Saudi Arabia

Non-oil economic growth decelerated in 2023 though remained robust at 3.8% (private sector +4.4%) as consumption expenditure proved resilient. We project non-oil growth to be broadly steady in 2024 (+3.7%) then potentially accelerate in 2025 helped by lower interest rates. Budget deficits in 2024-2025 should be limited given higher dividends from Aramco and a modest rise in government spending. The main upside risk is higher-than-forecast oil production in 2024-2025 while the major downside risk is a weaker-than-expected non-oil expansion that may be triggered by the projected deceleration in government spending growth and/or pressure from ongoing elevated interest rates.

Non-oil private sector growth to accelerate in 2025

Despite higher interest rates, non-oil economic growth remained robust in 2023, softening to 3.8% from 5.3% in 2022. The private sector continued to be the growth driver, although its expansion moderated to 4.4% in 2023 from a strong 5.6% in 2022. Sector-wise, trade, restaurants, and hotels contributed the most to GDP growth, expanding by 7% in 2023, supported by the strong focus on boosting tourism, both inbound as well as domestic. In terms of expenditure on GDP, private-sector investment continued to be the fastest growing, although it decelerated sharply to 6.2% in 2023 from a very strong 22% average in 2021-2022.

We expect the constructive macroeconomic dynamics to be sustained in 2024 and potentially accelerate in 2025 as the impact of lower interest rates starts to kick in. Consumer spending remains resilient, with the value of POS transactions up around 10% y/y through mid-April, in line with the increase recorded in 2023. Despite ongoing tight liquidity in the banking sector, credit growth (+11% y/y through February) remains buoyant, even showing signs of strengthening in the first months of 2024, driven by corporate credit (+15%). The PMI continues to be favorable (averaging 56.5 in Q1), and while it hit a recent low in January, has improved driven by the important sub-indices of output and new orders. We forecast the non-oil sector to grow by a broadly steady 3.7% in 2024 and then by 4.2% in 2025, driven by private sector gains of 4.5% and 5%, respectively.

This positive outlook is supported by the government's effective policymaking and the upgrade to the projected spending levels for 2024-2025 in the latest budget. There are challenges along the way, however. For example, given that government spending soared by an average of 12% in each of the past two years, the spending intensity is set to slow in 2024-2025, which could weigh on non-oil activity. In addition, given some stalling in the US disinflation progress so far this year, the cut in interest rates is being pushed out to late 2024, keeping Saudi interbank rates, and hence the cost of borrowing elevated, which is not supportive for non-oil activity this year. Consequently, the tailwind of lower interest rates (Saudi policy rates usually move together with US rates) will be mostly a story for 2025. Another key metric to monitor is foreign direct investment (given that higher investment levels are crucial to achieve Vision 2030 targets), which, after rising strongly in 2021-2022, dropped in 2023 to stand at 1.8% of GDP compared with a 5.7% target for 2030.

As for the oil sector, growth was negative in 2023 (-9%) given the production cuts, which deepened around the middle of that year. Given our house view on oil market dynamics, Saudi oil production is expected to remain at current levels throughout 2024 and increase only gradually next year, translating into oil GDP growth of -5.2% and +3.7%, respectively. However, KSA will likely continue to take a very proactive and nimble role in managing global oil supply, which could result in a steep deviation from our oil production assumptions for 2024-2025. All in all, total GDP is forecast to increase by a limited 1.2% in 2024, pressured by the oil sector, then grow by a stronger 4.2% in 2025 as oil GDP growth turns positive and non-oil growth strengthens.

Inflation to soften further; unemployment at a record low

Inflation (which remained relatively low, driven by subsidies, price caps, and strong competition) continued to soften, standing at 1.6% y/y through March, with housing rentals (+10.5% y/y) almost the sole driver of price pressures over the past year. Despite ongoing hot housing rentals, we project average inflation to continue softening, standing at 1.8% and 2% in 2024-2025, down from 2.3% in 2023. Solid non-oil growth and ongoing Saudization initiatives dropped the unemployment rate among Saudis to an all-time low of 7.7% at the end of 2023, down from 8% one year before, and a stone's throw from the 7% target set for 2030.

Manageable fiscal deficits; higher oil GDP upside risk

An 11% increase in spending in 2023, a 12% drop in oil revenues but a 11% rise in non-oil revenues resulted in a fiscal deficit of 2% of GDP. We project limited deficits of 1.7%-2% of GDP in 2024-2025, as government spending (which will likely continue to exceed budget) rises modestly, oil revenues increase on higher dividends from Aramco, and non-oil revenues continue growing, fueled by an expanding non-oil sector. Hence, debt levels should remain contained, below 27% of GDP by 2025. The main upside risk is higher-than-forecast oil production, leading to stronger GDP growth. The major downside risk is a weaker-than-expected non-oil expansion that may be triggered by the projected deceleration in government spending growth and/or pressure from ongoing elevated interest rates.

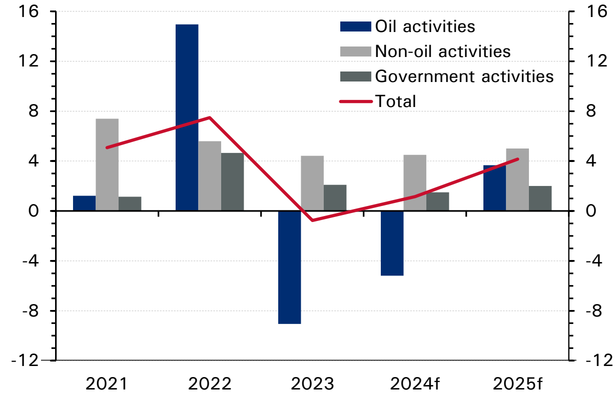
Table 1: Key economic indicators

		2022	2023	2024f	2025f
Nominal GDP	$ bn	1,109	1,068	1,102	1,164
Real GDP	% y/y	7.5	-0.8	1.2	4.2
- Oil	% y/y	15.0	-9.0	-5.2	3.7
- Non-oil	% y/y	5.3	3.8	3.7	4.2
Inflation (average)	% y/y	2.5	2.3	1.8	2.0
Fiscal balance	% of GDP	2.5	-2.0	-1.7	-2.0
Government debt	% of GDP	23.8	26.2	27.0	26.9
Current account	% of GDP	13.7	3.2	2.4	2.4

Source: Official sources, NBK forecasts

Chart 1: Real GDP growth

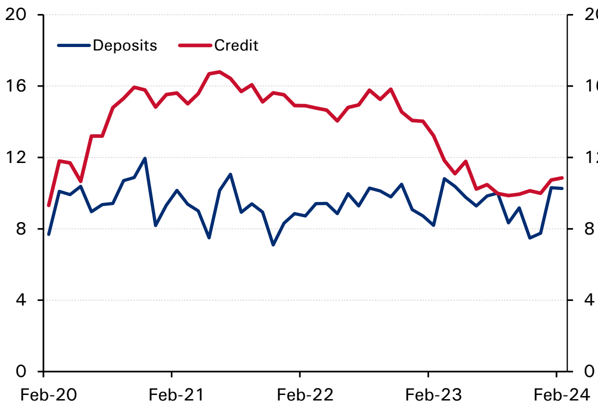
(% y/y)



Source: General Authority for Statistics (GASTAT), NBK forecasts

Chart 2: Credit and deposit growth

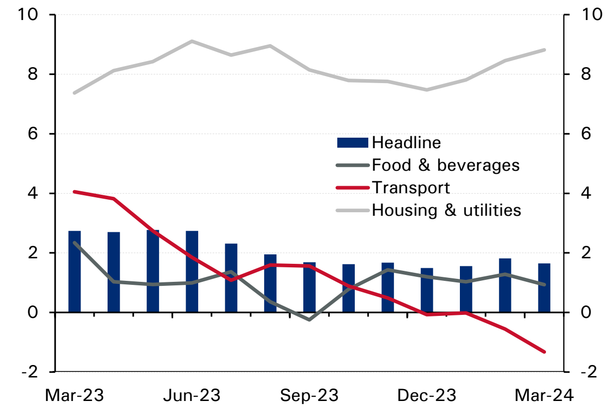
(% y/y)



Source: SAMA

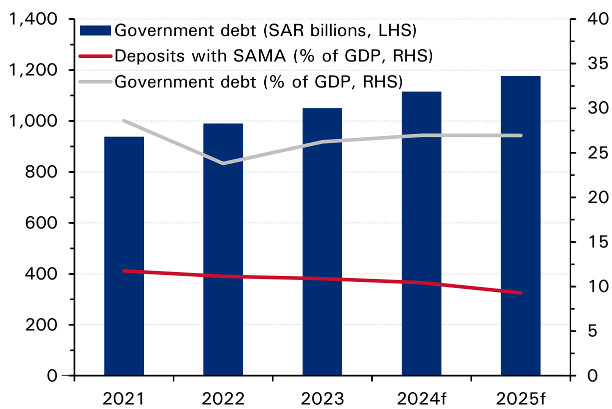
Chart 3: CPI inflation

(% y/y)



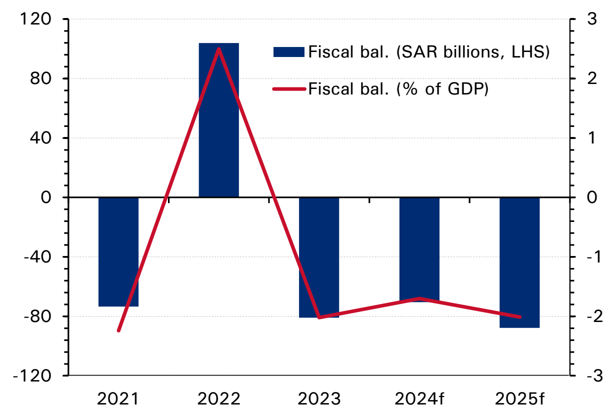
Source: GASTAT

Chart 4: Government debt and deposits with SAMA



Source: GASTAT, Ministry of Finance, SAMA, NBK forecasts

Chart 5: Fiscal balance



Source: Ministry of Finance, NBK forecasts