



Inflation update—March 2015

CPI slows for the Seventh consecutive month

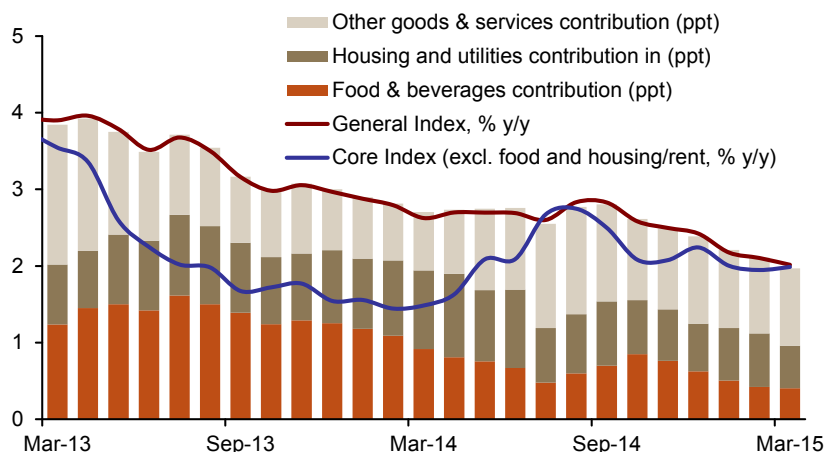
- Saudi CPI slowed to 2.0 percent year-on-year in March, its lowest point since December 2006.
- Food price inflation continued to slow for the fifth consecutive month to reach 1.7 percent.
- Housing inflation reversed its accelerating trend in the previous three months as it slowed to 2.2 percent in March.

The Central Department of Statistics and Information (CDSI) has released Consumer Price Index data for March, showing a deceleration in prices to 2.0 percent year-on-year compared to 2.1 percent in February. Foodstuffs continued to slow as the deflationary trend in international food prices grew further. Housing remained the major contributor to overall inflation despite a slowdown in March (Figures 1 and 2). Our estimate of core inflation, which excludes food and rent and other housing services, remained almost unchanged at 2 percent since the start of 2015, which we believe is being supported by strong domestic consumption. The combination of slowing food and housing inflation caused the contribution of the core index towards overall inflation to rise in March.

The contribution of both housing inflation and foodstuffs to overall inflation fell from 35 percent and 21 percent in February to 28 percent, and 20 percent in March, respectively (Figure 3). This was accompanied by a rise in the contribution of other components of the core index from 49 percent to 50 percent during the same period.

Foodstuffs reached 1.7 percent year-on-year in March, continuing its downward movement for the fifth consecutive month, impacted in part by the deflationary trend in international food prices (Figure 4). The recent fall in wholesale food inflation gives an indication of further declines to consumer foodstuffs in the coming months (Figure 5). On

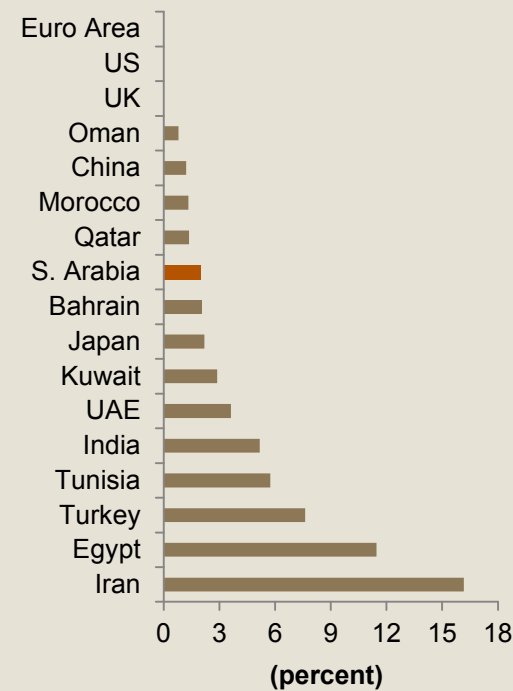
Figure 1: CPI inflation slows, but the core index unchanged



Saudi CPI inflation (percent)

| | Monthly change | Annual change |
|---------------|----------------|---------------|
| March 2015 | 0.1 | 2.0 |
| February 2015 | 0.0 | 2.1 |

Trading partner inflation rate (latest, year-on-year change)



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The rent segment slowed to 3.2 year-on-year in March.

The Ministerial approval to impose empty land fees will have a downward impact on rental inflation only in the longer-run.

Year-on-year inflation for clothing, furnishings, transport, and communication accelerated...

... with the two months salary bonus boosting consumer demand for such products.

We maintain our estimates for an average annual inflation rate at 2.5 percent for 2015.

monthly terms, food prices fell by 0.3 percent, continuing negative month-on-month growth for the fourth consecutive month.

Housing inflation recorded a slowdown in March to 2.2 percent, down from 2.8 percent in February. The rent segment -which plays a major part in the housing inflation component- slowed to 3.2 year-on-year in March, down from 4 percent recorded in the previous month (Figure 6). Nevertheless, the slow progress in government housing initiatives means that the shortage in supply of homes should persist through 2015, and thus continue to put upward pressure on home prices and rents. The Ministerial approval to impose empty land fees will have a downward impact on rental inflation only in the longer-run. The impact will particularly be felt in a second round effect following the announcement and implementation of a detailed mechanism for imposing such fees.

Most subgroups of the core index accelerated slightly during March (Figure 7). Year-on-year inflation for clothing, furnishings, transport, and communication accelerated. The transport subgroup -which has the third highest weight in the CPI basket- continued to accelerate for the third consecutive month to reach 0.9 percent, while the communication subgroup recorded the highest acceleration to reach 1.3 percent in March, up from 0 percent during the previous month. We see that the acceleration in most subgroups of the core index is a result of strong consumer spending in the economy. The two months salary bonus announced in late January has already caused monetary aggregates to grow significantly in February (Figure 8).

A combination of a strengthening USD, and falling global commodity prices, leads us to estimate that external food price pressure is likely to be muted in the short-term. Nevertheless, we expect domestic inflationary pressure to be the main source of inflation for the remainder of 2015. The continued housing supply shortage should persist throughout the year, while elevated government spending and strong growth in deposits should mean a continuation of strong domestic consumption. The combination of these factors leads us to maintain our estimates for an average annual inflation rate at 2.5 percent for 2015.

Figure 2: Main highlights of Saudi CPI inflation

(percent)

| | Weights | Month-on-month | | | Year-on-year | | | YTD |
|---------------------------|--------------|----------------|-------------|--------------------|--------------|------------|--------------------|------------|
| | | Feb-15 | Mar-15 | Contribution, ppt. | Feb-15 | Mar-15 | Contribution, ppt. | |
| Food & beverages | 21.7 | -0.3 | -0.3 | -0.1 | 1.7 | 1.7 | 0.4 | -1.2 |
| Housing & related items | 20.5 | 0.3 | 0.2 | 0.0 | 2.8 | 2.2 | 0.6 | 1.2 |
| Tobacco | 0.5 | 0.1 | 0.7 | 0.0 | 1.9 | 2.6 | 0.0 | 1.2 |
| Clothing & footwear | 8.4 | 0.0 | 0.7 | 0.1 | 2.2 | 2.4 | 0.2 | 0.6 |
| Home furniture | 9.1 | 0.1 | -0.2 | 0.0 | 2.8 | 3.0 | 0.3 | 0.1 |
| Medical care | 2.6 | 0.0 | 0.1 | 0.0 | 3.0 | 3.1 | 0.1 | 0.5 |
| Transport | 10.4 | -0.2 | 0.2 | 0.0 | 0.7 | 0.9 | 0.1 | -0.7 |
| Communication | 8.1 | 0.5 | 0.3 | 0.0 | 0.0 | 1.3 | 0.1 | 0.9 |
| Recreation & culture | 3.5 | -0.3 | 0.3 | 0.0 | 9.1 | 9.2 | 0.3 | 0.7 |
| Education | 2.7 | 0.0 | 0.0 | 0.0 | 0.5 | 0.5 | 0.0 | 0.0 |
| Restaurants & hotels | 5.7 | 0.0 | 0.5 | 0.0 | 0.4 | 0.2 | 0.0 | 0.2 |
| Other expenses & services | 6.8 | -0.4 | -0.3 | 0.0 | 2.2 | 0.6 | 0.0 | -0.6 |
| Core inflation* | 57.8 | 0.0 | 0.2 | 0.1 | 1.9 | 2.0 | 1.0 | 0.1 |
| General index | 100.0 | 0.01 | 0.07 | ... | 2.1 | 2.0 | ... | 0.1 |

² Note: *Core inflation excludes food and housing inflation and is Jadwa Investment's estimate.



Figure 3: Food, housing, and headline inflation
(year-on-year change)

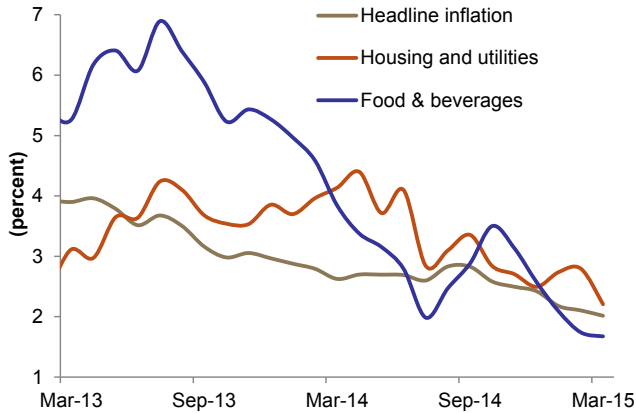


Figure 4: International and Saudi food prices
(year-on-year change)

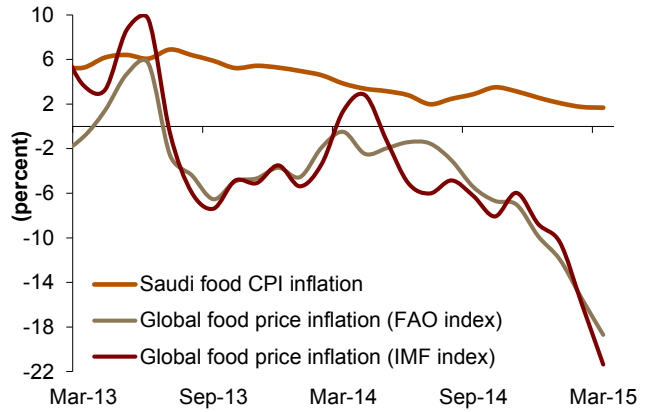


Figure 5: Wholesale and consumer food inflation
(year-on-year change)

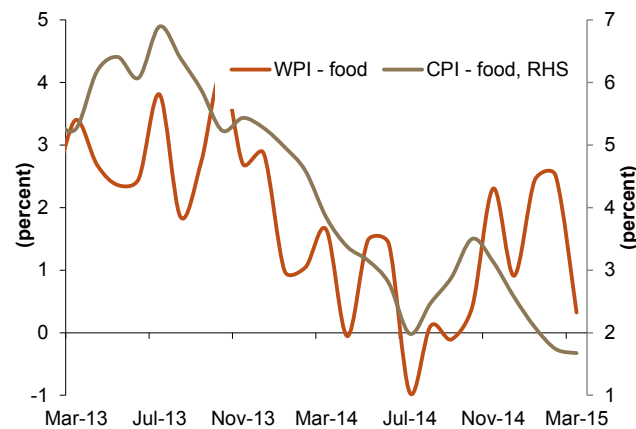


Figure 6: Rental inflation
(year-on-year change)

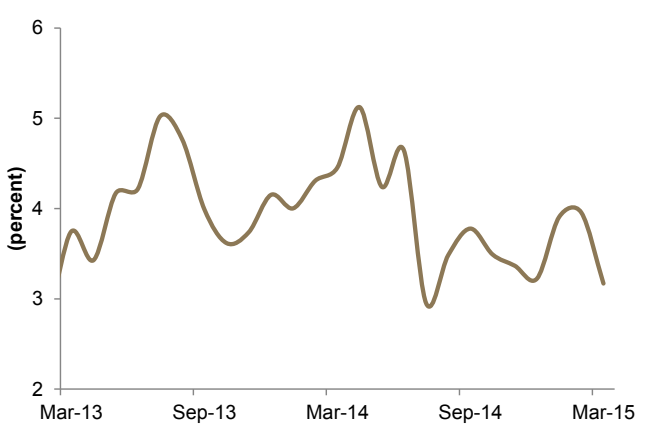


Figure 7: Components of core inflation
(year-on-year change)

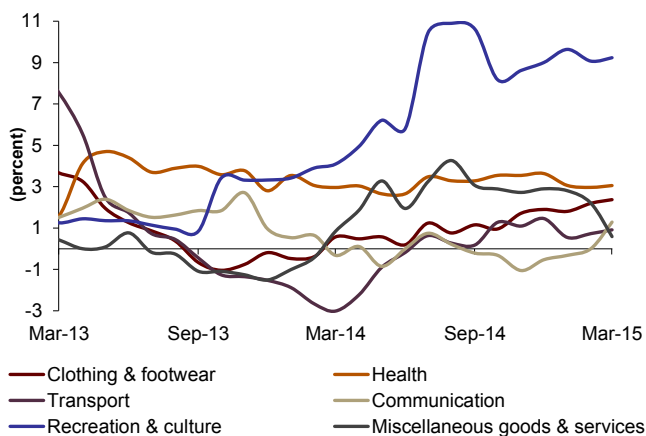
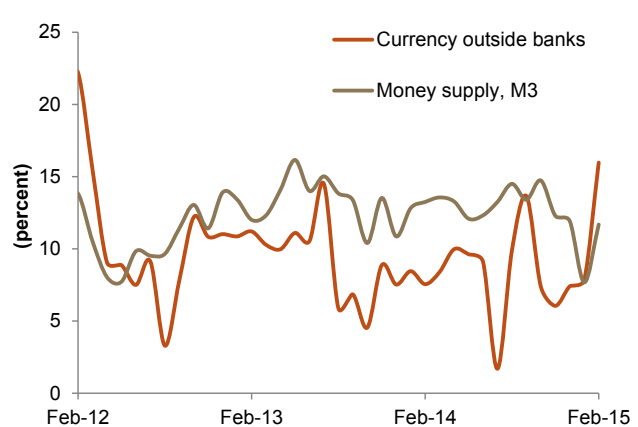


Figure 8: Monetary aggregates
(year-on-year change)



Sources: Central Department Of Statistics & Information, IMF, FAO, Reuters, Haver Analytics, Jadwa investment.



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