جدوى للإستثمار
Jadwa Investment

February 2023

The Saudi Economy in 2023

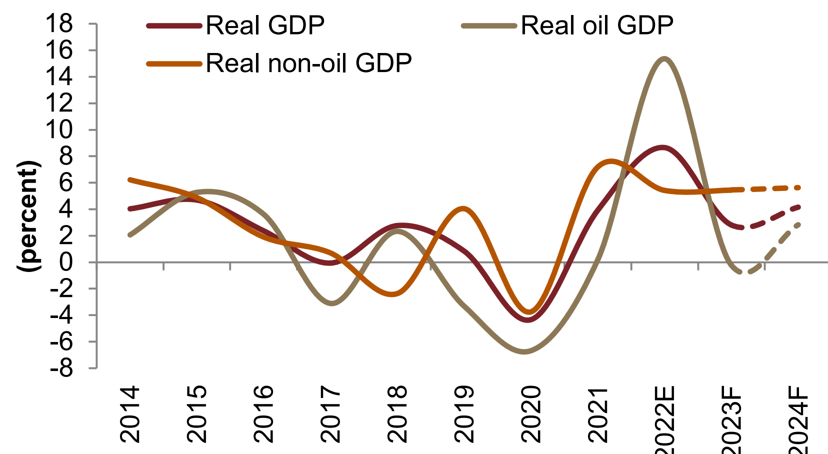
- Driven by sustained impulses from both investment and consumption, we expect Saudi Arabia's non-oil economy to continue growing well in excess of 5 percent in 2023. Overall GDP growth is set to slow to 2.8 percent from last year's world-leading 8.7 percent as oil production is reined in.

- The global economy provides reasons for cheer and gloom depending on the relative importance one gives to a) a possible US recession, and b) the resurgence of post-Covid-19 Chinese demand. Any US recession seems likely to be mild and short-lived, given comparatively strong household balance sheets and—the potential at least—for the US Federal Reserve to revive demand through interest rate cuts. China's structural issues are deep-seated, but these are unlikely to derail a vigorous recovery as the country's consumers make up for lost time. The eurozone too appears to be poised for some kind of revival as the uncertainties around energy supply dissipate. Still, a US recession—no matter how mild—will have an impact on global growth, and a slowdown in global GDP from 3.4 percent to 2.9 percent is anticipated by the IMF. Assuming the Fed *does* intervene, then things will probably look much brighter a year from now.

- Given these uncertainties, Saudi oil policy is set to remain conservative. The authorities are not yet convinced that oil demand is sufficiently robust to absorb an increase in supply, especially with non-OPEC output likely to stage a recovery this year. Thus, the authorities say they are committed to keeping output at the November 2022 level.

- We are more upbeat about the oil outlook given the vigor of China's rebound. We think demand will be strong enough to push the market into a moderate deficit this year, which in turn will allow Brent to average $90 per barrel (pb). Given this, there is some positive risk to the Saudi oil production stance, and with it the potential for some hydrocarbons GDP growth.

Figure 1: Saudi Arabia real economic growth
(year-on-year change)



For comments and queries please contact:

James Reeve
Chief Economist
jreeve@jadwa.com

Nouf N. Alsharif
Managing Director, Research
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

Jadwa Investment is licensed by the Capital Market Authority to conduct Securities Businesses, license number 6034-37.

View Jadwa Investment's research archive and sign up to receive future publications:
http://www.jadwa.com

Released: February-27-2023, 18:30 UTC+3

We see the Kingdom's overall GDP growth cooling to 2.8 percent in 2023 as oil production is trimmed, but non-oil growth will remain robust at 5.5 percent.

- Growth in the non-oil economy is increasingly broad-based. A notable feature is investment and consumption growing in tandem, with giga-projects driving the former and female labor force entry underpinning the latter. Meanwhile, the local private sector is shifting into expansion mode, as evidenced by the surge in IPOs last year. Growth sectors this year include Wholesale & Retail Trade, which has been the main beneficiary of female labor growth, a trend that still has some way to run. Construction will benefit from a further intensification of giga-project work, while there will also be support from a pickup in more mundane civil infrastructure projects, some of which stalled during the Covid-19 period. Non-oil exports (principally petrochemicals) will get a boost from China's reopening, though hydrocarbons exports, including refined products, will be held back by OPEC Plus policies. One sector that is likely to (further) soften this year is Real Estate as higher interest rates continue to take their toll on demand.

Inflation has not been a major problem and is expected to remain manageable.

- Saudi Arabia bucked the trend of rampant global inflation last year, and we do not see consumer price inflation accelerating much in 2023. The potential impact of a weaker US dollar should be offset by the general global trend of softening prices as supply chains normalize and higher interest rates weaken activity. In any case, Saudi consumers will continue to be partially insulated by subsidies on basic items.

The fiscal and current account balances are both expected to remain in surplus.

- The central government budget should record a small surplus this year, even as revenue declines slightly. Capex is expected to increase, but the general trend of the Public Investment Fund (PIF) and the National Development Fund (NDF) financing much of the project spending is expected to remain intact. The current account has shrugged off the surge in import spending, and should record another surplus this year thanks in part to the pickup in non-oil exports and enhanced tourism earnings.

Global Economic Outlook

The IMF sees global GDP growth weakening sharply this year as high interest rates take their toll.

The global economy endured a difficult 2022, with real growth recording a meagre 3.4 percent according to the IMF's estimate, down from 6.2 percent in 2021. More importantly, things tended to get worse as the year went on, with surging inflation eating into household incomes, and pressurizing demand--especially for goods. Inflation was driven largely by dislocations in commodities markets, but the full impact of a post-pandemic spending surge and tight labor markets also contributed.

The consequences of these dynamics will be apparent this year. The consensus is that the US will dip into recession, probably around the fourth quarter as corporate investment, hiring (and the housing market) falter in the face of higher interest rates. Yet most expect this recession to be short and shallow because a) US households are in reasonably good shape, and b) the US Federal Reserve will be willing to begin cutting rates again in order to head off a deeper downturn (Box 1). The IMF expects the US to maintain positive growth for full-year 2023, albeit of just 1.4 percent (Table 1, Figure 2).

Box 1: US economic gloom

Despite an apparently robust labor market, many think the US will soon succumb to the impact of higher rates and suffer a slowdown or even recession.

Many analysts are strikingly gloomy about the outlook for the US economy, with a late February Bloomberg poll of economists putting the chances of a recession this year at 60 percent. For casual observers this conviction jars with the current economic situation, which features a reassuringly robust employment picture. The economy added more than 500,000 jobs in January, and the unemployment rate fell to a new low of 3.4 percent. Over the entirety of 2022 the economy added 4.5 million jobs, the second strongest year on record.

So why the pessimism? The short answer is that many believe the Federal Reserve failed to act quickly enough against rampant inflation, and the economy is now set to pay the price. If inflation moves higher than targeted, central banks will usually react by raising interest rates in order to dampen activity and so reduce price pressures. They will attempt to do this as gently as possible in a bid to limit the subsequent economic fallout (the impact of rate rises is typically not felt for some 12-18 months). However, if the inflationary surge is particularly intense, then a more rapid response is usually called for.

In May 2020 US consumer prices were ticking along at just 0.1 percent year-on-year growth; twelve months later as pandemic-related supply disruptions began to be felt, prices were rising at a 5 percent clip. The Fed appeared unconcerned, characterizing the rise as a temporary phenomenon that did not warrant an interest rate response. By early 2022 as the full impact of post-pandemic spending was unleashed, US inflation was nearing 10 percent. Only then did the Fed act, and this time it had to be aggressive, raising its key interest rate (the Fed Funds Target Rate) by an aggregate 4.25 percentage points during the course of the year, generally in three-quarter point increments.

Any recession is likely to be short-lived, not least because the Federal Reserve is expected to begin cutting rates by the end of the year.

The Fed's aggression will eventually work to cool prices—indeed, wage growth is already falling back—but this will come at a cost. Higher borrowing costs, weaker corporate earnings and tighter bank lending standards are all weighing on business investment and hiring intentions. So while the January employment report showed a strong gain, forward-looking signals such as new vacancies and job "quits" were soft. Other leading indicators, such as PMI surveys, have also been very gloomy.

Economists hope that still-strong household balance sheets will allow most US families to weather the worst of any recession. But the main reason why most analysts see a "short and shallow" recession is—ironically—because they expect the Fed to begin *cutting* rates again in order to forestall a serious downturn.

Fed officials have repeatedly denied any such intention, and insist that inflation is far from beaten. Some analysts are taking these denials at face value and warn that rates could be "higher for longer". Yet a majority still thinks the Fed will "blink first" and expects rates to be cut later this year.

The main bright spot for the global economy is China, where the rapid unwinding of Covid-19 restrictions is triggering a consumption boom.

Prospects in the eurozone have also brightened a bit, with natural gas prices easing thanks to an unexpectedly mild winter (Figure 3). The IMF sees the zone's economy growing by 0.7 percent this year, which does not seem much but is significantly better than appeared likely in the closing months of 2022 when the weight of soaring energy prices threatened to drag the zone into a deep and protracted recession. Perhaps most importantly, China's economy is being jolted back into life by the rapid unwinding of Covid-19 restrictions. This relaxation has seen infections surge, but has also brought forward the revival of consumption, of which there are now clear signs. After three years of near-permanent lockdown, Chinese consumers are poised to ramp up spending with a vengeance, providing important positive spillovers for many Emerging Markets. The IMF expects China's GDP growth to reach 5.2 percent this year, with Emerging and Developing Economies expanding by 4 percent.

Risks to the global economic outlook are still elevated, however.

There are still plenty of risks to even this modest growth outlook. The main one remains inflation. True, supply chains are functioning much better than this time a year ago, and inflationary expectations remain contained. Yet there is a minority of analysts that are worrying about services inflation (which is still rising) and the possibility that China's recovery could stoke another rally in global commodities' prices. For this minority, rates are likely to stay "higher for longer" (Box 1).

Table 1: Global GDP growth
(percent; IMF and consensus projections)

	2021	2022E		2023F		2024F	
	IMF	IMF	Consensus	IMF	Consensus	IMF	Consensus
Global	6.2	3.4	3.0	2.9	1.8	3.1	2.6
US	5.9	2.0	2.1	1.4	0.5	1.0	1.2
UK	7.6	4.1	4.2	-0.6	-0.8	0.9	0.9
Canada	5.0	3.5	3.4	1.5	0.4	1.5	1.5
Euro zone	5.3	3.5	3.3	0.7	0.1	1.6	1.3
Japan	2.1	1.4	1.4	1.8	1.2	0.9	1.1
China	8.4	3.0	3.0	5.2	4.8	4.5	5.0
Russia	4.7	-2.2	-3.6	0.3	-3.0	2.1	1.3
Brazil	5.0	3.1	2.9	1.2	0.8	1.5	1.7
India	8.7	6.8	6.9	6.1	5.9	6.8	6.5

Note: Consensus forecasts are those of FocusEconomics.

Figure 2: Global economic growth expected to fall to 2.9 percent in 2023

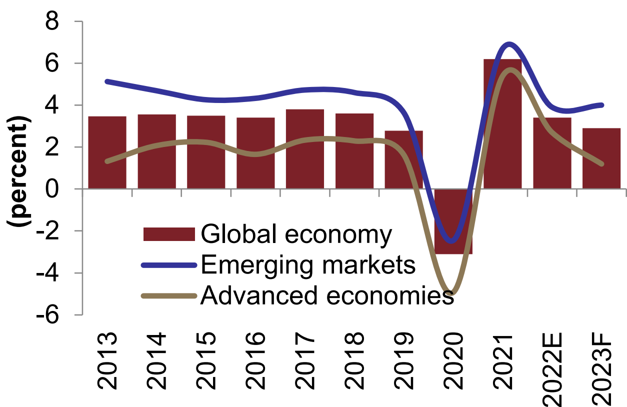


Figure 3: European gas prices have adjusted to the Russia-Ukraine shock

These are legitimate concerns, but we think that the coming weakness in US activity, which is likely to be all too evident by Q4, will be enough to push the Fed into making its first interest rate cut at the back end of this year.

The Oil Market in 2023

Elevated uncertainty is also dogging the outlook for oil prices.

The outlook for oil prices remains delicately balanced. On the demand side, many think that the looming US slowdown will be enough to tip the market into surplus and put downward pressure on prices. Others point to the release of China's long pent-up consumer demand as reasons for bullishness. The supply side of the story also offers different, but equally plausible scenarios. Some think the Russian supply squeeze and OPEC Plus production discipline will keep supply tight. Others are convinced that Russia will find new markets for its crude and a surge in non-OPEC supply will more than offset OPEC Plus's stance.

Russian supply is a key variable, with most expecting steep cuts to the country's supply as it struggles to find buyers.

Starting with supply, the main imponderable is obviously Russia. The EU appears determined to import as little Russian oil as possible, a stance that is unlikely to change over the next two years at least. In December the EU imposed a ban on imports of seaborne deliveries of crude oil. This appeared to have little immediate impact, as brisk demand from India, Turkey and China absorbed the Russian surplus (albeit at steep price discounts). However, the EU's ban on Russian oil product imports—introduced in February—promises to have a keener impact, given that China and India are themselves major exporters of diesel, gasoline, jet fuel, etc, and have no interest in taking the same products from Russia. In a sign of the difficulties this poses, the Russian authorities said they would be cutting oil production by 500,000 barrels a day (bpd) from March. It is not clear how long this cutback might last, but most analysts expect Russian liquids production to fall sharply over the next two years. The range of predictions is wide, but a loss of 500,000 bpd-plus from last year's total of 10.9 mbpd is plausible. (Figure 4)

However, the rest of OPEC Plus is likely to maintain a cautious stance given the cloudy demand outlook.

OPEC is unlikely to fill this gap given its concern about the demand outlook (see below), along with its own production capacity constraints and the strategic oil relationship between Saudi Arabia and Russia (Figure 5). Given this, it will fall to non-OPEC supply to make up the difference. Here, the US Energy Information Administration (EIA) is optimistic, projecting robust output gains from the US, Canada, Brazil, Norway and Guyana, among others. The US is expected to contribute roughly half of non-OPEC growth over 2023

Figure 4: Russia's total liquids output set to shrink

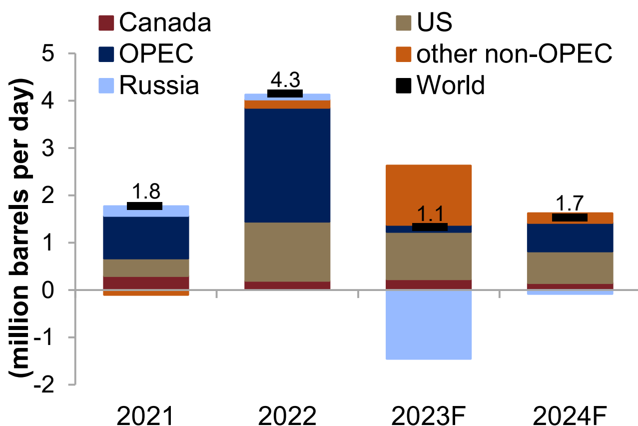
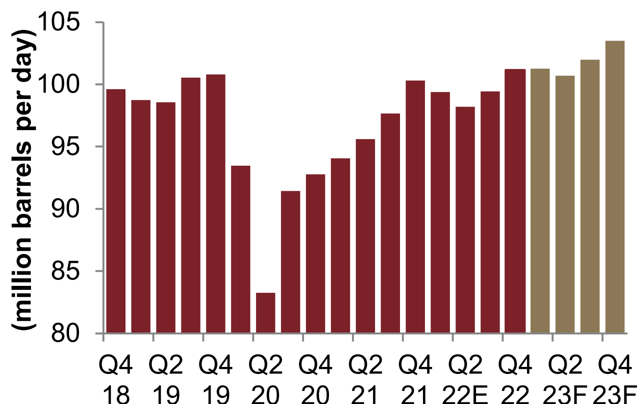


Figure 5: OPEC sees oil demand growing by just 2 percent this year



-24. The past couple of years have seen relatively restrained US production, reflecting enhanced capital discipline and a scarcity of labor and material. These issues have not gone away, and it is notable that 40 percent of the EIA's projected 1.2 mbpd gain for US liquids by end-2024 is set to come from natural gas liquids and biofuels rather than crude. At the other end of the spectrum is Guyana. The small South American country is a newcomer to the oil production scene, having only begun commercial extractions from its offshore field in 2019. Still, Guyana is expected to provide a non-negligible 500,000 bpd in extra output by the end of next year, according to the EIA.

That said, we think aggregate demand will strengthen somewhat as China's re-opening more than offsets the impact of any US recession.

In sum, the EIA expects non-OPEC supply comfortably to offset the loss of Russian liquids. Indeed, in net terms it sees total global oil production growing by 1.1 mbpd in 2023, and by 1.8 mbpd in 2024.

The demand outlook is, if anything, more uncertain than the supply picture. In broad terms, there are two opposing forces. One is the likelihood of a US recession, while the second is the Chinese re-opening. China's recovery is likely to be based around consumer spending on services, rather than a boom in industrial output or infrastructure spending. Thus, the boost to energy demand might be less than many analysts are expecting. That said, there will be a potent tailwind if Chinese consumers release pent-up demand for foreign holidays, something that would stoke demand for aviation fuel. China's property market is also being revived, thanks to the easing of regulatory restrictions, though confidence in this beleaguered sector is likely to remain fragile. Overall, however, there is little doubt that China's energy demand is likely to record a substantial annual gain.

Less positive is the US situation. Here, a robust top-line jobs report in January obscured some worrying forward looking indicators, confirming for many that a sharp slowdown (if not an outright contraction) is just around the corner.

Thus, we think the market will tighten moderately this year, allowing Brent to edge up from current levels to average $90 per barrel.

The US is the world's biggest oil consumer with roughly 20 percent of the total, while China comes in third (after the EU) with around 14 percent. Given the likelihood of a short and reasonably shallow US recession, and the prospect of a sharp and prolonged increase in China's demand, the prognosis is for a net gain in demand in 2023 and certainly in 2024. Putting a number to this gain is fraught with uncertainty: the International Energy Agency (IEA) projects an increase of 2 mbpd, though various investment banks are more bullish. Either way, it seems likely that demand growth will outstrip that of supply. Thus, we expect Brent to edge up from the late February level of around $83 per barrel (pb) to average around $90 pb for the year (though this is less than the 2022 average of $104 pb). In 2024 we assume that US and Chinese demand will be reasonably firm, though additional OPEC and non-OPEC supply points to Brent falling back to an average $87 pb.

Risks are skewed to the downside, however.

There are plenty of risks to this forecast. The most obvious one is the length and severity of any US recession: if inflation remains stubbornly high then the Federal Reserve may well resist calls to cut rates, potentially prolonging any downturn and denting oil demand by far more than is currently anticipated. On the supply side, Russia might decide to tolerate much deeper discounts in a bid to get more of its oil to market (a move that could have a dual downward impact on prices). Finally, OPEC could yet loosen its production commitments if it feels that there is enough demand to absorb the additional output.

Saudi Economic Growth

Consumption and investment are both growing briskly on the back of secular tailwinds…

The Saudi economy posted the strongest rate of real growth of any major country in 2022, with a full year rate of 8.7 percent (Figure 6). This was more than double the rate of 2021 and the fastest for more than a decade. Both investment and consumption are propelling growth, which is unusual for any nation, but especially one at Saudi Arabia's stage of development. Successful nations tend to have an investment surge followed by steady gains in consumption (the US, Japan, South Korea, and China are good examples).

...investment is being propelled by Vision 2030 giga-projects, while consumption is benefitting from female entry to the Saudi labor force.

In the Kingdom, consumption is experiencing a durable impulse from the large number of women who continue to enter the workforce (Figure 7), as well as from robust growth in home ownership, which provides a basis for both further consumption and borrowing. Meanwhile, investment is surging thanks to the increasing pace of work on various giga-projects, and also by private firms who are flocking to the equity markets in order to raise capital for their own investment plans. As such, government and private investment grew by a staggering 57 percent and 40 percent in the third quarter, year-on-year, respectively. For most nations, such gains in consumption and investment would entail a drag from net exports, as more and more imports are sucked in. But Saudi Arabia is in the happy position of having a massive hydrocarbons export base that consistently dwarfs its import demand and provides a further growth engine.

Last year's world-beating growth saw virtually every sector of the economy contribute.

"Wholesale & retail", "Construction" and "Transport" were at the forefront.

This GDP-by-expenditure profile is reflected in sectoral activity, with pretty much every major sector contributing robustly to last year's growth. Hydrocarbons remained the dominant sector, expanding by a brisk 15 percent in line with gains in crude oil production. Gas production also contributed, and although currently small, this is likely to become a more important adjunct to oil production in the years ahead. Wholesale & Retail Trade, which is the biggest non-oil segment, had a solid year as Saudi consumers spent more at home than in previous years and tourists returned to the Kingdom (mainly, but not exclusively, religious tourists). Construction gathered pace, and with it Transport, Storage & Communication, with the latter helped by further growth in subscribers to digital services. The main area of deceleration was in Real Estate activities (though it still contributed growth) reflecting much higher mortgage rates in the second half of the year.

Figure 6: Saudi Arabia led the way in global GDP growth last year (estimates)

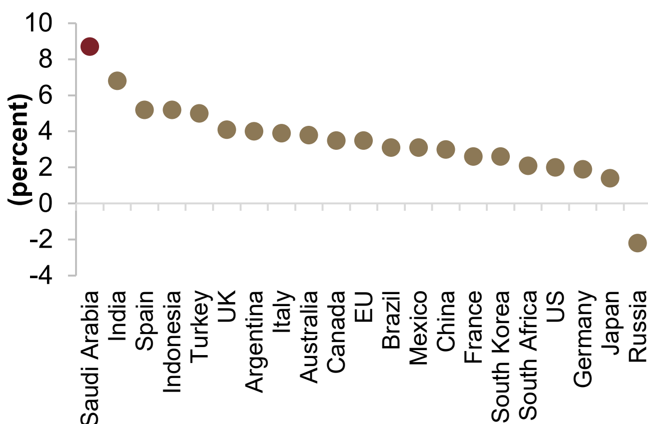
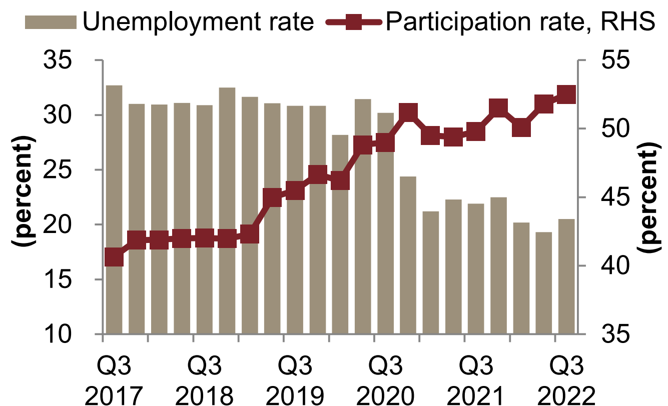


Figure 7: Notable rises in female participation rate in recent years



These fundamentals will remain intact in 2023…

These drivers should remain intact in 2023 and beyond. The main difference with 2022 will be on the hydrocarbons side, where OPEC-Plus caution indicates that Saudi oil production will decline very slightly this year (see below) enough to see overall hydrocarbons GDP edge down by 0.2 percent.

...and there should be a helpful boost to non-oil exports from China's re-opening.

As for the non-oil sector, China's reopening will stoke demand for Saudi petrochemicals, while progress on a range of giga- and mega-projects will underpin growth in the Construction and Transport sectors. Inflation should remain contained (see below) allowing further brisk expansion in Wholesale & Retail Trade, helped also by additional government support for low-income households. Real Estate activity is likely to remain subdued but should see a revival late in the year and into 2024 if, as we expect, interest rates begin to come down.

However, overall GDP growth will be dragged lower by slightly weaker oil production.

Overall, we see total GDP growth easing to 2.8 percent in 2023 as oil production flattens. Non-oil GDP is a more useful barometer of the Kingdom's economic situation, and this is expected to expand by 5.5 percent, a slight uptick on last year's estimate.

We see headline GDP growth cooling to 2.8 percent, but non-oil activity should edge up to 5.5 percent growth.

Table 2: Real GDP shares and growth rates

2022		2020	2021	2022E	2023F
% Share of:		% year-on-year			
Overall GDP		**-4.3**	**3.9**	**8.7**	**2.8**
Oil sector	**40**	-6.7	0.2	15.4	-0.2
Non-oil activities	**44**	-3.7	7.2	5.4	5.5
Govt. activities	**13**	-0.6	1.1	2.2	2.2
Non-oil GDP by sector	**100**	**% year-on-year**			
Agriculture	6.1	-1.7	2.6	3.2	3.1
Non-oil mining	1.0	0.4	6.2	6.3	6.8
Non-oil manufacturing	19.8	-6.6	9.5	9.1	8.5
Electricity, gas and water	2.7	-2.9	2.3	2.1	2.1
Construction	9.1	1.9	1.3	4.6	4.7
Wholesale & retail trade	21.0	-8.8	13.7	5.1	7.8
Transport & communication	12.3	-6.4	3.8	7.6	7.5
Real estate activities	11.6	0.9	5.6	1.4	0.5
Finance, insurance, & bus.	10.1	5.9	6.0	4.0	2.5
Community & social services	6.3	-7.0	7.7	3.3	2.4

Note: Non-oil GDP by sector for 2022 (growth and shares) is the year-to-Q3 2022 average. Overall GDP in 2022 also includes net taxes.

Crude oil output saw exceptionally strong growth of 16 percent last year, but production was reined in during the year as the demand outlook dimmed...

Hydrocarbons sector:

Saudi crude oil production was volatile in 2022, showing steady gains in the first half of the year, in line with OPEC Plus agreements, before a reversal from August onwards as global economic headwinds mounted and the demand outlook soured. Still, total production increased by 16 percent for the year as a whole, the first annual increase since 2018 and the strongest percentage gain since 2003.

...caution will remain the watchword this year.

China's rapid re-opening has brightened the global outlook somewhat (see above) but we think OPEC Plus's stance will remain cautious. It is not easy to dismiss the risks to the demand picture, which stem primarily from potential US economic weakness. And with the cataclysmic collapse in 2020 oil demand—and associated

Gas production is set to increase, as is refining, both of which will respond to firm domestic demand.

However, these gains will not offset the cuts to crude output and overall hydrocarbons GDP is set to contract by around 0.2 percent.

Retail trade and hospitality have benefitted from the ongoing workforce expansion as well as the upturn in tourism arrivals.

price crash —still fresh in the memory, we think that OPEC Plus will stick with its November 2022 production agreement. Thus, we see the Kingdom's average annual production easing slightly to around 10.5 mbpd in 2023.

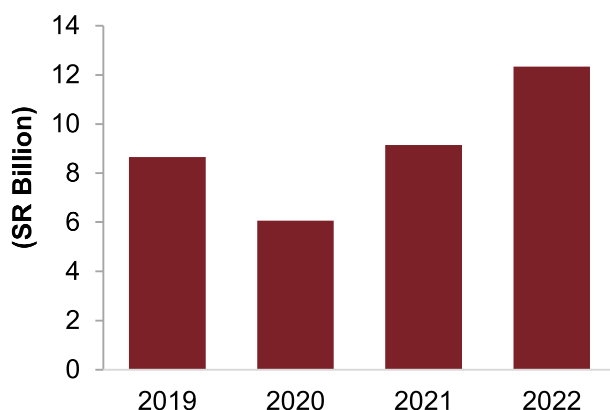
Gas production should add a bit to hydrocarbons GDP. Total Saudi gas production grew by some 4 percent in 2021 to reach 117 billion cubic meters, putting it third in the region behind Iran and Qatar, and production is likely to have accelerated in 2022. Currently, gas is still a minor element of overall hydrocarbons GDP, but we see it gaining in importance in the years ahead. Natural gas is a key ingredient of the Vision 2030 program, and also has an increasingly important—if temporary—role in the global energy transition. Aramco is committed to expanding its gas processing facilities, particularly of non-associated sources of gas, where production is not constrained by OPEC Plus agreements. The Kingdom's proximity to Europe, where gas demand is set to remain robust, also offers significant export potential.

The authorities include Refining as part of "oil activities" in their institutional accounting, and this subsector is expected to grow sharply this year given brisk domestic demand for oil products. Yet, like Gas, Refining is still quite small and its growth will not be enough to prevent overall hydrocarbons GDP declining by around 0.2 percent in real terms.

Wholesale & Retail, Restaurants & Hotels sector (21 percent of non-oil GDP) was up by 5.1 percent in the year to Q3 2022, year-on-year, maintaining the upward trend seen the year before, when the sector's contribution rose by 13.7 percent. The rise reflected a combination of many inputs. First, the rebound in the number of Hajj and Umrah visitors, as more particularly Umrah visitors rose from circa 6.5 million in 2021, to more than 7 million in 2022. Moreover, the growth in general tourism was notable, with 12,000 new hotel rooms estimated to have come on stream in the Kingdom during 2022 (up by 6 percent year-on-year) (Figure 8).

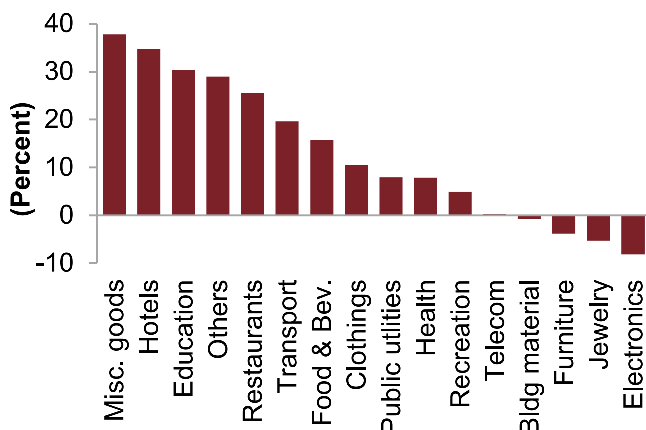
Also, full year consumer spending (POS, e-commerce & ATM cash withdrawals) rose 9.5 percent year-on-year to a total of SR1.2 trillion, higher by 19 percent than pre-pandemic levels. When looking at the sectorial breakdown of spending (via POS only) on 'hotels' and 'restaurants and coffee shops' rose by 35 percent and 26 percent year-on-year, respectively, ranking amongst the top sectors in yearly rises (Figure 9). At the same time, spending on 'jewelry', 'furniture'

Figure 8: Spending on 'hotels' saw impressive growth in 2022*



*POS spending

Figure 9: POS spending in 2022, by sector
(year-on-year change)



and ’electronics’ declined compared with the previous year, in a trend we noted in our previous report on the Saudi Economy 2022, which showed more spending on services rather than goods.

The sector will benefit from further growth in visitor numbers as more and more hotels are added.

Looking ahead, we expect to see continued growth in this sector, with a number of high-end hotels due to be launched around the Kingdom, including the ones affiliated with the PIF’s giga-projects in the Red Sea and Diriyah. In addition, the yearly growth in the number of tourism visitors and pilgrims should add support to this sector, with the number of Hajj pilgrims expected to go back to pre-pandemic levels, or even higher (Figure 10). In addition, a number of sports and entertainment events taking place across the Kingdom should add a helpful tailwind to the hospitality sector.

Non-oil manufacturing has been robust, and petrochemicals should get a further boost from the revival of Chinese demand.

Non-oil manufacturing (19.8 percent of non-oil GDP) has performed strongly, rising by 9.1 percent in the year-to-Q3 2022. The robust activity is, in part, associated with a notable increase in the value of the Kingdom’s non-oil exports, rising by 13 percent in 2022 year-on-year, despite a slight decline in Q4 (Figure 11). Moreover, a significant improvement in the manufacturing sector has been seen through the Index of Industrial Production (IIP), which rose by an average of 22 percent in 2022. Also, growth is likely to have been enhanced by more than 1,000 new industrial factories starting production in 2022 (worth SR29 billion of investments), creating some 44,000 new jobs over the same period.

For 2023, the anticipated rebound in global petrochemicals demand, especially from China, and the continued growth in manufacturing investment (SR1.7 billion of which came from FDI during 2022) will all provide additional support to this sector’s growth.

Manufacturing infrastructure continues to be built and soft loans are available.

Encouragingly, Saudi non-oil manufacturing grew despite the slowdown in global trade last year, particularly in H2. This gives reasons for optimism that Saudi manufacturers can take full advantage of the re-opening in China, which should see enhanced demand for a variety of industrial products, not least chemicals (see Global macro section). In addition, the Saudi Industrial Development Fund (SIDF), is planning to extend SR45 billion worth of new loans in 2023-2026. Moreover, the Ministry of Industry and Mineral Resources (MIM) plans to launch 105 new factories around the Kingdom’s industrial cities in 2023, and to nationalize ten industrial sectors such as cars and medical equipment, in line with the National Industrial Strategy launched in October 2022 (Box 2).

Figure 10: Annual Hajj numbers are set to have a significant rebound this year

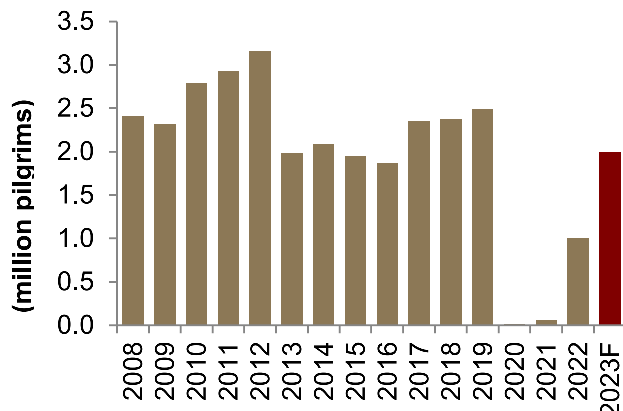
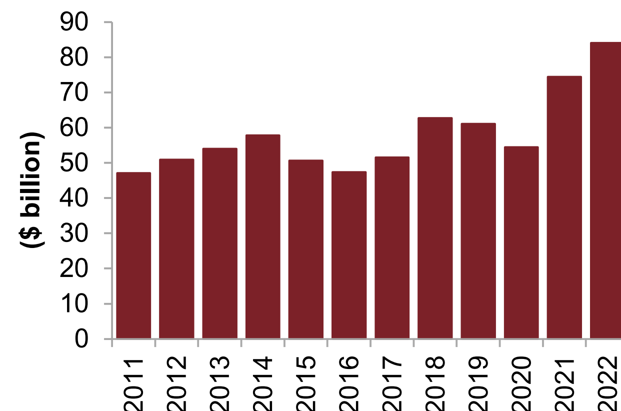


Figure 11: Annual non-oil exports hit a record high in 2022



The National Industrial Strategy gives the strategic underpinning to the Kingdom's industrial expansion plans.

Box 2: The National Industrial Strategy

In October 2022, the Kingdom launched the National Industrial Strategy, which focuses on 12 main sectors (Figure 12), and aims to enhance growth in the industrial sector by 2035. Also, the strategy plans to raise the number of factories to more than 36,000, and place the Kingdom amongst the top 15 countries worldwide within the Competitive Industrial Performance (CIP) Index, by 2035.

In addition to the strategy, the National Industrial Development and Logistics Program (NIDLP) is working towards a number of targets to be achieved within the coming 2 years. By 2025, the NIDLP aims to raise the localization of the pharmaceutical industry to 30 percent of local market share, and to increase the number of economic zones to eight.

Growth in the "Transport" sector was also propelled by the strong rebound in tourism...

The **Transport, Storage & Communication sector** (12.3 percent of non-oil GDP) saw a significant gain in the year to Q3 2022, growing by 7.6 percent over the same period in 2021. Growth in the sector was substantially supported by the rebound in travel, with a progressive lifting of restrictions for Umrah pilgrims during the course of the year encouraging the return of more than 7 million visitors by the end of 2022, and a higher yearly number of Hajj permits (at one million, compared with 60,000 in 2021). In addition, the sector witnessed a notable rise in other segments, such as railways, with Saudi Arabia Railways (SAR) carrying more than 5.8 million passengers during 2022, more than double the 2021 figure (including 1.35 million pilgrims through Jeddah, Makkah and Madinah). Cargo transportation also saw a healthy 22 percent gain, with Saudi ports witnessing a 13 percent rise in volumes handled in 2022. Added to this, the year saw the launch of five public bus transport projects in 11 cities and regions around the Kingdom.

...while the Communications subsector benefitted from further e-commerce penetration.

Meanwhile, the consolidated profitability of listed telecom companies rose 13 percent year-on-year in the year-to-Q3 2022 (latest available data), reflecting growth in both new services and subscribers. The sector also benefitted from digitalization, with e-commerce transactions growing by 65 percent in full year 2022.

A significant expansion of transport infrastructure is scheduled for 2023.

During 2023, various transport projects are expected to come on line around the Kingdom, which should translate into sizable growth in this segment (Figure 13). This includes more public transport projects, streets, roads, and airport terminals. Sector plans include

Figure 12: The National Industrial Strategy's main focus sectors

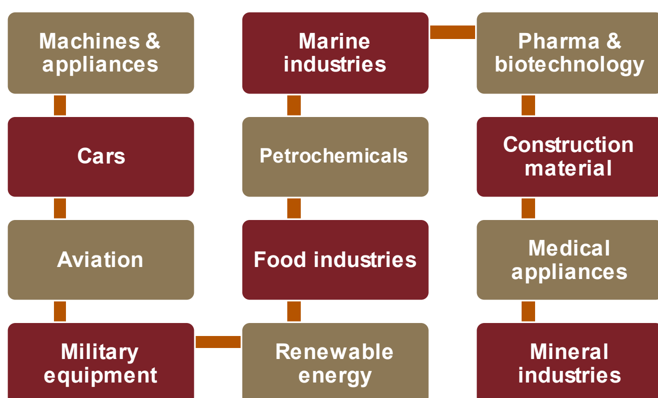
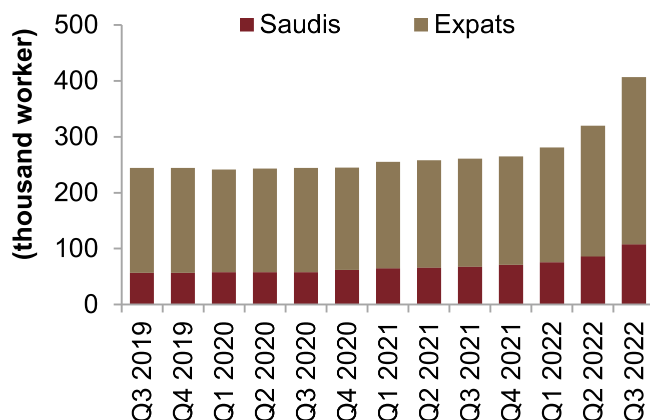


Figure 13: Expansion in 'transport' is reflected in the rise in the sector's* employment



**Classified as 'transportation and storage' in Gastat's labor market survey*

Communications will benefit from a further expansion in fiber-optic connectivity.

launching 12 logistic platforms and increasing railway freight capacity. Meanwhile, the communications sub-sector will be supported by an acceleration in the rollout of optical fiber for residential areas, with plans to raise coverage from 61 to 64 percent in 2023. Finally, the Kingdom plans a significant rise in Umrah and Hajj pilgrims, with numbers expected to reach 2 million for Hajj pilgrims, with 1.8 million of them coming from outside the Kingdom. In general, we expect robust growth for the sector in 2023 and beyond, as more travel and transport activities are rolled out, and more programs and projects are introduced under the National Transport and Logistics Strategy, announced in June 2021.

"Real Estate" saw a slowdown last year as higher interest rates weighed on mortgage demand.

Real Estate Activities (11.6 percent of non-oil GDP) grew at a modest 1.4 percent pace in the year to Q3 2022, a significant slowdown from the 5.6 percent recorded in the same period of 2021. Growth continued in various housing projects under the Ministry of Housing's (MoH) Sakani program, but new residential mortgages provided by banks and finance companies declined by 21 percent year-on-year in 2022, with the latest SAMA data showing that new mortgage lending totaled SR123 billion last year, down from SR156 billion in 2021 (Figure 14).

Higher rates will remain a headwind to demand this year, though Ministry of Housing supply should continue unabated.

For 2023, we see the MoH's Sakani program continuing to support the sector with plans to provide housing units to more than 120,000 families as the MOH strives to raise the home-ownership ratio to 70 percent by 2030. Despite this, the recent slowdown in mortgage loans is expected to continue, given that interest rates are expected to stay high this year. Looking at the mortgage data, it is notable that demand for villas was down 13 percent in 2022, while demand for cheaper apartments declined by only 3 percent (in terms of mortgages provided by both banks and financial companies). This suggests that the rollout of new apartments might be more resilient than the flow of new villas.

Construction had its best year since 2015 supported by progress in the giga-projects.

The **Construction** sector (9.1 percent of non-oil GDP) saw impressive growth of 4.6 percent in the year-to-Q3 2022, year-on-year, the highest since 2015. This rebound came as a result of a sizeable SR78 billion worth of construction projects being executed in Saudi Arabia during 2022, with various sites around giga-projects also going forward. There was also a sizable rebound in the number of workers in the sector, with 300 thousand workers added in the year-to-Q3 2022 on a net basis (86 percent of the new hires are expats), versus a net decline of 130 thousand in the previous year (Figure 15).

Figure 14: New mortgage loans were down in 2022 by 21 percent year-on-year

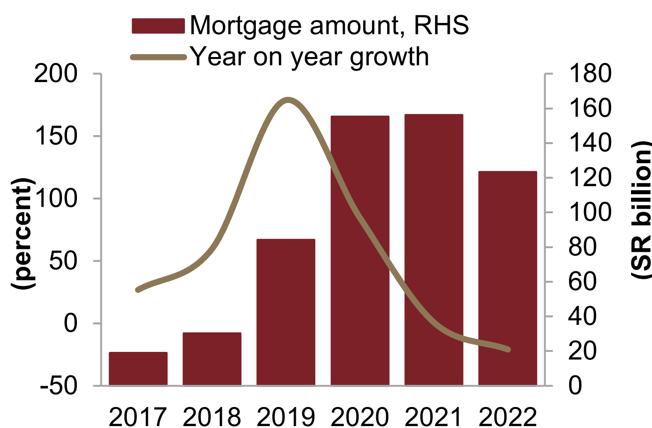
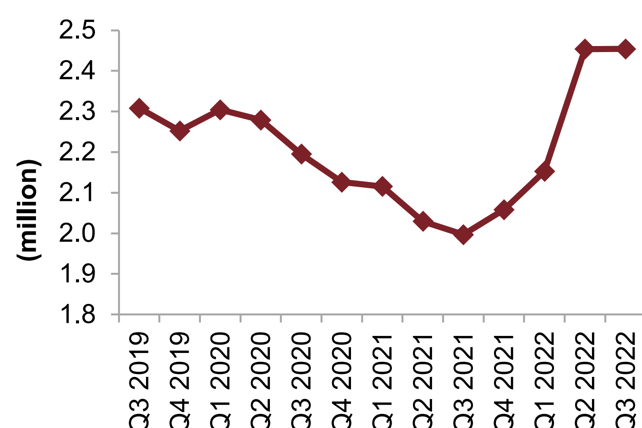


Figure 15: Employment in the construction sector saw a significant rebound in 2022



Projects in a range of other sectors will also lend support this year.

For 2023 and beyond, growth in this sector will be mainly supported by the progress in PIF's giga-projects: Neom, Red Sea, Roshn, Qidiya and Diriyah, all of which saw varying rates of progress during 2022. Moreover, the sector will continue to benefit from the rise in government capital expenditure, up to SR157 billion in 2023 from SR150 billion in 2022. As highlighted in the recent budget statement, the annual rise in capex stems from the government's plan to move forward with spending on mega-projects, growing sectors such as tourism, manufacturing and mining, and other infrastructure projects around the Kingdom.

Agriculture enjoyed a relatively strong 2022.

Agriculture (6.1 percent of non-oil GDP) rose by 3.2 percent in the year-to-Q3 2022, year-on-year. During 2022, the sector successfully dealt with the Ukraine-Russia conflict by devoting SR9.5 billion to deal with food supply shortages and global inflation. Also, the Ministry of Environment, Agriculture and Water (MEWA) approved more than SR1 billion for small agriculture enterprises throughout the year.

The Ukraine-Russia conflict has underscored the need to reduce vulnerability to global food price volatility.

Looking ahead, MEWA's efforts to secure self-sufficiency in various foods will be supplemented by additional funding from the Agricultural Development Fund (ADF) which has set aside circa 6.5 billion for various projects in 2023, up 3 percent on last year (Figure 16).

Growth in the finance sector was driven by a surge in IPO activity.

Finance, Insurance, and Business services (10.1 percent of non-oil GDP) saw decent growth of 4 percent in the year-to-Q3 2022, supported by various factors. The capital markets saw a surge in initial public offerings (IPOs), with a total of 49 offerings on the main and parallel markets, including two REIT funds, in 2022. More specifically, the main market, the Tadawul All Share Index (TASI), saw the first dual listing in association with Abu Dhabi Securities Exchange (ADX) (Figure 17). Moreover, the banking sector witnessed another sizable yearly rise in lending to the private sector, up by 13 percent in 2022, compared with 15 percent in 2021 (Figure 18). The sector's growth was also positively affected by a rise in the number of privately insured persons, up by a total of 1.5 million beneficiaries (or 15 percent) during 2022, with a rise in both Saudi and non-Saudi beneficiaries.

Bank lending to the private sector also saw double-digit percentage growth…

...even in the face of higher interest rates and some tightness of sector liquidity.

We expect the Finance, Insurance, and Business services sector to continue growing in 2023 in line with further expansions in the non-oil economy and the growing role of the private sector. While higher interest rates might weigh on bank lending, tightness here should enhance the appeal of the equity markets for firms looking to raise

Figure 16: ADF's loans by sector, up to 2021

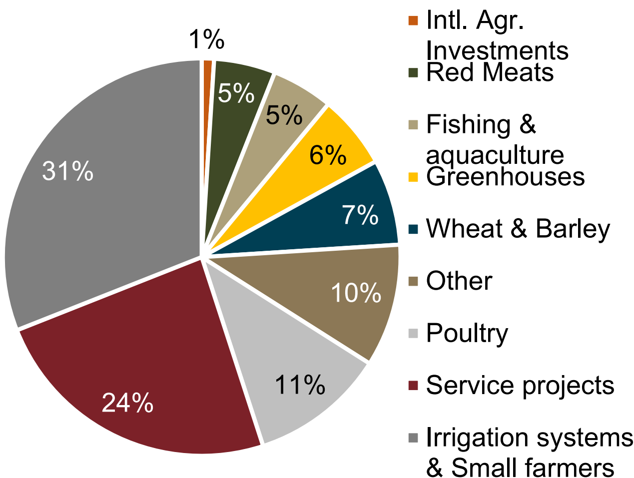
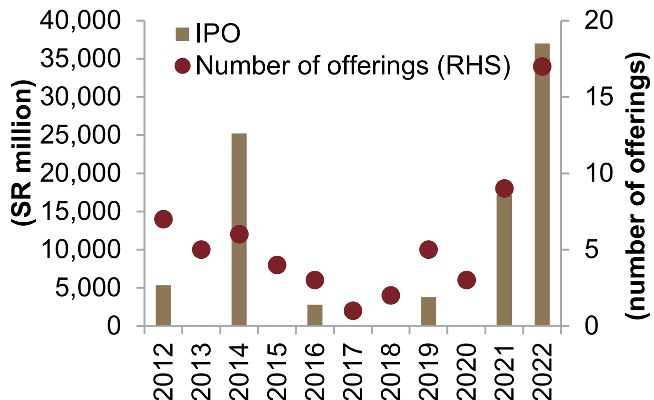


Figure 17: TASI's main market saw strong momentum in IPOs during 2022



"Community & Social Services" enjoyed a decent year and should continue to benefit from the growth of entertainment offerings.

The surge in sports and entertainment has gone hand-in-hand with the expansion of the labor force.

More than 1.5 million cubic meters of water production capacity (much of it from desalination) is set to be added this year.

The "Non-oil Mining" sector appears to be on the verge of realizing its potential.

capital. Health insurance should also continue expanding quite briskly given an expected increase in expat numbers as well as an ongoing shift among Saudi nationals towards private insurance.

Community, Social & Personal Services (6.3 percent of non-oil GDP) rose by 3.3 percent in the year-to-Q3 2022, year-on-year, including a sharp 7.6 percent rise in Q3. This sector includes various activities such as education, healthcare, arts, entertainment, and sports, which will have benefitted from a rebound in activity compared with the last two years during Covid-19 restrictions.

The sector is expected to see further solid growth in 2023 as the Quality of Life (QoL) VRP continues to plan for various events and activities. This program will be supported by the recent launch of the Events Investment Fund (EIF, one of the NDF's funds) which aims to boost investments in cultural and entertainment events in the Kingdom. In addition, the Ministry of Health plans to launch three hospitals with a total capacity of 900 beds, and to expand medical coverage around the Kingdom's regions through 60 mobile clinics providing primary health services.

Electricity, Gas, and Water (2.7 percent of non-oil GDP) saw a year-on-year rise of 2.1 percent in the year to Q3 2022, as the sector saw SR40 billion of water projects during the year, and an expansion in electricity subscribers around the Kingdom.

For 2023, growth in this segment will be spurred by the expected expansion in water production (through desalination) from 9.4 million cubic meters in 2022 to 11 million cubic meters. The sector will also benefit from projects worth SR21 billion coming on line, including electricity generation and transmission.

Non-oil Mining and Quarrying (1 percent of non-oil GDP) grew by 6.3 percent in the period to Q3 2022, year-on-year. This brisk growth came as a result of 673 new licenses being issued in 2022, including mineral exploration and exploitation licenses, generating more than SR120 billion worth of investments in the sector during the year, up from SR30 billion in 2021 (Figure 19). In addition, the year saw the first license auction for quarries of building materials in 13 sites around the Kingdom.

In 2023, the MIM is planning to auction five new mining exploration licenses, including for copper, zinc, lead, and iron deposits in different locations for local and international investors. In addition, the recently-launched National Industrial Strategy lists mining

Figure 18: Growth in bank lending to the private sector softened slightly last year

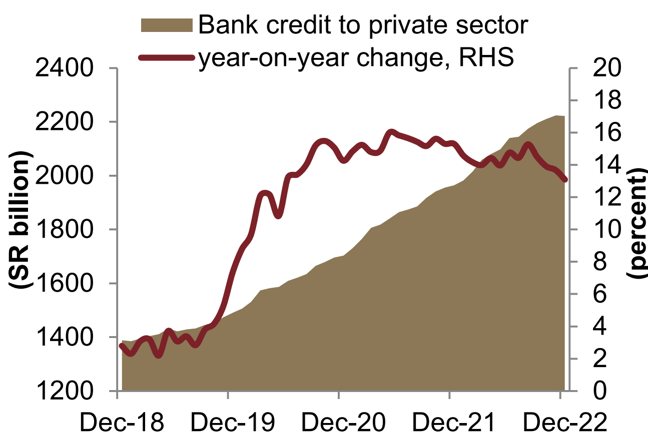
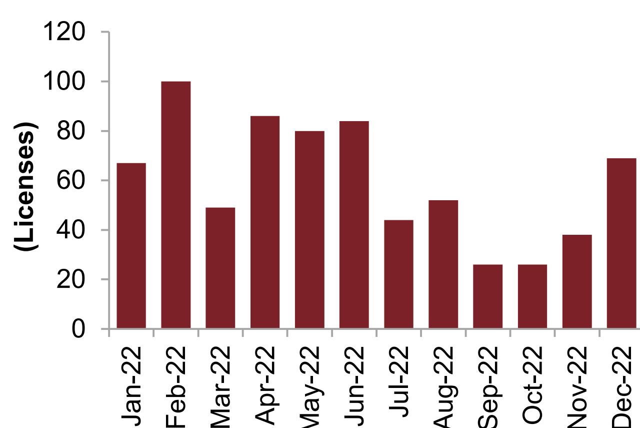


Figure 19: Mining licenses rose by an average of 60 new licenses per month in 2022



Mining is a key strategic sector. There is a world-wide race on to secure deposits of copper and titanium, which are key inputs for the electric vehicle industry.

industries as one of its main sectors, with focus on copper, steel, aluminum and titanium. Finally, the sector will also benefit, directly and indirectly, from the recently launched mining fund by PIF and Maaden. This fund plans to invest up to SR12 billion of capital in overseas mining assets, to ensure supply security for the domestic minerals downstream sector, and to position the Kingdom as a key partner in global supply-chain resilience. In general, such activities will boost the sector's growth in the longer run, and despite its modest contribution to non-oil GDP, we anticipate growth in this sector to rise significantly over the coming years.

Fiscal Policy

Projections in the 2023 budget are understandably cautious. A conservative oil price appears to have been assumed.

The 2023 budget was drawn up during a period of heightened volatility in global financial and oil markets (H2 2022) and there is understandable caution in its projections. The budget forecasts total revenue to reach SR1.13 trillion, an 8 percent increase on the 2022 budget but an 8.4 percent decline on 2022's estimated level. Much hinges on oil price and production assumptions, which are naturally not revealed by the authorities. We think that a figure in the range of $70/b-$75/b (Brent) guided their revenue assumptions, though the budget was likely finalized before the latest OPEC Plus agreement which reins in oil production. By contrast, non-oil revenue is projected to increase, with VAT takings expected to climb by 4 percent, which still seems a bit pessimistic especially when adjusted for inflation.

Total spending is budgeted to fall compared with the 2022 estimate. However, capex is scheduled to increase.

Total budgeted expenditure for 2023 is SR1.11 trillion. This puts it 16.6 percent above the 2022 budget, but some 1.6 percent below the official estimate of spending in 2022. Yet medium-term spending plans have been raised significantly compared with those set out in the 2022 budget: total spending in 2024 is now projected at SR1.13 trillion compared with SR951 billion in the 2022 budget. Despite this uplift, spending is still expected to narrow as a share of non-oil GDP-to around 41 percent in 2025 compared with 48 percent in 2022.

As in previous years, the PIF and NDF will continue to finance much of the Vision 2030 capital projects.

Budgeted capex rises to SR157 billion in 2023, from an estimated SR151 billion last year. The increase reflects enhanced spending on projects (mainly social infrastructure) that were delayed by the Covid-19 pandemic. Yet as the budget says, there will continue to be a significant "development contribution" from both the Public Investment Fund and the National Development Fund. These two extremely well-capitalized organizations will continue to deliver the giga-projects that underpin the Kingdom's structural transformation. Meanwhile, current spending has been budgeted at SR957 billion,

Figure 20: We see government spending growth of around 1 percent in 2023

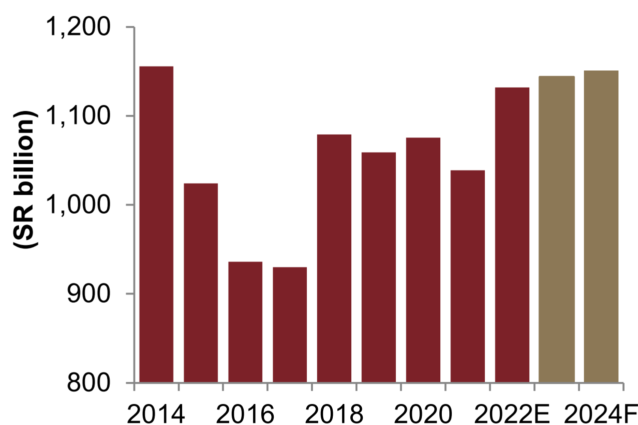
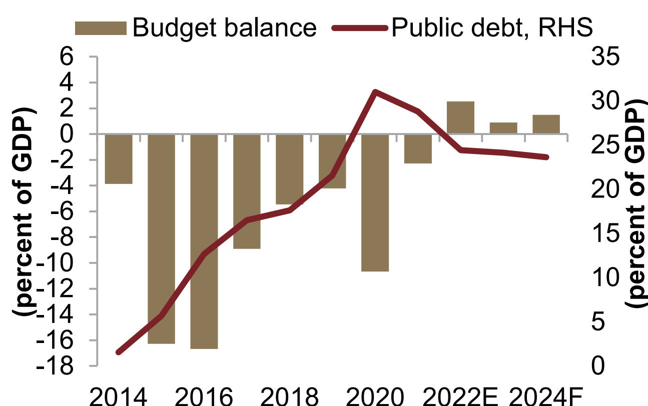


Figure 21: The budgetary and debt outlook is comfortable



Current spending is set to decline compared with 2022, even as spending on public sector wages is budgeted to rise…

representing an 11 percent gain on the 2022 budget, but a 2.4 percent cut compared with the official 2022 estimate. Current spending remains dominated by wages & salaries (some 46 percent of spending), which is earmarked to rise by 1.6 percent compared with the 2022 estimate. Yet despite this nominal increase, significant progress has been made in reducing this item as a share of output: spending on wages and salaries fell to 19 percent of non-oil GDP in 2022 (helped in part by significant growth in the GDP denominator) from 22 percent of non-oil GDP in 2021. Further progress on this front remains a key policy objective, and it is hoped that the investment growth noted above will open up significant private sector employment opportunities, allowing reductions in government salary costs in nominal as well as relative terms.

… the authorities are therefore banking on lower procurement costs as an offset.

Box 3: The changing role of the central government budget

Prior to the introduction of the Vision 2030 program in 2016, the Saudi government budget was the touchstone for the country's economic prospects in the year ahead. The central government was the dominant economic actor and its spending decisions affected pretty much every business and household.

Recent years saw an expanding role of the PIF and NDF, along with a gradual shift in the business model of local private firms.

In recent years three trends that have begun to change this perception. First has been the emergence of institutions such as the Public Investment Fund (PIF) and, to a lesser extent, the National Development Fund (NDF). These organizations have robust balance sheets that have been deployed independently of the central government. Indeed, PIF-sponsored projects are the cornerstone of the Vision 2030 program. Second, private sector firms are no longer as wedded to central government spending as they once were. Many firms have recognized the opportunities that Vision 2030 is generating and have boosted investment in a bid to take advantage. Hence, the surge in IPOs in recent years as firms rush to raise equity capital. Third, the central government budget is much more finely calibrated to specific needs of the local economy. Put another way, spending has become more targeted and disciplined.

Central government spending is a vital source of support for low-income households, and the source of funds for much civilian infrastructure.

Naturally, the central government budget is still very important. Its capex helps deliver much civilian and military infrastructure, and its spending remains the main source of contracts for many firms. Its transfers are a vital source of funding for low-income households, and the civil service is still seen as the employer of "first resort" for many Saudi nationals. Yet the private sector is sensing broader economic opportunities, and the central government's budget is no longer the single reference point for firms and households that it once was.

Looking at the budget from a sectorial level, 'Military' is now the largest single sector of spending, up 5.7 percent from last year's official estimate and now accounting for 23 percent of total budgeted spending. The emphasis is on enhancing military medical facilities, while a broader push to 'localize' the supply of some military equipment remains a priority. 'Education' and 'Health & Social Development'—which have historically accounted for the largest allocations—share second spot, though both see their allocations shrink slightly compared with last year's estimate. Meanwhile, 'General Items', which includes government contributions to social insurance and debt servicing obligations, sees a slight decline in its allocation, though a more pronounced (9 percent) cut compared with the 2022 budget.

Box 4: Jadwa's fiscal projections

Although we expect a higher average oil price than that likely used in the budget…

Our view of the 2023 fiscal outlook is broadly similar to that of the government. Oil revenue will be impacted by weaker production and lower average prices (Brent is expected to ease to $90 pb, from last year's average of $104 pb). However, we expect non-oil revenue to continue growing as the vibrant consumption scene continues to boost VAT takings. This suggests to us that overall revenue will be down by only 1.4 percent this year.

...we also expect oil production to be lower.

Employees' compensation is set to increase, but should be broadly contained to the population growth rate, and should continue to fall as a share of non-oil GDP. Spending on goods and services is a key area of uncertainty: much will depend on whether China's re-opening stokes a new round of commodity price increases or whether prices will ease following last year's substantial run-up. For Saudi Arabia the added complication is the US dollar, which we expect to weaken somewhat.

The net result of all this is a budget surplus forecast that is slightly higher than that of the authorities (0.9 percent of GDP).

On balance, we think spending on goods and services is set to rise again, but only modestly, with the impact of strong domestic demand being softened by weaker global commodities' prices. Capex is likely to increase but will remain slightly below the medium-term average. Thus, we see total spending growth contained to just 1 percent (Figure 20), which should allow a budget surplus of some 0.9 percent of GDP (Figure 21).

Debt management will remain proactive…

...and the National Debt Management Center will continue to refinance sovereign debt opportunistically.

Given the above, the budget expects a modest surplus of SR16 billion in 2023, or 0.4 percent of GDP, which is somewhat smaller than last year's 2.6 percent outturn. Notwithstanding the expected surplus, debt raising activities are set to continue, as evidenced by a $10 billion sovereign bond issue in January 2023 (Figure 22). This would appear to be both strategic and tactical: strategic in so far as it is aimed at bolstering the yield curve and diversifying the Kingdom's long-term funding options, but also tactical as the National Debt Management Center (NDMC) seeks to manage risk by refinancing opportunistically. This approach appears to be paying dividends: the cost of funding of the Kingdom's debt portfolio increased to 2.95 percent in 2022 from 2.77 percent in 2021, but this was well below the overall rise in global interest rates. In part, this reflects the shift to fixed rate debt in recent years (Figure 23).

Figure 22: Borrowing activities

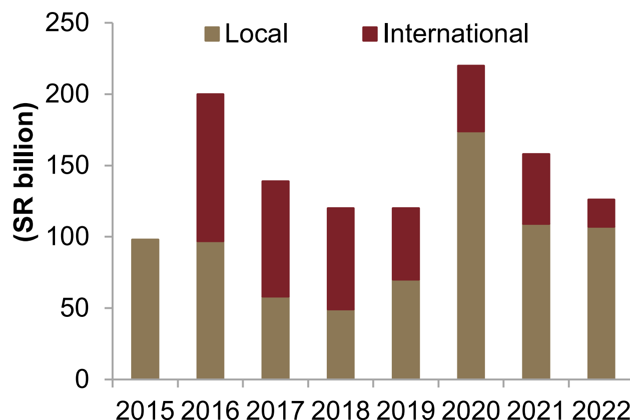
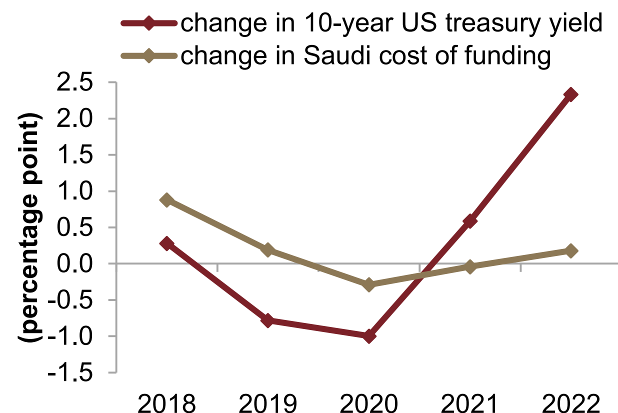


Figure 23: Cost of funding increased but by less than global rates



Monetary and Financial Developments

There was a shift from demand deposits into savings deposits last year…

In 2022, the broad measure of money supply (M3) rose by 8.1 percent, supported by a significant rise in time and saving deposits, which grew by 32 percent year-on-year. Meanwhile, demand deposits (constituting 53 percent of M3), declined by 2.3 percent on a yearly basis (Figure 24).

…this was driven by private depositors looking for better returns on their money.

When looking at the breakdown of time & saving deposits (which now make up 26 percent of M3, compared with 21 percent in 2021), we note that while government deposits (48 percent of total time & saving deposits) were up 45 percent in 2022, private deposits (52 percent of the total) were also up by 21 percent during the same period. As for demand deposits, the yearly decline was driven by private sector deposits (87 percent of demand deposits), which were down by 3.1 percent year-on-year. Government demand deposits were actually up by 3.2 percent, though these constitute just 13 percent of the total. The decline in private demand deposits during the year was previously anticipated in our report on the Saudi Economy in 2022, with more spending opportunities for households arising following the removal of Covid-19 related restrictions, especially in relation to services. Moreover, we think that businesses—and possibly households—are looking for better returns and shifting into time deposits, to benefit from rising interest rates.

Bank claims

Bank lending to the private sector continued to grow at a brisk pace last year…

...and now accounts for three-quarters of total lending.

Total bank claims rose by 12.2 percent year-on-year in 2022, supported by a 13 percent increase in credit to the private sector (75 percent of total bank claims), and by a 34 percent gain in claims on the public sector. When looking at the breakdown by sector (Figure 25), we find that “real estate activities” saw the largest rise by a net increase of SR49 billion, giving it a 33 percent share in total new loans to the private sector. This also saw the largest yearly rise in 2022 at 30 percent. As shown in the previous section, real estate activities witnessed some growth during the year, with rising demand for housing and various mega projects going forward around the Kingdom. That said, retail mortgage demand began to cool in the third quarter, as higher interest rates began to bite. New residential mortgages provided by banks and finance companies declined by 21 percent year-on-year in 2022.

Figure 24: Categories of bank deposits as a share of total deposits

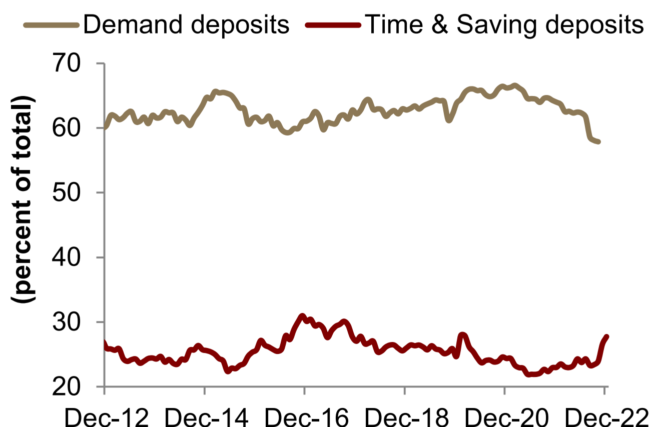
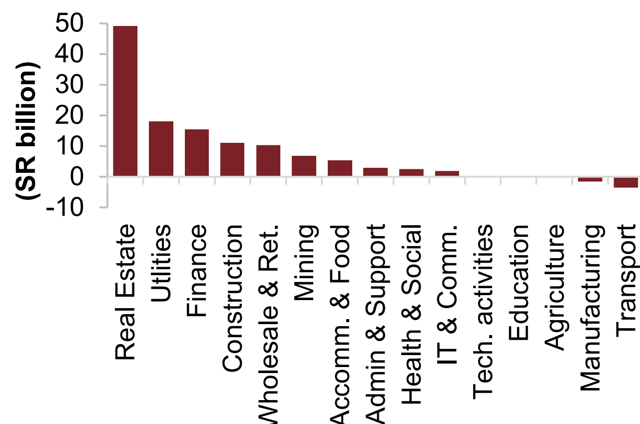


Figure 25: New bank loans in 2022, by sector



Lending to SMEs was virtually unchanged during the course of 2022.

Looking at the latest data on financial institutions lending to small and medium enterprises (SMEs), the share of SME loans in total credit provided by banks and finance companies stood at 8.2 percent at the end of Q3 2022 (virtually unchanged from Q4 2021), with a significant rise in lending towards micro-sized enterprises (up 45 percent in the year to Q3 2022).

Financial soundness indicators

Banking sector profitability is solid, with a sector-wide ROE of 12.5 percent.

Data on the banking sector (up to Q3 2022) showed that non-performing loans (NPLs) as a share of total loans continued improving, easing to 1.8 percent, from 2 percent at the end of 2021 and 2.2 percent at the end of 2020. Other banking indicators also improved through the year, with return on equity (at 12.5 percent) and return on assets (at 2.1 percent) both higher than pre-pandemic levels. Net interest margins widened substantially during 2022 giving a strong tailwind to sector profitability.

Outlook

Saudi interest rates should begin to level off in the next few months, albeit at a much higher level than a year ago…

...yet demand for credit from consumers and investors is likely to remain strong.

Looking ahead, we expect the Fed to halt its tightening cycle in the next few months, probably with only two further 25 basis point rises in its key rate. Thus, Saudi borrowing costs should begin to level off (albeit at a much higher level than a year ago). In any event, the demand for credit is likely to remain robust, with strong calls from both project-related activities and consumer demand. The latter is responding to ever-expanding spending opportunities, particularly with regard to services, along with the ongoing labor force expansion. We note that credit card loans gathered pace again in the second half of 2022 despite the higher interest rate environment (Figure 26). Mortgage demand could also pick up again if, as seems likely, interest rates begin to fall towards the end of the year.

Private sector credit-to-total deposits was above 100 percent in December.

Meanwhile, private sector bank deposits are likely to see subdued growth relative to loans. This could mean further tightness in overall system liquidity, and it is notable that the ratio of private sector credit to total deposits was above 100 in December 2022. That said, recent FX capital raises both by the central government and the PIF gives the potential, at least, for an easing of liquidity conditions in the near term.

Stable inflation

Saudi Arabia bucked the trend of sharp rises in global inflation with

Figure 26: Credit card loans rose in 2022 despite higher interest rates (year-on-year)

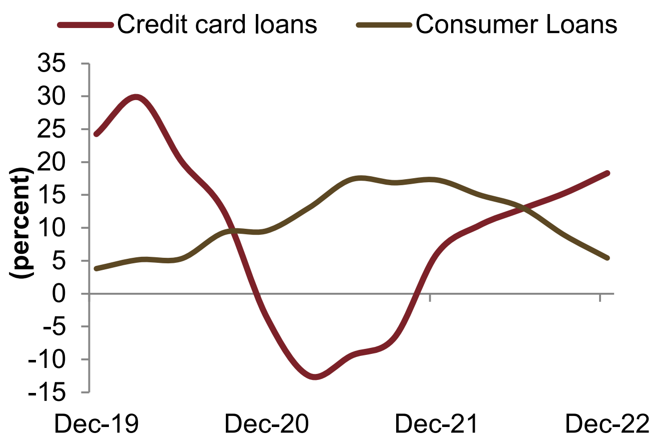
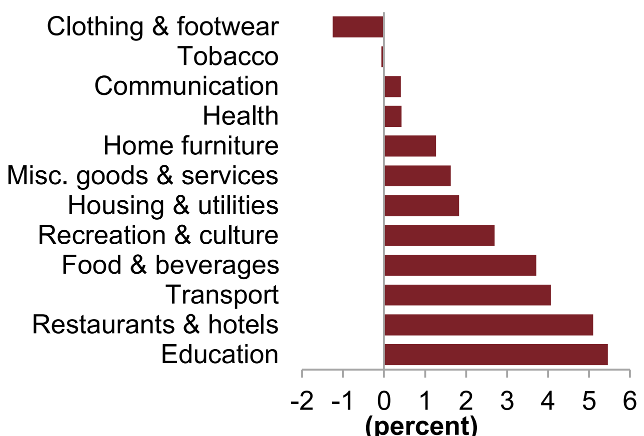


Figure 27: Inflation average in 2022, by sector



Saudi consumer price inflation was held to an average of just 2.5 percent in 2022, helped by a strong US dollar and subsidies on key items.

just a 2.5 percent gain in consumer prices during 2022 (broadly in line with our forecast of 2.4 percent). This put the Kingdom at the bottom end of the G20 inflationary scale, bettered only by Switzerland and China. A strong dollar helped to take the edge off imported price pressures from China and the eurozone, while subsidies on basic food items prevented a sharper pass-through to consumers. More generally, retailers have continued to absorb a large element of higher costs in an increasingly competitive market.

Price rises were most evident among services rather than goods.

Price rises in the Kingdom were led by 'education', as schools went back fully to pre-pandemic in-person classes. "Restaurants and hotels' came second, with higher input costs caused by robust raw materials and transportation prices, adding to the impact of released pent-up demand (Figure 27).

Housing inflation also picked up, reflecting in part growth in expat numbers.

Moreover, the two sectors with the largest weight in the CPI basket, 'food and beverages' (18.7 percent) and 'housing and utilities' (25.5 percent) both witnessed rises during the year. Indeed, 'housing and utilities' saw its first annual gain since 2016, rising by 1.8 percent in 2022, led by the sub-group item 'rentals for housing', which grew by an average of 2 percent. We view the rise in this segment mainly as a reflection of higher demand for housing, augmented by a rebound in the number of expat workers (Gastat labor market data showed a rise of 550,000 expats in the year-to-Q3 2022). Looking ahead, with robust levels of non-oil growth expected in 2023 (at 5.5 percent according to our forecasts), we expect further rises in the demand for housing, which, in turn, could see the 'rentals for housing' segment putting on further rises during the year. To support citizens in dealing with recent inflationary pressures, the Royal Order that was issued in July 2022 to allocate a total of SR20 billion through various channels of support was recently extended to the end of Q1 2023.

We anticipate a slightly weaker dollar this year, but the increase in inflation is likely to be slight, with a 2.6 percent average rate.

In 2023, we expect to see prices rising by an average of 2.6 percent, with lower rates forecasted for H2 than in H1 (Figure 28). The main factor behind this figure is expected further rises in 'rentals for housing' in the medium term, as we expect housing demand to continue the upward trend. In addition, we also see rises in 'restaurants and hotels', as tourism, entertainment and leisure events continue to be expanded around the Kingdom, with a larger number of visitors from outside the Kingdom expected this year. Elsewhere, we think that price pressures in 'food and beverages' should come down as shipping costs and other supply constraints ease during the year (Figure 29).

Figure 28: Consumer price inflation is expected to remain manageable

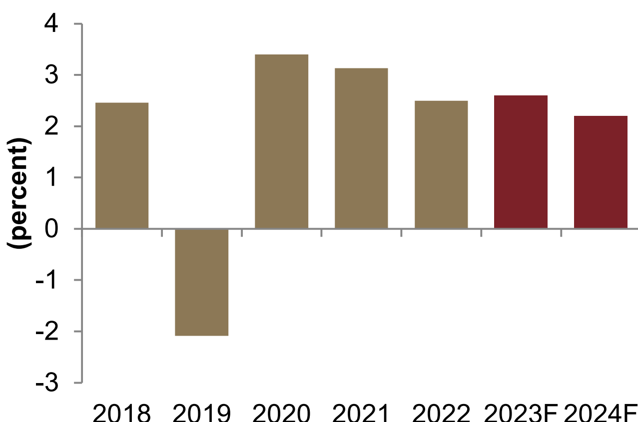
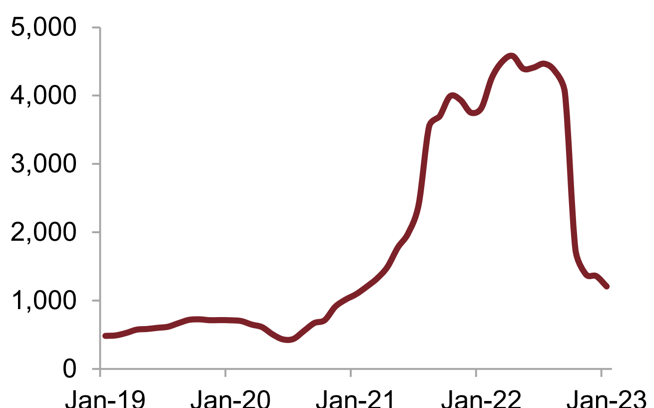


Figure 29: Global shipping costs are easing rapidly (index)



Box 5: The balance of payments

We estimate that the strong showing from oil earnings last year helped generate a trade surplus of $240 billion…

Having dipped into deficit during the pandemic-affected 2020, Saudi Arabia's current account returned to surplus in 2021 and is likely to have consolidated its position in 2022. Three quarters of data point to a very strong visible trade position, with oil export earnings and another good showing from non-oil exports easily offsetting a sharp increase in import spending. For the full year, we estimate that the trade surplus reached some $240 billion, which would be the largest since 2012 (Figure 30).

…which would be the largest since 2012.

Remittances outflows also picked up, though this did not prevent the current account recording a surplus of almost 12 percent of GDP according to our estimates.

The Kingdom runs a structural deficit on invisibles flows, with the biggest drag being workers' remittances outflows. These are highly cyclical, and are likely to have risen by at least 7 percent in 2022, reflecting the booming non-oil economy. Despite this, we estimate that the current account recorded a surplus of some 12 percent of GDP in 2022, around twice as large as the 2021 surplus. The financial account is a more complicated story, since it tends to feature large and quite volatile flows, often classified simply as "other". This was certainly the case in 2022, with the "other" account featuring sizeable outflows in the first and third quarters. Still, net flows for the balance of payments were still firmly positive, and the central bank's reserve assets are likely to have climbed by around $15 billion during the course of the year to $460 billion (a comfortable 40 months of import cover).

The current account surplus is expected to ease this year in line with weaker oil earnings (reflecting the slight cut to oil production)…

...nevertheless, the position will remain healthy at 8 percent of GDP.

The current account outlook remains positive. Oil revenue should exceed last year's total and firm demand from China for Saudi petrochemicals should provide further support to export earnings. Import demand is strong and rising, but even so the trade position should remain firmly in surplus. Workers' remittances outflows are expected to increase again, but tourism inflows should provide an offset, and the current account is expected to return a surplus of some $86 billion (8.2 percent of GDP). As indicated above, net financial flows are very difficult to predict, but the thesis of more capital searching out Saudi Arabia as investment opportunities expand should become more distinct in the years ahead. All told, we expect a substantial addition to the central bank's reserves during 2023 (Figure 31).

Figure 30: Large trade surpluses are anticipated

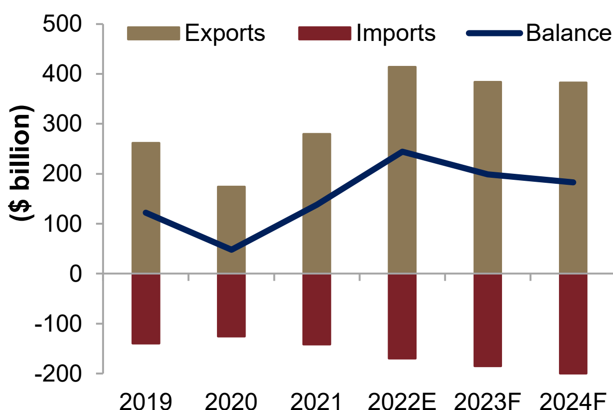
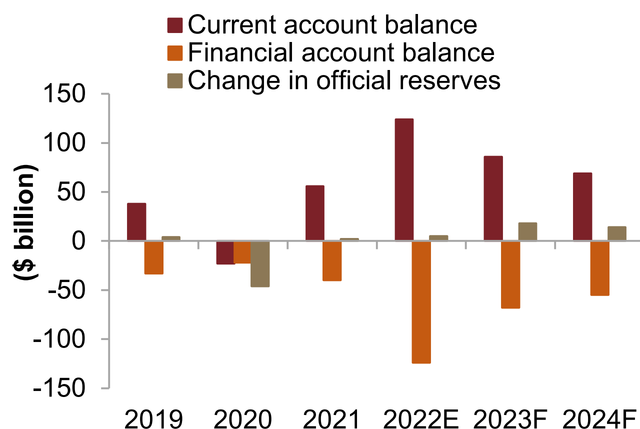


Figure 31: Financial account outflows are expected to narrow



The Outlook for 2024

Globally, 2024 is likely to be a brighter year than 2023.

By 2024 the global economy should be in much better shape than it is now. The Federal Reserve is likely to be in a loosening cycle which should stimulate demand in the world's biggest economy. China too should be a vital part of the growth equation: although the country has a number of structural issues and its population is now stagnant, it will become a more important engine of consumption as real incomes continue to rise. Other large Asian economies, such as India, Vietnam and Indonesia will also support global growth. We still see oil prices edging down in 2024, but this reflects an expected pick-up in non-OPEC supply rather than demand weakness. At an average of $87 pb for Brent, prices will be high enough to provide Saudi Arabia with fiscal and current account surpluses.

Oil prices are expected to ease slightly, but this will have little bearing on the Kingdom's economy, where investment and consumption are expected to remain brisk.

In any event, by 2024 the Kingdom will be further down the road of diversification, with new sources of capital continuing to develop. This capital will certainly be necessary to keep the Vision 2030 project on track, and we expect a pickup in project activity during the year as important deadlines begin to loom. The renewables transition (focused on hydrogen and wind/solar) should also gain more traction in 2024. Female labor force entry has further to run, and this will help propel economic expansion, while further expat growth will help marginally. Real non-oil growth should be above 5.5 percent in 2024, with overall growth exceeding 4 percent as oil output rebounds. Consumer price inflation should remain contained.

We think non-oil growth will exceed 5.5 percent in 2024.

Risks are largely project-related, with cost overruns and payment delays ever-present dangers. Financing constraints could also hold back progress, though we believe that the "Saudi growth story" is a compelling one and will attract sufficient flows of global capital (in various guises) to ensure that viable projects get financed. The long-term outlook remains positive with infrastructural investment raising potential GDP and—assuming this benefits productivity growth—allowing a durable rise in real incomes.

The main risk for the Kingdom lies in raising sufficient finance for all the various projects planned and underway.

Key Data

	2016	2017	2018	2019	2020	2021	2022E	2023F	2024F
Nominal GDP									
(SR billion)	2,497	2,681	3,175	3,145	2,754	3,257	4,034	3,941	4,060
($ billion)	666	715	847	839	734	869	1,076	1,051	1,083
(% change)	-0.5	7.4	18.4	-0.9	-12.4	18.3	23.9	-2.3	3.0
Real GDP (% change)									
Oil	3.6	-3.1	2.3	-3.3	-6.7	0.2	15.4	-0.2	2.8
Non-oil activities	1.9	3.0	-2.4	4.1	-3.7	7.2	5.4	5.5	5.6
Government activities	0.2	0.3	3.9	1.7	-0.6	1.1	2.2	2.2	2.1
Total	2.4	-0.1	2.8	0.8	-4.3	3.9	8.7	2.8	4.1
Oil indicators (average)									
Brent ($/b)	43	54	71	66	42	71	104	90	87
Production (million b/d)	10.4	10.0	10.3	9.8	9.2	9.1	10.6	10.5	10.8
Budgetary indicators (SR billion)									
Government revenue	519	692	906	926	782	965	1234	1181	1213
Government expenditure*	936	930	1,079	1,059	1,076	1,039	1132	1144	1151
Budget balance	-417	-238	-173	-133	-294	-74	102	37	62
(% GDP)	-16.7	-8.9	-5.5	-4.2	-10.7	-2.3	2.5	0.9	1.5
Gross public debt	317	443	560	678	854	938	985	951	959
(% GDP)	12.7	16.5	17.6	21.6	31.0	28.8	24.4	24.1	23.6
Monetary indicators (average)									
Inflation (% change)	2.1	-0.8	2.5	-2.1	3.4	3.1	2.5	2.6	2.2
SAMA base lending rate (%, end year)	2.0	2.0	3.0	2.25	1.00	1.00	4.50	5.00	3.00
External trade indicators ($ billion)									
Oil export revenues	137	171	232	201	120	203	331	297	294
Total export revenues	184	222	294	262	174	280	414	383	383
Imports	128	123	126	140	126	142	170	185	200
Trade balance	56	98	169	121	48	138	243	199	183
Current account balance	-24	10	72	38	-23	56	124	86	69
(% GDP)	-3.6	1.5	8.5	4.6	-3.1	6.5	11.5	8.2	6.3
Official reserve assets	536	496	497	500	454	455	460	478	492
Social and demographic indicators									
Population (million)	31.7	32.6	33.4	34.2	35.0	34.1	35.3	35.9	36.4
Saudi Unemployment (15+, %)	12.5	12.8	12.7	12.0	12.6	11.0	9.8	9.4	9.1
GDP per capita ($)	20,981	21,924	25,336	24,506	20,971	25,464	30,493	29,308	29,748

Sources: Jadwa Investment forecasts for 2023 and 2024. General Authority for Statistics for GDP and demographic indicators, Saudi Central 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.

Disclaimer of Liability

Unless otherwise stated, all information contained in this document (the “Publication”) shall not be reproduced, in whole or in part, without the specific written permission of Jadwa Investment.

The data contained in this Research is sourced from Reuters, Bloomberg, GaStat, SAMA, IMF, FocusEconomics, New York Federal Reserve, ’Tadawul, 2022 budget, CCHI, Vision 2030 VRPs, OPEC, EIA, IEA, IEF, and national statistical sources unless otherwise stated.

Jadwa Investment makes its best effort to ensure that the content in the Publication is accurate and up to date at all times. Jadwa Investment makes no warranty, representation or undertaking whether expressed or implied, nor does it assume any legal liability, whether direct or indirect, or responsibility for the accuracy, completeness, or usefulness of any information that contain in the Publication. It is not the intention of the Publication to be used or deemed as recommendation, option or advice for any action (s) that may take place in future.