جدوى للإستثمار
Jadwa Investment

December 2021

Saudi Arabia's 2022 Fiscal Budget

- The government's budget for the 2022 fiscal year was endorsed by the Council of Ministers on 12th December with some changes compared to the preliminary budget released earlier in September this year.

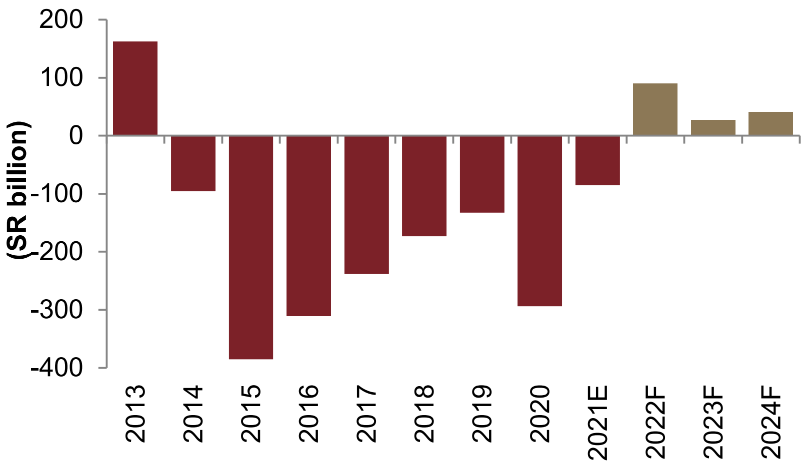
- Total expenditure for 2022 remained unchanged versus the preliminary budget, at SR955 billion, meaning it is expected to be 3.5 and 6 percent lower than 2021 budgeted (SR990 billion) and actual (SR1.02 trillion) expenditure, respectively. In-line with the observed medium term trend, budgeted government capital expenditure will continue declining in 2022 year-on-year. Meanwhile, current spending is expected to decline by 4 percent, year-on-year, to a budgeted total of SR863 billion.

- The baseline scenario of budgeted government revenue for 2022 is expected to total SR1.05 trillion according to the statement. In-line with the Ministry of Finance's (MoF) practice of not disclosing government oil revenue since the listing of Aramco, this segment is now aggregated into 'Other revenues', which is expected to rise by 19 percent year-on-year in 2022, to SR763 billion. We estimate that a Brent oil price of around $70-75 per barrel (pb) would represent a reasonable range for the budgeted oil price in the 2022 baseline revenue scenario.

- As anticipated, the Kingdom is expected to register its first fiscal surplus since 2013. Based on budgeted government revenue of SR1.05 trillion (16 percent higher than structural revenues scenario of SR903 billion initially used in the preliminary budget) the Kingdom will see a fiscal surplus of SR90 billion (2.5 percent of GDP) in 2022, with further surpluses expected in 2023 & 2024 (Figure 1).

- According to the budget statement, the Saudi economy registered real GDP growth of 2.9 percent in full year 2021 (compared to our forecast of 2.7 percent), and compared to -4.1 percent year-on-year in 2020. Looking out into 2022, the statement expects the Saudi economy to grow by 7.4 percent, which is based on sizable rises in oil GDP, as a result of higher yearly crude oil production.

Figure 1: The Kingdom is expected to register a fiscal surplus in 2022-24



For comments and queries please contact:

Asad Khan
Chief Economist & Head of Research
rkhan@jadwa.com

Nouf N. Alsharif
Director
nalsharif@jadwa.com

Head office:

Phone +966 11 279-1111
Fax +966 11 279-1571
P.O. Box 60677, Riyadh 11555
Kingdom of Saudi Arabia
www.jadwa.com

Released: December-13-2021, 03:30 UTC+3

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...meaning it is expected to be 3.5 and 6 percent lower than 2021 budgeted and actual expenditure, respectively.

Despite this, and as highlighted by the recently announced National Investment Strategy (NIS)…

...total domestic investment (including government capex, PIF, 'Shareek' and NDF investments)…

….will rise by 12 percent year-on-year in 2022, to SR686 billion.

Meanwhile, current spending is expected to decline by 4 percent year-on-year…

The government's budget for the 2022 fiscal year was endorsed by the Council of Ministers on 12th December with some changes compared to preliminary budget released earlier in September this year:

Expenditure:

Total expenditure for 2022 remained unchanged versus the preliminary budget, at SR955 billion, meaning it is expected to be 3.5 and 6 percent lower than 2021 budgeted (SR990 billion) and actual (SR1.02 trillion) expenditure, respectively (Figure 2).

In-line with the observed medium term trend, budgeted government capital expenditure (capex) will continue declining in 2022 year-on-year. The statement highlighted that SR92 billion (or 10 percent of total spending) will be allocated to capex, equating to a 18 percent yearly decline over 2021's actual sum of SR112 billion. Despite this, and as highlighted by the recently announced National Investment Strategy (NIS), total domestic investment (including government capex, PIF, 'Shareek' and NDF investments) will rise by 12 percent year-on-year in 2022, to SR686 billion (Figure 3, Box 1).

Box 1: Saudi Arabia's National Investment Strategy

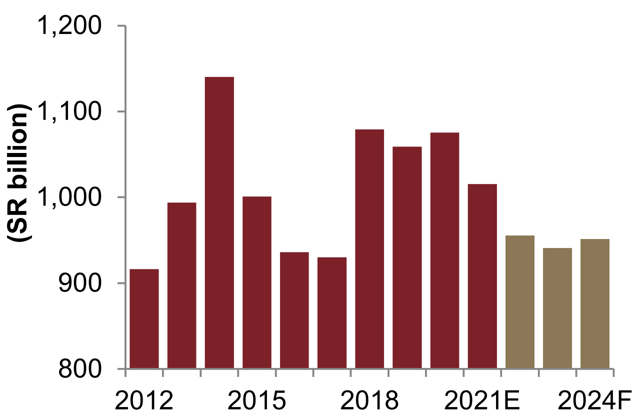
The National Investment Strategy (NIS) was announced in October 2021, with the main objectives focusing on increasing the quality and magnitude of investments, through the following strategies:

- Growing the private sector's contribution in the economy and the balance of payments
- Supporting strategic sectorial development
- Upgrading the investment ecosystem to spur innovation and help to develop local content

Related to this, an ambitious annual target of SR2 trillion of investments into the economy is earmarked by 2030. Of this, circa SR1.65 trillion is expected to come from domestic gross fixed capital formation and the remainder from foreign direct investment (FDI). In fact, the NIS states that cumulative investments should aim to total SR12.4 trillion by 2030. More specifically, the largest component of investment is expected to come from 'Shareek', a program which aims to forge a partnership between the public sector and certain listed private sector companies to target SR5 trillion in cumulative investments by 2030 (Figure 4).

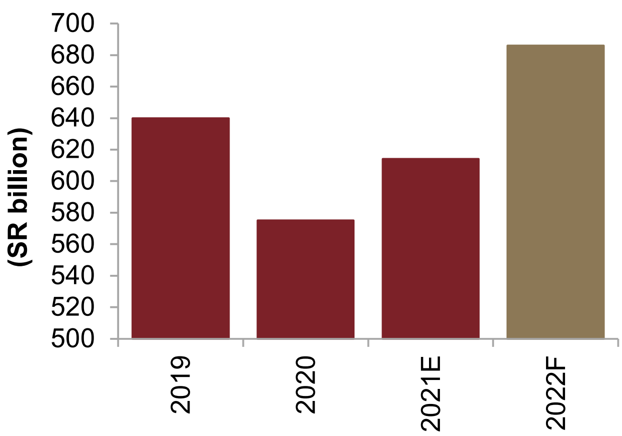
Meanwhile, current spending (the more rigid part of expenditure) is expected to decline by 4 percent, year-on-year, to a budgeted total of SR863 billion. The largest component of this segment (compensation

Figure 2: Government expenditure*



*actual till 2021, budgeted 2022-2024

Figure 3: Under the NIS, domestic investment is expected to rise 12 percent year-on-year in 2022



...to a budgeted total of SR863 billion.

Only 'general items' (which includes contribution to pension funds and social insurance, amongst other things)…

...and 'security and regional administration' are expected to show yearly rises between actual 2021 and budgeted 2022 expenditure.

There were no changes to expenditure projections for 2023 and 2024, reflecting the MoF's more prudent approach to fiscal affairs.

of employees) is expected to remain virtually unchanged versus last year's actual total (of SR497 billion), but because of lower yearly total expenditure, its proportion will rise to 52 percent of total expenditure, compared to 49 percent in 2021.

Looking at the budget from a sectorial level, 'education' (down 3 percent yearly) and 'general items' (up a sizable 39 percent on a yearly basis) are the largest portion of budgeted expenditure, both making up 19 percent of the total each. Meanwhile, 'military' expenditure (down 10 percent) makes up 18 percent of the total, whilst 'health & social development (down 28 percent) makes up 14 percent of budgeted expenditure. Overall only 'general items' (which includes contribution to pension funds and social insurance, amongst other things) and 'security and regional administration' are expected to show yearly rises between actual 2021 and budgeted 2022 expenditure (Table 1, Figure 5).

Table 1. 2022 Budget Allocation

(SR billion)

Budget Allocation	2021 B	2021 A	2022 B	Difference (2022B-2021A)
Expenditure	990	1015	955	-60
Education	186	191	185	-6
Health & Social Development	175	191	138	-53
Municipality Services	51	50	50	0
Military	175	190	171	-19
Infrastructure & Transport	46	48	42	-6
Economic Resources	72	82	54	-28
Public Administration	34	33	32	-1
Security & Regional Admin.	101	99	101	2
General Items	151	131	182	51

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

There were no changes to expenditure projections for 2023 and 2024, reflecting the Ministry of Finance's (MoF) more prudent approach to fiscal affairs, in-line with the Fiscal Sustainability Vison Realization Program (VRP) (Box 3). Overall, expenditure plans between 2023-24 (Figure 2) are expected to continue focusing on the improvement of government services, infrastructure development, mega-projects, and on the implementation of various VRPs, including, but not limited to, the Housing VRP, and the recently unveiled Human Capital Development VRP, which aims to enhance the education sector and improve labor market inputs.

Figure 4: 'Shareek' to make up 40 percent of SR12.4 trillion cumulative investments by 2030

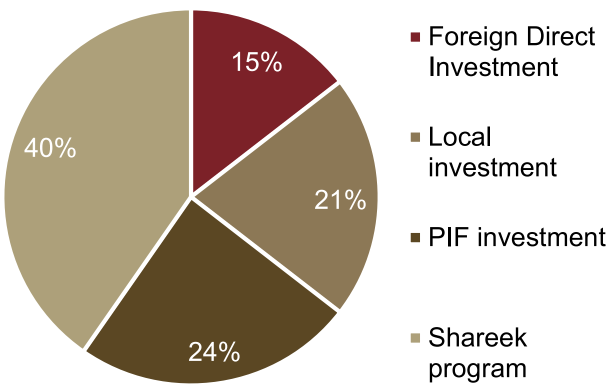
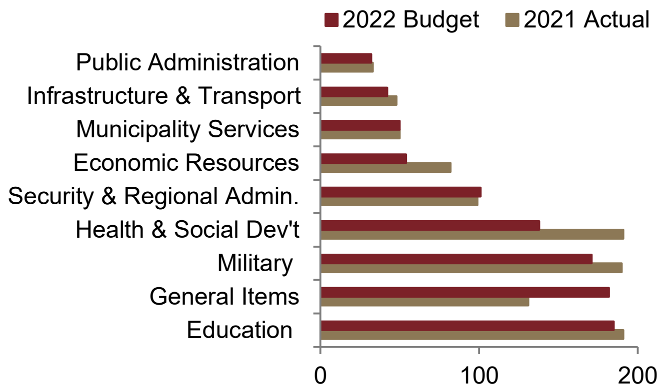


Figure 5: Yearly change in spending by sector
(actual 2021 versus budgeted 2022)



The baseline scenario of budgeted government revenue for 2022 is expected to total SR1.05 trillion according to the statement.

We estimate that a Brent oil price of around $70-75 per barrel (pb) would represent a reasonable estimate for the budgeted oil price in the 2022 baseline revenue scenario.

Due to the ongoing uncertainty related to Covid-19 pandemic, the MoF has introduced various revenue scenarios in this year's budget statement.

According the International Monetary Fund (IMF), a structural balances approach generally aims to quantify and remove the impact of…

Revenue:

The baseline scenario of budgeted government revenue for 2022 is expected to total SR1.05 trillion according to the statement (Box 2). In-line with the MoF's practice of not disclosing government oil revenue since the listing of Aramco, this segment is now aggregated into 'Other revenues', which is expected to rise by 19 percent year-on-year in 2022, to SR763 billion. Due to the number of miscellaneous items included within 'Other revenues' (such as investment income, confiscations, and collection of fines & penalties), the calculation of budget oil price is now a much more convoluted process. Having said that, however, we estimate that a Brent oil price of around $70-75 per barrel (pb) would represent a reasonable range for the budgeted oil price in the 2022 baseline revenue scenario.

The statement expects SR283 billion in tax revenue in 2022, showing a decline of 4 percent over 2021's expected total of SR296 billion. The main decline comes from a drop in 'taxes on goods and services' by 4 percent year-on-year, which, according to the statement, is a reflective of amendments in VAT collection from government contractors (Figure 6).

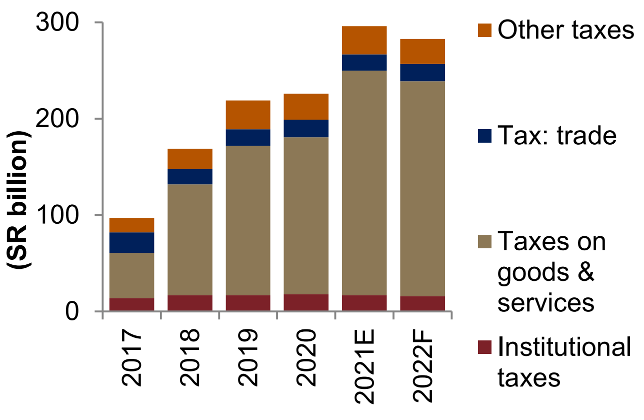
Box 2: Government Revenue

Due to the ongoing uncertainty related to Covid-19 pandemic, the MoF has introduced various revenue scenarios in this year's budget statement (Figure 7), which are classified as follows:

1) Structural revenues scenario is the most conservative estimate, at SR903 billion, and consistent with the Fiscal Sustainability Program's (FSP) calculations, which take into account historical long term average oil revenue, net of cyclical effects.
2) Baseline scenario, which is estimated at SR1.05 trillion through using current global economic and market developments. It is the most relevant forecast for the 2022 budget.
3) Lower revenue scenario is estimated at SR991 billion in 2022
4) Higher revenue scenario is estimated at SR1.13 trillion in 2022.

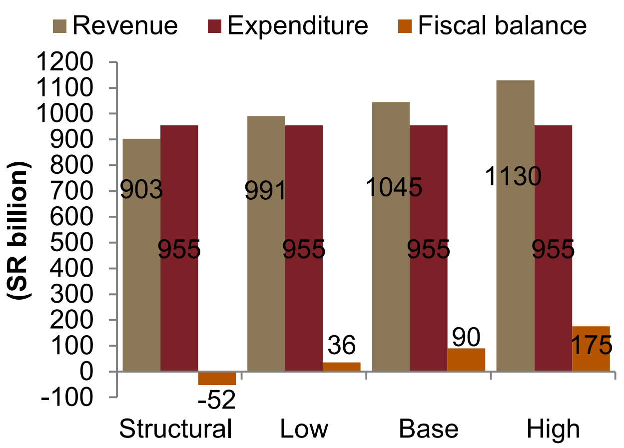
According to the budget statement, although government revenue for 2022 is based on current global economic and market development; the structural revenue approach is applied to both 2023 and 2024 revenue projections. According to the International Monetary Fund (IMF), a structural balances approach generally aims to quantify and remove the impact of:

Figure 6: Non-oil tax 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'

Figure 7: Various government revenue scenarios



...factors that are not closely correlated with the business cycle.

1) Factors that are not closely correlated with the business cycle, such as changes in asset or commodity prices.
2) One-off, or temporary, revenue or expenditure items, which do not affect the underlying fiscal position.

As such, in the case of Saudi Arabia, we assume that the structural revenues scenario is used as a process of eliminating the effects of oil price volatility (and indeed one-off non-oil revenue receipts) and thus reflects a more prudent approach to fiscal affairs over the medium term.

As anticipated, the Kingdom is expected to register its first fiscal surplus since 2013.

As anticipated in our recent macroeconomic update, the Kingdom is expected to register its first fiscal surplus since 2013. Based on budgeted government revenue of SR1.05 trillion (16 percent higher than structural revenues scenario of SR903 billion initially used in the preliminary budget) the Kingdom will see a fiscal surplus of SR90 billion (2.5 percent of GDP) in 2022, with further surpluses expected in 2023 & 2024 (Figure 1).

Budgetary Performance in 2021

As per preliminary budget, government revenue is expected to have totaled SR930 billion in full year 2021, up 19 percent, or SR148 billion, year-on-year.

As per preliminary budget, government revenue is expected to have totaled SR930 billion in full year 2021, up 19 percent, or SR148 billion, year-on-year. An improvement in global oil prices seemed to have pushed up oil revenue by 35 percent on a yearly basis, resulting in this segment's contribution rising to 60 percent of total revenue during the year (Figure 8).

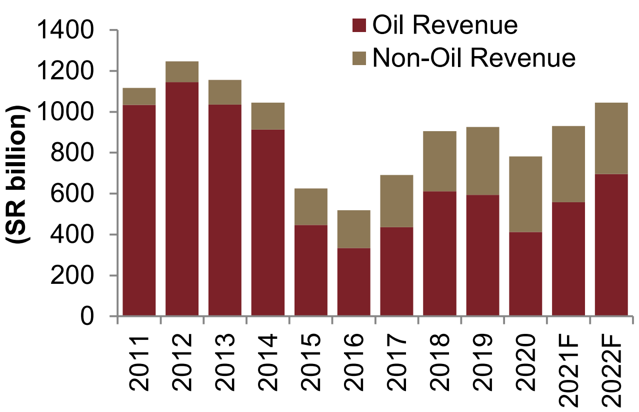
Meanwhile, non-oil revenue increased marginally by 1 percent, or SR3 billion, compared to last year.

Value added tax (VAT) revenue remains a key component of non-oil revenue.

Meanwhile, non-oil revenue increased marginally by 1 percent, or SR3 billion, compared to last year. Value added tax (VAT) revenue remains a key component of non-oil revenue, which is highlighted by the fact that 'taxes on goods and services' is expected to have contributed 63 percent of total non-oil revenue. In-line with this, we expect the VAT rate to remain unchanged (at 15 percent) during 2022, thus contributing to broadly similar levels of total non-oil revenue as 2021, at around 40 percent of the total. Meanwhile, 'Other revenues' declined by 52 percent (or SR83 billion) year-on-year. Due to the number of miscellaneous items included within this segment, 'Other revenues' is less predictable than non-oil tax revenue. That said, we note that this segment includes asset sales and public-private partnerships (PPP), and, as such, is likely to be negatively affected by the suspension of some privatization deals.

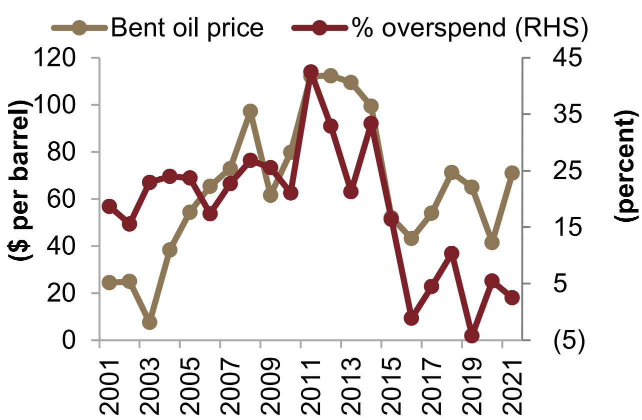
As per the preliminary budget, full year actual government expenditure was SR25 billion (or 3 percent) higher than budgeted in

Figure 8: Actual revenue by type*



*2022= Jadwa Investment's estimates

Figure 9: Brent oil prices and historical over-spend (actual versus budget expenditure)



As per the preliminary budget, full year actual government expenditure was 3 percent higher than budgeted in 2021.

2021, at a total of SR1.015 trillion (Box 3). Both capital (capex) and operational (current) expenditure saw rises over budgeted levels, with the former being 11 percent or SR11 billion higher than budgeted and the latter being 1.5 percent or SR14 billion higher. In fact, almost half of the revision in current expenditure (SR6 billion) was allocated to 'Compensation of Employees', but, despite this, this segment is expected to have risen only marginally (by 0.4 percent) over last year's total. Meanwhile, despite full year upward revision to capital expenditure**,** this segment is still expected to decline by 28 percent year-on-year.

Taking into account the upward adjustment in expenditure in 2021, the fiscal deficit hit -SR85 billion (or -2.7 percent of GDP) in full year 2021, in-line with estimates in the preliminary budget.

Box 3: Fiscal Sustainability Program

Despite actual spending rising 3 percent over budgeted levels in full year 2021, the rate of overspend has been declining since 2016. The statement highlights that between 2000-16, actual government spending was, on average, 23 percent higher than budgeted levels, but this declined to an average of 3.6 percent overspend between 2017-19 (Figure 9). The steep decline in average overspend has, according to the statement, largely been a result of the implementation of medium term financial plan under the Fiscal Balance Program (FBP). In fact, the FBP not only raised the efficiency of government expenditure, but also contributed to raising non-oil revenue from a number of diverse sources.

Looking ahead, the next phase of financial and economic reform will be rolled out under the Fiscal Sustainability Program (FSP).

Looking ahead, the next phase of financial and economic reform will be rolled out under the Fiscal Sustainability Program (FSP). More specifically, the FSP will aim to adopt a number of financial rules which help the Kingdom achieve financial stability and sustainable development. This will include developing spending ceilings derived from i) 'structural oil revenue' estimates (which take into account long term average historical oil revenue, net of cyclical effects) and ii) estimates of non-oil revenue linked to a percentage of non-oil GDP. The statement points out that the setting of limits on government expenditure will facilitate more optimal use of fiscal surpluses (if realized) by redirecting them towards enhancing government reserves, supporting the NDF and/or the PIF, or paying down public debt.

More specifically, the FSP will aim to adopt a number of financial rules which help the Kingdom achieve financial stability and sustainable development.

Figure 10: Real GDP growth

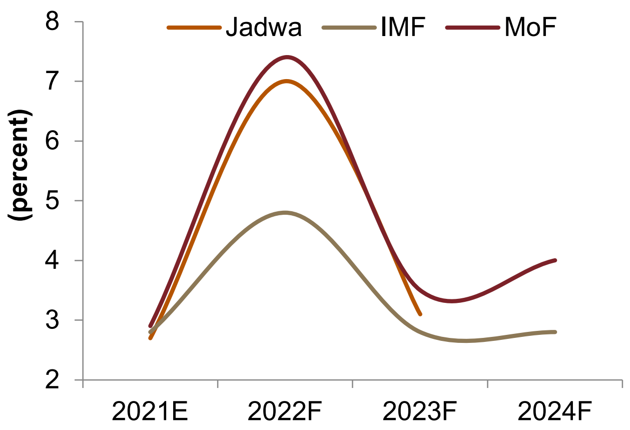
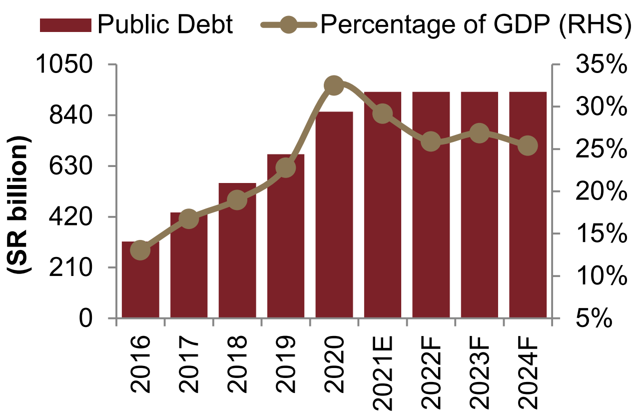


Figure 11: No change in total government debt from 2021-24



Economic Performance and Outlook

According to the budget statement, the Saudi economy registered real GDP growth of 2.9 percent in full year 2021.

According to the budget statement, the Saudi economy registered real GDP growth of 2.9 percent in full year 2021, (compared to our forecast of 2.7 percent) and compared to -4.1 percent year-on-year in 2020. The remarkable rebound in growth during 2021 is expected to have almost wholly been as a result of non-oil GDP, which, according to the statement, expanded by 4.8 percent year-on-year, with oil GDP likely registering nominal levels of growth during the year (in-line with our forecasts).

Looking out into 2022, the statement expects the Saudi economy to grow by 7.4 percent…

...which is based on sizable rises in oil GDP, as a result of higher yearly crude oil production.

Looking out into 2022, the statement expects the Saudi economy to grow by 7.4 percent, which is based on sizable rises in oil GDP, as a result of higher yearly crude oil production. As we highlighted in our recent *macroeconomic update*, a continued recovery in the global economy and higher vaccination rates, should, according to OPEC data, push oil demand 4 percent higher year-on-year (to 101 mbpd) in 2022, which will be met with higher oil supply from the Kingdom. Beyond 2022, real GDP growth is expected to hit 3.5 percent in 2023 and 4 percent in 2024 (Figure 10).

Meanwhile, inflation for full year 2022 is estimated to rise to 1.3 percent and 2 percent in 2023, versus our forecast of 1.7 & 1.5 percent, respectively. Also, due to expectation of a fiscal surplus in the next three years, debt is not expected to change over the medium term, and, as such, will decline as a proportion of GDP from 29.2 percent in 2021, to 25.4 percent by 2024 (Figure 11). That said, the statement highlights that MoF is working along side the National Debt Management Center (NDMC) to prepare an annual borrowing plan for 2022 (and likely beyond), with new borrowing used for either/or all of the following:

1) repayment of principal due in the future,
2) capitalizing on the right opportunities in the market to support government reserves,
3) or financing capital projects that can be accelerated through debt issuances.