



# USSABC Economic Brief: Prudent Policies Lift the Private Sector

## Overview

The competitiveness of Saudi Arabia's evolving economy has been spurred by robust policies aimed at placing the country among the world's top economies. Saudi Arabia jumped 30 places from 92nd to 62nd in the World Bank's recent Ease of Doing Business report with improved scores on 9 of 10 key indicators. The World Bank named Saudi Arabia the top global business reformer of the 190 countries analyzed and highlighted key reforms such as streamlining business registration and lifting foreign ownership restrictions in several sectors.

The report comes on the heels of the latest World Economic Forum (WEF) report which raised Saudi Arabia's global competitiveness ranking from 39th to 36th and gave the Kingdom the top rating in macroeconomic stability for the second consecutive year. The report also highlighted government responsiveness, long-term vision, and the growth of innovative companies as strong indicators of improved global competitiveness.

These findings are supported by macroeconomic trends that provide optimism for both domestic and foreign businesses operating in Saudi Arabia. While the short-term outlook for Saudi Arabia's economic growth has been subdued by lower oil prices and a general slowdown in the global economy, the private sector's contribution to GDP continues to increase on the back of a prioritization plan that promotes economic diversification.

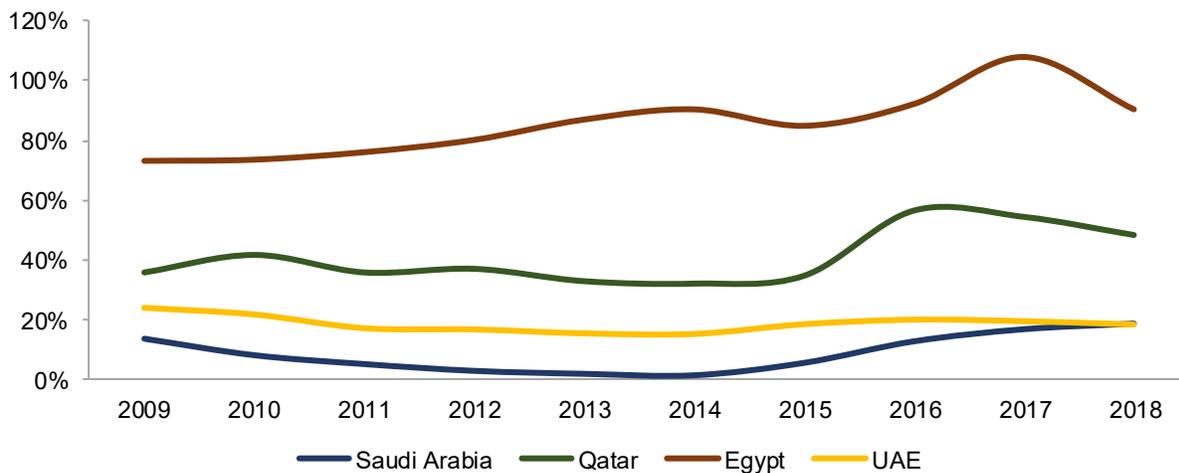
## Sustained Macroeconomic Stability

The IMF's GDP growth forecast for 2019 was recently reduced from 1.9 percent to 0.2 percent primarily due to reduced oil prices stemming from lower global demand, escalating trade tensions, and worries of a global economic slowdown. The government has countered lower oil prices by limiting production further than called for by the OPEC+ deal in an effort to reduce inventories and stabilize oil prices. Despite the downward revision in short-term outlook, the IMF raised its 2020 GDP projection to 2.2 percent on the expectation of a more stable oil market and continued momentum in the non-oil sector driven primarily by

private sector growth. Supporting this outlook is the most recent government data that shows the contribution of private sector activity to real GDP increased 2.8 percent YoY in Q2 of 2019. The private sector now accounts for 40.7 percent of GDP compared to 39.6 percent in the same period last year. In Q2 of 2019, 71 percent of non-oil sector GDP came from private sector growth. Real non-oil GDP climbed to 2.9 percent during H1 2019, fueling a positive outlook for the Kingdom's private business climate. Furthermore, the recently released IHS Markit Saudi Arabia PMI indicated the Kingdom's business conditions improved at the fastest pace since August 2015 as the index reached 57.8 points in October. The increase was largely attributed to the steep and accelerated increase in new business.

The WEF ranking for 'Macroeconomic Stability' considers inflation and debt dynamics where an annual percentage change in the consumer price index between 0.5 and 4 percent is considered stable inflation and debt dynamics measures the country's change in public debt weighted by its credit rating and debt-to-GDP ratio. Saudi Arabia received the top rating from the WEF for the second consecutive year on the back of sound macroeconomic fundamentals. Saudi Arabia's debt-to-GDP ratio has increased from 1.6 percent in 2014 to 19.1 percent in 2018 as the Kingdom ventured into both local and international debt markets to finance its expenditures amid lowered oil revenues. While this is a significant increase, the Kingdom's debt-to-GDP ratio remains low compared to global benchmarks for emerging economies.

### Government Debt-to-GDP Ratio Among MENA Countries



Source: TradingEconomics

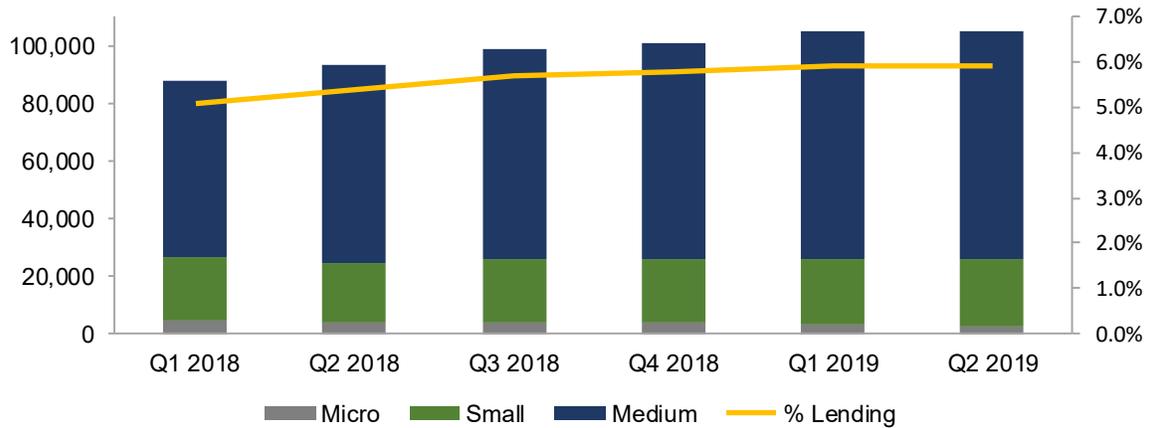
### Growth of New Businesses

'Starting a business' in Saudi Arabia, a key ranking in the World Bank report, jumped to 38th globally in 2019 from 141st the previous year due to substantial reductions in the minimum capital requirements to start a business as well as the relaxing and streamlining of business registration procedures. It now costs 5.4 percent of income per capita for an entrepreneur to start a new business according to the report. The continued rollout of Meras, the Ministry of Commerce's business registration platform, has allowed prospective business owners to obtain necessary licenses and investments, labor permits, and notarizations from multiple government agencies in a single online portal.

The WEF report raised Saudi Arabia's ranking in 'Financing of SMEs' to 19th globally in 2019 compared to 36th in 2018. The growth in credit to SMEs is likely a primary reason for the improved ranking. The

government's Financial Sector Development Program, which prioritizes improving the regulatory and financing ecosystem for micro, small, and medium enterprises (SMEs), has also supported the growth of private business. In Vision 2030, a 5 percent target of total bank credit to SMEs was set for the year 2020. At the close of 2018, bank lending to SMEs had reached 5.8 percent of total bank credit. In the first half of 2019, that figure increased to 5.9 percent of bank credit, well ahead of the 2020 target. Additionally, total bank lending to SMEs rose 12.4 percent YoY in Q2 of 2019.

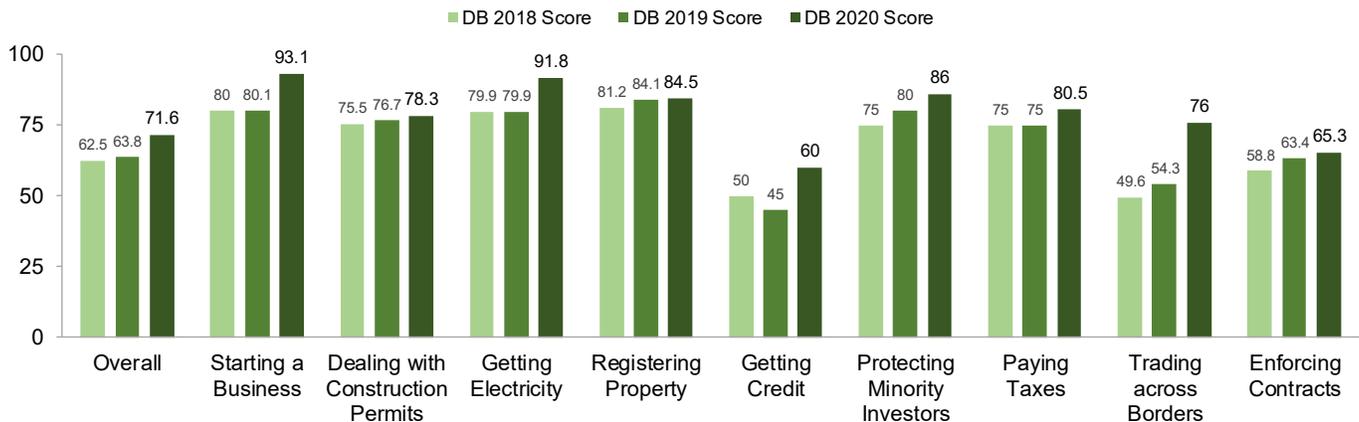
### Bank Lending to Micro, Small, and Medium Enterprises (SAR Million)



Source: SAMA

Access to electricity, another critical element of starting and expanding private business, was ranked 18th globally in 2019 compared to 64th the previous year due to the government streamlining connection and meter installation procedures and introducing a geographic information system for reviewing connectivity requests. According to the USSABC's Construction Contract Awards Index, SAR17.3 billion (\$4.6 billion) in power contracts encompassing new substations, expansion of transmission lines, and the construction of power plants have been awarded since 2017. Through the first nine months of 2019, the Saudi Electricity Company (SEC) has approved SAR1.9 billion (\$513.3 million) in such power contracts.

### The World Bank's Doing Business Scores (2018-2020)

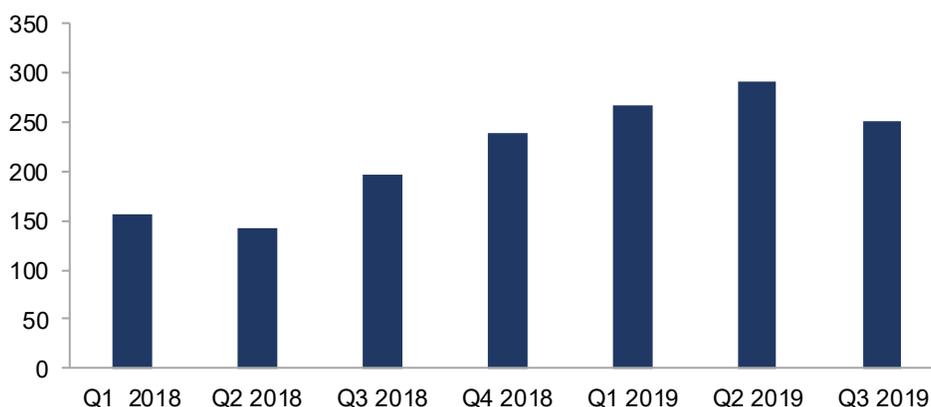


Source: The World Bank

## Increasing Foreign Investment

Another indicator of a growing appetite in the Kingdom's business landscape is the pace of foreign licensing, which picked up in 2019 with 809 foreign investor licenses granted in the first nine months of the year compared to 497 licenses over the same period in 2018. This marks a substantial 62.8 percent YoY increase. The sectors that comprised more than half of all issued licenses during that period were 'Information and Telecommunications', 'Construction', and 'Manufacturing'.

### Foreign Business Licenses



Source: SAGIA

The sustained positive trend in foreign business licensing is underpinned by key regulatory reforms aimed at attracting international investors. These reforms include an increase in the validity period of foreign investment licenses to five renewable years, introduction of digital licenses, a one-stop shop for business registration, an international loan program for foreign start-up companies, new laws protecting minority investors, and a new tenders and procurement law aimed at levelling competition between local and international contractors. Saudi Arabia's ranking in the WEF's 'Extent of market dominance' indicator, which measures the degree of corporate competitiveness, improved to 21st in 2019 compared to 29th in 2017. Its ranking in the growth of innovative companies rose sharply to 7th in 2019 compared to 21st in 2018.

### Foreign Direct Investment Inflows (SAR Million)



Source: SAGIA

Additionally, the Capital Market Authority aims to further boost foreign portfolio investments as it recently removed the 49 percent ownership cap for foreign strategic investors in Tadawul-listed companies in an effort to enhance the market's efficiency and attractiveness and to expand the institutional investments base. The Doing Business report ranked Saudi Arabia 3rd globally in 'Protection of minority ownership.' The WEF report similarly ranked Saudi Arabia 2nd globally in shareholder rights, a measure of governance safeguards against undue board control and entrenchment and corporate transparency.

Saudi Arabia has also continued to open full ownership access to wholesale and retail trade, education, healthcare, real estate services, and most recently the media sector. Foreign direct investment (FDI), which declined continuously after 2011, has shown a strong rebound since Q1 2018. In the first half of 2019, FDI grew 10.4 percent compared to the same period last year.

The Kingdom's diversification plans, which aim to lift the non-oil sector in line with global benchmarks are currently transitioning the economy away from strictly relying on oil revenues. Improved conditions for starting new businesses, the growth of bank credit to SMEs, and the expansion of foreign investment across numerous sectors are all promising signs that the Kingdom is progressing in its goals. Moreover, the introduction of key regulatory developments and laws such as Monsha'at, (helps remove administrative, regulatory, technical, and procedural obstacles facing SMEs) bankruptcy law, government tender and procurement law, new competition law, and the pending private sector participation law provide much needed transparency and controls to facilitate the growth of the private sector.

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