جدوى للإستثمار
Jadwa Investment

September 2014

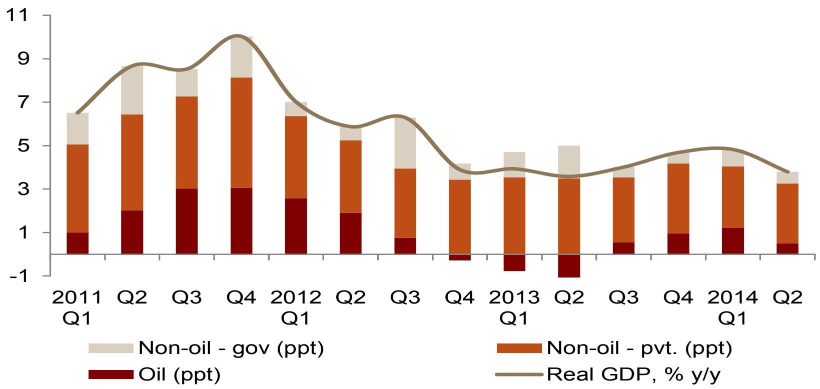
Quarterly GDP update:
Oil sector dragged down overall growth in Q2

- In real terms, the Saudi economy was 3.8 percent larger in the second quarter of 2014 than in the same quarter of 2013 and 1.3 percentage point lower than in the first quarter of this year.
- Contribution to growth has changed compared to the previous quarter and has became more dependent on the non-oil sector.
- We assume that year-on-year economic growth will be lower in the second half of the year, owing to a decline in oil sector output, while the non-oil private sector will remain robust.

The Central Department of Statistics and Information (CDSI) has released GDP data for Q2 2014 which showed a slight decline in real economic growth to 3.78 percent, year-on-year, compared with 3.79 percent in Q2 2013 (Figures 1 and 2). Contribution to growth has changed compared to the previous quarter and was more dependent on the non-oil sector. The contribution of the oil sector declined to 0.5 percentage points of the overall economic growth in the second quarter. The non-oil sector also recorded its slowest annual growth since such data was first published in 2010, though it still remains robust at 4.2 percent, year-on-year. The deceleration was due to a moderation in both the non-oil private sector and the government sector, compared to the same quarter last year. The slower annual growth in the private sector was observed in four out of nine sectors, including wholesale & retail trade, construction, transport, and finance subsectors.

The **oil sector** grew by 2.5 percent, year-on-year (Figures 2 and 4), compared to the previous quarter at 6.1 percent, but still higher year-on-year, when the sector contracted by 6.5 percent. Oil production is the central driver of the performance of the oil sector. Q2 2014 oil output rose by 1.9 percent, year-on-year, to 9.7 million barrel per day (mbpd). Looking forward, we think the contribution of the oil sector to

Figure 1: Slowing GDP, but robust private sector performance



Real GDP growth
(percent)

	Quarterly change	Annual change
2014-Q2	-3.1	3.8
2014-Q1	4.1	5.1

Comparative economic growth
(2014-Q2, year-on-year change)

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At 3.6 percent, real economic growth was lower compared to the previous quarter…

overall economic growth is likely to shrink -with the possibility of it turning negative in the second half of 2014- as rising domestic demand and lower oil prices set in for the remainder of 2014 .

… with the decline coming from both oil and non-oil sectors...

...however, non-oil sectors retained their position as the main contributor to economic growth…

Non-oil GDP growth expanded by 4.2 percent year-on-year compared with 4.5 percent in the previous quarter and 6.5 percent in the same period last year. Within the non-oil sector, the **government sector** grew by 2.6 percent year-on-year, expanding at a slower rate compared to the previous quarter. The contribution of government services to overall economic growth declined due to a larger base effect, but is projected to pick up again towards the end of the year. This is due to the nature of growth in government services which normally accelerates in the second half of the year. We also still maintain our view that labor market reform and enforcement of labor law will maintain elevated demand for government services.

… driven mainly by a robust private sector growing by 4.7 percent...

...whereas government services expanded at a slower pace...

At annual growth rate of 4.7 percent, the **non-oil private sector** remained the main contributor to overall economic growth. The growth rate was marginally higher than the 4.6 percent recorded in Q1 2014, but lower than the 6.1 percent recorded in the same period last year. We calculate that the sector contributed to 73 percent of overall growth in the second quarter of this year. We expect the private sector to maintain a robust level of growth supported by strong domestic demand, rising bank lending and public sector investment.

… meanwhile, oil sector growth slowed to 2.5 percent.

The utilities sector was the fastest growing private sector, rising by 8 percent.

While all sectors registered a positive year-on-year growth in the second quarter, their performance varies (Figures 2, 3 and 5). **The utilities sector** was the fastest growing private sector, rising by 8 percent. The rise was driven by more projects commencing operations to meet growing demand for electricity and water. Two leading examples include the completion of Saudi Electricity

Figure 2: GDP growth composition

	Percentage change (q/q)				Percentage change (y/y)			
	2013	2014	Q2-14		2013	2014	Q2-14	
	Q2	Q1	q/q	Contribution (ppt)	Q2	Q1	y/y	Contribution (ppt)
Oil Sector	-1.7	-0.8	-5.1	-1.0	-6.5	6.1	2.5	0.5
Non-Oil Sector	-2.4	5.6	-2.8	-2.2	6.5	4.5	4.2	3.3
Private Sector	-6.2	11.2	-6.2	-3.8	6.1	4.6	4.7	2.8
Government Sector	10.3	-9.9	8.5	1.6	7.6	4.2	2.6	0.5
By sector								
Agriculture	-4.7	24.0	-5.0	-0.2	0.8	1.9	1.6	0.1
Mining and quarrying	-2.1	-0.5	-5.8	-1.1	-6.6	5.8	1.9	0.3
Of which: crude petroleum & natural gas	-2.0	-1.0	-5.9	-1.0	-6.9	6.0	1.9	0.3
Manufacturing	-7.4	12.0	-7.6	-1.1	3.2	6.9	6.7	0.9
Electricity, gas and water	53.9	-17.9	63.0	1.0	0.8	1.9	8.0	0.2
Construction	-3.3	12.5	-3.0	-0.2	9.1	5.6	5.9	0.4
Wholesale & retail trade	-15.6	10.1	-15.5	-2.1	7.4	3.8	3.9	0.5
Transport & communication	-5.6	9.7	-6.0	-0.6	7.5	6.6	6.1	0.6
Finance	-3.8	11.5	-4.1	-0.6	6.5	3.7	3.4	0.5
Personal services	-0.7	5.8	-0.5	0.0	4.2	1.8	2.1	0.1
Government services	15.1	-15.4	13.0	1.7	7.9	3.5	1.6	0.3
Real GDP	**-1.8**	**4.1**	**-3.1**	**-3.1**	**3.8**	**5.1**	**3.8**	**3.8**

Manufacturing sector growth was also robust at 6.7 percent…

… with petroleum refining recording its highest year-on-year growth in two years at 8.5 percent…

… other manufactured products also recorded robust growth at 6.5 percent.

Changes in labor market continued to push down growth in leading sectors…

...nevertheless, growth remained robust, driven by strong fundamentals.

In quarter-on-quarter terms, the economy contracted by 3.1 percent…

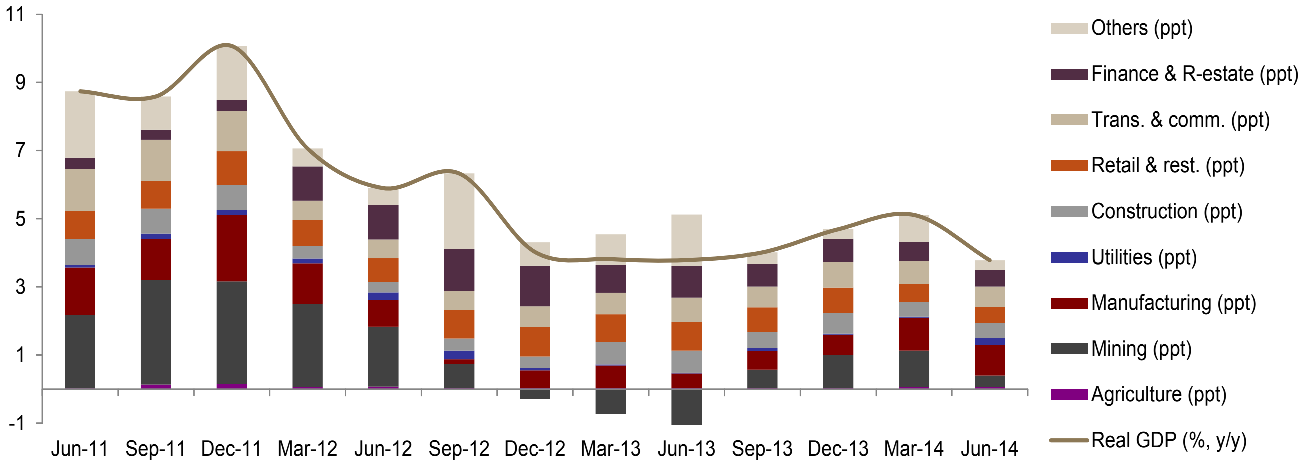
… which was in line with the seasonal trend.

Company's (SEC) USD 550 million combined power plant in the Eastern Province in June, adding a total of 800 mega watt power to the Kingdom's installed capacity . Another project includes the USD 150 million district cooling plant in Makkah, completed in May and adds 55,000 tons of refrigeration for the district. Further, the sector's total investments for 2014 are projected to reach USD 35.7 billion. **The manufacturing sector** grew by 6.7 percent year-on-year, with petroleum refining recording its highest year-on-year growth in two years at 8.5 percent. Output of other manufactured products was robust as it grew by 6.5 percent year-on-year, which is also its highest rate in two years. We expect the contribution of the petroleum refining to overall economic growth to gradually increase as the Kingdom expands its refining capacity over the next few years.

Year-on-year growth in the **construction, wholesale & retail trade, and transport** sectors was lower compared to the same period last year. However, growth for these sectors was again robust at 5.9 percent, 3.9 percent, and 6.1 percent respectively. We maintain our view that these sectors will remain amongst the fastest growing sectors despite an expected continuation of a year-on-year slowdown compared to last year's growth rates. The construction sector will remain the prime beneficiary of massive investments in buildings infrastructure, commercial and residential projects. According to the Middle East Economic Digest, the value of ongoing and planned projects in the Kingdom reached USD1.1 trillion at the end of July, most of which have an element of construction. The retail sector is likely to maintain robust growth over the coming quarters as indicated by solid domestic consumption demand. The slower year-on-year growth in both sectors can be partially attributed to both the recent labor market reforms as well as larger base effects. Transport growth stems from the need to move a high volume of goods around the Kingdom (both imports and construction materials), and is partially dependent on other sectors' performance.

In quarter-on-quarter terms, the economy contracted by 3.1 percent compared with a 4.1 percent expansion in the previous quarter. However, this was in line with the seasonal trend. All sectors recorded negative quarter-on-quarter growth rates except for utilities and government, which expanded by 63 percent and 13 percent, respectively. The expansion in the utilities sector reflects the rise in residential and commercial power consumption due to much higher

Figure 3: Sectoral contribution to real GDP growth



We assume that year-on-year economic growth will continue to ease in the third quarter…

use of air conditioning. Three sectors recorded large quarterly drops in output in the second quarter. The first was the wholesale & retail trade sector (down by 15.5 percent quarter-on-quarter), previous trend shows that the second quarter is generally the weakest quarter for this sector, reflecting both a seasonal trend as well as a continuation of the impact of recent changes in the market. The second and third sectors were manufacturing (down by 7.6 percent quarter-on-quarter), and transport (down by 6.0 percent quarter-on-quarter) reflecting a seasonal trend, and dampened output due to rising temperatures.

...with lower growth in oil production being a main factor…

… nonetheless, we expect both government and private sectors to maintain their solid performance.

We maintain our forecast for real GDP growth for 2014 at 4.2 percent.

We expect year-on-year economic growth to ease further in the third quarter. In addition to much lower projections for oil prices and rising domestic demand, the new norm for the domestic labor market will continue its negative impact on annual growth of the next two quarters. Nonetheless, we expect both government and private sectors to maintain robust growth which will sustain a healthy economic performance. Year-on-year bank lending continues to grow at double digits (Figure 6) and business surveys point to an expanding private sector (Figure 7). With solid local fundamentals, but considerable uncertainty over regional instability, we maintain our forecast for total real GDP growth for 2014 at 4.2 percent with risks tilted toward the downside if oil prices continue to decline.

Figure 4: Oil production and real oil GDP
(year-on-year)

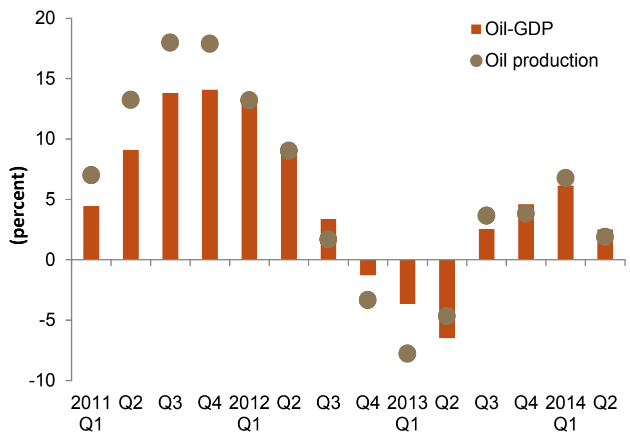


Figure 5: Quarterly real GDP growth
(year-on-year)

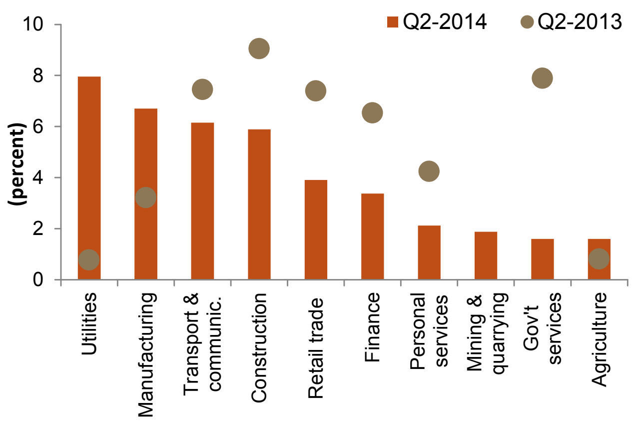


Figure 6: Credit to private sector

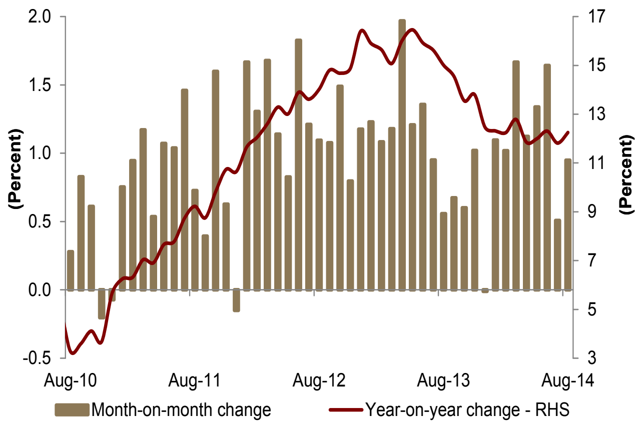
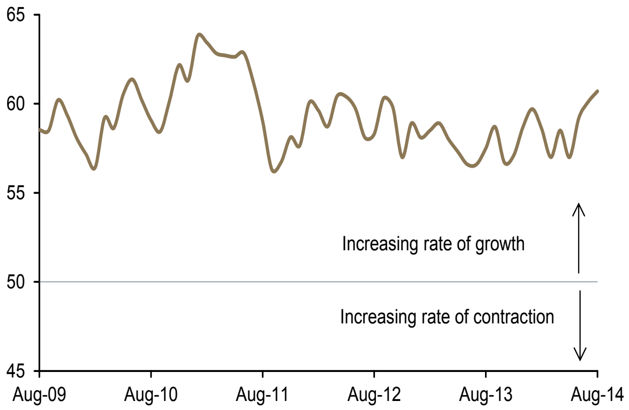


Figure 7: Purchasing Manager Index



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