



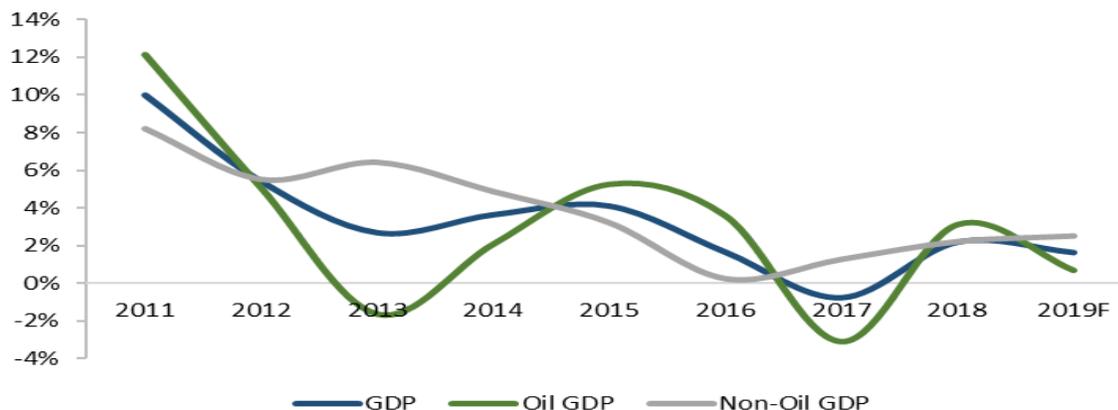
USSABC Economic Brief: Saudi Arabia's First Quarter GDP Update

First Quarter Overview

Saudi Arabia economy expanded by 1.66 percent year on year in real terms during the first quarter of 2019. The oil sector grew by 1.04 percent while the non-oil sector increased by 2.13 percent. Oil production cuts coupled with lower oil prices weighed down on the economy while encouraging developments in non-oil sectors contributed to the non-oil sector's growth rate. The private sector accounted for the highest growth at 2.3 percent while the government sector increased by 1.74 percent.

The impact of lower oil production will likely cause a slight drop in overall forecasted GDP growth in 2019 from 1.8 percent to 1.7 percent. Consequently, oil GDP is expected to grow by 0.7 percent for 2019. The non-oil side is expected to continue to push forward as the private sector's contribution reached its highest level since the third quarter of 2017 and is forecasted to grow by 2.5 percent for 2019. The transport, finance and mining sectors witnessed strong growth, reaching 4.93 percent, 4.85 percent, and 4.49 percent, respectively. Furthermore, the construction sector entered positive territory for the first time since the fourth quarter of 2015 as it reached 1.26 percent.

Real GDP Growth

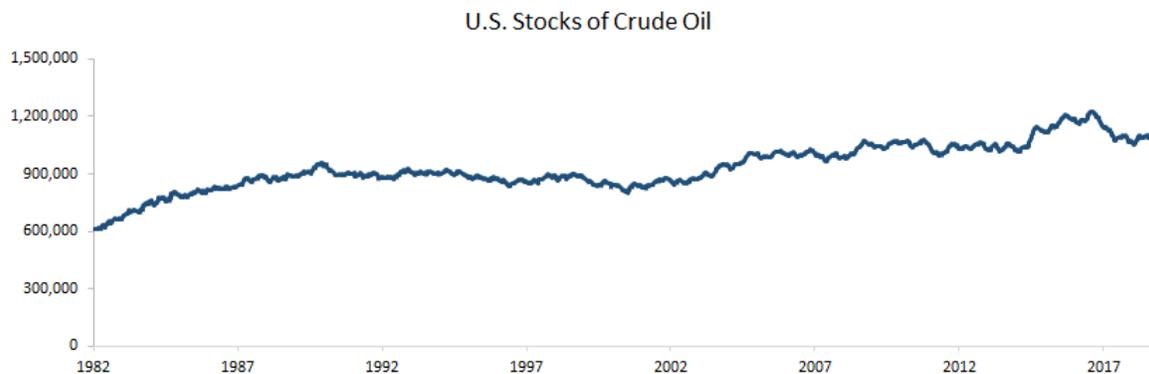


Source: GaStat, USSABC Estimates

Oil GDP

The moderation in oil GDP was largely anticipated on the back of OPEC's December 2018 production cut agreement and lower oil prices compared to last year. Saudi Arabia's production steadily decreased during the first quarter, as it went from 10.05 million barrels per day (mbpd) in January to 9.85 mbpd in March. While the goal of the cuts are to prop up oil prices, at least in the short-term, OPEC members are positioning to contend with lower demand from consumer countries. Moreover, lower oil production from member countries like Iran and Venezuela present supply concerns to meet baseline global demand given imposed sanctions on those respective countries.

Brent crude oil, which averaged \$71 in 2018, has decreased to an average price of \$64 in June and is likely to average around \$66 in 2019. Besides production cuts by OPEC, elevated tension in the region as well as larger than anticipated inventory declines in the United States during June and July will likely keep crude oil prices elevated for the second half of 2019.



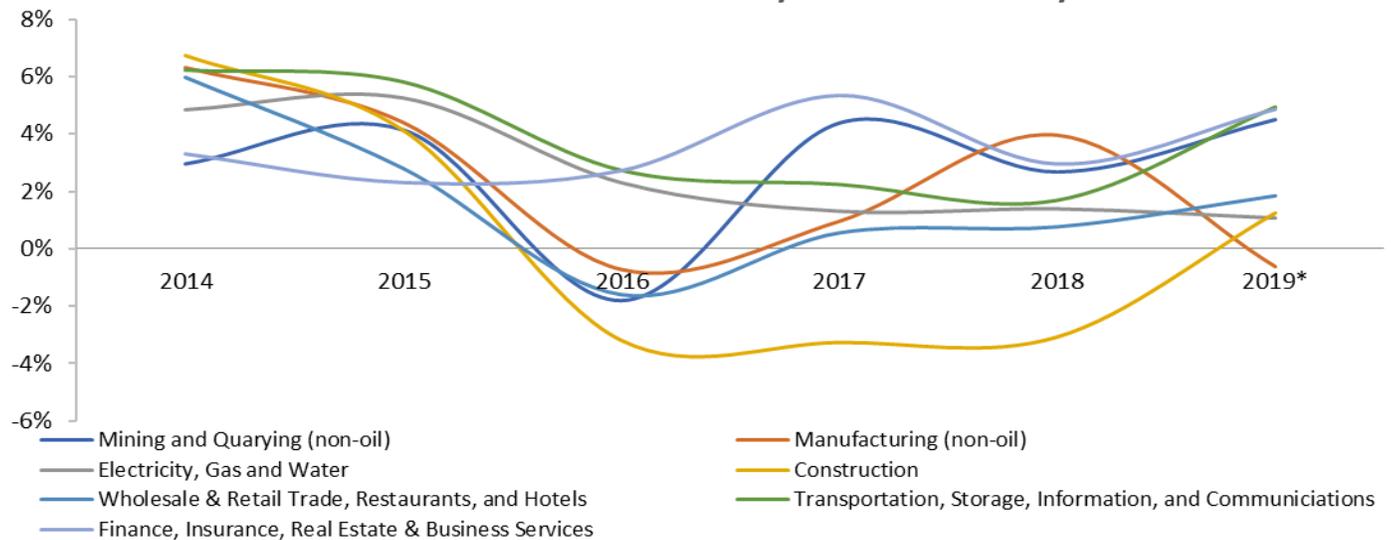
Source: EIA, USSABC Estimates

It is anticipated that oil GDP will grow at a decelerating rate given the projected 0.7 percent contribution for 2019. Saudi Arabia oil production, which has averaged 9.98 mbpd during the first half of 2019 is likely to be maintained as it is expected to average around 10 mbpd for 2019. In order to continue its current expansion of non-oil expenditures to fulfill its budgeted objectives besides going to debt markets to fund its projects and widen its fiscal deficit, the Kingdom continues to rely on oil income as its main source of liquidity. As the first quarter's performance reflected, oil income increased by 48 percent to SAR169 billion y-o-y, which gives the Kingdom some reprieve in supporting its expansion plans, albeit a majority of the increase was due to a SAR124 billion dividend that was received from Saudi Aramco.

Non-Oil GDP

The Kingdom's non-oil GDP during the first quarter outperformed forecasts to reach 2.13 percent. The growth was largely driven by the private sector, a key gauge on the health of the economy, which grew by 2.30 percent while the government sector grew by 1.74 percent. A strong driver of this growth has been the implementation of major projects as part of the stimulus program under Vision 2030, which has helped the mining, transport, and construction sectors.

Real Annual Growth Rate by Economic Activity



*Through Q1'19

Source: GaStat, USSABC Estimates

The development of the non-oil sector will allow for higher than forecasted growth, reaching 2.5 percent for 2019. The non-oil purchasing managers' index (PMI) for June witnessed an uptick in confidence levels as it increased to a 19-month high of 57.4. The jump was largely due to an acceleration in new business growth at businesses in the Kingdom. The rate of the PMI's expansion was the fastest in three months.

While still accounting for a marginal share of GDP, the growth of the mining sector is seen as a positive development given the importance it has been given under Vision 2030. The mining sector grew by 4.49 percent compared to last year and expanded even more compared to the previous quarter where it grew by only 0.79 percent.

Hailed as Saudi Arabia's third pillar after oil & gas and petrochemicals, the mining sector is undergoing significant investments as the government aims to boost the sector's contribution to GDP, provide numerous employment opportunities, enhance localization competencies, and become a global leader in exploration and extraction capabilities. Recent shifts to strategically focus on the mining sector coincide with the Kingdom's vast and relatively untapped mineral resource base.

The Kingdom's ambitious long-term plans for the mining sector will require significant amounts of investments in the exploration and mining of current and new sites, in addition to encouraging an open market for local and private players to participate on equal footing, and developing the immense human capital requirements. The Kingdom has already taken steps to develop these areas of focus by developing specialized entities that will oversee the proliferation of the mining sector. These entities include the National Industrial Development Program (NIDLP), the Industrial Clusters, and the Saudi Arabia Industrial Investments Company, also referred to as Dussur. These entities were borne out of Vision 2030 and are expected to be influential participants in the sector.

The Kingdom currently and in the future will maintain long-term large and growing domestic demand to go along with the abundance of mineral resources and very competitive energy costs. While some estimates ambitiously indicate that the Kingdom has approximately SAR5 billion (\$1.33 billion) worth of mineral endowments, especially in precious and base metals, the fact of the matter is that Saudi Arabia represents a growth market opportunity where strategic partners can make a significant positive impact on the economy. Ongoing government mandates that accelerate the exploration and development of mines also assist in the enhancement of midstream and downstream segments of the value chain.



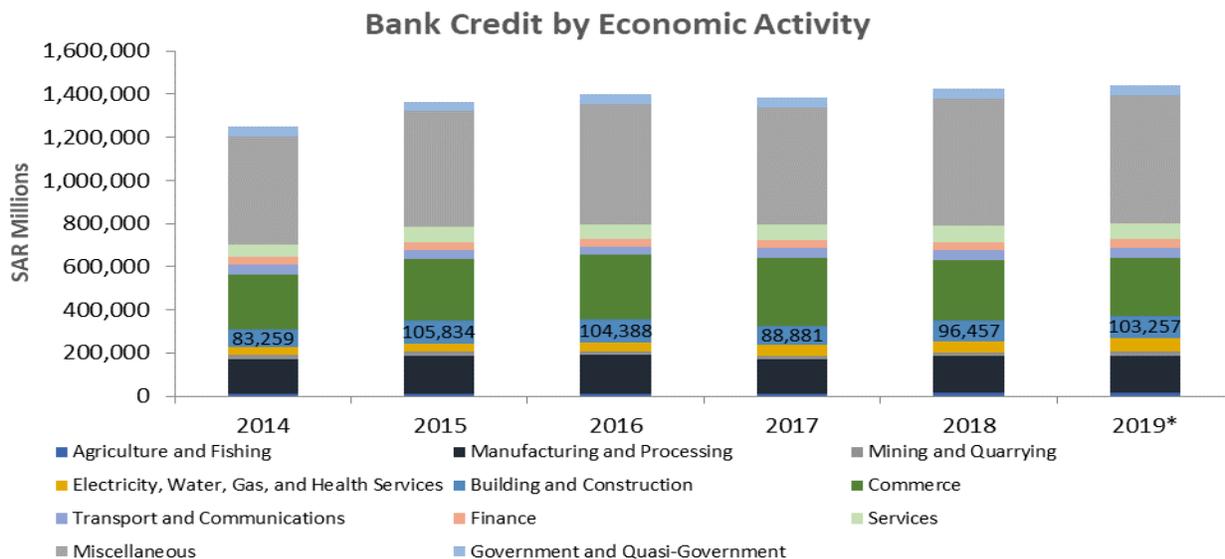
Source: GaStat, USSABC Estimates

The expansion of the construction sector, which grew by 1.26 percent marks a significant turning point in the economy. The construction sector has experienced continuous quarterly contractions dating back to the fourth quarter of 2015. The economic downturn led to sharp decreases in the number of awarded contracts in addition to many cancellations and suspensions. However, the construction sector witnessed a resurgence during the first quarter of 2019 on the back of the implementation of numerous projects as stipulated under the Kingdom's spending budget.

The SAR48.9 billion in awarded contracts during Q1'19 marks an overwhelming 113 percent increase compared to Q1'18, when the value was approximately SAR23 billion. Q1'19 had the highest value of awarded contracts dating back to Q1'15 when the value reached SAR88.6 billion. Furthermore, the value of awarded contracts in Q1'19 alone accounts for approximately 48 percent of the total value witnessed in 2018. Consequently, the pace of awarded contracts thus far indicates that construction activities across all sectors will remerge as a strategic focal point in the Kingdom.

The value of awarded contracts rebounded strongly during the first quarter after a relative dip over the last couple of years. This positive momentum is expected to continue as one of the largest drivers is the government's allocation of SAR246 billion in capital expenditures for 2019. With non-oil growth being a priority, continued heavy investments in capital projects will significantly aid in the proliferation of local employment opportunities, financing mechanisms, and localization & privatization schemes.

Another indication of a stronger construction sector is the increase in the level of bank credit extended to construction activities. The 'Building and Construction' category received SAR103.3 billion (\$27.5 billion) in bank lending during the first quarter of 2019. This comes after years of lowered credit extensions in 2017 and 2018. The level of contribution to total bank credit also increased, reaching 7.2 percent, marking the highest contribution since 2016 when it reached 7.4 percent.



*Through Q1'19
Source: SAMA, USSABC Estimates

The Kingdom's forecasted GDP is expected decline from its original forecast of 1.8 percent to 1.7 percent. Saudi Arabia will likely maintain an average oil production of 10 mbpd for 2019 as OPEC+ producers are expected to maintain production cuts into the first quarter of 2020. Lower oil prices for the remaining of 2019 in tandem with production cuts will keep the Kingdom's GDP growth in a moderation range. However, there are external factors that may affect growth rates which bear close monitoring. Ongoing trade tension between the U.S. and China and regional geopolitical concerns are the salient risks that could affect the Kingdom's growth momentum.

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