

THE NATIONAL ECONOMY UNDER THE EIGHTH DEVELOPMENT PLAN

1.1 INTRODUCTION

During the Eighth Development Plan, the national economy achieved positive growth rates, as evidenced by the evolution of various economic indicators; notably GDP, capital accumulation, foreign trade and balance of payments, manpower development, contribution of the private sector, and monetary and fiscal performance. During the period, the international economic environment improved significantly, and that, in turn, enhanced the chances of achieving the main goals and objectives of the plan. Oil prices continued to rise until the middle of the fourth year of the plan (2008) when the global economy suffered a financial crisis that led to a global recession accompanied by a sharp decline in oil prices and the prices of many goods and raw materials, which had seen unprecedented rises just before.

With regard to the local economic environment, the State maintained efforts to develop the business environment and expand private sector participation, in addition to developing basic infrastructure and industrial and technological cities; all of which contributed to high rates of investment, employment and productivity in various economic sectors and activities, thereby raising production and improving quality of life.

This chapter summarizes the most important features of the performance of the national economy under the Eighth Development Plan, at both macroeconomic and sectoral levels; highlighting various economic policies, foreign trade and balance of payments, human development, employment, and the capital market.

1.2 THE ECONOMIC SITUATION

1.2.1 Principal Growth Rates

The national economy continued improving under the Eighth Plan

period. GDP at constant 1999 prices increased from about SR722.2 billion in 2004 to about SR855.8 billion in 2009, i.e. at an average annual growth rate of 3.5%, which is less than the 4.6% rate targeted by the Plan, but nearly equal to the rate achieved under the Seventh Development Plan, which was about 3.7%. This is good performance if one considers the conditions created by the global financial crisis. As a result, average per capita real GDP improved significantly, from about SR43.7 thousand in 2004 to about SR46.2 thousand in 2009, which amounts to an overall increase of 5.7%.

Growth of real GDP under the Eighth Development Plan is attributable to the high level of investment, which enhanced productivity in many sectors. The annual rate of growth of investment under the plan amounted to about 11.2%, which led the average ratio of investment to real GDP to rise to about 28.1%, compared to 21.1% in 2004.

The following subsections present the performance of the oil and gas sector and the non-oil sectors under the Eighth Development Plan.

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1.2.1.1 Oil-and-Gas Sector

Given the external factors that had an impact on the volume of oil production, especially in the last two years of the plan, the real domestic product of the oil-and-gas sector dropped at a rate of around 0.2% per annum; which is lower than the rate of 2.7% targeted by the plan. At current prices, the product of the sector increased at an annual rate of 24.1% in the first three years of the plan, due to oil prices rising to record levels in that period. However, the decline in oil prices in the last two years of the plan led to a marked slowdown in growth rates. Hence, the domestic product of the sector at current prices grew at the rate of 15.5% over the period of the plan as a whole.

The oil-and-gas sector acquired 4.3% of the total investments during the Eighth Plan, with an average annual value of about SR10 billion, which amounts to an increase of about 129.3%, compared with the value of investments in 2004. It is worth noting that the sector is characterized by high capital intensity, as well as high labour

productivity. Over the period of the Plan, the average value of capital invested per worker in the sector (capital/ labour) was about SR1.8 million, while average worker productivity was about SR2.8 million.

1.2.1.2 Non-Oil Sectors

Over the Eighth Plan period, non-oil sectors achieved an average annual growth rate of about 4.7%, with the value added by these sectors rising, at constant 1999 prices, from about SR523.8 billion in 2004 to about SR659.7 billion in 2009; thereby increasing their contribution to the GDP from about 72.5% in 2004 to about 77.1% in 2009. This good performance reflects effectiveness of the efforts made to diversify the production base of the economy. The Eighth Development Plan had targeted for the non-oil sectors an annual growth rate of 5.2% and a contribution to the GDP of 75.7% by the end of the period in 2009.

The non-oil sectors accounted for approximately 95.7% of the total investments made under the Eighth Plan, with an annual average value of SR 218.8 billion; an increase of about 47.8%, compared with the value of investments in these sectors made in 2004.

Despite the differing conditions of the non-oil sectors and their varying levels of performance under the Eighth Plan, they all shared a strong direct relationship between the rate of growth of investment and the rate of growth of value added. Sectors that had high rates of investment growth experienced the highest growth in value added, irrespective of whether they were production or service sectors. Accelerating the rate of investment in a sector lead to expansion and enhancement of its productive capacities, as well as to enabling it to use modern technologies and adopt advanced management systems capable of elevating partial and total factor productivity; all of which resulted in continuous improvement of value added, and hence, acceleration of growth rates.

The following is a summary of the varied performance of some non-oil sectors.

1.2.1.3 Production Sectors

Production sectors achieved an annual growth rate of about 4.7%. Fixed capital formation constituted the driving force for this growth, with the annual growth rate of investment in these sectors amounting to some 11.8%, and the average ratio of investment to value added during the period amounting to about 50.9%:

- The ‘petrochemicals’ sector achieved under the Eighth Plan an annual real growth rate of 9.7%, which exceeds the rate of 7.3% targeted by the Eighth Plan. In consequence, the contribution of the sector to the GDP increased from about 1.2% in 2004 to about 1.7% by the end of the plan in 2009. Growth in this sector was driven primarily by the high growth rates of investments, which averaged 6.4% annually over the period.
- The ‘other manufacturing industries’ sector achieved over the period an annual growth rate of 6.8%, which is higher than the target rate of 6.7% set by the Eighth Plan. Importance of the good performance of this sector stems from its being one of the important sectors relied upon in diversifying the production structure of the national economy and exports, as well as from its impact on improving factor productivity, through expanded use of advanced technologies and modern methods of management and marketing. As for fixed capital formation in this sector, investment grew over the period at an annual rate of about 6.3%.
- The ‘electricity, gas and water’ sector achieved an average annual real growth rate of about 5.7%, which is higher than the rate of 4.2% set as a target by the Eighth Plan, while investment grew at the rate of about 4.2%. Under the Plan, the sector experienced reorganization and restructuring, including privatisation of some of its activities. Upon completion of these processes, the sector is expected to achieve great leaps and qualitative transformations in its future performance.
- Under the Plan period, the value added of the ‘construction’ sector grew at an annual rate of 4.7%, which is less than the 6.7% growth rate set by the Plan as a target. Investment in the sector grew steadily over the first four years, but declined in the last year of the

Plan, which indicated an overall decline at a rate of about 1.1% per annum.

- Other production sectors had actual and target growth rates as follows: oil refining, about 2% and 4.4%; non-oil mining and quarrying, about 3% and 7.9%; agriculture, forestry and fishing, about 1.4% and 3.2%.

1.2.1.4 Service Sectors

Service sectors consist of private services sectors and government services sector. The following are the most important features of the performance of these sectors.

A. *Private Services:*

Private services sectors grew at an annual rate of about 6%, which is slightly higher than the 5.7% growth rate set by the Plan as a target. The annual growth rate of investments was about 7.7%. Thus, investment constituted 24.5% of the domestic product of these sectors during the period. The following provides an overview of the most important developments in these sectors.

- The ‘transport and communications’ sector achieved the highest growth rates among private service sectors. It grew at an annual rate of about 9.1%, which exceeds the rate of 7.5% set as a target by the Eighth Plan. Thus, the sector was the fastest growing sector of the national economy after petrochemicals. The annual rate of growth of investment over the period was high, about 9.3%, which is one of the major factors contributing to the high rate of growth of this sector. The sector paralleled the rapid global developments in the field of information and communication technology and experienced strong domestic competition; which, in turn, spurred further development and led to reducing the cost of services, raising production efficiency, and promoting the growth of value added. Furthermore, the impact of air transport liberalization, which resulted in stimulating the growth of the ‘transport’ component of the sector, is noteworthy.

- The ‘financial, insurance, business and real estate services’ sector achieved good growth rates over the period, both in terms of value added and investment. The product of the sector grew at an annual rate of 5.2%, compared with a target of 5.9%, while investment grew at an annual rate of about 8.7%. These growth rates are attributable to the rapid growth of domestic liquidity and expansion of domestic credit. The sector expanded significantly with the addition of new production units, such as commercial banks, investment banks and brokerage firms (national, of the Gulf and foreign); all of which contributed to higher rates of investment. Accession by the Kingdom to the WTO by the end of 2005 enabled the national financial services sector to attract foreign capital. In consequence, over the period, activity in ‘finance, insurance and business services’ grew at an annual rate of about 6.9%.
- The ‘community, social and personal services’ sector grew at an annual rate of about 4.5%, which is higher than the target growth rate of 3.5%. At the same time, fixed investment grew by about 2.3%. These indicators reflect the expanding role of the private sector in the provision of public services, such as cleaning services and recreational activities, in addition to health and education services.

B. Government Services:

Over the Plan period, the government services sector grew at an annual rate of 2.7%, which is lower than the rate of 3.8% set as a target by the Plan. During the first three years of the period, growth of oil revenues and the expansionary fiscal policy adopted by the state made available additional resources that enabled the sector to increase its operational and investment expenditure. The state gave special attention to enhancing the capacities of the sector, allocating a large proportion of government spending to investment in its various activities and strengthened its capital assets. As a result of this expansion, investment in the government services sector grew over the period by 12.8% per annum.

1.2.2 Gross Fixed Capital Formation

Under the Eighth Development Plan, the annual growth rate of total fixed investment was 11.2%. As a result, its size increased, at constant 1999 prices, from about SR152.4 billion in 2004 to about SR259.3 billion at the end of the plan in 2009 when fixed investment amounted to 30.3% of real GDP, compared with 21.1% in 2004. During the period, investment was distributed between the non-oil sectors and the oil sector at about 95.7% for the former, compared with 4.3% for the latter.

Comparing the annual growth rate of total fixed investment of 11.2% under the Eighth Plan with the growth rate of about 5.2% achieved under the Seventh Plan aptly illustrates the quantum leap in investment made under the Eighth Plan, principally due to the oil boom and continued enhancement of the investment environment in the Kingdom.

The annual growth rate of investment in the oil sector under the plan was about 24.4%, and these investments accounted on average for about 4.6% of the value added in the sector.

During the period, government investment grew at an annual rate of 12.8% in constant 1999 prices; its share of the government domestic product grew from about 22.9% in 2004 to about 36.7% in 2009. In comparison, private sector investment grew at an annual rate of about 10.2%. As a result, its share of the private sector real domestic product grew to about 38.9% at the end of the period, compared with about 31.3% in 2004. This accelerated growth of the private sector investment reflects the positive response by the sector to the institutional and management reform efforts made by the state and to its incessant stimulation of, and removal of impediments to, domestic and foreign investment. It is also a consequence of the ambitious construction and development projects embarked upon by the State. Moreover, positive developments in the global oil market until mid-2008 enhanced the confidence of Saudi and foreign investors in the local investment environment and the availability of soft financing therein.

1.3 PRIVATE SECTOR

Under the Eighth Plan, the role of the private sector in the various production and service activities of the national economy grew significantly. As a consequence, its contributions to GDP, diversification of the economic base, gross fixed capital formation, provision of employment opportunities for nationals, and development of non-oil exports were enhanced.

Over the period, the value of the real GDP of the private sector increased from about SR376.7 billion in 2004 to about SR491.2 billion in 2009. As a result, its contribution to the real GDP increased from about 52.2% to about 57.4%, and the real value of investments carried out by the sector increased from about SR117.7 billion to about SR190.9 billion, which represents an annual growth rate of about 10.2%.

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Expansion of the production and investment activities of the private sector and its contribution to development under the Eighth Plan is a good indicator of its growing capabilities in finance, administration, management, and evaluation and capture of investment opportunities. It is also a result of the efforts made by the State to enhance the capacities of the private sector and create an environment conducive to its investment and various activities. Indeed, through specialized credit institutions, the State continued to provide the private sector with soft loans, in addition to providing the basic infrastructure and the well-developed industrial areas required by the activities of the sector. Moreover, the State maintained provision of basic services to the sector at supportive prices, and adopted programmes and policies aimed at raising the competitiveness of national products in domestic and foreign markets and opening new markets.

Clearly, expanding the role of the private sector in the activities of the national economy results in economic growth that is more dependent on the internal driving forces (population growth; growth of employment, productivity and incomes, growth of consumer spending and investment expenditure) and less vulnerable to external factors,

including fluctuations in world oil markets; thereby laying the foundations for firm and sustainable economic growth.

1.4 PUBLIC FINANCE

Over the first four years of the Eighth Plan, public revenues grew by about 12.7% to an average of about SR745.5 billion per annum, which represents a 90% increase over the revenues achieved in 2004.

Growth of oil revenues was the major driving force for the growth of public revenues over the first four years of the Eighth Plan. Oil revenues grew over the period by an average of about 31.4% per annum to reach an average of about SR663.7 billion per annum (Table 1.1); an increase of about 101.1% over the corresponding revenues in 2004. In consequence, the share of oil revenues in public revenues increased to about 89.3% in 2008, compared with about 84.1% in 2004.

Public expenditures also grew uninterruptedly over the period, to reach an annual average of about SR 431.5 billion over the first four years; an increase of about 51.3% compared with 2004.

It is worth noting in this context that the budget of the last year of the plan (2009), was the largest in the history of the Kingdom in terms of expenditure allocations, which totalled SR475 billion. Guided by the directives of The Custodian of the Two Holy Mosques, which were a reflection of the announcement at the G20 summit in November 2008 of the Kingdom's determination to continue implementing its investment programme, the budget allocated 47.4% of the expenditures for investment; an increase of 36% over the previous year. The budget emphasised the importance of continuing the implementation of strategic projects in education, health, infrastructure, development of economic resources, and other domains that contribute to accelerating and sustaining development and distribution of its benefits among citizens.

Table 1.1
Main Items of the State Budget
under Eighth Development Plan*

(SR billion)

Items	2004	2005	2006	2007	2008	Average for First Four Years of Eighth Plan
Total Revenues	392.3	564.3	673.7	642.8	1101.0	745.5
Oil Revenues	330	504.5	604.5	562.2	983.4	663.7
Total Expenditure	285.2	346.5	393.3	466.2	520.1	431.5
Investment Expenditure	37.6	62.3	70.9	119.0	131.2	95.9
Current Expenditure	247.6	284.2	322.4	347.2	388.9	335.6

* Actual values up to the end of the fourth year of the Eighth Development Plan.

Source: Saudi Arabian Monetary Agency.

Government investment spending continued to grow over the period of the Eighth Plan, at an annual rate of 36.7% in the first four years, with its ratio to total government spending rising from about 13.2% in 2004 to about 22.2% on average. Likewise, the ratio of government investment expenditure to total revenues increased from about 9.6% in 2004 to about 12.9% over the first four years of the plan. Within the context of reviewing the investment policy adopted by it, the Eighth Plan had stressed that it "seeks increasing the ratio of government investment expenditure to total revenues in order to ensure coping with the growing needs of the country for improved economic (physical), social and environmental infrastructure, whether to meet requirements of population growth and improve the quality of public services, or stimulate economic activity and investment in the Kingdom."

If the data on investment expenditure in the annual budgets over the period are augmented by the investment expenditure allocations within the programmes of the budget surplus for the years 2004–2006 (three stages), which amounted to a total value of SR108 billion, then average ratios of investment spending to the average value of government expenditure and government revenue in the general budget under the Eighth Plan rise to about 28.5% and 16.5%, respectively.

1.4.1 Expenditure on Development Sectors

Table 1.2 shows that under the Eighth Plan, total budget appropriations for the development sectors amounted to SR863.9 billion; an increase of about 78% compared with the total budget expenditure on these sectors under the Seventh Development Plan. Moreover, the relative distribution of budget appropriations was in line with the basic development directions of the Plan.

The largest share was that of human resources development, which was allocated about 55.6% of total expenditure on development sectors. The social services and health sector came second, with about 18%. The infrastructure sector was allocated 14.2%, while the share of the economic resources sector was about 12.2%.

Table 1.2
Government Expenditure under Seventh and Eighth Development Plans
by Development Sector

(SR billion)

Development Sector	Appropriations in Seventh Development Plan		Appropriations in Eighth Development Plan	
	Value	%	Value	%
Human Resources	276.9	57.1	480.0	55.6
Social and Health Services	92.6	19.1	155.9	18.0
Economic Resources	54.4	11.2	105.8	12.2
Infrastructure	61.4	12.6	122.2	14.2
Total	485.3	100.0	863.9	100.0

Source: Ministry of Economy and Planning.

Expenditure under the programmes and projects of the budget surplus was distributed among development sectors as shown in table 1.3.

Table 1.3
Appropriations to Development Sectors of Budget Surplus
for 2004–2006

Development Sector	SR billion	%
Human Resources	26.5	24.5
Social And Health Services	28.5	26.4
Economic Resources	26	24.1
Infrastructure	27	25.0
Total	108.0	100.0

Source: Ministry of Economy and Planning.

1.4.2 Public Debt and Government Foreign Assets

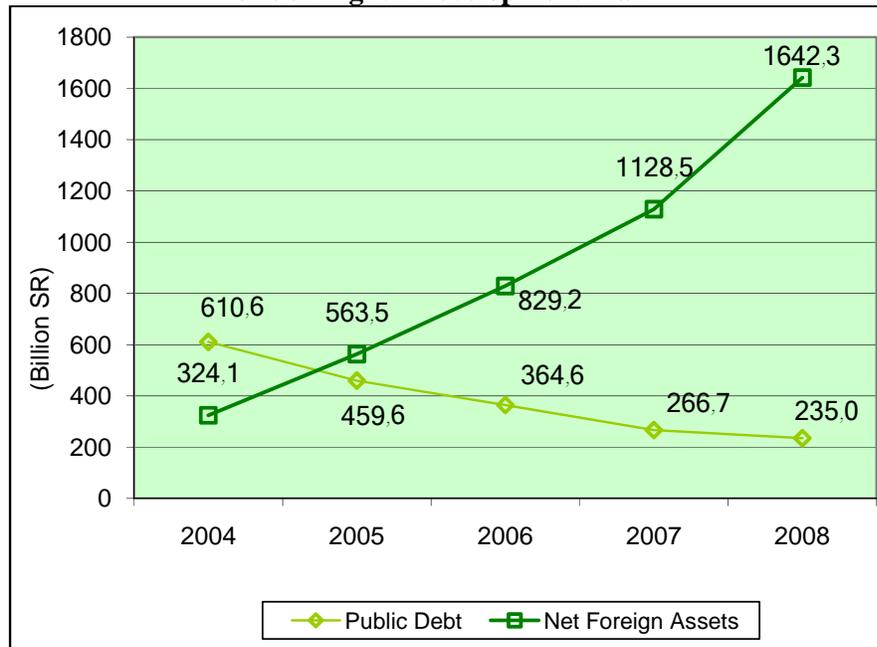
Growth of oil revenues during the period of the Eighth Plan, and the financial resources thus provided, enabled the State to accomplish two major tasks:

- Liquidation of a large part of the public debt.
- Enhancement of foreign assets owned by the government.

The State used a large part of income earned during the period of the Eighth Plan to liquidate the public debt, the total size of which decreased as a result from about SR610.6 billion at the end of 2004 to about SR235 billion by the end of 2008. Hence, its share of GDP declined from about 65% in 2004 to about 13.4% in 2008. One of the positive results of reducing the public debt is lowering the cost of servicing it, thereby freeing up part of the resources of the State, making them available for more efficient uses with high development returns.

The state invested part of the financial surpluses achieved under the Plan to enhance the net foreign assets owned by the government. These rose as a result from nearly SR324.1 billion at the end of 2004 to about SR1642.3 billion by the end of 2008 (Figure 1.1).

Figure 1.1
Public Debt and Net Foreign Assets of Government
under Eighth Development Plan*



* Up to the end of the fourth year of the Eighth Development Plan.
 Source: Saudi Arabian Monetary Agency.

The foreign assets are distributed among foreign exchange and deposits in banks abroad and investments in securities abroad, mostly in the form of government bonds. These assets support the fixed exchange rate of the Riyal against the dollar and provide support to the state finances when oil revenues decline, in addition to generating financial revenues that support both the state budget and the balance of payments.

1.5 FOREIGN TRADE AND BALANCE OF PAYMENTS

Over the period of the Eighth Development Plan, Saudi foreign trade underwent notable quantitative and qualitative developments. These enhanced the significant role played by trade in the national economy, through penetration into foreign markets able to absorb Saudi oil and non-oil products, and provision by these markets of the consumer, capital, and intermediate goods and the advanced techniques required for production and investment processes and implementation of

development projects. The total value of exports and imports of goods and services rose by an annual average of 26.2% over the first four years of the plan. As a result, the ratio of foreign trade flows to GDP at current prices rose from about 78.6% in 2004 to approximately 106.5% in 2008. Accession by the Kingdom to the WTO in December 2005 is an important step towards increasing the degree of openness of the Saudi economy and its integration into the global economy.

The period under consideration also witnessed several positive developments in terms of the structure of merchandise imports and exports. Non-oil exports grew at an annual rate of about 20.3% in the first four years of the plan, rising from about SR58.2 billion in 2004 to about SR121.8 billion in 2008. At the forefront of growth of exports were exports of petrochemicals, plastics and re-exported goods.

Exports of crude oil and refined petroleum products rose in value from about SR414.2 billion in 2004 to about SR1053.7 billion in 2008; an overall increase of 154.4%.

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As for imports, there was an important structural development represented by an increase in the relative importance of imports of machinery, equipment and intermediate goods, in response to the accelerating pace of economic growth and efforts to diversify the economic base. The percentage of these imports to total imports rose from about 61.7% in 2004 to about 70.4% in 2008.

Moreover, the relative share of imports of consumer goods declined from about 38.3% in 2004 to about 29.6% in 2008, which indicates improved competitiveness of national products and their growing role in meeting domestic consumer demand.

The favourable developments in both exports and imports, particularly the upward trend in the value of oil exports, resulted in a significant increase in the surplus of the balance of trade over the first four years of the Eighth Plan, the value of which went up from about SR308.3 billion 2004 to about SR795 billion in 2008; a total increase of about 157.9%. This, in turn, contributed to enhancing the current account of

the balance of payments, which maintained a surplus that increased in value from about SR184.8 billion in 2004 to about SR502.7 billion in 2008; a total increase amounting to some 172%. The latter surplus was achieved despite persistent deficits in the balance of “services and transfers”, due to the growth of private sector services payments, mostly for international freight and insurance, and government services payments, which together accounted for approximately 51.8% of the total payments in that balance.

On the other hand, private transfers, mostly remittances by foreign workers, accounted on average for about 93.4% of total transfers over the first four years of the Eighth Plan.

1.6 HUMAN RESOURCES DEVELOPMENT AND EMPLOYMENT

The Eighth Development Plan attached a great deal of importance to human resources development as fundamental to comprehensive development, aiming to raise total labour force participation rates, continuously upgrade its skills and develop its capacities, and provide it with opportunities for gainful employment, particularly in the various activities of the private sector. The plan incorporated several programmes and policies aimed at achieving qualitative and quantitative expansion of education and vocational training; giving priority in employment to the national workforce; and addressing macroeconomic and structural imbalances in the labour market, especially youth unemployment and reliance on foreign labour.

The efforts made under the Eighth Plan resulted in an increase of national employment by a total of around 18.7%, from about 3.3 million workers in 2004 to about 3.9 million 2009. Over the same period, the ratio of employment of nationals to total employment rose to nearly 47.9% in 2009, compared with 45.9% in 2004.

Table 1.4 provides details of the contributions of various economic sectors to the provision of employment opportunities to nationals over the period of the Eighth Plan.

Table 1.4
Contributions of Major Sectors of National Economy
in Provision of Employment Opportunities to National Labour
Eighth Development Plan

Sector	2004		2009		Average Annual Growth %
	Number of employees*	Contribution %	Number of employees*	Contribution %	
1. Non-Oil Sector					
a. Production Sectors	278.24	8.4	413.71	10.6	8.3
b. Private Service Sectors	2074.48	63.0	2392.49	61.1	2.9
c. Government Sector	878.85	26.6	1048.64	26.8	3.6
2. Oil and Gas Sector	66.61	2.0	59.74	1.5	(-2.2)
Total for national economy	3298.18	100.0	3914.58	100.0	3.5

* Number of employees is in thousands, and data for 2009 is preliminary.

Source: Ministry of Economy and Planning.

According to data presented in the table, non-oil production sectors achieved the largest expansion of employment opportunities for national labour, with the number of Saudis working in these sectors rising at an annual rate of 8.3%, which led to an increase of their relative contribution to employment of nationals from 8.4% in 2004 to 10.6% in 2009. The number of Saudis working in the government sector increased at an annual rate of 3.6% and its relative contribution to employment of nationals increasing over the period from 26.6% to 26.8%. Thus, the combined share of the production sectors and the government sector of employment of nationals increased to about 37.4% in 2009, compared with about 35% in 2004. In contrast, the relative contributions of the private service sectors and the oil and gas sector to employment of nationals declined over the period, as a result of the rates of growth of the numbers of Saudis working in them being less than the overall average of 3.5%. For the private service sectors, this rate was about 2.9%, leading to their share in the employment of nationals declining from 63% in 2004 to 61.1% in 2009; while in the oil and gas sector, there was decline at a rate of about 2.2% per annum, leading to its share declining over the period from 2% to 1.5%.

1.7 THE FINANCIAL SECTOR

1.7.1 Banks

The banking sector performed well under the Eighth Plan, benefiting from the high level of activity in the local economy, particularly private sector activity, as well as from good management by banks of their financial resources. The good performance of the banks was reflected in expansion of activity, as well as in enhancement of their financial position.

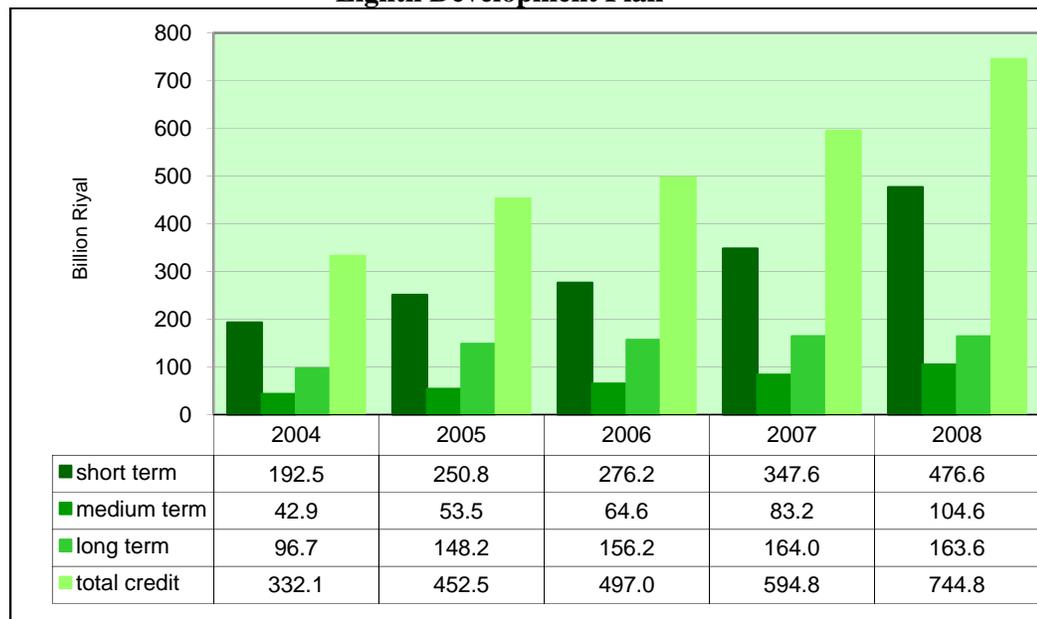
Over the period, the number of operating commercial banks increased to nineteen, and the number of bank branches, including branches of foreign and Gulf banks, to 1410. Moreover, during the period (2006–2008), ten international banks, established branches in the Kingdom, leading to increased competition in this sector. Similarly, following accession by the Kingdom to the WTO, investment banks witnessed a remarkable growth, as the competent authorities issued licenses to about 80 investment banks, mostly Saudi- foreign joint ventures.

Moreover, the financial positions of commercial banks strengthened significantly. Over the first four years of the plan, their total assets grew at an average of 98.7%. Likewise, the investment funds, managed by commercial banks, expanded their activities, with their total assets growing by about 24% over the same period.

Performance indicators of the banking sector, based on international standards, improved significantly. Capital adequacy ratio, measured by the ratio of capital to total risk-weighted assets, was stable at an excellent level, averaging about 19.1% over the first four years of the Plan, which exceeds the international rate of 12%, the standard set by Basel 2. The banks also continued to expand introduction and intensified use of modern banking technology, and they have become able to offer comprehensive banking services using most modern technology.

Furthermore, commercial banks played a vital role in expanding the resources available to the private sector, as well as in expanding its activities. Total liabilities of the private sector to the banks (loans and advances, discounted bills, and investments in securities) grew over the first four years of the Plan by a total of around 134%, representing about 75.2% of the total liabilities to the banks in 2008. In the same year, bank credit to the private sector amounted to about 96% of the total credit granted to all sectors. In addition, over the first four years of the Plan, total “medium-term” and “long-term” credit accounted for about 36% of total bank credit provided (Figure 1.2).

Figure 1.2
Distribution of Bank Credit by Maturity
Eighth Development Plan*



* Up to the end of the fourth year of the Eighth Development Plan.

Source: Saudi Arabian Monetary Agency.

1.7.2 Saudi Banks and the Global Financial Crisis

Despite the repercussions of the global financial crisis which adversely affected many international banks and financial institutions, the Saudi financial system was able to maintain its soundness, as commercial banks maintained normal levels of liquidity and high net worth; thereby continuing to achieve high performance and profitability rates.

In support of the Saudi banking sector during the global financial crisis, the Supreme Economic Council declared, right at the outset, that the government would continue to underwrite deposits and ensure the safety of the banking system. Furthermore, the Council directed the Saudi Arabian Monetary Agency to continue to monitor the performance of Saudi banks and provide them with the necessary liquidity. Guided by this directive, the Agency took a series of measures aimed at easing restrictions on banks in order to increase their capacity to lend, as well as enhancing their liquidity levels, and verifying their compliance with banking safety standards.

Over the past decades, the Agency has followed make strict policies towards banks aiming at introducing international best practices to the Saudi financial system. It established numerous rules, regulations and instructions that in total formed an effective risk management framework, ensuring adherence to the standards of capital adequacy, concentration of credit, liquidity management, classification of loans and allocations, operational and market risks, international accounting standards, and internal and external auditing. In addition, the Agency was keen to review processes of credit risk management to branches of foreign banks operating in the Kingdom according to Basel 2 standards. It also stepped up supervision and control over the banks after the crisis, as well as intensifying the measures aimed at boosting liquidity and strengthening the lending capacity of the banks.

1.7.3 Specialized Lending Institutions

Under the Eighth Plan, specialized lending institutions continued to perform their developmental role. Through providing soft loans to citizens, private sector institutions and the public, they supported development of the industrial and agricultural sectors, all branches of the service sector, and the real estate sector, particularly housing, as well as enhancing urban development to meet requirements of economic and population growth.

The state expanded the financing capacity of the specialized lending institutions by increasing their capital by SR81 billion from budget

surpluses for 2004 and 2005. The increases were as follows:

- Public Investment Fund SR 20 billion
- Real Estate Development Fund SR43 billion
- Industrial Development Fund SR 13 billion
- Saudi Credit and Saving Bank SR5 billion, in addition to the deposit of SR10 billion from the Budget.

As a result of the increase in the capital of the specialized lending funds, total lending by them to the private sector and to public institutions increased significantly over the first four years of the Eighth Plan. Outstanding loans were SR155.2 billion in 2008; an increase of about 30.3%, compared with about SR119.1 billion in 2004. This remarkable growth in funding provided by these institutions was in response to the emphasis by the Eighth Development Plan on accelerating the pace of economic growth and improving living standards.

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1.7.4 Domestic Liquidity

Money supply (in broad M3 terms), which consists of currency circulated outside banks and bank deposits of all types and maturities, grew by about 17% on average over the first four years of the Eighth Plan. Growing over that period by about 28.1% per annum on average, time and savings deposits were the fastest growing component of the money supply (M3), accounting for about 39.6% of total money supply. In contrast, demand deposits grew annually by around 12.9% on average, constituting about 36.9% of total money supply (M3), while currency in circulation outside banks and other quasi-monetary deposits grew by about 8.4% and 11.5% on average per annum, respectively, accounting together for about 23.5%.

Growth of the money supply over the period of the Eighth Plan is attributable in the first place to the remarkable growth in both government expenditure and credit facilities provided by commercial banks to the public and private sectors.

1.7.5 Saudi Financial Market

Given its important role in financing development and enhancing the role of the private sector, by providing investment channels that contribute to attracting domestic and foreign capital and enhance opportunities for expansion of national companies, the Saudi Financial Market received great care and attention from the State. Over the period of the Eighth Development Plan, the Capital Market Authority continued preparing, issuing and developing the executive regulations necessary for regulating the market. In 2006, it issued several regulations, including the Real Estate Investment Funds Regulation, the Corporate Governance Regulation, the Investment Funds Regulation; and in 2007, it issued the Mergers and Acquisitions regulation.

During the period from 2005 to 2008, investors from 20 Arab and foreign countries entered the Saudi stock market, either with direct investments or in partnership with Saudi capital, to set up securities businesses, practice stock market activities through provision of technical advice to investors, portfolio management, and sale and purchase of shares on their behalf.

The estimated share of foreign capital in the securities firms in the Saudi stock market in 2008 was about 22.4%, with a total value of about SR2.55 billion while the estimated share of the capital of Saudi companies and individuals was about 77.6%, with a total value of SR8.85 billion.

In general, the performance of the Saudi stock market over the period of the Eighth Plan was strong. The number of companies that went public nearly doubled, and the total number of companies listed in the market rose from 73 in 2004 to 127 in 2008; an overall increase of about 74%. Moreover, the number of traded shares increased from 10,298 million by the end of 2004 to 58,727 million by the end of 2008, and their value rose over the same period from SR1,773.9 to SR1,962.9 billion.

Despite the remarkable activity in the Saudi stock market, speculative pressures and market attempts for self correction, as well as the global financial crisis, led to a decline in the general share price index from about 8,206.2 points at the end 2004 to approximately 4,803 points at the end of 2008, while market capitalization (market value of issued shares) decreased over the same period from about SR1,149 billion to about SR924 billion.

The magnitude, depth and efficiency of the Saudi market become clear when compared with the fifteen Arab stock markets covered by the database of the Arab Monetary Fund. By the end of December 2008:

- The market value of the issued shares (market capitalization) in the Saudi stock market was about 6.6 times the average market value of issued shares in the other Arab stock markets.
- The Saudi stock market ranked first among Arab markets, with the value of shares traded in it amounting to around 110.3% of the total value of shares traded in these other markets.
- The average share turnover in the Saudi market was about 212.3%, compared with an average of about 61.8% for the other Arab markets, which testifies to the higher efficiency of the Saudi stock market.
- The Saudi stock market was in a leading position among Arab stock markets listed in the database of the Arab Monetary Fund in terms of degree of market depth, which amounted to about 53% for the Saudi market, compared with an average of 51.4% for the other Arab stock markets.

1.8 PRICES OF GOODS AND SERVICES

The cost of living index is the most commonly used measure of inflation in the Kingdom. It monitors prices of 406 commodities and services, assembled in eight main groups, namely: food and beverages; textiles, clothing and footwear; renovation, rent, fuel, and water; home furnishings; medical care; transport and communications; education and recreation; and other goods and services.

Inflationary trends began in 2006, when the inflation rate was about 2.2%. Price rises were concentrated in three major groups of commodities: food and beverages; renovation, rent, fuel, and water; and other goods and services; with rises of about 5.4%, 3.1%, 7.7%, respectively, compared with the end of 2005. Over the following years, the rate of inflation continued to rise to about 4.1% in 2007 and about 9.9% in 2008. As in 2006, price rises over the 2007–2008 were mainly concentrated in food and beverages, with an annual rate of increase of about 10.5%; renovation, rent, fuel and water, with 12.7%; and other goods and services, with 8%.

Inflationary trends emerged in the last three years of the Eighth Plan, as a result of a combination of factors, including:

- Growth of aggregate demand for goods and services at high rates, driven up by the large size of government spending, which was boosted by surging oil revenues; as well as by the large volume of private spending, financed to a large extent by bank credit.
- Drought conditions and their negative impact on the overall supply of locally produced agricultural commodities.
- Shortage of supply of residential units causing rent rises.
- Shortage of supply of skilled labour at a time of growing demand, which led to higher wages.
- Global prices for agricultural products rising to unprecedented levels.
- The low exchange rate of the Riyal against major currencies (except the U.S. dollar), raising the cost of imports from several European countries and Japan, particularly with the gradual shift in the structure of imports to these markets at the expense of imports from the United States.
- The high shipping and insurance at cost.

In an effort by government to fight inflation and to contain its negative effects, especially on citizens with low and limited incomes, the Council of Ministers issued resolution No. 11 of January 2008, which involved an integrated package of policies and urgent measures designed to fight inflation, including:

1. Adding a 5% cost of living allowance to salaries of state employees for three years.
2. Increasing social security benefits by 10%.
3. The State bearing for three years 50% of fees for passports, driving licences, transfer of ownership, and renewal of residence permits of household labour.
4. Continued subsidy for commodities to mitigate high prices, and reviewing this after three years.
5. Intensifying efforts to monitor prices and combat commercial fraud.
6. Expediting the draft policy on supply of foodstuff.
7. Accelerating the activation of the General Housing Authority and enabling it to carry out its tasks.
8. Accelerating construction of public housing, especially following the appropriation of SR 10 billion for it.
9. Expediting the issuance of mortgage law and associated regulations.
10. Preventing all monopolistic practices and reviewing the system of commercial agencies to guard against monopoly and promote competition.

The above measures contributed to the alleviation of inflationary pressures and their impact on citizens, as did the subsequent Council of Ministers resolution No. 89 of 2008, which reduced customs tariffs on 180 goods, including numerous foodstuff and other commodities. Inflation pressures then began to ease as of July 2008 for two main reasons: first, the fall in imported inflation, and secondly some measures to combat inflation, which had already been taken by the State, began to take effect fully, particularly the monetary policy measures taken by the Saudi Arabian Monetary Agency to limit growth of domestic liquidity. Thus, the inflation rate dropped to about 4.1% over the period from August 2008 to August 2009, and forecasts indicate continuing decline in the coming period.