جدوى للإستثمار
Jadwa Investment

December 2019

# Saudi Arabia's 2020 Fiscal Budget

The government's budget for the 2020 fiscal year was endorsed by the Council of Ministers on 9th December and was in-line with the recently released preliminary budget:

- As outlined in the preliminary fiscal budget in November, budgeted government expenditure will total SR1020 billion in 2020. Based on revenues of SR833 billion, the government is budgeting for a higher year-on-year deficit at SR187 billion in 2020 (6.4 percent of GDP), compared to SR131 billion in 2019 (4.7 percent of GDP).

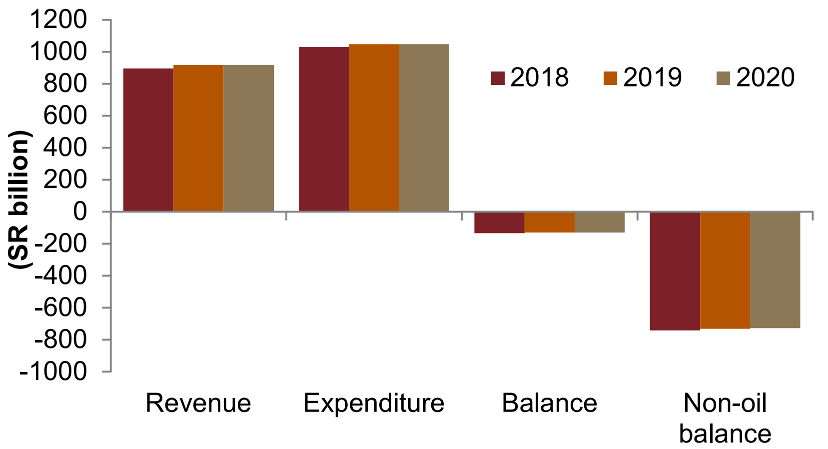
- A larger fiscal deficit is not expected to translate into higher levels of debt. According to the budget statement, total debt requirement for next year will be SR76 billion, which is expected to push up total debt to SR754 billion by end of 2020, equivalent to 26 percent of GDP, as per the budget statement.

- Looking at the budget from a sectorial level, 'education' is expected to make up the largest portion of budgeted expenditure, at 19 percent of the total. Meanwhile, a sizable reduction in 'military' expenditure is budgeted for the second consecutive year, and is expected to decline by 8 percent year-on-year in 2020. Overall only 'general items', which includes a number of different sub-items such as spending on government pensions, social insurance and financing costs, is expected to show yearly rises.

- According to the statement, budgeted capital spending will amount to SR173 billion in 2020, compared to SR172 billion in 2019. Whilst this is a nominal rise, as we have highlighted previously, the Public Investment Fund (PIF) and indeed the National Development Fund (NDF) are expected to take a leading role in investments within the Kingdom going forward.

- In line with this, once proceeds from Aramco's SR96-110 billion ($25.6-29.4 billion) IPO flow to the PIF, and indeed PIF's sale of its 70 percent stake in Sabic to Aramco, totaling SR259 billion ($69 billion), is completed in installments, this will all contribute to raising the level of capital spending within the domestic economy by the sovereign wealth fund significantly.

**Figure 1: Fiscal data in line with recent preliminary budget data**

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*As outlined in the preliminary fiscal budget in November, budgeted government expenditure will total SR1020 billion in 2020….*

- Meanwhile, current spending (the more rigid part of expenditure) is expected to decline slightly by 3 percent, year-on-year, to a budgeted total of SR847 billion. At the same time, the compensation of employees (wage bill) is expected to make up around 49 percent of total expenditure (SR504 billion), compared to a total of 48 percent in 2019, with the extension of the inflation allowance till the end of 2020 included within the wage bill figures.

*...based on revenues of SR833 billion, the government is budgeting for a higher year-on-year deficit at SR187 billion in 2020 (6.4 percent of GDP).*

- The government has budgeted for non-oil revenue to reach SR320 billion in 2020, showing marginal growth of 2 percent over 2019's actual total of SR315 billion. The rises are expected to come about largely as a result of rises in non-oil-non-tax revenue, considering that tax revenue is expected to decline marginally year-on-year in 2020.

*According to the statement, budgeted capital spending will amount to SR173 billion in 2020, compared to SR172 billion in 2019.*

- Government oil revenue is budgeted to reach a total of SR513 billion in 2020, down 14 percent year-on-year. As we outlined in our *Preliminary Budget Update*, the combination of changes in the tax structure related to Aramco announced last month, and a more subdued outlook on oil markets, are likely to be reflected in overall government revenue for 2020 and subsequent years.

*Compensation of employees (wage bill) is expected to make up around 49 percent of total expenditure (SR504 billion), compared to a total of 48 percent in 2019.*

- Brent oil prices have been on a downward trajectory since early 2019 and are currently trading around $65 per barrel (pb) versus highs of $71 pb seen in April 2019. Year-to-date, Brent oil prices average $65 pb, slightly below our forecast of $66 pb for full year. Looking ahead, oil markets remain challenged, with current OPEC oil demand projections for 2020 representing the lowest level of annual growth since at least 2012. That said, a recent agreement by OPEC and partners (OPEC +) to further moderate oil output till at least March 2020, has lifted oil prices in the last few days. Despite this, we see limited upside to oil prices at the moment, with prices likely to trade around the current range, and we therefore expect Brent oil to average $65 pb in 2020 as a whole.

*The government has budgeted for non-oil revenue to reach SR320 billion in 2020, showing marginal growth of 2 percent over 2019's actual total of SR315 billion.*

- We calculate that a Brent oil price of $60 per barrel (pb) and crude oil production of 9.8 million barrels per day (mbpd) in 2020 are consistent with the oil revenue projections of SR513 billion contained in the budget. Moreover, in light of the fact that potentially 98.3 percent of Aramco's expected base dividend of $75 billion (SR281 billion) is expected to flow to government in 2020, we see SR513 billion as being a conservative estimate.

*Government oil revenue is budgeted to reach a total of SR513 billion in 2020.*

- Looking at the performance of 2019's budget, the fiscal deficit came in 24 percent lower than 2018's total of SR174 billion. It seems that the continuous monitoring of expenses related to the various Vision Realization Programs (VRPs) resulted in marginally lower expenditure than budgeted, at SR1048 billion (compared to SR1106 billion stated in the 2019 fiscal budget report). On the non-oil revenue side, this segment was up by 7 percent year-on-year in 2019, mainly as a result of yearly increase from taxes on goods and services. Meanwhile, government oil revenue was down marginally year-on-year by 2 percent at SR602 billion, as Brent crude oil prices are expected to have declined by 9 percent year-on-year to average $65 pb during 2019.

*We calculate that a Brent oil price of $60 per barrel (pb) and crude oil production of 9.8 mbpd is consistent with the oil revenue projections in the budget.*

- According to the fiscal budget statement, provisional 2019 real GDP growth was 0.4 percent compared to our forecast of 0.2 percent. In 2020, GDP growth is expected to reach 2.3 percent compared to our current forecast of 2.1 percent. Also, the statement outlined that inflation is expected to average 2 percent in 2020, compared to our forecast of 1.1 percent, versus an expected –1 percent in 2019 (versus our forecast of –1.2 percent).

*According to the fiscal budget statement, provisional 2019 real GDP growth was 0.4 percent compared to our forecast of 0.2 percent.*

## The 2020 Budget

*In line with the preliminary budget outlined in November…*

*...the 2020 fiscal budget shows that the Kingdom will still see a sizable level of budgeted expenditure…*

*...at SR1.02 trillion, despite a yearly decline of SR86 billion or 3 percent versus actual spend in 2019.*

*Total government revenue for 2020 was budgeted at SR833 billion according to the statement…*

*…this was split 63/37 percent between oil revenue (SR513 billion) and non-oil revenue (SR320 billion).*

*On the non-oil side, the government has budgeted for SR320 billion in 2020, showing marginal growth of 2 percent over 2019's actual total of SR315 billion.*

In line with the preliminary budget outlined in November, the 2020 fiscal budget shows that the Kingdom will still see a sizable level of budgeted expenditure at SR1.02 trillion, despite a yearly decline of SR86 billion or 3 percent versus actual spend in 2019 (Figure 2). As has been the theme in recent budgets, the emphasis of the 2020 budget will be on continued implementation of the Vision 2030, through expenditure on Vision Realization Programs (VRPs). As a result, the budget aims to bring about sustainable economic growth which is tied to diversifying the non-oil economic base. Lastly, the budget underlines the government's commitment to improving the quality of life and raising the standard of living for citizens through targeted social protection programs such as the Citizen's Account, the inflation allowance, but also indirectly through spending on education, healthcare and social infrastructure.

Total government revenue for 2020 was budgeted at SR833 billion according to the statement. This was split 63/37 percent between oil revenue (SR513 billion) and non-oil revenue (SR320 billion). As we outlined in our preliminary budget update, the combination of changes in the tax structure related to Aramco announced last month, and a more subdued outlook on oil markets, are likely to be reflected in oil government revenue for 2020 and subsequent years. On the non-oil side, the government has budgeted for SR320 billion in 2020, showing marginal growth of 2 percent over 2019's actual total of SR315 billion. The rises are expected to come about largely as a result of higher non-oil-non-tax revenue, considering that tax revenue is expected to decline year-on-year in 2020 (Figure 3).

Due to budgeted revenue of SR833 billion versus expenditure of SR1.02 trillion, the fiscal deficit is forecasted at SR187 billion in 2020 (6.4 percent of GDP). This is in line with the preliminary budget published last month, which revised a number of key fiscal indicators compared to the Fiscal Balance Program 2019 (FBP).

A larger fiscal deficit is not expected to translate into higher levels of debt. According to the budget statement, total debt requirement for next year will be SR76 billion, which is expected to push up total debt to SR754 billion by end of 2020, equivalent to 26 percent of GDP (Figure 4). Since around 41 percent of the deficit will be financed through debt, this will result in higher levels of SAMA deposits being used for deficit financing in 2020, which in turn is expected to pressure SAMA FX reserves.

**Figure 2: Actual and budgeted expenditure and yearly change**

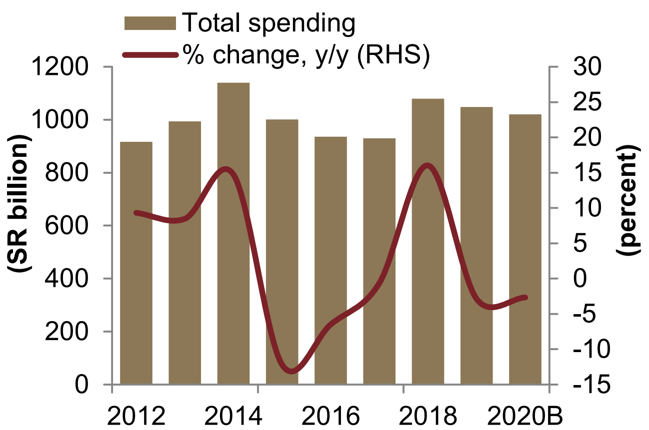
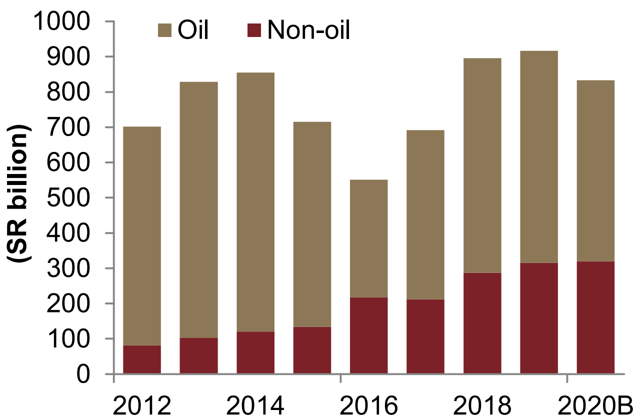



**Figure 3: Actual and budgeted revenue by type**



*Total expenditure is budgeted at SR1.02 trillion in 2020, down 8 percent from the 2019 budgeted expenditure of SR1.1 trillion…*

*...and down 3 percent from 2019 actual expenditure of SR1.05 trillion.*

*In fact, 2019 was the largest level of budget underspend since at least 2003.*

*According to the budget statement, a number of initiatives in the last few years have contributed to raising overall spending efficiency…*

*...and thus contributed to reducing both operating and capital expenditure.*

## Expenditure

Total expenditure is budgeted at SR1.02 trillion in 2020, down 8 percent from the 2019 budgeted expenditure of SR1.1 trillion and down 3 percent from 2019 actual expenditure of SR1.05 trillion. In fact, 2019 was the largest level of budget underspend since at least 2003 (Box 1, Figure 5).

### Box 1: Raising efficiency in expenditure

According to the budget statement, a number of initiatives in the last few years have contributed to raising overall spending efficiency and thus contributed to reducing both operating and capital expenditure. Below we discuss the three main areas we see as directly contributing to raising the efficiency of expenditure:

1) Work done in collaboration with the Center of Spending Efficiency (CSE), through continuous revision of the various expenditure items and projects have contributed to raising overall effectiveness of economic and social spending.

2) Reductions in expenditure are also due to continuous monitoring of the various VRPs. For example, recent reviews have found that some VRPs have achieved a good level of progress in terms of delivering to various targets, including programs such as the Housing VRP and the entertainment aspect within the Quality of Life VRP. Additionally, the private sector's contribution in establishing and operating several projects including water, sanitation and energy sectors, have also contributed to reducing the need to finance such projects from the budget.

3) Lastly, the roll-out of the electronic Etimad portal will have also helped improve the management of expenditure. The Etimad portal is now mandatory for all government projects and allows public sector entities and private sector contractors to make use of the digital services for procurement, budget management, vendor selection, and contract and payments management. This combined with the approval of a new Government Tendering and Procurement law, which is designed to improve the allocation and management of financial resources of government, is expected to greatly improve the budget execution process.

**Figure 4: Public debt and percent of GDP**

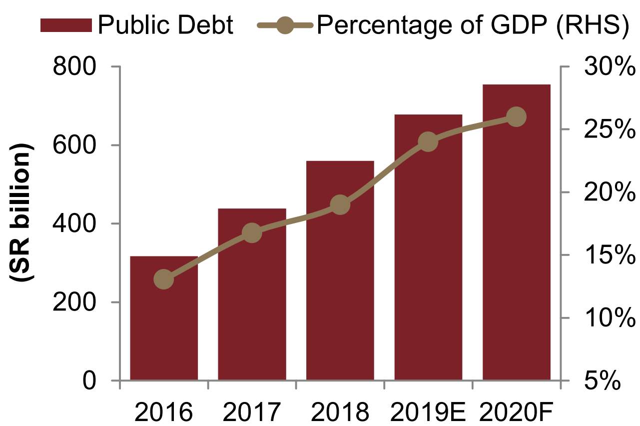
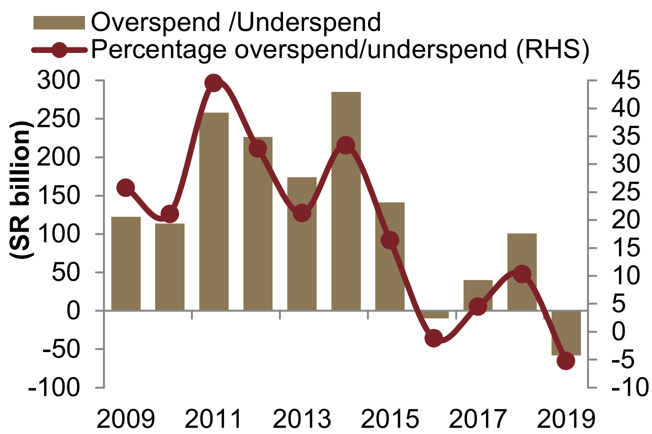



**Figure 5: Historical overspend/underspend (actual versus budgeted spending)**



*Meanwhile, current spending is expected to decline slightly by 3 percent, year-on-year, to a budgeted total of SR847 billion.*

*At the same time, the compensation of employees (wage bill), which will be flat year-on-year…*

*...is expected to make up around 49 percent of total expenditure (SR504 billion).*

*The combined level of social benefit and subsidies expenditure is expected to decline by 8 percent year-on-year in 2020.*

*The yearly decline is reflective of the fact that in 2019 a large one-off rise in spending related to the collective bill was seen.*

Whilst the above mentioned points in Box 1 will have also contributed to a nominal yearly rise in budgeted capital spending of SR173 billion in 2020 (Figure 6), it is important to note the role of other institutions in investment spending within the Kingdom. As we have highlighted previously, the Public Investment Fund (PIF) and indeed the National Development Fund (NDF) are expected to take a leading role in investments within the Kingdom going forward.

In line with this, once proceeds from Aramco's SR96-110 billion ($25.6-29.4 billion) IPO flow to the PIF, and indeed PIF's sale of its 70 percent stake in Sabic to Aramco, totaling SR259 billion ($69 billion), is completed in installments, this will all contribute to raising the level of capital spending within the domestic economy by the sovereign wealth fund significantly. With respect to the NDF, whilst the more recently created entity is in the process of integration and coordination between the various development funds, its contribution to domestic economy is expected to pick up in the forthcoming years.

Meanwhile, current spending (the more rigid part of expenditure) is expected to decline slightly by 3 percent, year-on-year, to a budgeted total of SR847 billion. At the same time, the compensation of employees (wage bill), which will be flat year-on-year, is expected to make up around 49 percent of total expenditure (SR504 billion), compared to a total of 48 percent in 2019, with the extension of the inflation allowance till the end of 2020 included within the wage bill figures.

The combined level of social benefit and subsidies expenditure is expected to decline by 8 percent year-on-year in 2020. The yearly decline is reflective of the fact that in 2019 a large rise in spending related to the collective bill was seen. The bill, which was introduced in early 2019, is expected to have provided one-off rebates totaling SR10.8 billion during this year to various companies who exhibited high levels of 'Saudization' (*for more on this please refer to our Labor Market Update published February 2019*). Because this rebate is not re-occurring, it is not budgeted for in 2020, and hence why the 'Subsidies' segment is expected to see the largest yearly percentage declines in 2020. This apart, social benefit and subsidies are expected to account for 9 percent of total expenditure, underlining the government's commitment to improving the quality of life and raising the standard of living for citizens.

**Figure 6: Actual and budgeted expenditure by type**

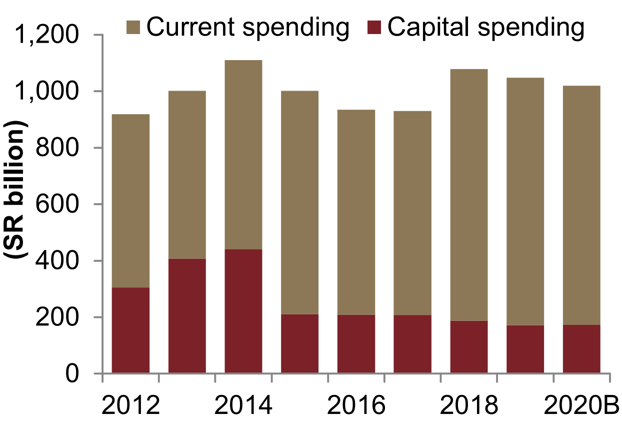
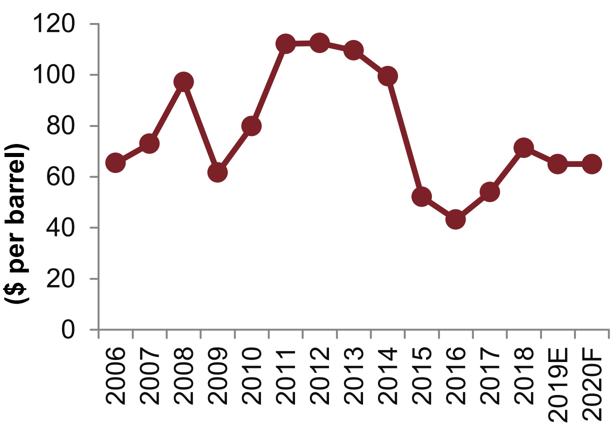



**Figure 7: Brent oil prices**



*Looking at the budget from a sectorial level, 'education' is expected to make up the largest portion of budgeted expenditure, at 19 percent of the total.*

Looking at the budget from a sectorial level, 'education' is expected to make up the largest portion of budgeted expenditure, at 19 percent of the total. Meanwhile, a sizable reduction in 'military' expenditure is budgeted for the second consecutive year, with declines of 8 percent year-on-year expected in 2020. Overall, only 'general items', which includes a number of different sub-items such as spending on government pensions, social insurance and financing costs, is expected to show yearly rises (Table 1).

**Table 1. 2020 Budget Allocation**

(SR billion)

| Budget Allocation | 2019 B | 2019 A | 2020 B | Difference (2019A-2020B) |
|---|---|---|---|---|
| Expenditures | 1106 | 1048 | 1020 | -2.6% |
| Education and Training | 193 | 202 | 193 | -4.4% |
| Health & Social Development | 172 | 174 | 167 | -4.0% |
| Municipality Services | 62 | 59 | 54 | -9.1% |
| Military and Security Services | 191 | 198 | 182 | -8.2% |
| Infrastructure & Transport | 70 | 62 | 56 | -9.5% |
| Economic Resources | 131 | 99 | 98 | -1.2% |
| Public Administration | 28 | 29 | 28 | -2.5% |
| Security & Regional Admin. | 103 | 104 | 102 | -1.6% |
| General Items | 156 | 121 | 141 | 15.9% |

Note: "B" refers to budgeted spending, "A" refers to actual spending

## Revenue

Total government revenue for 2020 was budgeted at SR833 billion according to the statement. This was split 63/37 percent between oil revenue (SR513 billion) and non-oil revenue (SR320 billion). As we outlined in our Preliminary Budget Update, the combination of changes in the tax structure related to Aramco announced last month, and a more subdued outlook on oil markets, are likely to be reflected in oil government revenue for 2020 and subsequent years.

*We calculate that a Brent oil price of $60 per barrel (pb) and crude oil production of 9.8 mbpd in 2020...*

*...are consistent with the oil revenue projections of SR513 billion contained in the budget.*

Brent oil prices have been on a downward trajectory since early 2019 and are currently trading around $65 per barrel (pb) versus highs of $71 pb seen in April 2019. Year-to-date, Brent oil prices average $65 pb, slightly below our forecast of $66 pb for full year. Looking ahead, oil markets remain challenged, with current OPEC oil demand projections for 2020 representing the lowest level of annual growth since at least 2012. That said, a recent agreement by OPEC and partners (OPEC +) to further moderate oil output till at least March 2020, has lifted oil prices in the last few days. Despite this, we see limited further upside to oil prices at the moment, with prices likely to trade around the current range, and we therefore expect Brent oil to average $65 pb in 2020 as a whole (Figure 7).

*In light of the fact that potentially 98.3 percent of Aramco's expected base dividend of $75 billion (SR281 billion) is expected to flow to government in 2020…*

*...we see SR513 billion as being a conservative estimate.*

We calculate that a Brent oil price of $60 per barrel (pb) and crude oil production of 9.8 million barrels per day (mbpd) in 2020 are consistent with the oil revenue projections of SR513 billion contained in the budget (Figure 8). Moreover, in light of the fact that potentially 98.3 percent of Aramco's expected base dividend of $75 billion (SR281 billion) is expected to flow to government in 2020, we see SR513 billion as being a conservative estimate.

On the non-oil side, the government has budgeted for SR320 billion in 2020, showing marginal growth of 2 percent over 2019's actual

*On the non-oil side, the government has budgeted for SR320 billion in 2020, showing marginal growth of 2 percent over 2019's actual total of SR315 billion…*

*...with tax revenue being the fastest growing item in non-oil revenue in 2020.*

total of SR315 billion. The rises are expected to come about largely as a result of higher non-oil-non-tax revenue, considering that tax revenue is expected to decline year-on-year in 2020.

Tax revenues are projected to reach SR200 billion in 2020, mildly lower than the expected total for 2019. This is due to the collection of non-recurrent settlements from the telecom sector in 2019, which contributed around SR7.5 billon to the 'Taxes on goods and services' segment within overall tax revenue. Looking ahead, tax revenue will remain the fastest growing item in non-oil revenue in 2020, with the vast majority of rises expected to come about due to scheduled rises in expat levies (Figure 9).

## Budgetary Performance in 2019

*It seems that the continuous monitoring of expenses related to the various VRPs…*

*...expenditure efficiency gains from the CSE…*

*…and the private sector's contribution in establishing and operating several projects…*

*...resulted in marginally lower expenditure than budgeted, at SR1048 billion in 2019.*

It seems that the continuous monitoring of expenses related to the various VRPs, expenditure efficiency gains from the CSE and the private sector's contribution in establishing and operating several projects resulted in marginally lower expenditure than budgeted, at SR1048 billion in 2019 (compared to SR1106 billion stated in the 2019 fiscal budget report). Targeted cost cutting and more efficient spending is underlined by the fact that despite a reduction of 9 percent year-on-year in the more growth enhancing capital spending (which was also 30 percent lower than the SR246 billion originally budgeted for in 2019), non-oil private sector growth is expected to improved significantly in 2019 (see economic performance in 2019 below)

That said, the compensation of employees (wage bill) remained the major component of total expenditure. In 2019, the wage bill constituted 49 percent of total expenditure (at SR504 billion) and grew by 4 percent over the same period last year, despite a budgeted decline of 6 percent year-on-year outlined in last year's budget statement.

Meanwhile, government revenue, whilst being up 1 percent year-on-year in 2019, came in lower than budgeted by 6 percent (SR917 billion versus 975 billion). The main culprit behind lower than budgeted revenues was lower oil revenue. Oil revenue was down marginally year-on-year by 2 percent at SR602 billion, and 9 percent lower than the budgeted SR662 billion. The decline reflective of Brent crude oil prices, which are expected to be down by 9 percent year-on-year in 2019.

**Figure 8: Saudi crude oil production**
(direct communication)

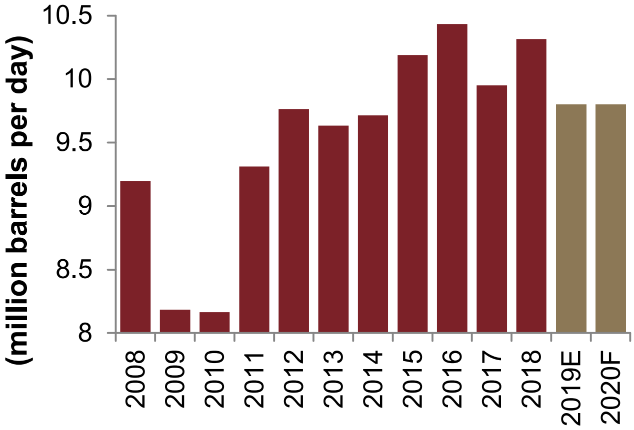
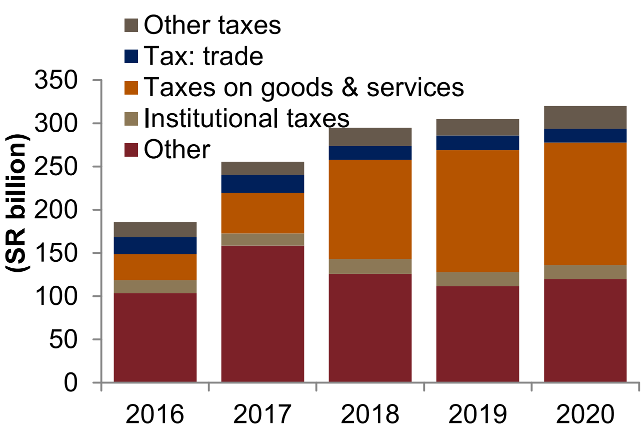



**Figure 9: Non-oil revenue by type**




Other taxes = 'Other Taxes (including Zakat)'
Tax: trade = 'Taxes on trade and transactions (customs duties)'
Institutional taxes = 'Taxes on income, profits and capital gains'
Other = 'Other revenues (including returns from SAMA and PIF)'

*On the non-oil revenue side, this segment was up by 7 percent year-on-year in 2019…*

On the non-oil revenue side, this segment was up by 7 percent year-on-year in 2019, mainly as a result of yearly increase from taxes, which rose by 21 percent year-on-year to SR203 billion. Revenues from 'Other taxes' (including Zakat) are expected to reach SR29 billion in 2019, an increase of 42 percent compared to last year and 55 percent higher than the budget estimate. This is mainly due to an increase in the number of Zakat payers registered with the General Authority of Zakat and Tax (GAZT) and the collection of revenues from banks' Zakat settlements. Taxes on goods and services are expected to reach SR141 billion in 2019, an increase of 22 percent over the previous year, and mainly driven by rises in expat levies and one-off settlements from the telecoms sector.

*...mainly as a result of yearly increase from taxes, which rose by 21 percent year-on-year to SR203 billion.*

*Within this segment, taxes on goods and services are expected to reach SR141 billion in 2019…*

Despite government revenue coming in lower than budgeted in 2019, an equally lower level of spending (of SR58 billion) is expected to have resulted in the fiscal deficit being in line with MoFs forecasts, at SR131 billion (4.7 percent of GDP), and 24 percent lower than 2018's total of SR174 billion (Table 2).

**Table 2. 2019 Budget data**
(SR billion)

| | Budget | Actual | Difference |
|---|---|---|---|
| **Revenues** | 975 | 917 | 58 |
| **Expenditures** | 1106 | 1048 | 58 |
| **Balance** | -131 | -131 | 0 |

## Economic Performance in 2019

*...an increase of 22 percent over the previous year, and mainly driven by rises in expat levies and one-off settlements from the telecoms sector.*

According to the budget statement, real GDP growth is expected to have risen by 0.4 percent year-on-year in 2019 compared to our forecast of 0.2 percent and compared to 2.4 percent year-on-year in 2018. As we have stated previously, GDP in 2019 was affected by a decline in the oil sector. In fact, Saudi crude oil production is expected to average 9.8 mbpd in 2019, compared to 10.3 during the same period last year. The reduction in output is reflective of Saudi Arabia's commitment to the OPEC and non-OPEC (OPEC+) agreement.

*According to the budget statement, real GDP growth is expected to have risen by 0.4 percent year-on-year in 2019…*

Meanwhile, the budget statement illustrated that non-oil GDP is expected to grow by 2.8 percent in 2019, in-line with our forecasts. As we highlighted in our recent macroeconomic update, non-oil growth has seen a notable uptick since the start of the year, with our non-oil private sector composite index showing an elevated level of economic activity within the Kingdom. Meanwhile, preliminary 2019 data from the budget statement expects inflation to average -1 percent in 2019, compared with our forecast of -1.2 percent, and 2 percent in 2020, versus our forecast of 1.1 percent.

*….compared to our forecast of 0.2 percent and compared to 2.4 percent year-on-year in 2018.*

## The Economic Outlook for 2020

*We expect an improvement in the Saudi economy in the year ahead, with our growth forecasts at 2.1 percent overall, compared to 2.3 percent outlined in the budget statements*

We expect an improvement in the Saudi economy in the year ahead, with our growth forecasts at 2.1 percent overall, compared to 2.3 percent outlined in the budget statements (Table 3). We see the main driver of growth being the non-oil sector, which we see rising by 2.8 percent in 2020. According to our forecast, oil sector GDP is expected to rise by 1.2 percent despite Saudi Arabia continuing to engage in oil production moderation as part of the OPEC+

*More specifically, we see progress under various VRPs directly contributing to growth in numerous sectors next year.*

*Moreover, we expect additional uplift in the non-oil private sector as a result of Saudi Arabia hosting the G20 summit next year.*

agreement. The main source of oil sector growth is expected from the start up of the large Jazan refinery and Fadhli gas complex. On the non-oil side, despite recent downward revisions in budgeted government expenditure, as detailed in the statement, we still expect growth to improve. More specifically, we see progress under various VRPs directly contributing to growth in numerous sectors next year. Accordingly, under the PIF program, we expect growth in the construction sector as a result of progress on mega-projects, whilst growth in the finance sector will be driven by insurance, housing and mortgage finance (via the [Financial Sector Development Program] and Housing VRP), whilst sizable growth rates in wholesale & retail trade and social services sectors are expected as a result of rapid expansion in the tourism, sports and entertainment sectors under the Quality of Life VRP. Moreover, we expect additional uplift in the non-oil private sector as a result of Saudi Arabia hosting the G20 summit next year.

Moreover, we expect additional uplift in the non-oil private sector as a result of Saudi Arabia hosting the G20 summit next year. Specifically, global economic developments, in particular with regards to the US and Chinese trade dispute, as well as regional geopolitical tensions, stand out as the main risks to our forecast.

**Table 3. 2019 results and 2020 forecasts in budget statement**

| | 2019 Actual | 2020 Forecast |
|---|---|---|
| Real GDP (% change) | 0.4 | 2.3 |
| Inflation (2013 = 100, %) | -1.0 | 2.0 |