Saudi Arabia: Balanced budget within reach

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- **Saudi Arabia's 2020 fiscal budget highlights the authorities' aim to meet their balanced budget target by 2020 in a phased manner and with lesser impact on economic growth.**
- **Strengthening the private sector and creating more jobs will remain key focus areas for the government in the next financial year.**
- **With the winding down of its role in Yemen, spending by Saudi Arabia on the military is set lower than last year, but at around 6% still ranks first globally as a percentage of GDP.**

Rebound in non-oil growth

Saudi Arabia's overall economic performance in 2019 and its 2020 budget goals both highlight the kingdom's policy of pushing private economic activity and shifting to multiple economic resources to reduce dependence on oil.

- Growth is forecast by the government at 2.3% in 2020, a significant recovery from the 0.4% posted in 2019, as ongoing diversification reforms should yield dividends.
  - The OPEC+ deal to deepen output cuts by 500 Kb/d until March 2020, however, could weigh on the kingdom's economic recovery in the early part of this year.
  - Preliminary economic data shows that real GDP growth in 2019 was slightly better than the 0.2% forecast by the IMF. But the 0.4% was still minimal, driven by the decline in oil prices resulting from a slowdown of in global demand and the decline in oil production under the OPEC+ agreement.
  - Oil revenues in the majority of GCC countries average close to 60% of total revenues. In the case of Saudi Arabia, this figure is closer to 90%.
    - This is in contrast with other resource-rich, yet diversified economies, such as Norway, where revenues from oil account for just about 30% of government revenues.
- Saudi Arabia is, however, gradually diversifying its economy away from oil. We expect non-oil growth to fuel the economy in 2020 despite a drop in government spending, which had been the main catalyst for growth in previous years.
  - We see the main drivers of growth as the construction sector (assuming progress on mega projects[3]), finance (housing and mortgage), as well as wholesale retail trade (driven by a rapid expansion in the tourism, sports and entertainment sectors).

Table 1 - IMF Macroeconomic Indicators[1]

	2016	2017	2018	2019	2020f
Real GDP Growth (%)	1.7	-0.7	2.4	0.2	2.2
Crude Oil Production (M Bpd)	10.4	9.9	10.3	9.7	9.9
Oil GDP Growth (%)	3.6	-3.1	3.1	-3.1	1.7
Non-oil GDP Growth (%)	0.2	1.3	2.2	2.7	2.5
CPI Inflation (%)	2.0	-0.9	2.5	-1.1	2.2
Fiscal Balance (% of GDP)	-17.2	-9.2	-5.9	-6.1	-6.6
C/A Balance (% of GDP)	-3.7	1.5	9.2	4.4	1.5
Total Gov't. Gross Debt (% of GDP)	13.1	17.2	19.0	23.2	28.4
Total Gross Extrn'l Debt (% of GDP)	24.6	27.7	28.1	30.4	32.3
Gross Official Reserves (Mos. of Imports)	31.7	28.2	27.2	26.4	24.1
Nominal GDP (USD B)	644.9	688.6	786.5	779.3	783.3
Population (Millions)	32.4	33.1	33.7	34.2	34.8

Table 2 - Ministry of Finance Macroeconomic Indicators[2]

	2018	2019	2020f	2021	2022
Real GDP	2.3%	0.4%	2.3%	2.2%	2.3%
Nominal GDP (USD, B)	783	750	774	807	838
Inflation	2.6%	-1.0%	2.0%	2.0%	1.8%

  - Moreover, we expect additional uplift in the non-oil private sector as a result of Saudi Arabia hosting the G20 summit next year. This increased global profile is likely to stimulate progress on structural reforms as the kingdom continues to improve its image internationally.
- The government forecasts inflation at 2% in 2020 with YoY pressures waning.
  - With growth remaining below potential, inflation remained subdued in 2019, averaging -1% from 2.6% in 2018 and -0.8% in 2017, in line with IMF projections.

Austerity makes a comeback

The new budget cuts spending, signalling an end to the last two years of expansionary fiscal policy. But it does project a higher deficit. Based on revenues of USD 222B, the government is budgeting for a YoY deficit of USD 50B in 2020 (6.4% of GDP), compared with USD 35B in 2019 (4.7% of GDP) and a high of USD 87B (13.7% of GDP) in 2016. Spending, however, has been curtailed from both last year's actual and targeted outlays.

- The kingdom's Fiscal Balance Program (FBP) aims for a balanced budget by 2030. Realising this will be contingent on sustained fiscal consolidation and higher oil prices.
  - In the 2019 budget statement, the government indicated that its debt-to-GDP ratio will not be allowed to exceed 25% over the balancing phase.

[1] Arabia Monitor; IMF.
[2] Arabia Monitor; Ministry of Finance, Saudi Arabia.

[3] Construction is scheduled to start on the first major parts of the Qiddiya Entertainment City project and Diriyah Gate in Q1 2020, and the Red Sea tourism project is also expected to start full-scale construction later this year.

- However, the target was raised to 30% in the updated FBP document in late December 2019 which means the kingdom has room to accumulate up to USD 238B in net debt by 2023 (another USD 57B from end-2019's level).
- The debt-to-GDP ratio is forecast at 26% for 2020 and 29% by 2022, from 24% in 2019. This remains significantly lower than many of Saudi Arabia's peers and, indeed, most advanced economies (Figure 1).

➢ The deficit was USD 35B in 2019 (4.7% of GDP), 24% lower than 2018's and in line with the MoF budget for 2019.
- As usual, the budget did not specify the average expected Saudi crude export price (or the percentage of revenue expected to be derived from oil sales) but the Ministry of Finance (MoF) has a history of using conservative price estimates, considerably below the market level.
- The IMF estimates Saudi Arabia's breakeven oil price for 2020 at USD 83.6 pb from USD 86.5 pb in 2019. Brent is forecast to average USD 60.5 pb this year, according to the US Energy Information Administration.

➢ In 2020, expenditure is budgeted at USD 272B (35.1% of GDP), 2.6% lower than actual 2019 spending and 8% lower than what was planned.
- At USD 46.1B (17% of total expenditure), capital spending is unchanged from actual 2019 levels, which were also 2% higher than initially budgeted for that year. However, the Public Investment Fund and the National Development Fund are expected to take a leading role in investments within the kingdom, providing additional stimulus to the economy.[4]
- Current spending, which is the more rigid part of expenditure, is budgeted at USD 226B, 3.4% lower than actual 2019 levels.
  - However, the most economically vulnerable households will continue to benefit directly from support under initiatives such as the Citizen's Account, but also indirectly through spending on education, healthcare and social infrastructure.
  - We do not rule out that one-off and lumpy spending measures, such as bonuses usually granted to government workers, could cause some overruns.
  - Spending on subsidies in 2020 is budgeted at USD 4.5B, 23% lower than actual 2019 and almost 50% lower than what was planned. The impact of planned subsidy cuts would most likely be felt in 2021 and could come in below expectations.
- A sectoral breakdown shows a pattern in expenditure that is in line with recent years. Education, military, healthcare, security services and economic resources were allocated 72.7% of the total budget.
  - Though budgeted 4.4% YoY lower for 2020, education makes up the largest portion, at 19% of the total. For comparison, this is lower than that of Mexico (24%) but higher than that of India (12.7%) and China (12.1%).
    - Spending will continue to focus on new schools, restoration of old ones, as well as on the Overseas Scholarship Program.
    - We believe that on the back of such strong initiatives, the current gap between wages, skills and productivity can be significantly reduced.
  - Meanwhile, a sizeable reduction in military spending is budgeted for the second consecutive year and is expected to decline by 8% YoY in 2020 to 6.2% of GDP. Globally, this still ranks 1st. The decline highlights the winding down of Saudi Arabia's role in Yemen.
  - Only the "general items" category, which includes spending areas such as on government pensions, social insurance and financing costs, is expected to show yearly rises.

Figure 1 - Debt-to-GDP Ratio (%)[5]

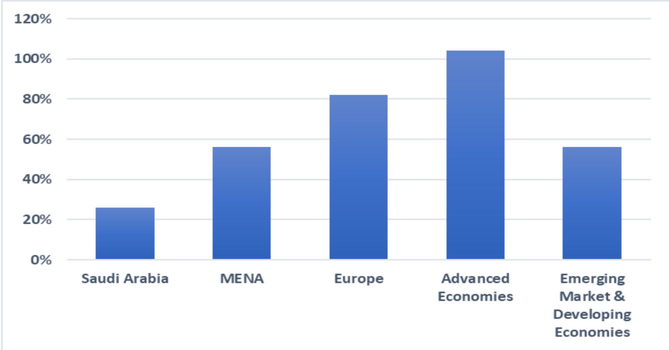

Table 3 - Budget Performance (USD, B)[6]

	Budgeted Expenditure	Actual Expenditure	Budgeted Revenue	Actual Revenue
2009	127	146	109	134
2010	144	167	125	196
2011	155	214	144	296
2012	184	228	187	331
2013	219	247	221	302
2014	228	293	228	279
2015	229	260	191	162
2016	224	220	137	141
2017	237	248	185	184
2018	261	275	208	239
2019	295	279	260	245
2020f	272	…	222	…

Non-oil revenue on the rise

Revenue is budgeted at USD 222B in 2020 split 63-37 between oil revenue and non-oil.

➢ Oil revenue is forecast at USD 137B in 2020, 15% lower than actual 2019 estimates due to volatility in oil prices.[7]

➢ In 2020, non-oil revenue is expected be 2% YoY higher than actual 2019, largely as a result of taxes on income, profits, capital gains and goods and services.

[4] This is a subject of some controversy because of fears they will crowd out others.

[5] Arabia Monitor; IMF.
[6] Arabia Monitor; Ministry of Finance, Saudi Arabia.
[7] Brent averaged USD 63.9 pb in 2019, 9% YoY lower.

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