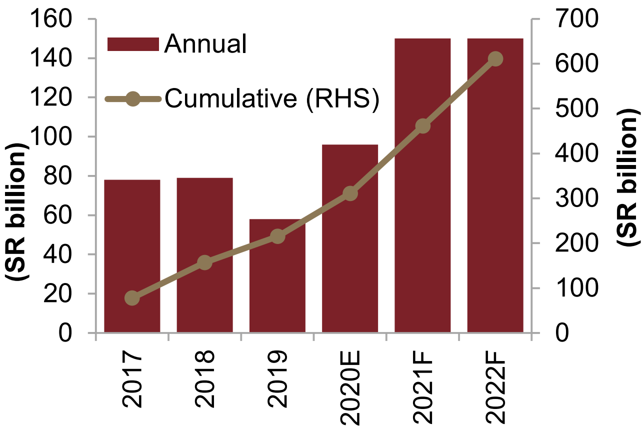
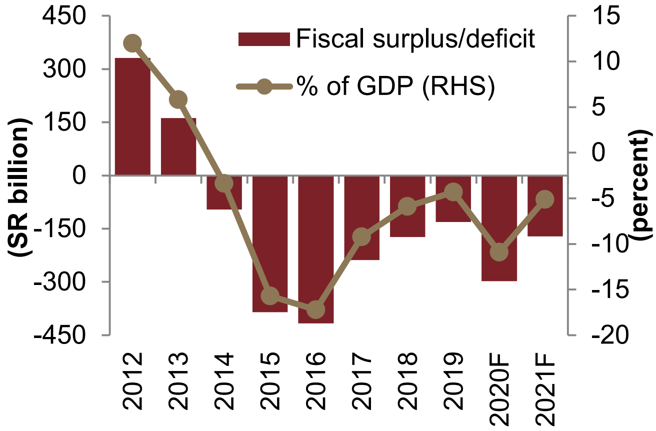


Figure 7: Fiscal deficit will narrow in 2021, but remain sizable



Looking ahead, we expect non-oil exports to continue struggling during the remainder of the year…

...with a slight improvement in 2021.

-September. Looking ahead, we expect non-oil exports to continue struggling during the remainder of the year, especially as a number of key export markets (such as the EU) grapple with a second wave of COVID-19. Looking ahead into 2021, we see an improvement in both oil and non-oil exports. Whilst higher oil prices and crude oil output will push oil exports up 23 percent year-on-year, we estimate non-oil exports rising less aggressively, at around 8 percent year-on-year.

We see the overall economic recovery supporting an improvement in import demand…

...although this will be capped by the existence of higher VAT and import duties as well continued weakness in the trade weighted dollar.

Meanwhile, year-to-September data shows that the value of goods imported fell by 16 percent on a yearly basis. Unsurprisingly, the steepest declines were seen during Q2, when the Kingdom's economy was affected by pandemic induced lockdowns. Looking at the remainder of 2020, we expect imports to struggle, with import volume data (till October) showing no sign of a recovery. Next year, we see the overall economic recovery supporting an improvement in import demand, although this will be capped by the existence of a higher VAT and import duties (since H2 2020) as well as continued weakness in the trade weighted dollar. All of these factors will raise the relative cost of imports for Saudi Arabia, thus preventing a sharp rebound in 2021.

"Remittances" are up 19 percent year-to-date compared to the same period last year…

...but we expect these to decline next year due to a decline in the number of expats.

As we highlighted previously, some items in the invisible balance such as "Travel" and "Transportation", are likely to see lower levels of outflow due to pandemic related travel restrictions during 2020. At the same time, "Remittances", which are up 19 percent year-to-date compared to the same period last year, were likely to rise despite a large number of expat departures (*please refer to our previous macroeconomic update*). In 2021, we see a reversal in both of these trends. Firstly, "Travel" and "Transportation" outflows will rise as a ban on commercial air travel is lifted, and "Remittances" will decline due to a decline in the number of expats (with private healthcare insurance data implying a departure of around 800 thousand expat and expat dependents so far this year).

Overall, whilst we now expect 2020 current account balance to hit a deficit of $17 billion (or -2.4 percent of GDP)…

….this should flip to a surplus of next year equal to 2.3 percent of GDP.

Overall, whilst we now expect 2020 current account balance to hit a deficit of $17 billion (or -2.4 percent of GDP), this should flip to a surplus of next year equal to 2.3 percent of GDP, according to our forecast (Figure 9).

Figure 8: Trade balance has swung back into a surplus recently

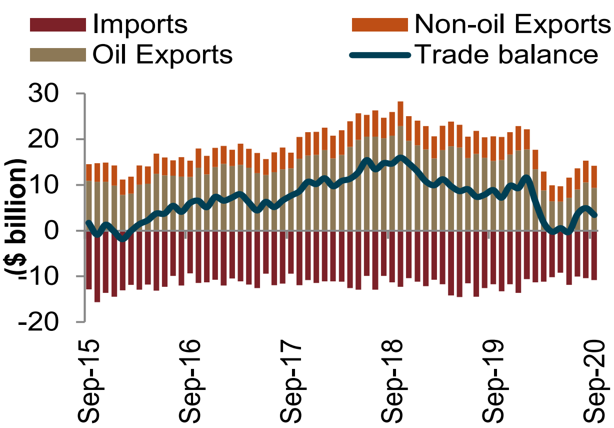
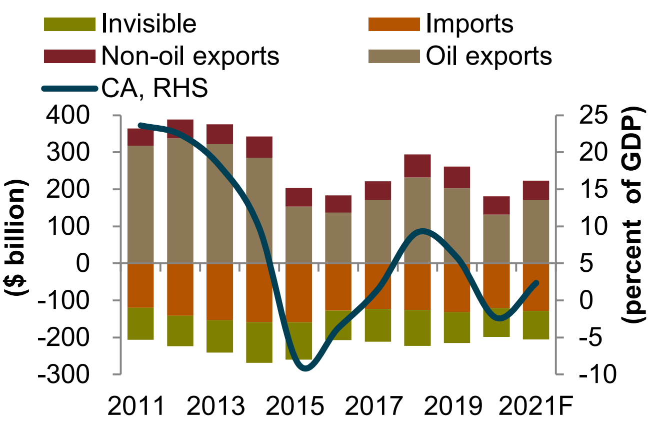


Figure 9: Current account expected to flip into a modest surplus in 2021



Overall, total bank credit to the private sector picked up dramatically during Q3 2020…

...rising by 15 percent on a year-on-year basis.

Looking forward, higher levels of credit are expected to continue in Q4 and the year ahead…

...especially so in sectors that remain under precautionary measures related to COVID-19.

Looking ahead, we expect see some rises in the cost of borrowing next year.

In 2021, we expect to see prices rising by 3.7 percent…

Interest rates, liquidity and credit:

Overall, total bank credit to the private sector picked up dramatically during Q3 2020, rising by 15 percent on a year-on-year basis (whilst a rise of 4 percent year-on-year was seen during the same period last year). More specifically, "Utilities: Water and Electricity " saw the largest rise in credit amongst sectors, with around SR2.7 billion in new credit, quarter-on-quarter. "Commerce" saw the second largest rise, which is unsurprising considering it was one of the more deeply affected sectors by pandemic related lockdowns earlier this year. Meanwhile, "Agriculture" and "Mining" saw lower levels of credit compared to the previous quarter (Figure 10). Looking forward, higher levels of credit are expected to continue in Q4 and the year ahead, especially so in sectors that remain under precautionary measures related to COVID-19 (such as "Commerce", "Transport" and "Services").

Meanwhile, SAIBOR (the price of lending between banks for Riyals) remains at five year lows having been on a downward trend since the end of 2018 (Figure 11). Looking ahead, we expect to see some rises in the cost of borrowing next year due to a number of expected developments. On the one hand, measures such as the Saudi Central Bank's (SAMA) deferred payments program and a SR50 billion zero-interest one-year deposit at banks are set to expire at the end of 2020 and mid-2021, respectively, which will likely weigh on the banking sector's loan-to-deposit ratio and loan loss provisions. Additionally, higher levels of liquidity so far this year have been partly supported by the lack of spending opportunities for households, especially during severe periods of lockdown, which, in turn, has contributed to higher households savings (a trend we highlighted in our previous update). As the economy recovers during the course of next year, more spending opportunities for households are likely to arise, especially in relation to services. As such, we expect the build in private deposits at banks to slow, or even reverse for some time during 2021, adding to moderately tighter liquidity conditions.

Inflation:

In the year-to-October, prices rose by 3 percent year-on-year, boosted mainly by a rise in VAT from 5 to 15 percent from July onwards. More specifically, Q3 inflation rate hit 6 percent, compared to a lower average of almost 1 percent during Q2 2020. In 2021, we expect to see prices rising by 3.7 percent, supported by a rebound in activity and higher demand in many sectors such as 'Restaurants and Hotels' and 'Transport'. At the same time, we expect deflationary

Figure 10: Credit by sector in Q3 2020 (vs. Q2 2020)

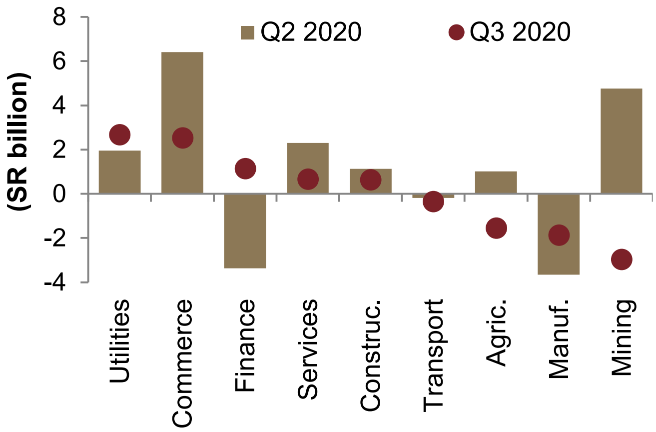
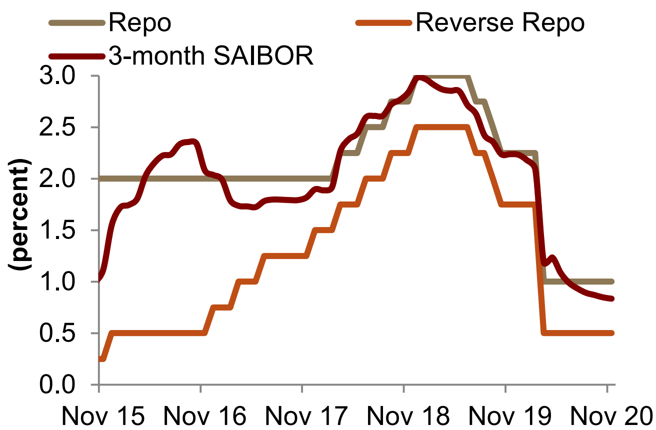


Figure 11:SAIBOR likely to trend mildly higher in 2021



...supported by a rebound in activity and higher demand in many sectors.

pressures to continue in the 'Housing and Utilities' segment as a result of 'Rentals for Housing' being affected by higher rates of home ownership (as discussed in our latest *inflation* report).

Risks to forecast

The main risk to our forecast relates to a second wave of COVID-19, or indeed a delay in current assumed timeline related to the roll-out of an effective vaccine.

Whilst uncertainty related to COVID-19 will persist, the overall business environment is expected to progressively improve in the remainder of 2020 and 2021, with this recovery being more vigorous in the second half of 2021. That said, the main risk to our forecast relates to a second wave of COVID-19 occurring in the Kingdom before the roll-out of a vaccine, or indeed a delay in current assumed timeline related to the roll-out of an effective vaccine.

Disclaimer of Liability

Key Data

	2014	2015	2016	2017	2018	2019	2020F	2021F	2022F
Nominal GDP									
(SR billion)	2,836	2,454	2,419	2,582	2,934	3,044	2,730	3,069	3,299
($ billion)	756	654	645	689	782	812	728	818	880
(% change)	1.3	-13.5	-1.4	6.8	13.6	3.7	-10.3	12.4	7.5
Real GDP (% change)									
Oil	2.1	5.3	3.6	-3.1	3.1	-3.6	-4.8	4.3	12.0
Non-oil private sector	5.4	3.4	0.1	1.5	1.9	3.8	-3.6	3.2	3.0
Non-oil government	3.7	2.7	0.6	0.7	2.9	2.2	-0.5	1.5	1.0
Total	3.7	4.1	1.7	-0.7	2.4	0.3	-3.6	3.4	6.4
Oil indicators (average)									
Brent ($/b)	99	52	43	54	71	66	43	55	55
Production (million b/d)	9.7	10.2	10.4	10.0	10.3	9.8	9.2	9.6	10.9
Budgetary indicators (SR billion)									
Government revenue	1,044	616	519	692	906	917	770	819	900
Government expenditure*	1,140	1,001	936	930	1,079	1,048	1,068	990	955
Budget balance	-96	-385	-417	-238	-173	-131	-298	-171	-55
(% GDP)	-3.4	-15.7	-17.2	-9.2	-5.9	-4.3	-10.9	-5.6	-1.7
Gross public debt	44	142	317	443	560	678	854	941	1016
(% GDP)	1.6	5.8	13.1	17.1	19.1	22.3	31.3	30.7	30.8
Monetary indicators (average)									
Inflation (% change)	2.2	1.2	2.1	-0.8	2.5	-2.1	3.0	3.7	1.5
SAMA base lending rate (%, end year)	2.0	2.0	2.0	2.0	3.0	2.3	0.75	0.75	1.25
External trade indicators ($ billion)									
Oil export revenues	285	153	137	171	232	202	132	171	202
Total export revenues	342	204	184	222	294	262	181	224	259
Imports	158	159	128	123	126	132	121	128	130
Trade balance	184	44	56	98	169	129	61	96	129
Current account balance	74	-57	-24	10	72	47	-17.3	19	54
(% GDP)	9.8	-8.7	-3.7	1.5	9.2	5.8	-2.4	2.3	6.1
Official reserve assets	732	616	536	496	497	500	432	428	443
Social and demographic indicators									
Population (million)	30.3	31.0	31.7	32.7	32.5	32.6	31.8	32.0	32.3
Saudi Unemployment (15+, %)	11.7	11.5	12.5	12.8	12.7	12.0	12.0	11.8	10.5
GDP per capita ($)	24,962	21,095	20,318	21,048	24,065	24,890	22,856	25,543	27,235

Sources: Jadwa Investment forecasts for 2019 and 2020. General Authority for Statistics for GDP and demographic indicators, Saudi Arabian Monetary Agency for monetary and external trade indicators, Ministry of Finance for budgetary indicators.
*Note: 2016 government expenditure includes SR105 billion in due payment from previous years.