<u>Saudi Arabia on RECHARGE</u>

There are eight, equally important reasons for investors to be bullish about Saudi Arabia. RECHARGE, an acronym, adequately sums up the key initiatives and current dynamics which are reshaping the largest economy across the Middle East and North Africa. The Kingdom is leading the region from the front and has surprised those who were skeptical about the pace at which the country is transforming itself. As with any major transformation, Saudi Arabia offers multiple opportunities to both domestic and foreign investors to capitalize from this RECHARGE.

(R) - Reforms

Under the leadership of the Crown Prince Mohammed bin Salman, Saudi Arabia has been at the forefront in undertaking major reforms to rejuvenate and diversify its economy, and most significantly, away from oil. As far as the economy is concerned, reforms relating to opening up the entertainment sector, allowing women to drive and implementing measures to boost both religious and non-religious tourism will likely have an immediate impact. Additionally, the pace at which capital market reforms have been undertaken, and which eventually led to the inclusion of the benchmark Emerging Market Index by both FTSE and MSCI, have boosted investors' confidence on the seriousness and ability to carry out structural reforms.

(E) - Embrace

Running in parallel to the national reforms above, there has been a focus on embracing investors and encouraging them to invest in the Kingdom with a long view, through both foreign direct investment (FDI) and Foreign Institutional Investment (FII) route. While actual FDI inflow usually takes a while to accelerate as opportunities, for example, in significant projects such as NEOM or in entertainment such as cinemas materialise, we have already seen a significant jump in the number of Qualified Foreign Investors (QFIs) obtaining license to invest directly in the Kingdom's capital markets. Further, the government is also incentivizing domestic private investors through favorable regulations and creating specialized funds to become more involved in the economic opportunities in the Kingdom.

(C) - Corruption clampdown

The current regime has made it clear that no one is above the law, and there is zero tolerance towards corruption and leakages within the system. This effectively implies a more efficient and transparent way of functioning and should improve the ease of doing business.

(H) - Higher disposable income for citizens

Contrary to popular belief, citizens in Saudi Arabia (particularly in lower income households) are actually better off financially now than they were previously. Creation of Citizen's account will enable SAR 32bn to be credited to households in 2018 through monthly instalments based on income levels, as well as a one–off payment of SAR 50bn has been provided to public sector employees in 2018 to cover the cost of a living allowance. During the first quarter of 2018, compensation to employees and social benefits jumped by SAR 31bn year-on-year, while government income from VAT, excise duties and gasoline (borne by citizens and expatriates), was only SAR 17bn higher year-on-year. Accordingly, the focus has been on ensuring that the disposable income of citizens is not affected due to rising inflation from taxes and lower subsidies. Social benefit distribution, through the Citizen's Account, is an excellent way of compensating the most vulnerable people in society. However, expats will be hit hard, with many of them leaving the country for good or sending their families back, but government's near term priority will ideally be towards its citizens.

(A) - Accelerated Capex

The Kingdom has embarked on an expansionary budget in 2018 to kick start the economy. Proposed capex spending, including contributions from the Public Investment Fund and The National Development Fund to support key infrastructure projects and the private sector, is 88% higher year on year, at SAR 338bn. Despite a slow start to spending in 2018, capex is likely to pick up considerably in 2H18.

(R) - Road map

Having launched Vision 2030 and a more focused National Transformation Program (NTP) 2020, the Saudi government has provided a clear road map for its ministries, citizens and investors on where it wants to be and how it intends to get there. Several sweeping reforms are being undertaken as part of this road map resulting in many structural changes. Although there will be challenges and setbacks, continuous guidance and leadership will ensure that the economic and socio-cultural transformation of Saudi Arabia maintains pace and progress, with the ultimate aim of benefiting it in the medium to long term.

(G) - GDP Growth

Oil remains the single largest enabler and driver of Saudi Arabia's GDP contributing c.45% of the output, and also accounts for the bulk of government revenues. While non-oil revenues will also show strong YoY growth led by income from taxes and lower subsidies, the current oil price above USD 70 will significantly boost government revenues, which can provide the government more flexibility to boost consumption and capital expenditure. The International Monetary Fund has already revised Saudi Arabia's GDP growth forecast for 2018 upwards from 1.1% in October 2017 to 1.9% now while the Saudi government's own forecast is 2.7%. This marks significant progress from the 0.8% GDP decline in 2017.

(E) - Employment opportunities

With unemployment levels close to 13%, one of the top priorities for the government is to create employment opportunities for its citizens. Measures such as 'Saudisation', the regulatory push under the revamped Nitaqat system, and incentives under the Human Resource Development Fund are all being taken to address this issue. Accordingly, more jobs for citizens will ensure economic prosperity is inclusive and empowering.

However, as with every economy in the middle of structural changes of such magnitude and executing reforms swiftly, there are and will be challenges for the government to address and overcome. For instance, Saudi government's stringent Saudisation ratio of 100% on specific sectors has affected Small and medium enterprises (SME) operations and it is now seem to be considering to lower this ratio to 70%. However, as unemployment levels continue to remain c.13%, the challenge will be to find a practical solution to employing nationals without a major impact on the companies, especially the SME segment. Further, FDI's has taken a hit in 2017, according to the latest UN Conference on Trade and Development (UNCTAD) World Investment Report, foreign direct investment (FDI) into Saudi Arabia last year amounted to only USD 1.4bn, down from USD 7.5bn (2016) and as much as USD 12.2bn in 2012.

Accordingly, although, the country is in a sweet spot to grow, reform and deliver results to its stakeholders there is no denying on the real practical challenges on the ground, accordingly a lot also depends on the government's willingness to listen to feedback from stakeholders and revisit measures, wherever required, which it seems to be doing.