NCB

September, 2013
www.alahli.com

Saudi Economic Review

NCB Monthly Views on Saudi Economic and Financial Developments

Contents

3 *Oil Market*

4 *Foreign Exchange*

5 *Commodities*

6 *Money and Inflation*

7 *Capital Markets*

8 *Loans Market*

9 *External Trade*

10 *Special Focus: A Virtuous Link between Savings and Investments*

Said A. Al Shaikh
Group Chief Economist | **s.alshaikh@alahli.com**

Tamer El-Zayat
Senior Economist | *Editor* | **t.zayat@alahli.com**

Majed A. Al-Ghalib
Senior Economist | **m.alghalib@alahli.com**

Yasser Al-Dawood
Economist | **y.aldawood@alahli.com**

Executive Summary

- Prices are expected to cross the USD125 a barrel for Brent and USD117 a barrel for WTI, if a strike on Syria actually takes place.
- The Eurozone had successfully averted an immediate crisis in Cyprus, tail risk mitigation will require a policy mix that will support near-term growth.
- After soaring to record highs in August and September of 2012, more favorable weather this growing season is likely to yield record US corn crop and large US soybean harvest.
- Due to the heavy reliance on imports for food, the rise in prices was partially driven by global price hikes as the Reuters/Jefferies CRB index recorded a gain of 3.0% during July.
- As the Syrian crisis continues, stock prices will be pressured despite the rise in oil prices which will trickle down to corporate results. Support will be provided by third quarter earnings next month which can limit the drain expected to continue this month.
- Local banks seem to have shifted their focus towards corporate credit rather than retail. Banks' maturity distribution is noticeably shifting towards long term credit which has expanded by 33.3% on an annual basis, reaching SAR310.3 billion by the end of July.
- Saudi non-oil exports are in line with last year's trend which also moderately grew in June before it nose-dove in July and August.

View of the Month

Although the accumulation of savings from the oil windfall was important, the utilization of savings in the most efficient manner will be critical, and apparently the Kingdom is enhancing this virtuous link between savings and investments.

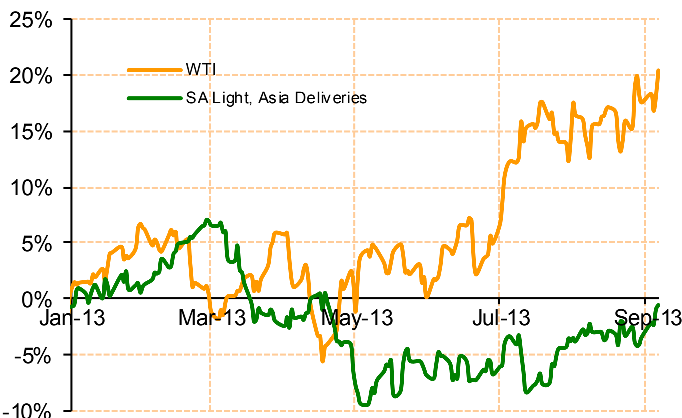
Macroeconomic Indicators

	2007	2008	2009	2010	2011P	2012F	2013F
Real Sector							
Average KSA Crude Spot Price, Arab Light, USD/BBL	68.3	94.9	59.2	77.6	108.1	110.2	105.0
Average Daily Crude Oil Production, MMBD	8.8	9.2	8.2	8.2	9.3	9.9	9.5
GDP at Current Market Prices, SAR billion	1,442.6	1,786.1	1,412.6	1,690.5	2,511.4	2,727.4	2,720.2
GDP at Current Market Prices, USD billion	385.2	476.9	377.2	450.8	670.6	728.3	726.3
Real GDP Growth Rate	2.0%	4.2%	0.1%	4.6%	8.5%	6.8%	3.0%
Oil Sector GDP Growth Rate	(3.6%)	4.2%	(7.8%)	2.4%	4.3%	5.5%	-3.1%
Non-oil Sector GDP Growth Rate	4.7%	4.3%	3.5%	5.5%	7.8%	7.2%	7.6%
Population, million	24.9	25.8	26.7	27.6	28.4	29.2	30.1
Population Growth Rate	3.4%	3.4%	3.4%	3.4%	2.9%	3.0%	3.0%
GDP /Capita, USD	15,444.2	18,495.4	14,147.9	16,354.7	23,632.8	24,917.7	24,127.9
CPI Inflation, Y/Y % Change, Average	4.1%	9.9%	5.1%	5.3%	5.0%	4.8%	4.5%
External Sector							
Merchandise Trade Balance, USD billion	150.6	212.0	105.2	153.7	244.7	268.4	231.6
Oil Exports, USD billion	205.3	281.0	163.1	215.2	317.6	347.6	324.6
Non-oil Exports, USD billion	27.8	32.3	29.1	35.8	46.9	48.9	42.2
Merchandise Imports, USD billion	(81.5)	(100.6)	(86.4)	(96.7)	(119.1)	(128.2)	(135.2)
Net Unilateral Transfers, USD billion	(17.0)	(23.0)	(27.7)	(27.9)	(29.4)	(32.1)	(114.5)
Current Account Balance, USD billion	93.3	132.3	21.0	66.8	158.5	178.7	117.1
Current Account Balance/GDP	24.2%	27.7%	5.6%	14.8%	23.6%	24.5%	16.1%
Net Foreign Assets with SAMA, USD billion	301.3	438.5	405.9	441.0	535.9	648.5	713.4
Fiscal Sector (Central Government)							
Budgeted Expenditure, SAR billion	380.0	410.0	475.0	540.0	580.0	690.0	820.0
Actual Revenues, SAR billion	642.8	1,101.0	509.8	741.6	1,117.8	1,239.5	1,076.6
Actual Expenditure, SAR billion	466.2	520.1	596.4	653.9	826.7	853.0	870.1
Expenditure Overrun, %	22.7%	26.8%	25.6%	21.1%	42.5%	23.6%	6.1%
Total Revenues/GDP	44.6%	61.6%	36.1%	43.9%	44.5%	45.4%	39.6%
Total Expenditure/GDP	32.3%	29.1%	42.2%	38.7%	32.9%	31.3%	32.0%
Overall Budget Balance, SAR billion	176.6	580.9	(86.6)	87.7	291.1	386.5	206.5
Budget Balance/GDP	12.2%	32.5%	(6.1%)	5.2%	11.6%	14.2%	7.6%
Break-Even Oil Price	40.5	40.2	60.8	64.1	71.1	67.0	72.8
Financial Sector							
USD/SAR Exchange Rate	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Growth in Broad Money (M3)	19.6%	17.6%	10.7%	5.0%	13.3%	13.9%	8.1%
Growth in Credit to the Private Sector	20.6%	27.9%	-0.6%	4.8%	11.0%	16.4%	18.8%
Average 3M SAR Deposit Rate	4.9%	3.3%	0.9%	0.7%	0.7%	0.9%	1.0%
Average 3M USD Deposit Rate	5.2%	3.0%	0.7%	0.4%	0.3%	0.4%	0.4%
Spread, in Basis Points, SAIBOR-LIBOR	(39.2)	37.4	26.4	39.8	40.9	55.2	60.0

Oil Market
Prices on the Rise

Uncertainty over rising tension in the Middle East region along with the risk of a western military action against Syria has driven oil prices to fresh high levels in recent weeks. After peaking to USD118 a barrel for Brent and USD112 a barrel for WTI, prices retreated slightly to USD115 a barrel, and USD108 a barrel, respectively. The WTI, US benchmark, was also supported on expectations of a revival in demand growth after US automobile sales gained at their fastest pace since October 2007. With the recent backing of US congress to the US president of a military intervention, the possibility of a strike on Syria is rising. The prices are expected to cross the USD125 a barrel for Brent and USD117 a barrel for WTI, if a strike on Syria actually takes place. Oil prices will likely remain firm because of supply risks from other oil producers, particularly, Libya and Iran. However, Brent at USD125 a barrel would be a significant headwind for the already weak global economy, making it not sustainable for long. Judging mainly on the supply and demand fundaments, excluding the regional political risk premium, oil prices are around USD90 a barrel for Brent and USD85 a barrel for WTI.

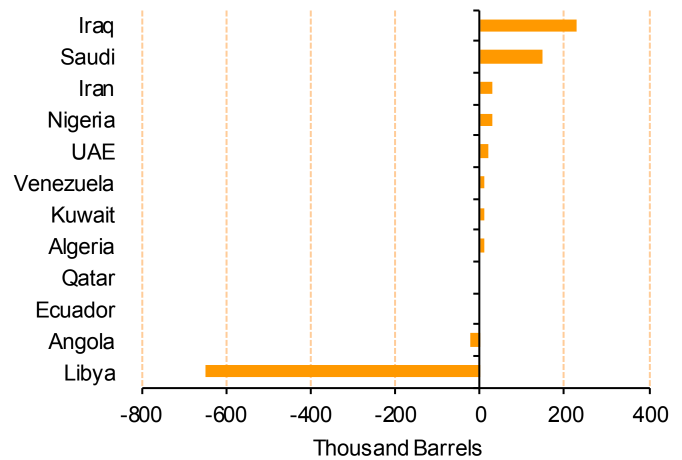
Chart 1: Oil Price Developments, YTD



Source: Thompson Reuters

On the demand side, disparity between the core European countries and periphery persists, with the demand by core rising 3.3% Y/Y, while the demand by periphery posting a decline of 6% Y/Y in May. China's oil demand eased by 2% M/M from 9.94mmbd in June to 9.77mmbd in July, yet YTD demand reached 9.87mmbd, up 5.1% Y/Y from January- July 2012. Crude imports by China outpaced demand, gaining a sharp 20% Y/Y to 6.17mmbd, which is believed to have led to a build-up in stocks. Global oil demand growth is expected to accelerate in 2014 to 1.1mmbd, compared with 0.9 MMBD in 2013. The forecast of oil demand growth for 2014 has been trimmed by 0.1 MMBD on reduced GDP expectations from the IMF, while that for 2013 is kept unchanged.

Chart 2: OPEC's Monthly Oil Production Changes



Source: OPEC Survey

On the supply side, OPEC crude production climbed in August as Saudi Arabia produced oil at a faster pace, along with UAE to make up for the massive shortfall from Libya. Output by OPEC increased 0.4% to an average of 31.04mmbd from a revised 30.92mmbd in July. Saudi output increased by 0.15mmbd to 9.95mmbd in August, and expected to remain at the same level in September. The UAE increased production to 2.92mmbd, while Libya output tumbled to 0.575mmbd in August, sending production to the lowest level since October 2011. Angola reduced production to 1.74mmbd, while Nigeria's output rose to 2.02mmbd. Iran produced 2.57mmbd in August, which was down about 0.18mmbd from August 2012. OPEC's spare oil production capacity is now estimated to be only 2.2mmbd as compared to an average of 3mmbd in 2010-2012. Outside OPEC, US crude oil production increased to an average of 7.5mmbd in July 2013, the highest monthly level of production since 1991. The EIA forecasts US total crude oil production to average 7.4mmbd in 2013 and 8.2mmbd in 2014.

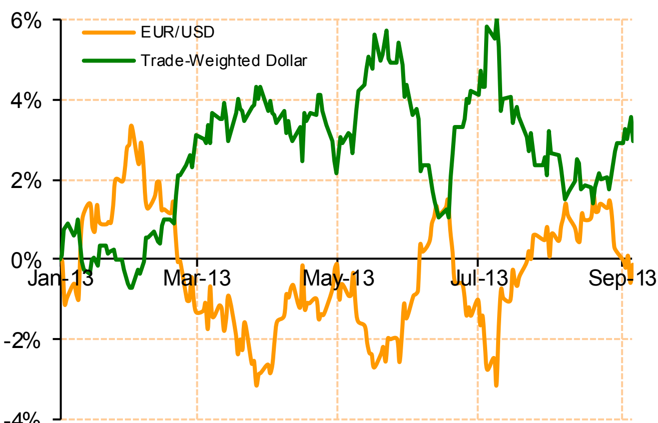
Said A. Al Shaikh
Group Chief Economist | **s.alshaikh@alahli.com**

Foreign Exchange

Macroprudential and Geopolitical Concerns

Financial and equity markets have been exhibiting heightened volatility since May after the Federal Reserve began hinting towards finally putting the lid on its open-ended QE3 program. This came contemporizing with a rising geopolitical tension in the Middle East, increasing the likelihood for a US military intervention; thus, adding an element of uncertainty. Although the Eurozone had successfully averted an immediate crisis in Cyprus, tail risk mitigation will require a policy mix that will support near-term growth. On the other hand, key emerging economies are adjusting for lower growth rates due to deficient consumer demand and falling commodity prices. Infrastructure bottlenecks, financial stability concerns, and weak policy support are the main culprits for the weaker-than-expected economic growth. Consequently, the International Monetary Fund's World Economic Outlook has revised its forecast for global economic growth this year downwards to remain at 3.1%, erasing the 0.2% expected acceleration over last year's rate.

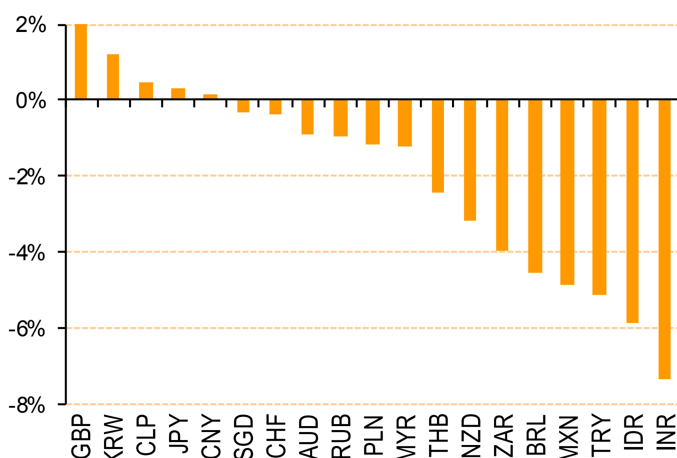
Chart 3: Trade-Weighted Dollar and the Euro



Source: Thompson Reuters

The late improvement in the US economy indicated by the recent labor market figures implies resilience to the Federal Reserve's tapering signals, paving the way for it to push forward with unwinding its unconventional monetary policy stimulus. In August, unemployment reached its lowest levels since December of 2008, a rate of 7.3%, down from 7.6% the previous month. Non-farm payroll added 169,000 jobs which is well above expectations. In contrast, due to the overly appreciating housing market, new single-family home sales fell to their lowest levels in 9 months, dropping by 13.4% to an annual rate of 394,000 homes. Sharp rises in mortgage rates are acting as a drag on consumer appetite which may weaken the case for the Federal Reserve to pull out of the market in September. The spillover effect of taper talks and the possible military intervention in Syria is adversely affecting risk-seeking behavior, and causing investors to shy away from the bond and equity markets. Benchmark 10-year treasury yield rose by 7.8% in August to a 22-month high of 2.8%. In a normalization of the record highs, Wall street dipped as the Dow fell by 4.4% to fall down to 1,4810.3, and S&P 500 slid by 3.1% to 1,632.9 in their worst debacle since June. As the USD became the safe haven of choice, the DXY strengthened by 0.78% over the month of August to remain on the 82 level.

Chart 4: Monthly Foreign Exchange Rate Changes



Source: Thompson Reuters

According to the IFO business climate index, manufacturing picked up in the Eurozone, driving German business sentiments up to 107.5 from 106.2 in July, the highest since April 2012. However, due to key trade partners being largely in recession, long-term optimism remains subdued. The ECB struck dovish tone but didn't commit to further easing, which confirms that refinance rate will remain at the low 0.5%. This ignited worries that risk of inflation might erode purchasing power, capping short-term expectations. Furthermore, the EUR stayed range-bound at 1.33 indicating relative stability.

In response to the Fed's decision, fears that the narrowing trading band will no longer attract hot money led the BRICS' central banks to jack up interest rates in an attempt to counteract capital flow reversals. The BRL weakened against the USD by 4.77% down to 2.38, the INR plummeted by 7.95% to 65.71. The CNY/USD, however, strengthened by 0.14% to stand at 6.12 due to China's capital controls which limits the concern for capital flight.

Yasser Al-Dawood
Economist | **y.aldawood@alahli.com**

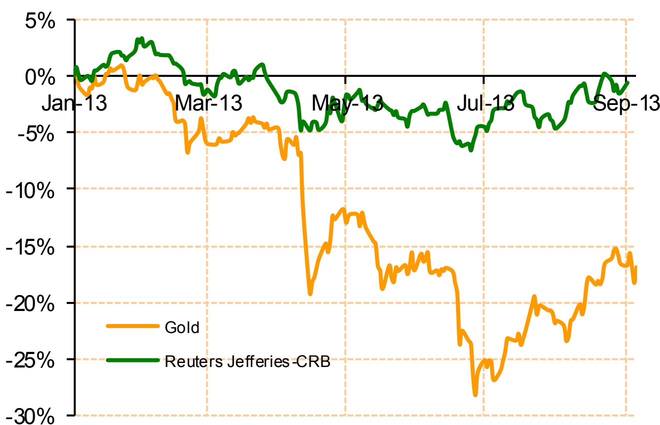
Commodities

Agriculture in Red, Metals Flourish

Despite a rough month for most asset classes, commodity prices edged higher in August as China stepped up efforts to combat its economic slowdown via heavy railway investment and construction of public housing. In addition, it aims to establishing new frameworks to help struggling small companies in order to boost consumer confidence and strengthen demand. HSBC Purchasing Managers' Index (PMI) rose to 50.1 in August from an 11-month low of 47.7.3 in the previous month. The overall commodity futures price index Thomson Reuters/ Jeffries CRB recorded a 2.5% upturn from last July, standing at 291.2. Precious metals gained momentum in August due to the uncertainty that stemmed from the QE3 tapering signals and the political dithering regarding Syria. Investors from affected emerging markets rushed to park their money in gold which spiked demand for the yellow metal to surge by 5.5% over the 30 day period, reaching 1,397.1 USD/Oz . Demand for silver also came in favorable, pushing prices upwards by 18.4% to stand at 23.6 USD/Oz. Boosted economic activity in Chinese steel mills have stimulated restocking of base metals, which pressured prices up. Copper prices went up by 3.2% to 7,100 USD/ton, while Aluminum inched up by 0.5% to 1,830.5 USD/ton. According to London Metal Exchange, increased demand led copper and aluminum stocks to shrink by 3.7% to 0.5 megatons and 1.4% to 5.4 megatons, respectively.

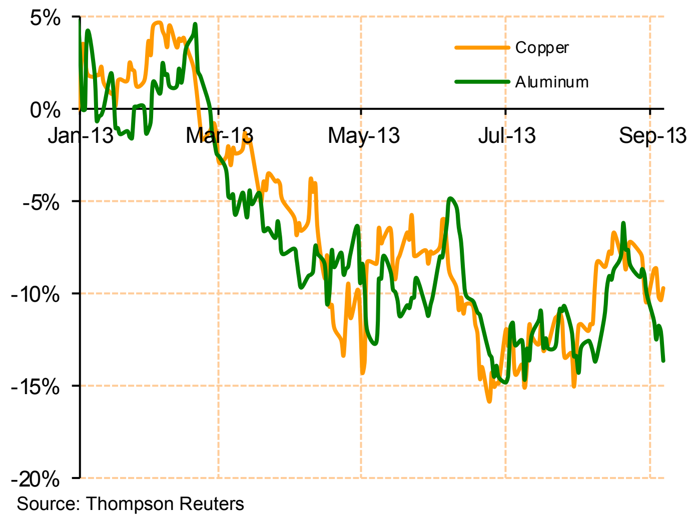
Agricultural commodities are unwinding from the spike of last year caused by drought in the US Midwest. After soaring to record highs in August and September of 2012, more favorable weather this growing season is likely to yield record US corn crop and large US soybean harvest. According to United States Department of Agriculture (USDA), corn production this year is forecast at 13.8 billion bushels, propelling by 28% from 2012's figure. If realized, it will be the highest US corn production on record. As for soybean, it is forecast to yield 3.26 billion bushels, up by 8% from last year, which if materialized will be the third largest on record.

Chart 5: Reuters Jefferies vs. Gold



Source: Thompson Reuters

Chart 6: Base Metals



Source: Thompson Reuters

Consequently, ample supply will send prices markedly lower. Although prices of corn futures are still high compared to the long-term average between year 2000 and 2013, which is 3.73 USD/bushel, CBIT near-by corn futures have fallen to 4.99 USD/bushel in August, gauging a 40.6% annual price decline. Compared to last month's contract, however, corn futures are up 0.5%. Global wheat crop is also expected to spurt due to favorable weather in Canada, the Black Sea region and a good monsoon in India, which will replenish stocks in worldwide inventories. Wheat futures in August averaged 6.64 USD/bushel, up 3.6% from last month .Geopolitical supply risk remains distant from soft commodities while keeping international oil prices strong (please refer to the oil market section on page 3.)

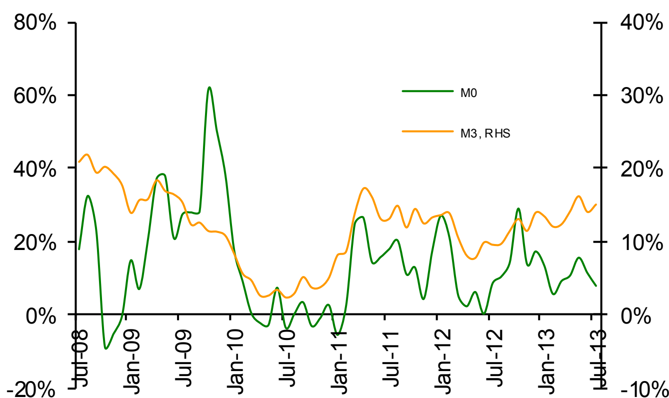
Yasser Al-Dawood
Economist | **y.aldawood@alahli.com**

Money & Inflation

Consumer Prices Edging Higher

The Arab Spring uprising's prolonged transition phase has kept oil prices elevated, positively impacting Saudi's balances. The economy's liquidity level facilitated the growth of local businesses and the buildup of net foreign assets which act as a cushion for the Saudi economy. The monetary base (M0) recorded a rise of 7.8% Y/Y during July, the slowest annual growth rate since February. SAMA's conservative policy is reflected in banks' deposits with SAMA as by the end of 2012 deposits represented 56.4% of M0, while ten years ago in 2002 deposits only held a share of 29.3% of the monetary base. Deposits with SAMA have decreased to the lowest level this year at SAR124.9 billion. In addition to an expanding credit market, banks have been seeking better quality assets, which resulted in deposits with SAMA declining by 36.9% since the beginning of 2013. Meanwhile, cash in vault increased by 31.5% annually bringing bank reserves to SAR152.1 billion, a 2.1% annual gain. In addition, currency outside banks also increased at an annual 14.5% to reach SAR146.2 billion by the end of July.

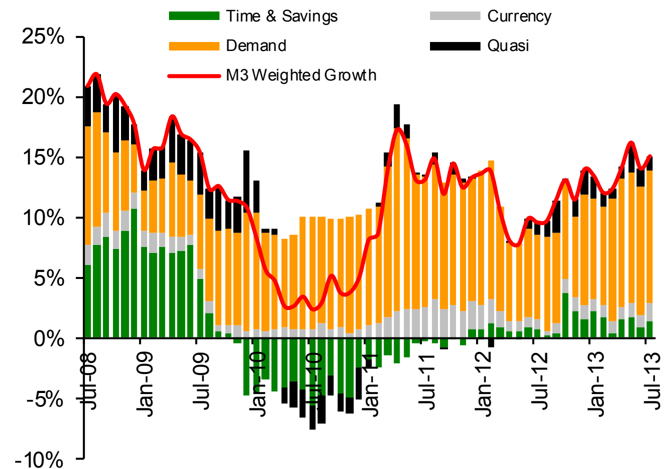
Chart 7: Growth in Monetary Aggregates



Source: SAMA, NCB Estimates

As for the broad money (M3), it posted a rise of 15.0% Y/Y, the eleventh consecutive double digit growth. The level of liquidity is likely to maintain an upward trajectory for the remainder of the year and surpass the SAR1.5 trillion level. Given market anticipations of higher interest rates in the near future due to the expected change in US policy, demand deposits increased by 20.3% Y/Y, the fastest pace since February 2012. Furthermore, time and savings deposits expanded by 6.1% annually. We expect capital to shift towards time and savings deposits from its non-yielding counterpart as the local stock market run ends. The peg with the USD ensures that Saudi will not suffer from damaging capital outflows experienced in other emerging economies.

Chart 8: Money Supply, Contribution



Source: SAMA, NCB Estimates

The holiday season supported higher consumer prices during July which increased at an annual 3.7% in comparison to June's 3.5% Y/Y. In addition, businesses and consumers alike were in preparation mode for the holy month of Ramadan. Consequently, food prices posted the highest increase at 6.9% for the sub-index. Prices for vegetables, bread & cereals, and fruits contributed greatly to higher food prices as they increased 14.8%, 11.3%, and 10.5%, respectively, on an annual basis. Due to the heavy reliance on imports for food, the rise in prices was partially driven by global price hikes as the Reuters/Jefferies CRB index recorded a gain of 3.0% during July. Furthermore, the sub-category of housing and utilities, the second largest contributor to rising local prices, accelerated at 4.2% by the end of June. Inbound tourism supported higher rental prices by 5.0% annually. The lack of real estate development continues to inflate housing prices. Numerous projects have been announced, yet, very few have passed the initial planning and design phases. The newly codified mortgage system will need to be implemented and tested to raise confidence between lenders and borrowers, until then, prices will remain elevated.

Majed A. Al-Ghalib
Senior Economist | **m.alghalib@alahli.com**

Capital Markets

Geopolitics Deter Fundamental Gains

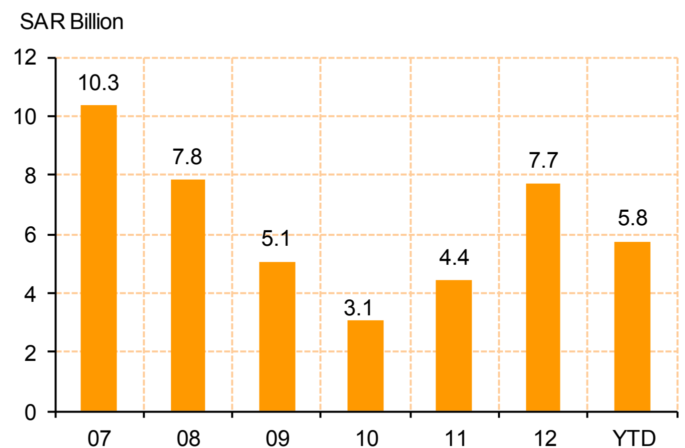
The geopolitical standoff in the Middle East intensified, thus, capping indices on a global scale. The riskier asset class, according to the MSCI World index, dropped 2.3% last month. Given the recent changes in policy agendas, namely US, equity investors are likely to reassess their geographical interest. As for the Saudi stock market, Tadawul recorded a loss of 1.9% during August. The market peaked at 8,214.85, a gain of 20.8% since the beginning of the year. However, the possible military decision on Syria pushed investors to reap capital benefits and seek safer asset classes. Only three sub-indices posted gains last month, cement, hotel & tourism, and petrochemicals at 1.5%, 1.4%, and 0.1%, respectively. The cement market has been backed by sound corporate earnings which have been supported by a vibrant construction sector. Moving forward into this month, stocks have dropped 1.7% during the first week of trading in September. The hotel & tourism sub category suffered the most by declining 5.7% last week, lowering its YTD gains to 83.6%. As the Syrian crisis continues, stock prices will be pressured despite the rise in oil prices which will trickle down to corporate results. Support will be provided by third quarter earnings next month which can limit the drain expected to continue this month.

Chart 9: Tadawul All-Share Index

Source: Tadawul

Despite the strong performance up to August 21, investor appetite was rather modest and daily trading volumes averaged at SAR5.8 billion for the whole month. The positive trajectory started mid-June and ended late August, during that period daily traded volumes averaged SAR5.2 billion. However, once risk levels start to escalate, investors are quick to withdraw their capital as witnessed by daily traded volumes post the index's peak which averaged at SAR6.3 billion. The lack of confidence in the local market is somewhat unwarranted given the economy's strong fundamentals. Furthermore, Tadawul's majority of traders are Saudi individuals, yet Saudi institutions increased their portfolios last month by contributing 11.1% of buying transactions, compared to 10.9% in July. Foreign, other than GCC, traders' activity recorded less than 4% during August. The market is at a healthy stage where price-to-earnings ratio stood at 14.27 by the end of August, indicative of lucrative long-term opportunities especially with oil prices on a rising trajectory.

Chart 10: Average Daily Traded Value



Source: Tadawul

The primary market was non-active for a second month and there are no initial public offerings planned for September either. Meanwhile, the secondary market witnessed a new turning point. Middle East Specialized Cables Co. offered 20 million shares in the form of a rights issue of one for every two shares owned. Tadawul introduced and executed the new tradable rights framework which provides the option of trading and listing the right to buy share entitlements. The main purpose of this new framework is to limit losses for share owners of respective company by allowing them to cash in on their right if they are unwilling to increase their shareholder equity. Despite the insignificant size in comparison to the market, Tadawul's willingness to add depth and diversification in the market is a positive notion.

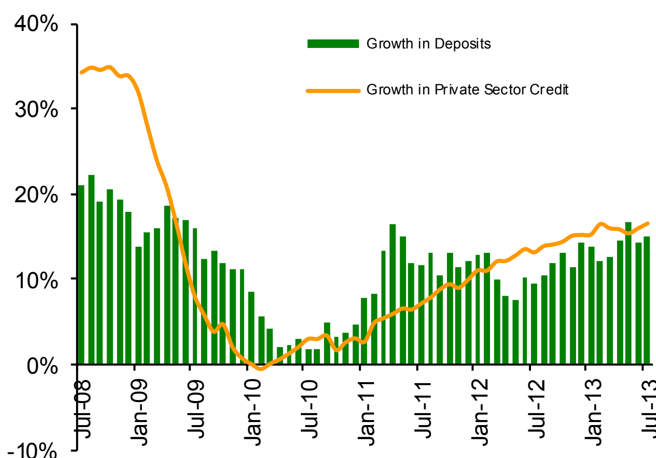
Majed A. Al-Ghalib
Senior Economist | **m.alghalib@alahli.com**

Loans Market

Corporate Credit Continues to Rise

As one of the essential components of determining the ability of local banks to accommodate the expansion in the credit market, deposits in the financial system remain at a healthy level. The depositary base of Saudi banks has reached SAR1.33 trillion during July according to the latest SAMA bulletin, a rise of 15.1% over the same month last year. The suppressed interest rate environment pushes individuals and businesses to prefer demand deposits which have climbed by 20.3% annually. Government and entities also preferred to place their capital in the form of demand deposits which grew by 25.7%, compared to their time and savings deposits smaller growth of 10.7% by the end of July. Total time and savings deposits grew by 6.1% Y/Y as the low deposit yield fails to attract funds as business and individuals seek other opportunities, albeit riskier. Furthermore, other quasi-monetary deposits increased at an annual 9.3% as foreign currency deposits expanded by 8.3% during July. Additionally, the new labor market regulations for expatriates resulted in increasing outstanding remittances by 14.3% Y/Y. The deadline for rectifying labor statuses has been postponed till November 3, we expect remittances to be elevated as uncertainty looms over the future of workers.

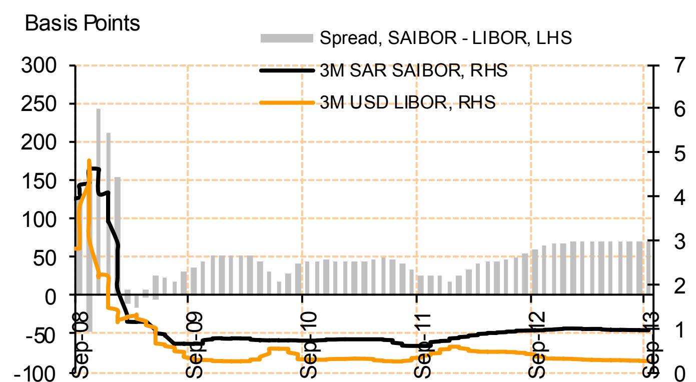
Chart 11: Private Sector Financing



Source: SAMA, NCB Estimates

Total claims of the banking system, excluding T-bills and government bonds, decelerated for the fourth consecutive month by recording an annual growth of 15.1%, the slowest since June 2012. Local banks seem to have shifted their focus towards corporate credit rather than retail. Banks' maturity distribution is noticeably shifting towards long term credit which has expanded by 33.3% on an annual basis, reaching SAR310.3 billion by the end of July. Medium term credit recorded a gain of 19.3% Y/Y while short term credit only increased by 6.2% Y/Y. Since the beginning of 2013, local banks have added SAR95.1 billion in fresh lending and the figure is expected to grow at a slightly slower pace. The loans to deposits ratio increased to 82.5% during the month of July with SAMA closely monitoring risk indicators for the Saudi financial system.

Chart 12: Liquidity and Risk Detector



Source: Thompson Reuters

Banks provided SAR10.9 billion in credit lines for the private sector during July, an annual gain of 15.3%. The momentum of private sector growth has been sustainable as the economy benefits from elevated oil prices. However, claims on the public sector has also been on the rise for the past few months. During July, claims on the public sector increased by 21.3% annually. The bulk of the increase was new issuances of Treasury Bills which have reached a record SAR179.8 billion, climbing by 38.6% Y/Y. We expect SAMA has been a little wary of rising local prices but the supervision have ensured that government bonds have been replaced by T-bills. Government bonds have decreased by 16.8%, the 13th annual decrease. Liquidity risks remain low and SAMA will certainly attempt to maintain a healthy market. Once the US switches to a hawkish policy, SAMA will possess more tools to limit rising liquidity risks and inflationary pressures.

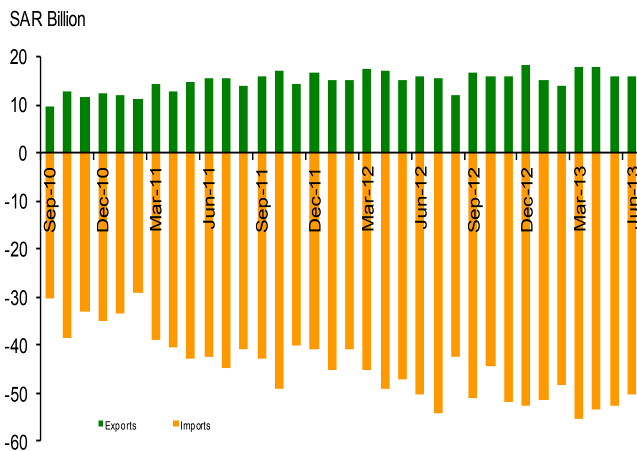
Majed A. Al-Ghalib
Senior Economist | **m.alghalib@alahli.com**

External Trade

Global Demand Remains Supportive

External trade in the month of June realized SAR17.1 billion of export revenue, leaping over last year's figures by 6.4%. This came despite the 9% decrease in tonnage which recorded 3.8 megatons. Imports, on the other hand, grew in value by 0.2% over the previous year, amounting to SAR50.210 billion. Volume-wise, imports receded by 3.4% Y/Y to 6 megatons. The appreciating returns from exports indicate that prices are still supportive.

Chart 13: Saudi Non-Oil Trade Balance

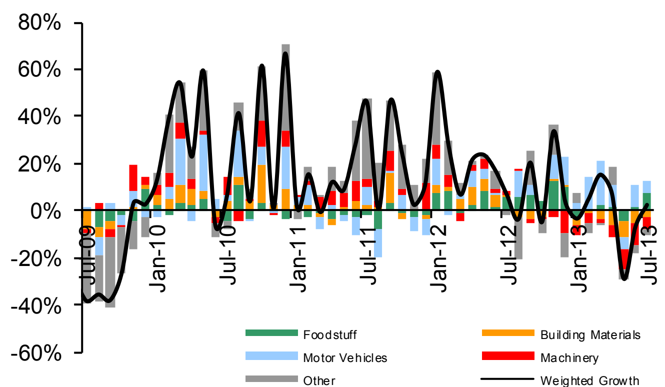


Source: CDSI, NCB Estimates

Saudi non-oil exports are in line with last year's trend which also moderately grew in June before it nose-dove in July and August. By export category, we find that plastics still dominate non-oil exports by 31.4%, generating SAR5.4 billion. They surged by 22.7% compared to the same period last year. Chemical products, which make up 31.1% of non-oil exports fell by 10.8% Y/Y to SAR5.3 billion. Transport equipment has been gaining traction since the beginning of the year, expanding to constitute 14% of non-oil exports and surging by a staggering 67.7% compared to last year. It reached SAR2.4 billion in value. This might be due to a transition from base-metals into more processed goods, or a change in the category's definition. Base metals, which make up 5.4% of non-oil exports rose by 4.4%Y/Y, totaling SAR0.92 billion. By Destination, 13.3% of non-oil exports headed to the UAE. The value of exports went up by 38.9% Y/Y, registering SAR2.3 billion. China received 12.9% of the exports advancing by 17.9% over last year to record SAR2.2 billion. Bahrain, for the first time, took over Singapore as the third largest trade partner. It received 8.2% of exports, surging by 160.3% over last June, marking SAR1.4 billion.

Non-oil imports continued a mildly downward sloping trend that started in March. This limited major increases over last year's figures. By import category, machinery and electrical equipment, which make up 25.8% of non-oil imports decreased by 4.1%, settling at SAR12.9 billion. Transport equipment, which occupies 18.3% of the imports made SAR9.2 billion, an increase of 12.2%. Base metals makes up 13.5% of non-oil imports. It relapsed by 5.5% Y/Y, registering SAR6.8 billion. By origin, the USA is home of 14.9% of non-oil imports. It surpassed China since last year to exponentially grow by 20.7%. 14.9% of June's non-oil imports total balance was allocated for US imports which realized SAR7.4 billion. China comes as a close second with 14.5% of imports allocation. Imports of Chinese non-oil imports rose by 9.3% Y/Y, recording SAR7.2 billion. Germany is the third largest importer to the kingdom with accounting for 6.4% of imports allocation. German imports shrunk by 11.1% in comparison to June of 2012.

Chart 14: Attribution Analysis of Letters of Credit Opened



Source: SAMA, NCB Estimates

Settled letters of credit (LCs) in the month of July grew annually by 1% to SAR22.7 billion. The overall growth was affected by negative growth in machinery and building materials by 14.% and 26.5%, respectively. It was counterbalanced by a solid 23.6% growth in demand for motor vehicles. Open LCs for July confirmed the same direction as it increased annually by 2.4%, a total of SAR17.2 billion. Motor vehicles rose by 30.2%, while machinery and building materials tumbled by 33.6% and 29%, respectively.

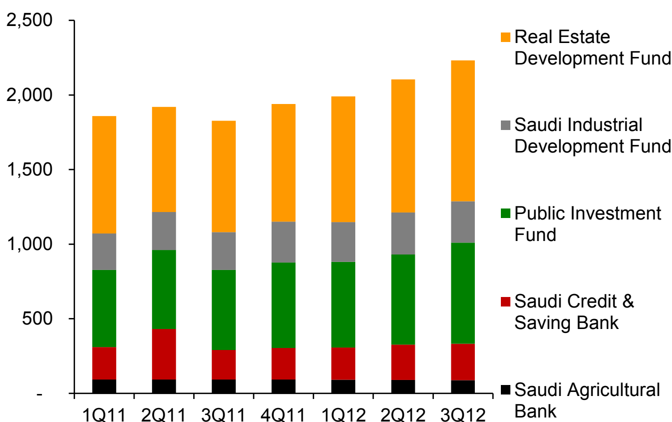
Yasser Al-Dawood
Economist | **y.aldawood@alahli.com**

Special Focus:

A Virtuous Link between Savings and Investments

The Saudi government is adamant in pursuing policies that continue to support a predominantly young population through the creation of job opportunities, the provision of housing, and the rectification of regional imbalances. This is why Specialized Credit Institutions (SCIs) such as the Public Investment Fund (PIF), Saudi Industrial Development fund (SIDF), Saudi Credit & Saving Bank (SCSB), and the Real Estate Development Fund (REDF) represent a pivotal role in achieving the above-mentioned strategy. According to the latest available data published in SAMA's 2Q2013 bulletin, the consolidated balance sheet for government SCIs points to: (1) a significant increase in the disbursements of new loans by SAR29.3 billion, 20.5% Y/Y growth, during the first three quarters of 2012, which is the largest disbursement on record compared to prior periods, reflecting the drive to support domestic activity, (2) a decrease of 17.4% in the total value of investments to around SAR124.7billion by the end of 3Q2012, which was attributed to a shrinking domestic portfolio that fell from a record SAR136.96 billion by the end of 2012 to SAR108.7 in 3Q2012, (3) an insignificant increase in foreign investments that remained around SAR15.9 billion mark, and (4) a 35.8% Y/Y increase in deposits with SAMA that stood at SAR95.4 billion, indicating the impending plans to extend loans to local companies rather than passive international or local investment. In our opinion, the budget appropriations for 2013 that amounted to SAR68.2 billion coupled with this latest data reflect the central role played by SCIs as a catalyst in the domestic economy, and it will not be surprising if this year posted new historical figures.

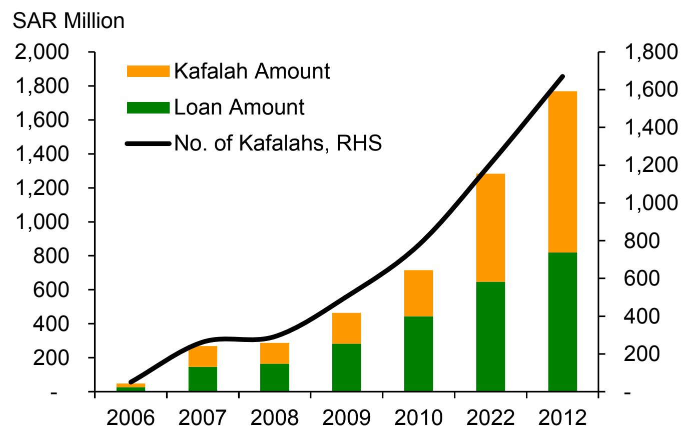
Table 15: SCIs outstanding loans and Investments



Source: SAMA

As expected, the REDF was largest among these institutions in terms of the outstanding loans that registered SAR94.5 billion, and it is our believe that such figure might have crossed the SAR100 billion threshold as will be shown in the coming data releases. It is no surprise that REDF will maintain its status as the largest lender among SCIs with the government trying to mitigate the market imbalances especially at the demand side. The PIF and SIDF had also maintained the second and third rank given their participation in project finance across different sectors that enhance the kingdom's absorptive capacity, with the outstanding loans to both standing at SAR67.7 billion and SAR27.7 billion, respectively. On the Small and Medium scale Enterprises (SMEs) front, the Loan Guarantee Program "Kafalah", which is a collaboration between the Ministry of Finance represented by SIDF and Saudi banks continued to gain ground, facilitating credit worth around SAR1.59 billion by the end of 2Q2013 to 574 establishments, representing 16.5% of the aggregate beneficiaries since the inception of the program in January 2006. Bottom-line, although the accumulation of savings from the oil windfall was important, the utilization of savings in the most efficient manner will be critical, and apparently the Kingdom is enhancing this virtuous link between savings and investments.

Table 16: Loan Guarantee Program "Kafalah"



Source: SAMA

Tamer El Zayat
Senior Economist | **t.zayat@alahli.com**

Economics Department

The Economics Department Research Team

Head of Research

Said A. Al Shaikh, Ph.D
Group Chief Economist
s.alshaikh@alahli.com

Macroeconomic Analysis

Tamer El Zayat, Ph.D
Senior Economist/Editor
t.zayat@alahli.com

Majed A. Al-Ghalib
Senior Economist
m.alghalib@alahli.com

Yasser Al-Dawood
Economist
y.aldawood@alahli.com

Sector Analysis/Saudi Arabia

Albara'a Alwazir
Senior Economist
a.alwazir@alahli.com

Mai Al-Swayan
Economist
m.alswayan@alahli.com

Shahrazad A. Faisal
Economist
s.faisal@alahli.com

Management Information System

Sharihan Al-Manzalawi
Financial Planning & Performance
s.almanzalawi@alahli.com

To be added to the NCB Economics Department Distribution List:

Please contact: Mr. Noel Rotap
Tel.: +966-2-646-3232
Fax: +966-2-644-9783
Email: n.rotap@alahli.com

Disclaimer: The information and opinions in this research report were prepared by NCB's Economics Department. The information herein is believed by NCB to be reliable and has been obtained from public sources believed to be reliable. However, NCB makes no representation as to the accuracy or completeness of such information. Opinions, estimates and projections in this report constitute the current judgment of the author/authors as of the date of this report. They do not necessarily reflect the opinions of NCB as to the subject matter thereof. This report is provided for general informational purposes only and is not to be construed as advice to investors or an offer to buy or sell or a solicitation of an offer to buy or sell any financial instruments or other securities or to participate in any particular trading strategy in any jurisdiction or as an advertisement of any financial instruments or other securities. This report may not be reproduced, distributed or published by any person for any purpose without NCB's prior written consent.