جدوى للإستثمار
Jadwa Investment

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The Financial Sector Development Program

Delivery Plan 2020

- In April 2018, as part of the ongoing implementation and planning towards the Vision 2030, the Financial Sector Development Program (FSDP) was launched.

- In many ways, the FSDP is one of the most important Vision Realization Programs (VRPs), in that the success of the other 11 VRPs are wholly dependent on it. Ultimately, due to the scale of funding required for various projects and investments to be realized under the Vision, a fully developed, modern and inclusive financial sector is the only way in which the economic aspirations to increase the size of the Saudi economy threefold, by 2030, will be achieved.

- Accordingly, the FSDP charter seeks to develop a diversified and effective financial services sector, which supports the development of the national economy by stimulating savings, finance and investment.

- The FSDP details a number of measurable sector specific targets through to 2020, which lay the foundation of more far reaching 2030 aspirations.

- Overall, the key areas of focus are; opening up to FinTech players, SME growth, insurance industry expansion, development of debt & capital markets, moving towards a cashless society and raising the level of financial literacy to help improve household savings.

Table 1: Vision 2030 and the Financial Sector Development Program

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Introducing the FSDP

In April 2018, as part of the ongoing implementation and planning towards the Vision 2030, the Financial Sector Development Program (FSDP) was launched.

In April 2018, as part of the ongoing implementation and planning towards the Vision 2030 (Vision), the sixth, and arguably the most important, Vision Realization Program (VRP) was launched. The Financial Sector Development Program (FSDP) is crucial in that the success of the other 11 VRPs are wholly dependent on it (Figure 1). Ultimately, a fully developed, modern and inclusive financial sector is the only way in which the economic aspirations to increase the size of the Saudi economy threefold, by 2030, will be achieved, due to the scale of funding required for various projects and investments to be realized under the Vision. Accordingly, as the FSDP charter highlights, the program 'seeks to develop the financial sector as a diversified and effective financial services sector, which supports the development of the national economy by stimulating savings, finance and investment'.

The FSDP charter goes about setting definitive and measurable sector specific targets.

As with the other five VRPs launched to date, the FSDP charter goes about setting definitive and measurable sector specific targets. The charter also provides further details and clarity on the FSDP, and highlights the governance system driving the implementation of the program.

Overview of the FSDP

Three main pillars of the FSDP include;...

Back in May 2017, a document entitled *KSA Vision 2030, Strategic Objectives and Vision Realization Programs*, was published. The publication elaborated on three key themes under the Vision, namely; a vibrant society, a thriving economy and an ambitious nation. These themes were broken down in six overarching objectives, which were then split into 27 branch objectives, and further split into 96 strategic objectives. Three of 27 branch objectives also form the main pillars of the FSDP (Table 2). These are as follows;

...enabling financial institutions to support private sector growth...

Vision 2030 pillars

1) Enabling financial institutions to support private sector growth
2) Developing an advanced capital market
3) Promoting and enabling financial planning

...developing an advanced capital market...

Whilst these three pillars outline the overarching aims of the FSDP, the charter reveals five, more detailed, 2030 objectives, or 'aspirations';

...promoting and enabling financial planning

2030 aspirations

i) having a sector that is large enough to fund all Vision 2030 objectives. As such level of financial assets relative to gross domestic product (GDP), should be raised.
ii) offering a diverse set of products and services through traditional (mortgages/insurance) and newly emerging (FinTech) players.
iii) significant improvement toward inclusive structure through higher bank account penetration and SME/mortgage lending
iv) moving more towards a digitized economy which includes raising the level of non-cash transactions
v) maintain financial stability, through compliance with international standards

At the same time, the FSDP outlines more specific targets, or commitments, to 2020…

At the same time, based on above five aspirations, more specific targets, or commitments, are detailed for 2020;

2020 commitments

i) increasing the total size of financial assets to GDP from 192 percent in 2016 to 201 percent by 2020
ii) raising capital markets assets registered on the exchange from 41 percent in 2016 to 45 percent by 2020 as well as introducing at least three financial technology players into the market
iii) raising the share of SME financing from 2 to 5 percent by 2020 and share of mortgages financing from 7 to 16 percent by 2020
iv) increasing the share of non-cash transactions from 18 to 28 percent by 2020
v) maintaining financial stability, through compliance with international standards

2020 Commitment Metrics

...with a number of measurable sector specific targets for all five of the 2020 commitments.

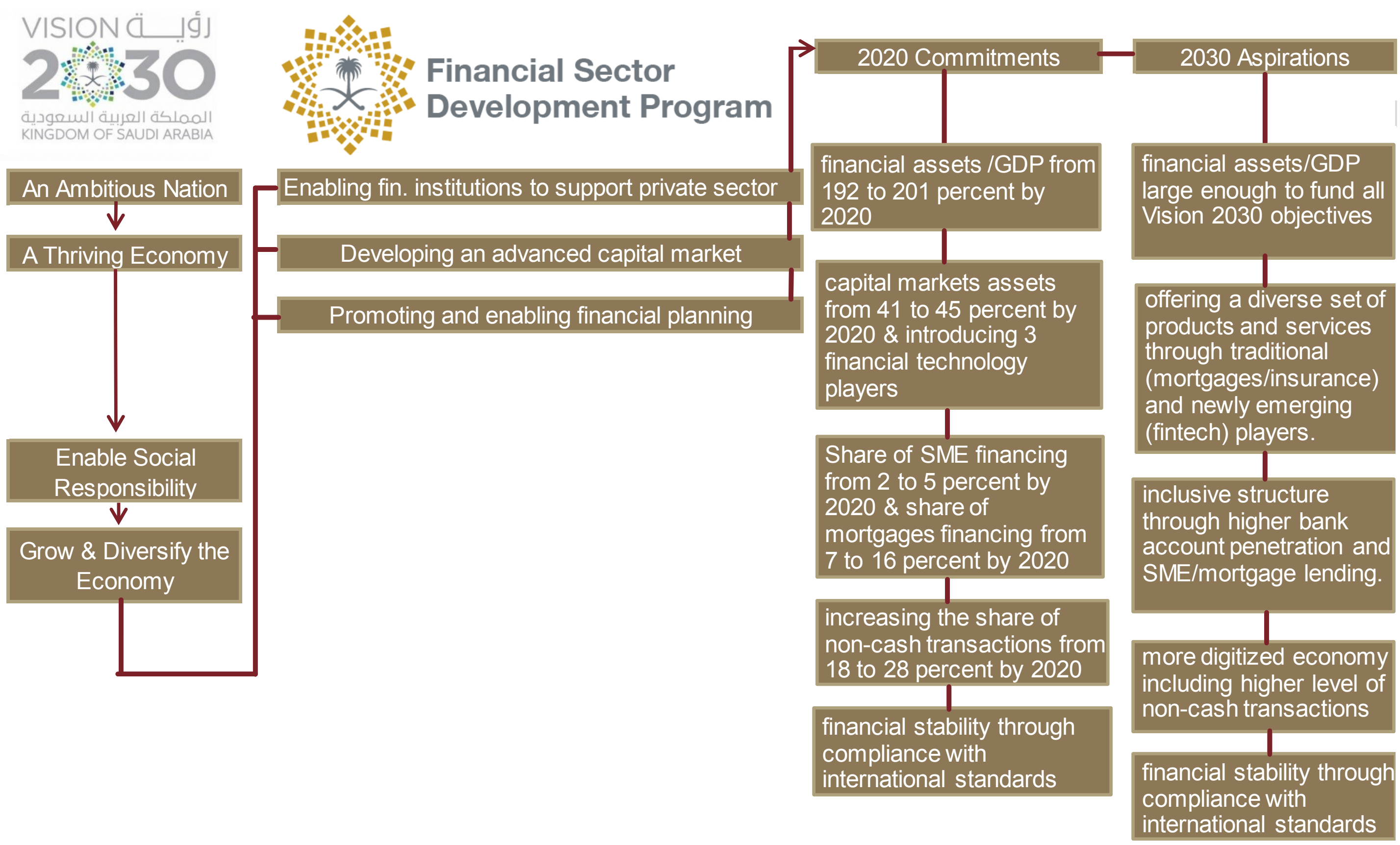
The FSDP charter details a number of measurable sector specific targets for all five of the 2020 commitments highlighted above. Placed under the corresponding 2030 pillar, the charter elaborates upon each commitment. Below we look at some of the key 2020 metrics in detail.

1) Enabling financial institutions to support private sector growth

Metric Name	2016	2018	2019	2020
Total GWP to non-oil GDP(%)	2.1	2.5	2.7	2.9

Total gross written premiums (GWP) to non-oil GDP:
The insurance sector has been afforded a fair amount of attention within the FSDP charter, with three 2020 commitments allocated to

Table 2: The FSDP's commitments and aspirations



The insurance sector has been afforded a fair amount of attention within the FSDP charter…

...with three 2020 commitments allocated to the sector.

The first of these relates to raising the level of gross written premiums (GWPs) (the amount of premiums customers are required to pay for insurance policies) compared to non-oil GDP.

the sector. The first of these relates to raising the level of gross written premiums (GWPs) (the amount of premiums customers are required to pay for insurance policies) compared to non-oil GDP. According to the Saudi Arabian Monetary Authority's (SAMA) Saudi Insurance Market Report 2017, GWPs totaled SR36.5 billion in 2017, resulting in GWP to non-oil GDP declining for the second consecutive year to 1.99 percent.

According to our calculations, GWPs will have to increase by SR1.56 billion between 2017-2020 in order for this metric to be attained (Figure 1). Whilst this seems a very achievable target, it comes at time when the sector is facing a number of challenges.

In 2017, motor and health insurance together represented around 82 percent of total GWPs, with the former representing 30 percent and the latter 52 percent. Whilst year-on-year growth was seen in health insurance GWPs, motor insurance GWPs saw a yearly decline. A combination of subdued overall economic growth as well as the introduction of expat dependency fees, which will have facilitated the repatriation of some foreigners, is likely to have pushed motor insurance GWPs down. Additionally, the rise in gasoline prices in both 2016 and 2018, may have encouraged the trading down of higher priced suburban utility vehicles (SUVs) to less expensive fuel efficient cars, which is also likely to have negatively affected GWPs. In fact, General Authority for Statistics (GaStat) data shows a near 25 percent year-on-year decline in both the value and number of passenger cars and jeeps imported during 2017, following a similar yearly decline in 2016 (Figure 2).

Looking ahead, insurance is likely to face more challenges in the year ahead as rises in both the expat dependency fees and expat levies lead to more expats leaving the Kingdom. Furthermore, the full effects of gasoline price hikes in 2018 are still to be felt, whilst the introduction of value added tax (VAT) will raise the purchase price of vehicles. That said, with females permitted to drive in the Kingdom, as of 24th June this year, this could help to increase GWPs. According to the latest population survey, there are 9 million females of driving age in the Kingdom. Whilst all these females will not choose to drive, and indeed the net-effect on GWPs will be mitigated by a decline in personal drivers/chauffeurs, this still offers a strong potential for growth in GWPs going forward.

Figure 1: GWPs will have to rise by a total of SR1.56 billion by 2020

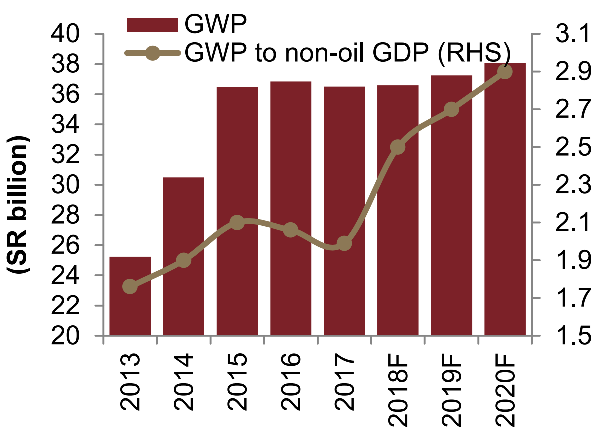
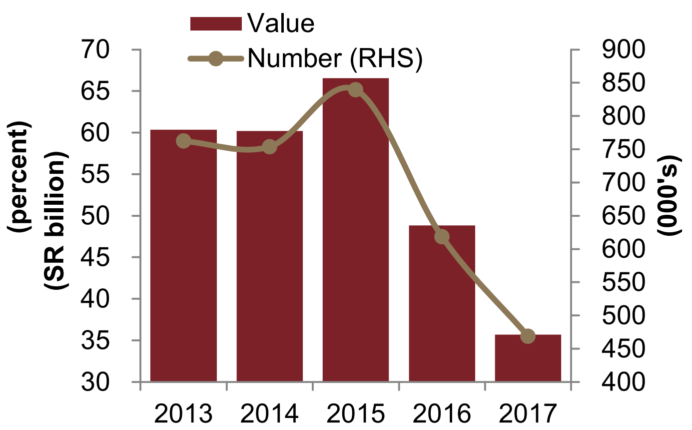


Figure 2: Number and value of imported passenger cars and jeeps



The FSDP charter highlights that there will be increased focus on…

Another way in which GWPs are likely to rise is through more rigorous enforcement of mandatory insurance (Box 1). According to one Saudi insurance service provider, around 55 percent of vehicles on the Kingdom's roads are not insured against accidents. The FSDP charter highlights that there will be increased focus on enforcement of mandatory motor insurance for all vehicles as well as mandatory health insurance. Whilst SAMA will be expected to lead the drive towards enforcement, the charter also highlights more closer cooperation between the Ministry of Health (MoH) and Ministry of Interior (MoI) in achieving this metric.

...enforcement of mandatory motor insurance for all vehicles as well as mandatory health insurance.

Box 1: Enforce Mandatory Insurance

In a separate section of the FSDP charter, eight 'game changers' are detailed, all of which focus on separate areas within the financial sector, one of which is the insurance sector. These 'game changers' describe what action will be taken in order to attain not only the 2020 commitments, but also the 2030 aspirations.

The insurance 'game changer' focuses on enforcing mandatory motor insurance for all vehicles, enforcing mandatory health insurance and eliminating fraudulent insurance policies. It also highlights the inclusion of insurance on government property and vehicles in addition to a new mandatory insurance stream. According to the charter, besides raising the number of written premiums, and thereby expanding the insurance sector, mandatory insurance is expected to drive down premium costs by improving the scale of insurers.

It also highlights that the inclusion of insurance on government property and vehicles in addition to a new mandatory insurance stream.

A minimum of three licensed FinTech players by 2020:

Metric Name	2016	2018	2019	2020
# of Fintech players	-	-	-	3

According to the International Monetary Fund (IMF), financial technology (FinTech) is defined as new technologies whose applications may affect financial services, artificial intelligence, big data, biometrics, and blockchain.

On a global level, in the last decade at least, there has been a rapid acceleration in a broad range of FinTech products and services.

On a global level, in the last decade at least, there has been a rapid acceleration in a broad range of FinTech products and services. This, in turn, has given rise to new technological applications which have simplified day-to-day financial processes such as making payments, saving, borrowing, managing risk and getting financial advice (Table 3). Concurrently, FinTech firms have attracted substantial investment in recent years. According to figures cited by the IMF, total global investment in FinTech companies increased from $9 billion in 2010 to over $25 billion in 2016. Venture capital (VC) investment has also risen steadily, from $0.8 billion in 2010 to $13.6 billion in 2016.

Despite the developments on a global level, the progress within the Saudi FinTech space has been limited to-date.

Despite the developments on a global level, the progress within the Saudi FinTech space has been limited to-date. As the FSDP charter highlights, Saudi Arabia is one of the only countries, amongst the leading FinTech countries, to disallow non-banking licenses for FinTech companies. That said, the FSDP has set out detailed guidelines to transform Saudi Arabia into a leading FinTech hub (Box 2). In fact, weeks prior to the unveiling of the FSDP, SAMA launched the FinTech Saudi initiative which lists many of the targets identified within the charter as its objectives. Moreover, moving forward, FinTech Saudi is expected to launch a number of workshops,

That said, the FSDP has set out detailed guidelines to transform Saudi Arabia into a leading FinTech hub.

educational and awareness activities to help spur innovation in the FinTech space.

Efforts will also be made to attract investment in this area…

Box 2: Opening Sector to New Types of Players

According to the charter, this game-changer will focus on opening financial services to non-banking players with the objective of promoting innovation and competition in the financial sector. It lists a number of actions that will be taken, including; establishing a Central Payments Unit at SAMA to regulate payments, creating and issuing new licenses to innovative non-banking players, including fast-tracking sandboxing (testing) of new products. Efforts will also be made to attract investment in this area, with an emphasis on developing FinTech focused funds/accelerators/incubators which provide VC funding, whilst ways to attract foreign direct investment into the sector will also be explored.

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One of key measurements outlined in this ‘game changer’ relates to a satisfaction index survey which will be rolled out in early 2019. The aim of the survey will be to gauge the view of potential entrants on the readiness of the FinTech ecosystem within the Kingdom. This will be done by assessing various factors, such as the regulatory environment and access to funding.

Saudi Arabia’s FinTech ambitions will also be supported by PIF…

...which has in the recent past demonstrated its willingness to invest in such ventures.

Saudi Arabia’s FinTech ambitions will also be supported by PIF, which has in the recent past demonstrated its willingness to invest in such ventures. Although the PIF’s more high-profile investments have been more internationally focused so far, such as its flagship investment into the Softbank Vision Fund, this is expected to change going forward. The PIF’s own Vision 2030 program, which was launched in the inaugural Future Investment Initiative (FII) in 2017, outlines the sovereign fund’s role in, amongst other things, developing the Kingdom’s technological expertise. Specifically, one of PIF Program’s objectives is to help develop digital banking ecosystems and support banks in their digital transformation plans in line with global trends and practices. With this in mind, the PIF is expected to be a key investor in FinTech, at both home and abroad.

Table 3: Major Technologies Transforming Financial Services

Technology		Financial Services				
Foundations	Innovations	Pay	Save	Borrow	Manage Risks	Get Advice
AI Big Data	Machine Learning Predictive Analytics		Investment advice (robots)			
				Credit decisions		
		Regtech, fraud detection				
			Asset trading			
Distributed Computing	Distributed Ledger (Blockchain)	Settle Payments				
		B2B				
		Back-office and recording				
		Digital currencies				
Cryptography	Smart contracts Biometrics	Automatic transactions				
		Security				
		Identity protection				
Mobile Access Internet	APIs Digital wallets	Easy to use digital wallets; Finance dashboards; P2P				
			Crowd-funding			
		Inter-operability and expandability				

Historically, with policy objectives in the Kingdom centered around building up larger companies that could compete internationally, the SME sector was overlooked.

According to the SMEA, bringing Saudi SMEs economic contribution in line with global peers could add a further SR1.1 trillion to GDP.

In the recent past, a number of SME related initiatives have been launched…

...the most notable has been the Kafalah Program…

…a Saudi Industrial Development Fund (SIDF) backed initiative to promote the participation of commercial banks in SME lending.

SME loans as a percentage of total bank loans

Metric Name	2016	2018	2019	2020
SME loans as a percentage of bank loans	2	2	3	5

SMEs play an essential role in building a competitive private sector and contributing significantly to employment and economic activity. In study conducted back in 2007, the World Bank found that SMEs accounted for more than 60 percent of manufacturing employment across 76 developed and developing economies.

Historically, with policy objectives in the Kingdom centered around building up larger companies that could compete internationally, the SME sector was overlooked. As a result, according to the Small & Medium Enterprises Authority (SMEA), SMEs contribution to the Kingdom's non-oil GDP is around 21 percent, which is lower than the average of 46 percent amongst the 15 largest global economies (Figure 3). This lower contribution to GDP is also mirrored in Saudi exports, with SMEs contributing 5 percent to total exports and 15 percent to total non-oil exports, again, lower than global peers. In terms of employment opportunities, whilst SMEs create over 50 percent of all jobs within the private sector, these jobs are mainly low value adding in nature and require cheap, and invariably imported labor.

According to the SMEA, bringing Saudi SMEs economic contribution in line with global peers could add a further SR1.1 trillion to GDP. The benefits of nurturing an environment where SMEs can grow is therefore quite obvious. Accordingly, the National Transformation Plan (NTP) has pinpointed three strategic areas through which SMEs can help the Saudi economy. These include (1) increasing the culture of entrepreneurship (2) raising the contribution of SMEs to the GDP and (3) contributing to the creation of employment opportunities.

In the recent past, a number of SME related initiatives have been launched. The most notable has been the Kafalah Program, a Saudi Industrial Development Fund (SIDF) backed initiative to promote the participation of commercial banks in SME lending. Whilst the program has seen a decent level of success (Figure 4), ironically, its success highlights one of the main reasons for the lack of SME

Figure 3: SMEs contribution to Saudi non-oil GDP vs. global peers

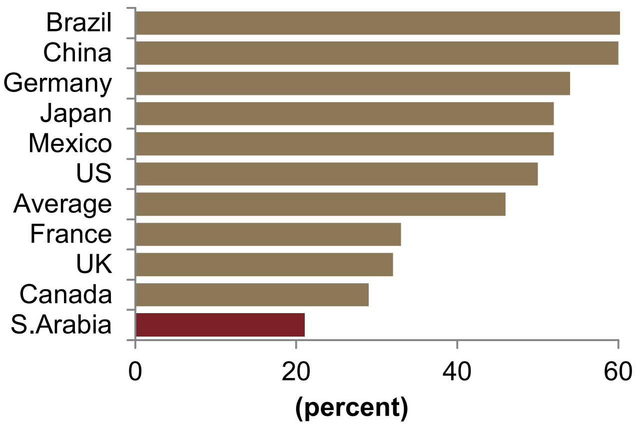
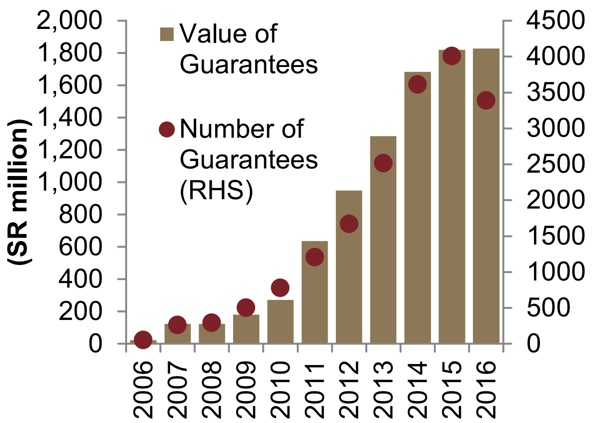


Figure 4: Number and value of SME guarantees under Khafalah program



Looking ahead, the FSDP highlights the need to establish an 'ecosystem' prior to incentivizing banks…

...part of this includes restructuring of Kafalah program...

...but it also stresses enabling the two Saudi credit bureaus, Bayan and SIMAH, in collecting and updating comprehensive SME data.

A recently launched initiative that aims to boost SME financing is the Musharakah program…

...this program can be seen as directly helping with FSDP metric related to raising the level of private equity and venture capital financing to SME funding.

financing by banks in the first instance. This is because the Kafalah program encourages financing of SMEs which cannot provide guarantees or financial records for themselves. As a 2010 joint report by the World Bank and Union of Arab Banks pointed out, a lack of SME transparency and the weak financial infrastructure (weak credit information, weak creditor rights and collateral infrastructure), was one of the main obstacles for further engagement in SME finance by banks. Seemingly with this in mind, the FSDP highlights the need to establish an 'ecosystem' prior to incentivizing banks. Whilst part of this includes restructuring of Kafalah program, it also stresses enabling the two Saudi credit bureaus, Bayan and SIMAH, in collecting and updating comprehensive SME data (Box 3).

Overall, whilst guarantee schemes, such the Kafalah have played an important role in providing finance to SMEs, the FSDP charter emphasizes that the strengthening of credit information systems and creditor rights will be the priority item going forward.

Box 3: Incentivize Financial Sector to Finance SMEs

Two specific initiatives are outlined to incentivize financial services providers to engage with SMEs in this 'game changer';

1) Improving the SMEs financing ecosystem through
- Strengthening the legal framework
- Restructuring the Kafalah program
- Government committing to allocate more contracts to SMEs
- Enabling Bayan and SIMAH to collect and update comprehensive SME data
- Establishing a local rating agency for SME credit assessment
- Providing alternative SME funding options (e.g. PE and VC)

2) Communicating lending targets to banks by 2020

<u>Value of SME Funding through Private Equity/Venture Capital</u>

Metric Name	2016	2018	2019	2020
Value SME Funding through Private Equity/Venture Capital (SR bn)	-	-	13	23

Another recently launched initiative that aims to boost SME financing is the Musharakah program. This program can be seen as directly helping with FSDP metric related to raising the level of private equity and venture capital financing to SME funding. The Musharakah program, which is part of a larger government-backed SR4 billion fund, aims to develop a system where the required types of capital for all stages of an SMEs lifecycle are made available on a Shariah compliant basis. The key attraction, from an investor's point of view, is that Musharakah will exactly match an investor's loan, with the investor retaining the profits on the whole (investor plus Musharakah) loan amount. The Musharakah program specifically aims to facilitate funding from venture capital, debt, mezzanine and private equity funds and therefore is hugely relevant in achieving this particular metric.

Raising the level of homeownership for citizens has been a long-standing priority within the Kingdom…

...but measures to tackle the comparatively lower ownership levels have accelerated in recent years.

Some recent measures have been introduced to target both new and existing mortgage holders in order to boost home ownership through home financing….

...including the licensing of a national home finance company called Bidaya.

Raising the level of outstanding real estate mortgages:

Metric Name	2016	2018	2019	2020
Outstanding real estate mortgages, SR bn	290	304	368	502

Raising the level of homeownership for citizens has been a long-standing priority within the Kingdom, but measures to tackle the comparatively lower ownership levels have accelerated in recent years. According to our calculations, Saudi Arabia's outstanding real estate mortgages relative to GDP stood at around 11 percent in 2016, compared to 74 percent in the UK, 69 percent in the US, 32 percent in Malaysia and 18 percent in China (Figure 5).

Some recent measures have been introduced to target both new and existing mortgage holders in order to boost home ownership through home financing. For example, in 2017, SAMA announced that existing mortgage holders would be exempt from administrative fees for switching between floating to fixed rates mortgage rates. SAMA also tried to make it easier for first time buyers by raising the loan-to-value ratio for home financing from 70 to 85 percent ,initially, and then to 90 percent, more recently.

Aside from making adjustments to existing mortgage products, a number of developments have taken place to raise the level of home financing options available in the Kingdom. For example, back in 2016, SAMA licensed a national home finance company called Bidaya, and introduced an affordable mortgage program in conjunction with the Ministry of Finance (MoF). More recently, towards the end of 2017, the PIF launched the Saudi Real Estate Refinance Company (SRC). Part of SRC's mandate is to raise the real estate market's contribution to the economy and increase the level of home ownership among Saudis to 52 percent by the end of 2020, from the current rate of 47 percent. Finally, the Ministry of Housing's Sakani program has also distributed 126 thousand mortgage products since its inception back in February 2017

Whilst only one major metric relating to mortgages is listed in the FSDP for 2020, the charter does refer to a Housing VRP, suggesting more elaborate and detailed targets.

Figure 5: Mortgage financing in Saudi Arabia and other countries as a percentage of GDP

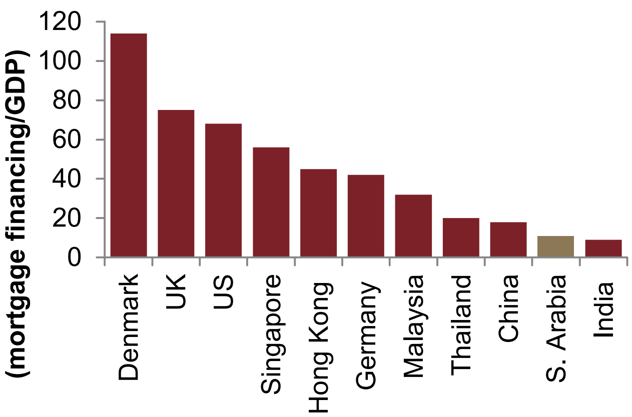
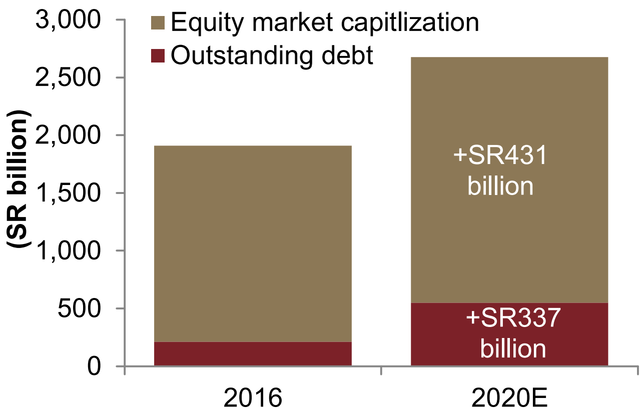


Figure 6: Total market capitalization of debt and equity expected to reach SR2.68 trillion by 2020



Other metrics:

Three other metrics make up the rest of the 'enabling financial institutions to support private sector growth' pillar.

Three other metrics make up the rest of the 'enabling financial institutions to support private sector growth' pillar. Although all three are distinct metrics, they can be seen as off-shoots of the metrics outlined above. Thus, **increasing life insurance GWPs from SR33 in 2016 to SR40 per capita,** forms a part of overall GWP to non-oil GDP target, as does the **increasing coverage ratios of health and motor insurance** from 38/45 percent to 45/75 percent. Lastly, raising the level of **non-cash transactions, from 18 to 28 percent by 2020** (Box 4)**,** can be partially achieved if the FinTech metric is realized.

Box 4: Drive Towards a Cashless Society

A number of initiatives are outlined in this 'game changer' which aim to reduce cash in circulation by 2030. Naturally, one of the key objectives relates to raising the number of point of sales (POS) terminals within the Kingdom, as well as expanding the number of SADAD billers.

Although all three are distinct metrics, they can be seen as off-shoots of the metrics outlined above.

According to the FSDP, the cash cost to the Saudi economy is equivalent to 1.3 percent of non-oil GDP, or SR18.8 billion in 2017. Therefore, reducing cash in circulation will lower costs to the economy as a whole. This is because less cash will mean lower infrastructure costs related to cash circulation, but also lower incidences of fraud and VAT avoidance.

2) Developing an advanced capital market

Developing an advanced capital market' makes up the second pillar on the FSDP, with eight separate metrics outline for 2020.

'Developing an advanced capital market' makes up the second pillar on the FSDP, with eight separate metrics outline for 2020. As the charter highlights, a large number of the metrics are also covered under the Saudi Capital Market Authority's (CMA) own Financial Leadership Program to 2020. Whilst the CMA's program is more qualitative in nature, the FSDP outlines a number of measurable targets to 2020.

Increasing total market capitalization to GDP:

Metric Name	2016	2018	2019	2020
Total market capitalization (equity & debt), percent of GDP	78	>=81	>=83	>=85

Two key strategies are outlined to achieve the above metric;

Two key strategies are outlined to achieve the above metric; firstly, by increasing the market capitalization of the Saudi stock exchange and, secondly, encouraging growth within existing debt capital markets. The FSDP states that debt and equity capital market assets combined totaled SR1.9 trillion, or 78 percent of GDP, back in 2016. Of this, around SR213 billion, or 9 percent of GDP, related to outstanding bond and sukuks, leaving SR1.7 trillion in equity market capitalization. The FSDP also states that by 2020 total capitalization should reach SR2.68 trillion, with SR550 billion of this being outstanding debt. As a result, by 2020, the FSDP implies that equity market capitalization should reach SR2.1 trillion, a growth of 25 percent, or SR431 billion, over 2016's total (Figure 6). The charter envisages part of the growth in equity capital market capitalization will be driven by initial public offerings (IPOs) through both the government's privatization program and private sector listings (although Saudi Aramco's capitalization is excluded within the metric calculation) (Box 5).

firstly, by increasing the market capitalization of the Saudi stock exchange…

...and, secondly, encouraging growth within existing debt capital markets.

The charter envisages part of the growth in equity capital market capitalization will be driven by initial public offerings (IPOs)…

…through both the government's privatization program and private sector listings.

At the same time, the program will seek to further deepen the debt capital markets in Saudi Arabia…

...in order to provide an alternative funding away from banking and equity…

...with SAMA, MoF and private banks are currently considering changes that would enhance marketability of government debt.

Box 5: Privatize State-Owned Entities Through IPOs

The Privatization Program, published just prior to the FSDP, gives an insight into how government's privatization program will contribute to reaching this metric (this also forms one of the 'game changers' highlighted in the charter). The Privatization Program specifies five current government-owned assets to be privatized come 2020, although the transfer of ownership will be done in several forms, including full or partial assets sale, management buy-outs, public-private partnerships (PPP), concessions/outsourcing and IPOs. The five assets to be partially privatized will be the Saline Water Conversion Corporation (SWCC), four flour mills, Saudi sports clubs, the Saudi Post services (which could include a PPP) and a number of transport projects (also potentially a PPP).

To govern the privatization process, the Kingdom has established the National Center for Privatization (NCP) and Supervisory Committees. The NCP's role is to develop the framework that will enable and manage privatization, whilst the committees is expected to provide technical, financial and legal framework for privatization *(for more on this please see our Privatization and Vision 2030 report published June 2018)*.

At the same time, the program will seek to further deepen the debt capital markets in Saudi Arabia in order to provide an alternative funding away from banking and equity (Box 6). Accordingly, the charter outlines that by 2020, SR550 billion of debt is expected to be registered on the Saudi stock exchange, representing an increase of SR337 billion compared to 2016. Whilst some of this will come from private debt, a large portion is expected to come from government debt.

Back in April 2018, Tadawul began trading local currency government bonds, with around SR204 billion in Saudi government debt instruments being listed. This is seen as an initial step in developing deeper capital markets with the ultimate goal being the application of market-oriented practices to the domestic debt market. In this context, SAMA, MoF and private banks are currently considering changes that would enhance marketability of government debt. This is likely to include the introduction of primary dealers as well as a switch to an auction system for tradable debt rather than over the counter (OTC) system. In fact, in March 2018, SAMA successfully completed the development of a SAMA bills and Murabahas issuance system using Bloomberg's Auction System, and we see this system likely being extended to government debt in the near future.

Box 6: Deepen Debt Capital Markets

This game-changer focuses on deepening the debt capital markets to 2030 and consists of:

- Improvement of offering rules
- Issuances of Special Purpose Vehicle regulations
- Addressing of related Zakat and withholding tax obligations and calculations
- Reducing of single obligor limits (maximum amount a bank is allowed to lend a single borrower).
- Investigating enhancements to current Private Placement model

In addition to government debt, the charter expects debt from the SRC to be listed on the exchange too…

As mentioned above, around SR204 billion of riyal denominated government debt is listed on Tadawul, but this is likely to increase in the next few years. According to the Fiscal Balance Program (FBP) total government debt is expected to rise to SR749 billion in 2020, compared to SR533 billion at the end of May 2018 (Figure 7). Around 55 percent of total current public debt is locally issued, and assuming this remains the case to 2020, another SR108 billion of additional debt could be listed onto the exchange by the end of the decade.

...especially since one of main purposes of the SRC is to act as a financial intermediary to acquire, aggregate and package portfolios into mortgage-backed securities.

In addition to government debt, the charter expects debt from the SRC to be listed on the exchange too. One of main purposes of the SRC is to act as a financial intermediary to acquire, aggregate and package portfolios into mortgage-backed securities. In doing this, the SRC will aim to free up liquidity in the Kingdom's mortgage market to promote home ownership. So far, the SRC has acquired mortgage portfolios of two Saudi-based companies, and is expected to refinance up to SR75 billion worth of mortgage debt over the next five years.

Raising institutional investors share of value traded:

Metric Name	2016	2018	2019	2020
Institutional investors' share of value traded (%)	18	>=19	>=19	>=20

The Saudi stock exchange's trading activity is dominated by local retail investors…

The Saudi stock exchange's trading activity is dominated by local retail investors. According to the CMA, at the end of 2017 there were around 4.6 million retail investors, compared to 5,500 institutional investors. Currently, retail investors in Saudi Arabia account for a higher proportion of value traded, at around 85 percent of the total, marginally higher than China, much higher than India, where retail trade volumes account for around 34 percent, and very far off the US, where retail investors account for less than 2 percent (Figure 8).

...with retail investors, in general, tend to have larger risk appetites and shorter investment horizons compared to their institutional counterparts.

Retail investors, in general, tend to have larger risk appetites and shorter investment horizons compared to their institutional counterparts. In the Saudi Stock Exchange, retail investors look to make shorter term profits by focusing on smaller sectors in the stock market, which are more susceptible to price movements, and, by doing so, add volatility within these sectors. A prime example of this can be seen in the trading patterns of the Media sector, one of the

Figure 7: Total government debt expected to reach SR749 billion by 2020

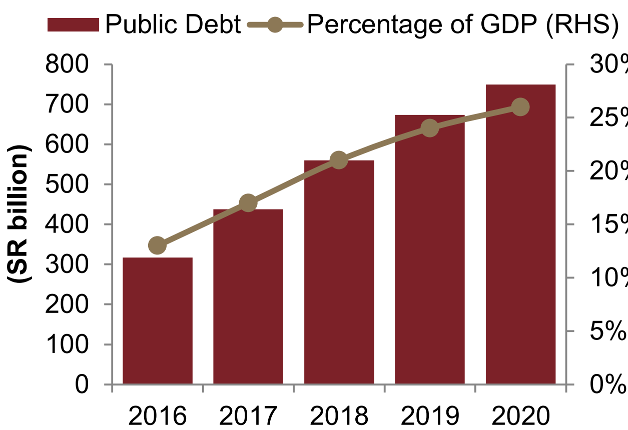
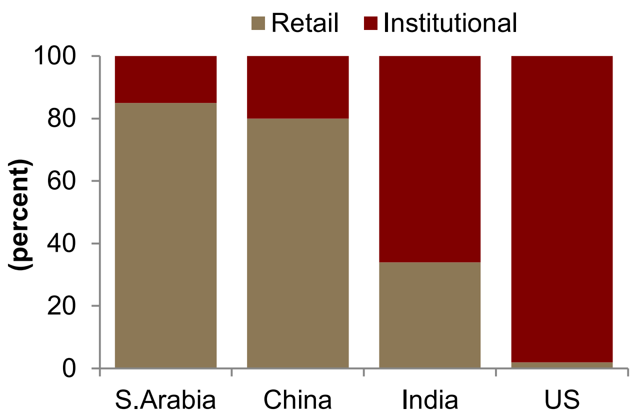


Figure 8: Traded value by retail and institutional investors



Institutional investors, on the other hand, play an important role in developing financial markets…

...since they act as conduit to channel individual savings into capital markets through longer term investment horizons.

This is one reason why raising the level of institutional investment also makes up a key strategic objective within the CMAs Financial Leadership Program.

In recent years, the CMA has been actively trying to open up capital market to foreign investors.

smallest sectors by market capitalization. During the course of 2017, the Media sector was in either the top three worst or best performing sectors in nine out of the twelve months of the year, quite often oscillating between sizable losses and gains. At one point in July 2017, the Media sector rose by 107 percent during the month for no discernible reason (Figure 9).

Institutional investors, on the other hand, play an important role in developing financial markets since they act as conduit to channel individual savings into capital markets through longer term investment horizons. This is one reason why raising the level of institutional investment also makes up a key strategic objective within the CMAs Financial Leadership Program. Whilst the program emphasizes that stable, efficient and transparent markets are more difficult to achieve with the prevalence of retail investors, it also outlines how the CMA aims to promote institutional investment going forward. Thus, whilst encouraging inexperienced individuals to invest in investment funds is a key objective, diversifying distribution channels for investment funds and facilitating the establishment and development of endowment funds is also earmarked to help raise the level of institutional involvement.

Raise the level of foreign investor ownership within equity markets

Metric Name	2016	2018	2019	2020
Foreign Investor ownership of the equity market cap (%)	4	>=5	>=10	>=15

In recent years, the CMA has been actively trying to open up capital market to foreign investors. Since allowing qualified foreign investors (QFIs) to trade directly in Tadawul back in mid-2015, the CMA has progressively loosened the rules. In the most recent development, earlier this year, the CMA reduced the minimum requirement for assets under management of QFIs for buying publicly-traded companies, to US$500 million from $1 billion previously. Further, the CMA streamlined the registration process for QFIs with itself, and updated the Independent Custody Model (ICM) to enhance QFIs access to the market.

In the first quarter of 2018, net purchases of SWAPs and buying by QFIs totaled SR7.9 billion. In fact, March saw the largest ever net inflow of combined SWAPs and QFI purchases, at SR3.8 billion

Figure 9: Monthly performance of TASI Media index during 2017

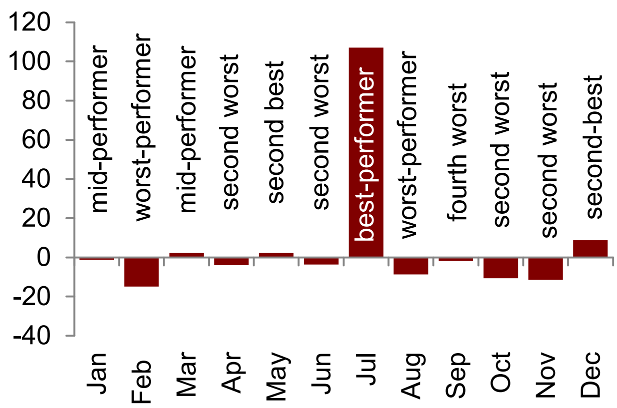
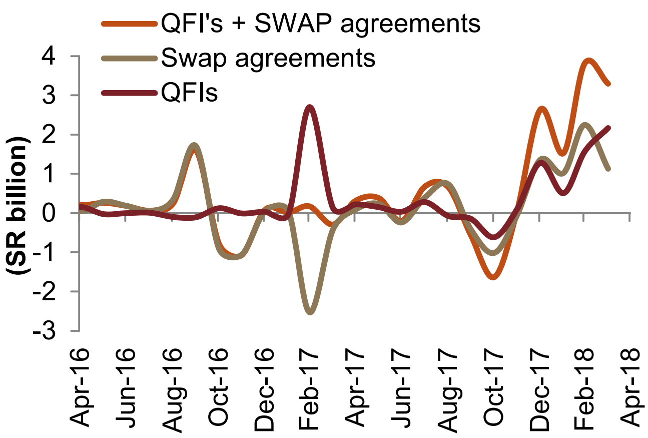


Figure 10: Net purchases of SWAPs and QFIs



The Financial Leadership Program provides more detail on how the CMA intends to increase market attractiveness in general for foreign investors…

…with some of the objectives listed within the program having already been implemented.

Back in Feburary 2017, the CMA officially launched a parallel market (Nomu) in the Kingdom…

...and we see this as being the driving force behind this particular metric being achieved.

Looking at the Musharakah program (see above) and Nomu together…

...we can see the strategic thinking behind government policy in trying to develop a path for SMEs that allows them to progress from a small scale start-up to a listed entity.

(Figure 10). Looking ahead, we expect inflows from QFIs and SWAPs seen so far in 2018 to continue, precipitated by Saudi Arabia's recent inclusion into the MSCI Emerging Market index.

The Financial Leadership Program provides more detail on how the CMA intends to increase market attractiveness in general for foreign investor, with some of the objectives listed within the program having already been implemented. This includes the introduction of a new operating model in April 2017, which included the introduction of a T+2 settlement system (for more on this please see our [Recent CMA announcements related to Tadawul] report published May 2016). Additionally, International Financial Reporting Standards (IFRS) for listed companies has also been adopted. Other efforts to raise QFI attractiveness are likely to continue; including the objective related to increasing compliance with the Standards of the International Organization of Securities Commissions (IOSCO) as well as fostering organizational convergence with regional capital markets.

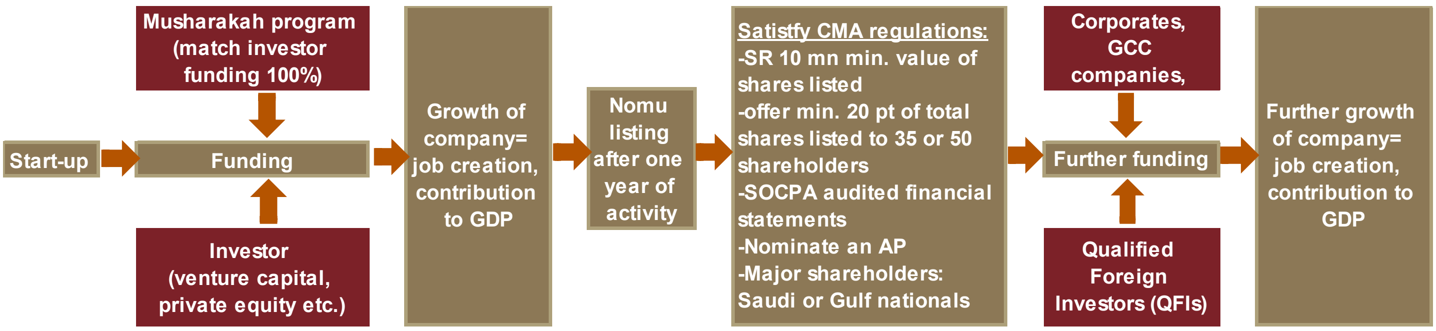
Raising the number of listed micro/small companies

Metric Name	2016	2018	2019	2020
Number of micro/small companies listed as percentage of total listed companies	34	>=36	>=39	>=40

Back in Feburary 2017, the CMA officially launched a parallel market (Nomu) in the Kingdom and we see this as being the driving force behind this particular metric being achieved. Whilst Saudi Arabia is the first country in the Gulf region to launch a parallel market, such markets have existed since the 1970's in many mature economies. Perhaps the best example of a parallel market is the US NASDAQ, which was set-up in the early 1970's. During the mid to late 1990's, many European exchanges also went about launching their own versions of a parallel market, including AIM (UK), Neuer Markt (Germany) and the Nouveau Marché (France).

By in large, global parallel markets have been a relative success, helping spawn a number of prosperous companies, which have ultimately sought full listing in the main market. In the same way, Nomu presents the possibility for companies to transition into the main market. Specifically, as Nomu listed companies increase in size, a move to the main market could result in an accompanying increase in its profile as well as increased equity analyst coverage, both of which may help ensure higher demand for the company's securities. Looking at the Musharakah program (see above) and Nomu together, we can see the strategic thinking behind government policy in trying to develop a path for SMEs that allows them to progress from a small scale start-up to a listed entity (Table 4) (*for more on this please see our report [The Saudi Parallel Market (Nomu)] published March 2017*).

Table 4. The path of an SME from start-up to Nomu listing



Four other metrics make up the rest of the 'developing an advanced capital market' pillar…

Other metrics:

Four other metrics make up the rest of the 'developing an advanced capital market' pillar. Again, although all these metrics are distinct, their achievement can be seen as feeding off the above identified metrics. In particular, raising the level of **assets under management from 18 to 22 percent of GDP** could be facilitated by raising the level of market capitalization and raising the level of institutional investors' value traded. Similarly, this could also be applied to the metric related to keeping **market free float equity market capitalization above 45 percent of total market capitalization.** Also, **reducing the level of market concentration of the top 10 companies by market capitalization from 57 to 55 percent**, could be achieved by increasing the number of SMEs listings and through the government's privatization program. Lastly, **raising the share of investment accounts opened through eKYC,** will be helped by the promotion of FinTech companies.

...again, although all these metrics are distinct, their achievement can be seen as feeding off the above identified metrics.

3) Promoting and enabling financial planning

'Promoting and enabling financial planning' is the third and last pillar on the FSDP, with the metrics under this pillar being narrower (in that they all specifically focus on raising the level of savings), making the level of interdependence between them more apparent (Table 5). Most of these metrics are linked to a yet to be published National Savings Strategy, which is expected to outline how financial planning will be promoted and enabled throughout the Kingdom (Box 7).

'Promoting and enabling financial planning' is the third and last pillar on the FSDP…

…with most of these metrics are linked to a yet to be published National Savings Strategy…

Table 5 Metrics Under the Promoting and Enabling Financial Planning Pillar

Metric Name	2016	2018	2019	2020
Total amount held in savings products (SR bn)	315	345	367	400
Number of available types of savings products	4	4	5	9
Percantage of household saving on a regular basis	19	19	25	29
Share of accounts opened through eKYC, (%)	-	2	5	10
Household savings ratio (percentage of disposable income)	6.2	6.4	70	7.5

...which is expected to outline how financial planning will be promoted and enabled throughout the Kingdom

As the charter highlights, the level of Saudi household savings is very low, at around 2.4 percent of annual disposable income compared to a global average of 10 percent (Figure 11). This low level of savings seems to be a result of both supply and demand side factors. On the supply-side, as the charter highlights, there seems to be limited appetite from the private sector (especially banks) to promote interest-bearing savings. In fact, the FSDP plan shows that two of the largest retail banks, with a combined market share of 51 percent, currently offer no savings products at all.

As the charter highlights, the level of Saudi household savings is very low…

Part of the reluctance in offering such products may be related to the fact that a major component of bank liabilities are demand deposits, on which no interest is paid, which enables banks to keep their cost of funding low (Figure 12). That said, on the demand side, some Saudi household's aversion to non-sharia compliant interest bearing

...at around 2.4 percent of annual disposable income compared to a global average of 10 percent

...with this low level of savings seems to be a result of both supply and demand side factors.

accounts may explain also why demand deposits are more heavily used compared to time and savings deposits. Another demand side factor inhibiting the level of savings is perhaps a consequence of lower level of financial literacy within the Kingdom. According to the World Bank, Saudi Arabia exhibits some of the lowest levels of financial literacy in comparison to similar countries, with around 30 percent of adults considered financially literate.

Two separate 'game-changers' outline how the level of savings will be raised in the Kingdom.

The first of these relates to the establishment of a National Savings Entity (NSE)…

...and the second 'game-changer' focuses on the establishment of a Financial Literacy Entity (FLE).

Box 7: National Savings & Financial Literacy Entities

Two separate 'game-changers' outline how the level of savings will be raised in the Kingdom. The first of these relates to the establishment of a National Savings Entity (NSE). This is expected to be a stand-alone, government-backed retail savings scheme with the objective of encouraging private savings in the Kingdom. It will consist of:

- Designing and developing a portfolio of tailored retail savings schemes (e.g., retail savings, Sukuks) to be distributed via direct channels and via banks.
- MoF savings schemes or approved savings schemes backed by MoF guarantees.
- Enabling retail customers to save in government guaranteed products indirectly.

The second 'game-changer' focuses on the establishment of a Financial Literacy Entity (FLE), also a stand-alone government entity, with the objective of improving financial literacy and awareness. It will consist of:

- Coordinating and driving financial education across Saudi Arabia and all entities involved in financial education
- Developing financial literacy content
- Creating an entity funded by a levy charged on the financial services industry

Overall, it seems a broad initiative to support the growth of private savings will be done through incentivizing consumers to save, encouraging banks to introduce new savings products, and helping citizens improve their level of financial education.

Figure 11: Comparable household saving rates
(percent of household disposable income, 2014)

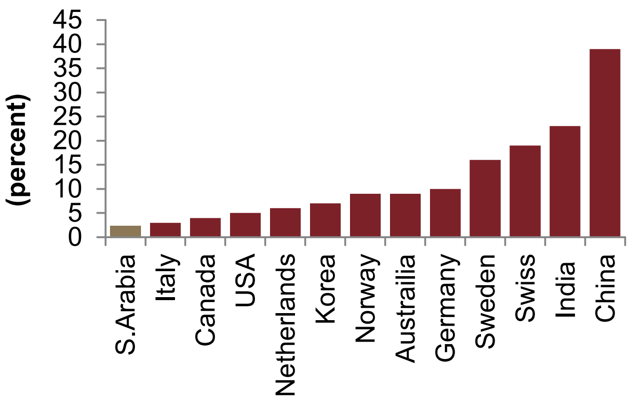
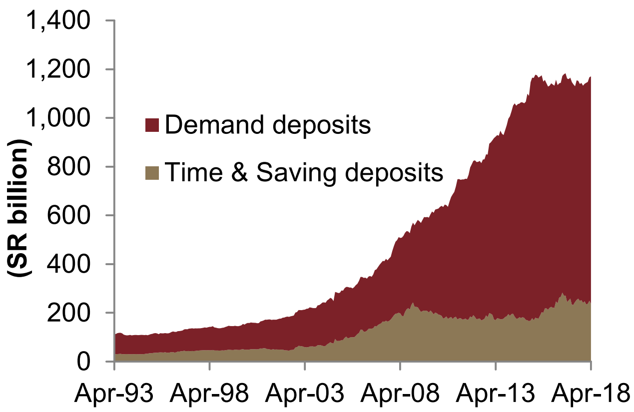


Figure 12: Majority of banks liabilities are non-interest bearing demand deposits



The 2020 commitments outlined above provide the foundation on which the FSDP's Vision 2030 aspirations are built upon.

Whilst the charter outlines how each aspiration will be achieved…

...through providing a holistic overview of the program's execution strategy…

...the aspirations are detailed through a number of initiatives.

Vision 2030 Aspirations

The 2020 commitments outlined above provide the foundation on which the FSDP's Vision 2030 aspirations are built upon. Whilst the charter outlines how each aspiration will be achieved, through providing a holistic overview of the program's execution strategy, the aspirations are detailed through a number of initiatives (Table 6). Below we highlight the main strategy under each Vision 2030 objective:

<u>Enable financial institutions to support private sector growth</u>

⇒ <u>Enhancing depth and breadth of financial services and products offered</u>
- Opening the sector to FinTech players, removing obstacles that hinder growth of finance companies, unlocking finance for SMEs, and increasing mortgage penetration.

⇒ <u>Building an innovative financial infrastructure</u>
- Implementation of the Integrated Digital Payment Strategy to move toward a cashless society, digitizing KYC and end-to-end digital processing at banks.

⇒ <u>Managing risks through a thriving insurance sector</u>
- Enhancing the existing regulatory environment to drive consolidation and strengthening balance sheets.

⇒ <u>Enhancing capabilities of the talent force</u>
- Enhancing the professional and technical capabilities of existing talent by establishing a Financial Sector Academy.

<u>Ensure the formation of an advanced capital market</u>

⇒ <u>Facilitating raising capital by government and private sector</u>
- Deepening liquidity of the equity and debt capital markets and further diversifying alternative sources of available funding.

Table 6. The FSDP Vision 2030 Strategic Pillars

Pillar	Target
Enable financial institutions to support private sector growth	Enhancing depth and breadth of financial services and products offered
	Building an innovative financial infrastructure
	Managing risks through a thriving insurance sector
	Enhancing capabilities of the talent force
Ensure the formation of an advanced capital market	Facilitating raising capital by government and private sector
	Offering an efficient platform to encourage investment and diversify investor base.
	Providing a safe and transparent infrastructure (maintaining financial markets stability)
	Enhancing market participants capacity and sophistication
Promote and enable financial planning	Stimulate and bolster sustainable demand for savings schemes
	Drive expansion of savings products and channels available in the market
	Improve and strengthen savings ecosystem
	Enhance financial literacy

Ultimately, due to the scale of funding required for various projects and investments to be realized under the Vision…

...a fully developed, modern and inclusive financial sector is the only way in which the economic aspirations to increase the size of the Saudi economy threefold, by 2030, will be achieved.

Accordingly, as the FSDP charter highlights, the program 'seeks to develop the financial sector as a diversified and effective financial services sector…

...which supports the development of the national economy by stimulating savings, finance and investment'.

⇒ Offering an efficient platform to encourage investment and diversify the investor base
- Developing investment and trading strategies through the introduction of derivatives.
- Establishing co-trading linkages with selected developed markets to provide remote access to Saudi markets to attract foreign liquidity.

⇒ Providing a safe and transparent infrastructure
- Strengthening cyber security to secure the stability and safety of the infrastructure.
- Upgrade post-trade and risk management model.

⇒ Enhancing market participants capacity and sophistication
- Establishing a regulatory entity to supervise the audit offices of listed companies to ensure compliance with highest standards of disclosures and transparency.
- To promote and enable financial planning as part of the National Savings Strategy.

Promote and enable financial planning

⇒ Stimulate and bolster sustainable demand for savings schemes
- The establishment of a National Savings Entity which distributes government-backed retail savings products (e.g., savings Sukuks)

⇒ Drive expansion of savings products and channels available in the market
- Tailoring products around key basic needs (e.g., home ownership, retirement, education)
- Encouraging the distribution of certain collective investment schemes through non-Associated Persons entities and simplifying access to banking savings products.

⇒ Improve and strengthen savings ecosystem
- Seek to introduce incentives for banks to attract long-term deposits.

⇒ Enhance financial literacy
- Encourage the establishment of a dedicated "Financial Literacy Entity"

Ultimately, due to the scale of funding required for various projects and investments to be realized under the Vision, a fully developed, modern and inclusive financial sector is the only way in which the economic aspirations to increase the size of the Saudi economy threefold, by 2030, will be achieved. Accordingly, as the FSDP charter highlights, the program 'seeks to develop the financial sector as a diversified and effective financial services sector, which supports the development of the national economy by stimulating savings, finance and investment'.

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