



Inflation update - December 2014

Inflation averaged 2.7 percent in 2014

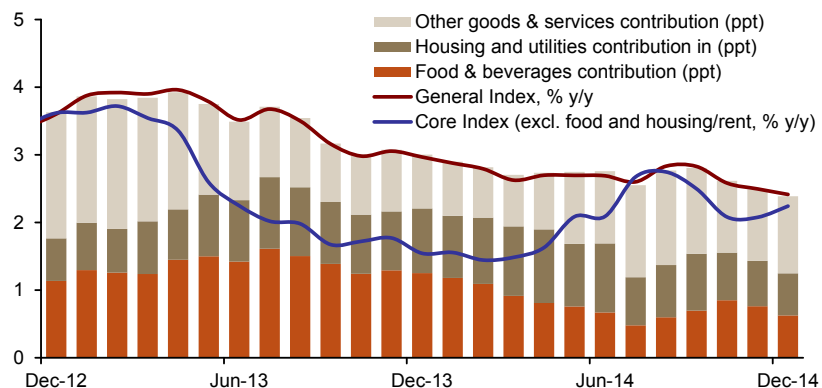
- Year-on-year CPI slowed in December for the fourth consecutive month to 2.4 percent, its lowest since October 2009.
- Overall inflation averaged 2.7 percent in 2014, down from 3.5 percent in 2013.

The Central Department of Statistics and Information (CDSI) has released Consumer Price Index data for December, showing a deceleration in prices to 2.4 percent year-on-year compared to 2.5 percent in November (Figure 1). This puts the annual inflation for last year at an average of 2.7 percent (Jadwa Investment: 2.8 percent). For 2015 we expect inflation to be mainly subdued, but still driven by rent and housing related services as well as food prices. Whilst the latter is expected to be less of a concern as international food prices continue to decline (Figure 2), housing inflation is to be the main source for upward pressure given the continued shortage in housing supply. As such, we expect average annual inflation in 2015 to reach 2.6 percent.

Taking the average for 2014, most components of the headline index recorded a slowdown compared to 2013 (Table 1). Foodstuffs slowed to an average of 3.3 percent, compared to 5.8 percent in 2013. Housing inflation slowed slightly from 3.5 percent in 2013 to 3.4 percent last year. Our estimate of core inflation, which excludes food and rent and other housing services, also slowed to 2.1 percent in 2014, down from 2.5 percent in 2013.

Five of the components in the core index recorded annual increases during 2014, while the other five recorded a slowdown (Table 1). Recreation and culture recorded the highest acceleration at 7.2 percent, up from 1.8 percent in 2013. Education, health, and furnishings also recorded slight increases. Transport, the largest

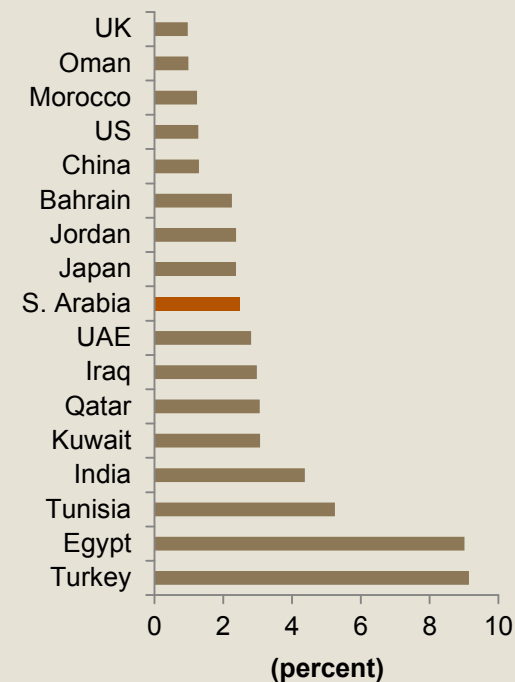
Figure 1: Foodstuffs and housing slowed in December



Saudi CPI inflation (percent)

	Monthly change	Annual change
December	0.1	2.4
November	0.2	2.5

Trading partner inflation rate (latest, year-on-year change)



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Transport, the largest component of the core index, recorded an annual contraction in prices of 0.5 percent.

Foodstuffs and housing slowed, year-on-year, for the third consecutive month, reaching 2.6 percent, and 2.5 percent respectively.

We expect that the rental segment will be the main source for inflationary pressure in 2015.

We expect inflation to be subdued throughout 2015...

...with external factor's contribution to inflation to remain weak.

We estimate an average annual inflation rate of 2.6 percent for 2015.

component of the core index, recorded an annual contraction in prices of 0.5 percent, compared to positive inflation of 2.5 percent in 2013. Communication was the only other component to record a decline in prices between 2013 and 2014.

Data for December shows that inflation for both foodstuffs and housing continued to slow, year-on-year, for the third consecutive month to reach 2.6 percent, and 2.5 percent respectively (Table 2 and Figure 3). The contribution from foodstuffs to overall inflation fell to 26 percent in December, equaling the contribution from housing inflation. Core inflation accelerated slightly to 2.2 percent year-on-year compared to 2.1 percent in November.

The slight fall in housing inflation came on the back of a slowdown in the rent segment. Rental inflation, which plays a major part in the housing inflation component, slowed to 3.2 percent year-on-year in December, down from 3.4 percent recorded in the previous month (Figure 4). We expect that the rental segment will remain the main source for inflationary pressure at least until government-led housing initiatives contribute to increased supply of affordable housing units, which should meet the strong demand for homes around the Kingdom.

We expect inflation to be subdued throughout 2015. External factors' contribution to inflation will remain weak, particularly given a strengthening USD and the weaker prospects of global economic growth. Domestic inflationary pressure will also be low relative to recent years given the cool down in the non-oil economy, although it would still be the main source of inflation during 2015. Foodstuffs and housing inflation -with the highest two weights in the CPI basket - are set to continue being the main sources for inflation. We maintain our view that the steady increase in the housing inflation rate should resume after a seasonal slowdown in recent months, with the increase being driven partially by a smaller base effect and partially by strong demand for housing units. The combination of these factors together with an expected continuation in the slowdown of the core index leads us to estimate an average annual inflation rate of 2.6 percent for 2015 (Figure 5).

Table 1: Annual change in inflation
(percent, period average)

	2009	2010	2011	2012	2013	2014
Food & beverages	2.4	3.8	5.2	4.5	5.8	3.3
Housing & related items	10.7	7.6	11.4	3.3	3.5	3.4
Tobacco	2.1	11.1	6.3	11.5	8.4	6.0
Clothing & footwear	0.6	-0.5	-1.4	3.6	1.4	0.7
Home furniture	2.3	1.3	7.9	1.8	4.3	4.5
Medical care	0.0	0.1	0.0	2.2	3.2	3.2
Transport	1.2	1.5	3.5	5.0	2.5	-0.5
Communication	0.1	-0.5	-5.8	0.1	1.7	-0.1
Recreation & culture	1.5	-2.0	7.7	-0.2	1.8	7.2
Education	1.4	1.3	-3.9	1.3	2.2	2.9
Restaurants & hotels	6.6	3.5	2.8	3.9	4.3	2.2
Other expenses & services	3.2	5.0	3.4	3.5	-0.2	2.1
Core inflation	1.9	1.3	2.0	2.8	2.5	2.1
General index	4.1	3.8	3.7	2.9	3.5	2.7



Table 2: Main highlights of Saudi CPI inflation

(percent)

	Weights	Month-on-month			Year-on-year			YTD
		Nov-14	Dec-14	Contribution, ppt.	Nov-14	Dec-14	Contribution, ppt.	
Food & beverages	21.7	0.2	-0.4	-0.1	3.1	2.6	0.6	2.6
Housing & related items	20.5	0.1	0.4	0.1	2.7	2.5	0.6	2.5
Tobacco	0.5	0.0	0.1	0.0	2.6	1.9	0.0	1.9
Clothing & footwear	8.4	1.2	0.5	0.0	1.7	1.9	0.1	1.9
Home furniture	9.1	0.6	0.1	0.0	3.5	3.2	0.3	3.2
Medical care	2.6	0.1	0.1	0.0	3.5	3.6	0.1	3.6
Transport	10.4	-0.2	0.5	0.0	1.1	1.5	0.1	1.5
Communication	8.1	0.1	-0.3	0.0	-1.1	-0.5	0.0	-0.5
Recreation & culture	3.5	0.5	0.2	0.0	8.6	9.0	0.3	9.0
Education	2.7	0.0	0.0	0.0	0.5	0.5	0.0	0.5
Restaurants & hotels	5.7	-0.3	0.4	0.0	1.0	1.2	0.1	1.2
Other expenses & services	6.8	-0.2	0.0	0.0	2.7	2.9	0.2	2.9
Core inflation*	57.8	0.2	0.2	0.1	2.1	2.2	1.1	2.2
General index	100.0	0.23	0.08	...	2.5	2.4	...	2.4

Note: *Core inflation excludes food and housing inflation and is Jadwa Investment's estimate.

Figure 2: International and Saudi food inflation
(year-on-year)

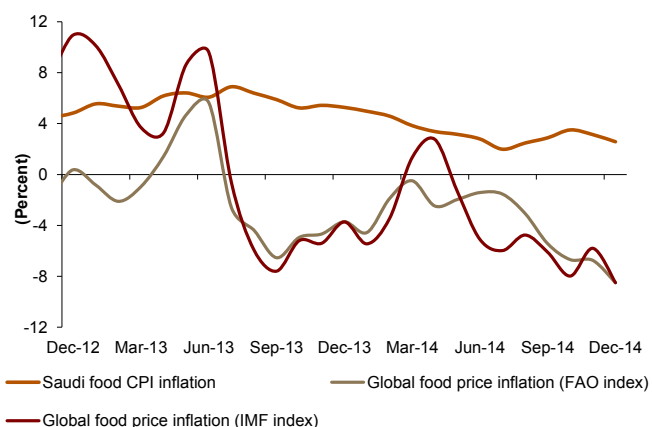


Figure 3: Food, rental, and headline inflation
(year-on-year)

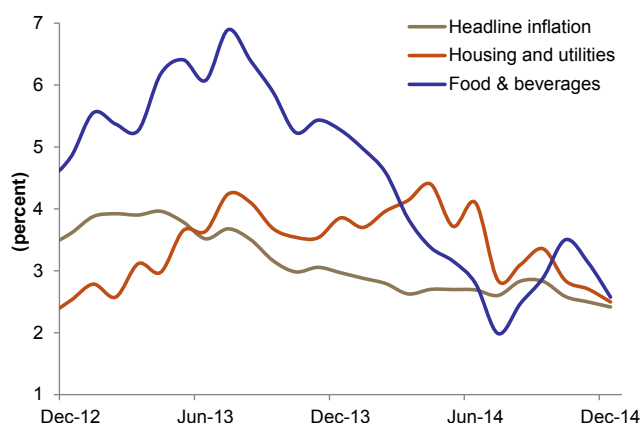


Figure 4: Rental inflation
(year-on-year)

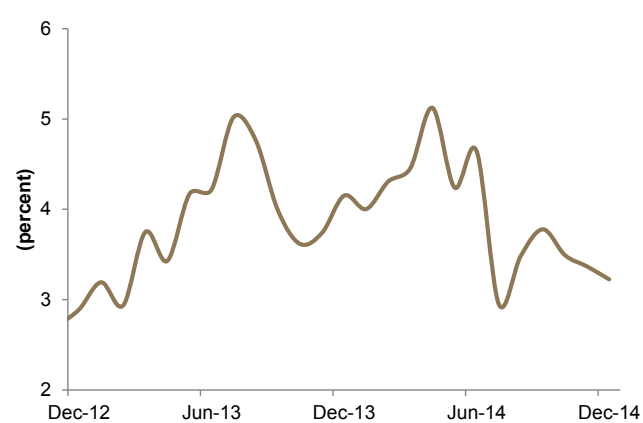
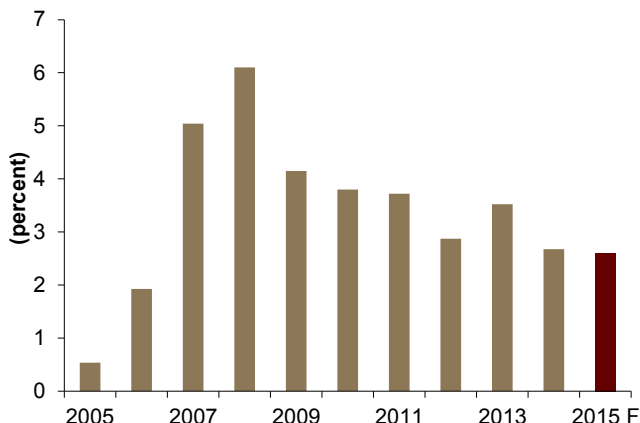


Figure 5 Inflation forecast
(year-on-year)



Sources: Central Department Of Statistics & Information, IMF, FAO, Reuters, Haver Analytics, Jadwa investment



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