IMF Country Reports 23/323

Saudi Arabia: 2023 Article IV Consultation-Press Release; Staff Report; and Informational Annex

INTERNATIONAL MONETARY FUND

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IMF Country Report No. 23/323

SAUDI ARABIA

September 2023

2023 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND INFORMATIONAL ANNEX

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2023 Article IV consultation with Saudi Arabia, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its July 20, 2023, consideration of the staff report that concluded the Article IV consultation with Saudi Arabia.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 20, 2023, following discussions that ended on May 28, 2023, with the officials of Saudi Arabia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 7, 2023.
- An **Informational Annex** prepared by the IMF staff.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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International Monetary Fund
Washington, D.C.

IMF Executive Board Concludes 2023 Article IV Consultation with Saudi Arabia

FOR IMMEDIATE RELEASE

Washington, DC – September 6, 2023: On July 20, 2023, the Executive Board of the International Monetary Fund (IMF) concluded the 2023 Article IV consultation[1] with Saudi Arabia.

Saudi Arabia was the fastest growing G20 economy in 2022. Overall growth reached 8.7 percent, reflecting both strong oil production and a 4.8 percent non-oil GDP growth driven by robust private consumption and non-oil private investment, including giga projects. Wholesale, retail trade, construction, and transport were the main drivers of non-oil growth. The output gap is estimated to have closed during 2022, with the non-oil growth momentum continuing in 2023.

The Saudi unemployment rate is at a historical low. Amid an increase in labor force participation, total unemployment dropped to 4.8 percent by end-2022—from 9 percent during Covid—reflecting both an increase in Saudi workers in the private sector and expatriate workers (mostly in the construction and agricultural sectors) rising back above pre-Covid levels. Youth unemployment was halved to 16.8 percent in 2022 over the past two years while female participation in the labor force reached 36 percent in 2022, exceeding the 30 percent target set under the authorities' Vision 2030 reform agenda.

Despite a booming economic activity, inflation remains low and appears to be easing. Average CPI grew by 2.5 percent y-o-y in 2022, in part contained by domestic subsidies/price cap and a strong US dollar. Despite an uptick in early 2023 to 3.4 percent y-o-y, headline inflation is back at 2.8 percent y-o-y in May 2023, as declining contributions from transport and food prices offset the substantial increase in rent.

The banking system remains on a strong footing. The aggregate capital adequacy ratio is strong, profitability—driven by net interest margins—is high and above pre-pandemic levels, and the NPL ratio is low and declining. While growth in mortgages has recently moderated, demand for project-related and consumer loans remains strong, helping offset the impact on profitability from rising funding costs linked to higher interest rates and a greater share of time and saving deposits in banks' liabilities.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

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Favorable oil market dynamics strengthened the fiscal position, with turned to a 2.5 percent of GDP surplus—the first since 2013. The surplus would have been higher, if not for additional spending that was not initially budgeted for. This mostly reflect increases in goods and services and capital spending. About 2½ percent of GDP of additional expenditures were estimated to be one-off non-recurrent spending (about half in goods and services). At 23 percent of GDP public debt is low and sustainable, with ample fiscal space available to address potential headwinds.

Higher oil prices and stepped-up oil production improved the current account to a 10-year high surplus in 2022. However, the 13.6 percent of GDP surplus did not lead to a corresponding increase in official reserves in view of the large accumulation of assets abroad, albeit these remain at comfortable levels (almost 20-month import cover).

Risks to the outlook are balanced. On the upside, higher oil prices—as expectations of strong oil demand for the rest of the year persist—possible change in OPEC+ oil production cuts and accelerated structural reforms and investment could spur growth. Conversely, too rapid a rise in non-oil investment could further raise domestic demand, thereby adding pressure on prices and external accounts. On the downside, lower oil prices due to subdued global activity represent a key short-term risk while a quicker shift in demand for fossil fuel could hamper growth in the medium to long term.

Executive Board Assessment[2]

Executive Directors agreed with the thrust of the staff appraisal. They welcomed Saudi Arabia's ongoing economic transformation, supported by commendable reforms under the Vision 2030 agenda and higher oil prices, which has helped create high growth, record low unemployment, contained inflation, and strong external and fiscal buffers, while reducing reliance on oil. Directors noted that risks to the positive outlook are balanced, but that contingency measures, such as tighter fiscal policy, should be considered if demand pressures materialize.

Directors welcomed the impressive non-oil revenue mobilization efforts already initiated which have resulted in doubling non-oil revenues since 2017 and called for additional fiscal adjustment over the medium term which would allow Saudi Arabia to maintain stronger buffers and meet intergenerational needs while mitigating risks from oil price volatility. To support such a strategy, Directors called for additional non-oil revenue efforts, including by maintaining the VAT rate. Most Directors recommended faster increases in energy prices to reduce subsidies, although a few Directors called for continuing the gradual implementation articulated in the Vision 2030 road map. Directors agreed that energy subsidy reforms should

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summing ups can be found here: https://www.imf.org/external/np/sec/misc/qualifiers.htm

be accompanied by scaling up well-targeted social programs to limit the impact on the most vulnerable. They also emphasized the importance of the ongoing rollout of the Medium-Term Fiscal Framework and enhanced disclosure which would support the implementation of a fiscal rule and help delink spending decisions from oil price fluctuations. Directors welcomed the ongoing work on a Sovereign Asset Liability Management Framework and called for its quick completion.

Directors agreed that the exchange rate peg continues to serve the country well. They noted that the monetary policy framework should continue to use market-based instruments to align the interbank rate with the policy rate, which should continue to move in line with the Fed's policy rate.

Directors agreed that the banking sector remains on a strong footing. They welcomed ongoing efforts to modernize the regulatory and supervisory frameworks and recommended maintaining vigilance and considering a gradual tightening in macroprudential guidelines/regulations and phasing out of fiscal incentives in the case of persistently elevated credit growth.

Directors noted the significant progress made in implementing Saudi Arabia's structural reform agenda. In particular, they welcomed the marked improvement in female labor force participation and improvements in regulatory and business environment, which have contributed to higher private sector investment, and encouraged building on this positive progress. They called for careful calibration of investment programs to ensure catalytic effects are in place and avoid private sector crowding out. Directors agreed that the authorities' industrial policy agenda should be supporting these structural reform efforts while minimizing associated risks. They welcomed the progress made to strengthen governance and emphasized the importance of ongoing actions and called for these efforts to be accelerated.

Directors welcomed Saudi Arabia's Green Initiative, whose implementation will be essential to meet the net emissions reduction target with minimal losses. They welcomed staff's assessment that even in a transition scenario where all countries implement their National Determined Contributions (NDC), the impact on the Saudi economy is expected to be limited. Directors looked forward to the elaboration of specific programs and investments related to each goal. Directors commended the enhancements in economic data, which should continue. Directors looked forward to Saudi Arabia's continued leadership in addressing global challenges.

It is expected that the next Article IV Consultation with Saudi Arabia will be held on the standard 12-month cycle.

Saudi Arabia: Selected Economic Indicators, 2021-24

Population: 32.2 million (2022)

Quota: SDR 9,992.6 million (2.10% of total)

Main products and exports: Oil and oil products (79.5%)

Key export markets: Asia, U.S., and Europe

	2021	Est. 2022	Proj. 2023	Proj. 2024
Output				
Real GDP growth	3.9	8.7	1.9	2.8
Non-oil real GDP growth	5.7	4.8	4.9	4.4
Prices				
CPI Inflation (avg, %)	3.1	2.5	2.8	2.3
Central government finances				
Revenue (% GDP)	29.6	30.7	28.4	28.4
Expenditure (% GDP)	31.9	28.2	29.7	30.0
Fiscal balance (% GDP)	-2.3	2.5	-1.2	-1.6
Public debt (% GDP)	28.8	23.8	25.1	25.8
Non-exported oil primary balance (% Non-oil GDP)	-27.2	-29.6	-23.7	-21.4
Money and credit				
Broad money (% change)	7.4	8.1	8.0	6.3
Credit to the private sector (% change)	15.4	12.6	9.6	9.5
Balance of payments				
Current account (% GDP)	5.1	13.6	6.5	3.5
FDI (% GDP)	2.2	0.7	0.7	0.8
Reserves (months imports)[1]	20.3	19.4	17.5	15.7
External debt (% GDP)	31.7	23.9	24.9	26.1
Exchange rate				
REER (% change) [2]	0.8	4.2	2.1	…
Unemployment rate				
Overall (% total labor force)	6.6	5.6	…	…
Nationals (% total labor force)	11.3	9.4	…	…

Sources: Country authorities and IMF staff estimates and projections.

[1] Imports of goods and services.

[2] For 2023, data is latest available.

INTERNATIONAL MONETARY FUND

SAUDI ARABIA

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION

July 7, 2023

KEY ISSUES

Context. Saudi Arabia's economy is booming, unemployment is at a record low, the output gap is closed, inflation is contained, and fiscal and external buffers have been rebuilt. The continuation of Vision 2030 reforms has helped advance the country's economic diversification agenda, including through reduced reliance on oil.

Outlook and risks. Non-oil GDP growth momentum is expected to remain strong, as strong consumption spending and accelerated project implementation boost demand. Oil production—which depends on OPEC+ decisions—will be subdued in the near term. Risks to the outlook are balanced, but contingency measures will be needed in case an overheating risk scenario materializes.

Fiscal policy. With an upward shift in total spending in 2022, fiscal accounts are projected to stay close to balance in the medium term. Additional fiscal adjustment is needed to mitigate risks from oil price volatility and meet intergenerational needs. Such consolidation should continue to rely on non-oil revenue mobilization, energy price reforms, and the continued rollout of transformative structural fiscal reforms. The efforts to delink spending from oil price fluctuations should be strengthened by a strict application of a fiscal rule. An integrated asset-liability management framework would help mitigate risks.

Monetary and Financial sector. A tight monetary policy in line with the Fed—supported by strengthened liquidity management—should continue supporting the exchange rate peg, which continues to serve the country well. The banking system remains on a strong footing, underpinned by ongoing efforts to modernize the regulatory and supervisory frameworks.

Structural reforms. The implementation of the Vision 2030 reform agenda—which led to substantial improvements in the regulatory and business environment—is continuing unimpeded towards a productive and green economy. Careful calibration of investment programs is needed to ensure catalytic effects and avoid crowding out the private sector. The industrial policy agenda should be supporting structural reform efforts, with guardrails put in place to minimize inefficiencies. Fully implementing the Green Initiative is necessary to help Saudi Arabia meet its net zero emissions target.

Approved By
Zeine Zeidane

Discussions were held in Riyadh during May 14-28, 2023. The team comprised Amine Mati (head), Jerome Vacher, Sidra Rehman, Yuan Gao Rollinson, Greta Polo (all MCD) and Vassili Prokopenko (MCM). Jihad Azour (MCD) participated in the concluding meetings. Advisor to the Executive Director for Saudi Arabia, Ms. Hend Alshaikh, accompanied the mission and the Executive Director for Saudi Arabia, Mr. Abdullah BinZarah, joined for the concluding meetings. The team met with Minister of Finance Al Jadaan, Governor of the Saudi Central Bank (SAMA) Alsayari, Minister of Energy Al Saud, Minister of Investment Al-Falih, Minister of Economy Alibrahim, Minister of Industry and Mineral Resources Alkhorayef, Minister of Communications and Information Technology Alswaha, and other senior officials, as well as representatives of the private sector and academics. The IMF DIGNAR team (RES) provided excellent assistance in model simulation. Esther George (MCD) provided excellent support from headquarters and contributed to the report.

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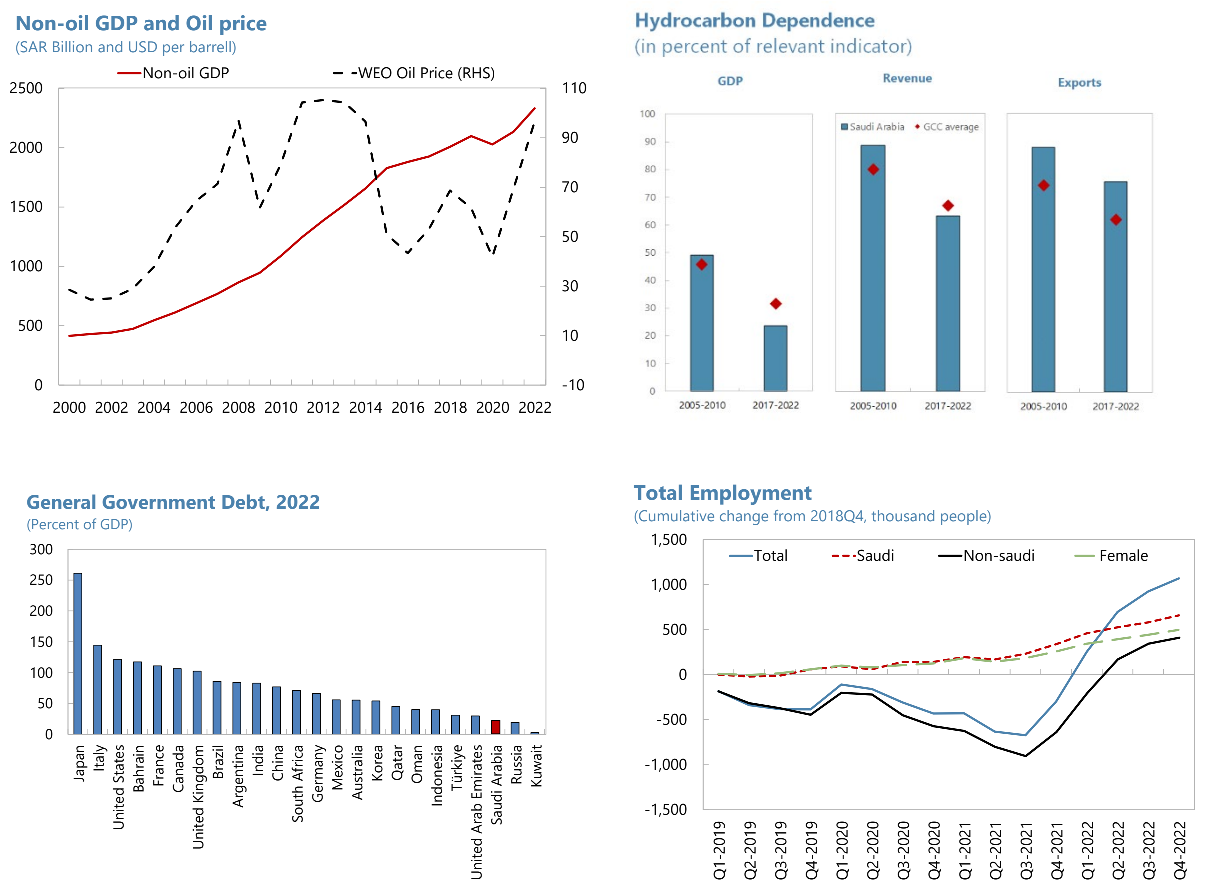
BACKGROUND

1. **Saudi Arabia's economic transformation is advancing rapidly.** Since the onset of the Vision 2030 reform agenda in 2016, and despite the slowdown associated with COVID-19, Saudi Arabia advanced in its diversification through a reduction of the oil sector's contribution across revenue, export, and output. External and fiscal buffers have been rebuilt, non-oil revenue mobilization doubled, unemployment is at record lows, female labor force participation surpassed its 30 percent 2030 target, and government efficiency has improved (including through digitalization).

Saudi Arabia—Economic Context

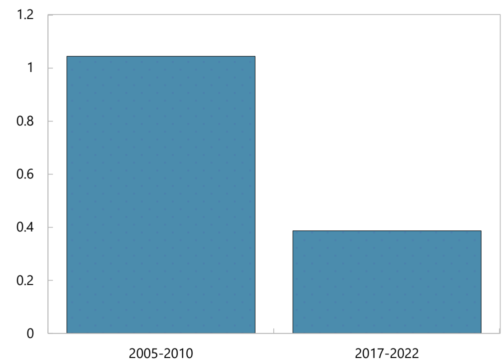


Sources: World Economic Outlook, country authorities and IMF staff calculations.

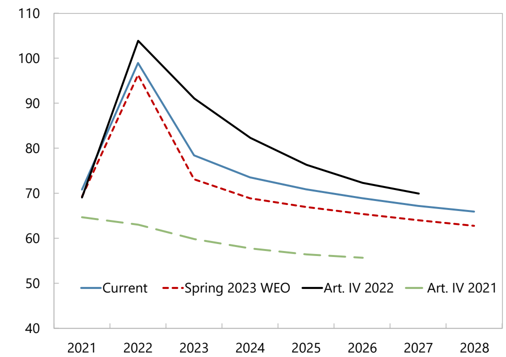
2. **Sustaining the reform momentum irrespective of the level of oil prices will be key to generate inclusive growth and enhance resilience**. The implementation of the National Investment Strategy (NIS) with continued structural reforms would foster competitiveness and enhance total factor productivity thus boosting non-oil growth significantly, which will be necessary to further reduce unemployment, diversify the economy, and respond to the changing global energy mix dynamics. Calibration of investment spending—supported by fiscal reforms—should avoid

procyclicality and potential risk of overheating while reducing risks from ambitious giga projects and industrial policies. The take-up of the most recent Article IV recommendations is indicative of the authorities' efforts to reform (Annex I).

TFP Contribution to Non-Oil Real GDP
(Percent)



WEO Oil Price Assumptions
(USD per barrel)

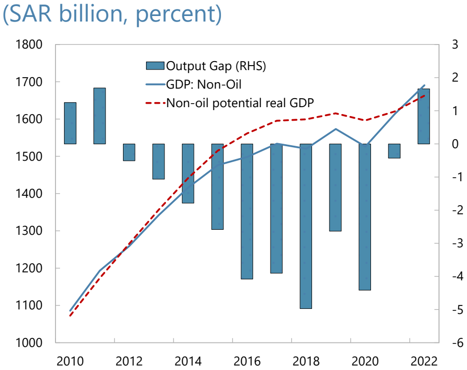


Sources: World Economic Outlook, country authorities and IMF staff calculations.

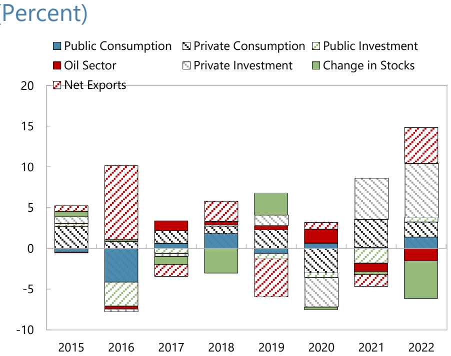
RECENT ECONOMIC DEVELOPMENTS

3. **Saudi Arabia was the fastest growing G20 economy in 2022.** Growth reached 8.7 percent y-o-y—reflecting both the 16 percent increase in crude oil production and 4.8 percent y-o-y increase in non-oil growth driven by a rebounding wholesale, retail trade and restaurant sectors, higher ICT growth, and construction—with higher mortgage rates dampening the contribution of the real estate sector in the second half of the year. On the demand side, private consumption increased by 4.8 percent y-o-y, but the largest impulse came from non-oil private investment rising by 45 percent, spurred by the increasing pace of various giga projects. Spillovers from the war in Ukraine and tighter global financial conditions have been limited, and the output gap is estimated to have been closed during 2022.

Non-oil GDP, Potential and Output Gap
(SAR billion, percent)



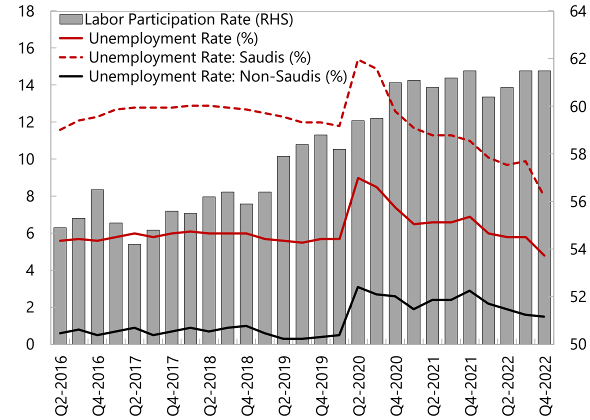
Demand Side Growth Decomposition
(Percent)



Sources: World Economic Outlook, country authorities and IMF staff calculations.
Note: Potential real GDP was estimated based on a production function using a one-sided HP filter.

4. The unemployment rate dropped to a historical low. Reflecting the significant growth in the economy, total unemployment reached 4.8 percent in 2022Q4, down from 9 percent during Covid—reflecting both a healthy rise of Saudi workers in the private sector and expatriate workers (mostly in the construction and agricultural sectors) back above pre-Covid levels amid an increase in overall labor force participation. The Saudi unemployment rate has dropped to 8 percent in 2022—its lowest level on record; youth unemployment has also been halved to 16.8 percent in 2022 relative to its level during Covid; and women unemployment reached 12.9 percent amidst female labor force participation for nationals reaching a record high of 37 percent (from 18 percent in 2017).

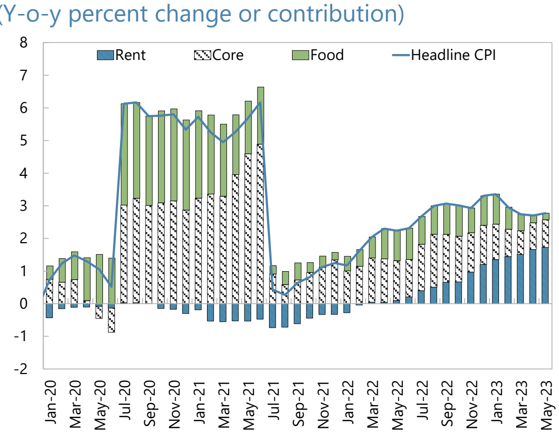
Unemployment Rate and Labor Participation
(Percent)



Sources: GASTAT and IMF staff calculations.

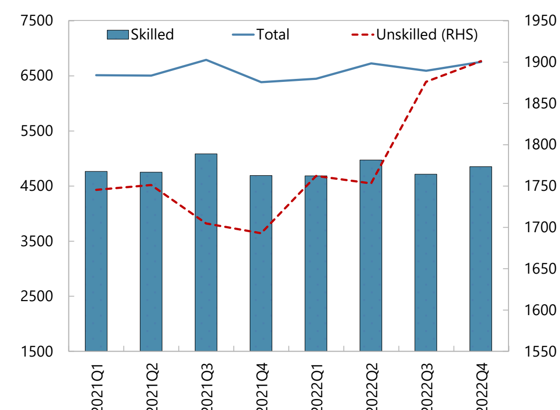
5. Inflation has been contained. Headline CPI averaged 2.5 percent in 2022, with inflation partly contained by domestic subsidies/price cap and the strength of the U.S. dollar, with the latter more recently abating. Despite an uptick in early 2023 to 3.4 percent, headline inflation has fallen again to 2.8 percent in May 2023, spurred by favorable base effects while the continued increase in rents is offset by declining contributions from transport and food prices. While wages for low-skilled workers rose by 12 percent y-o-y in 2022Q4, inflationary pressures have been limited as average wages have been contained—including because of a relatively elastic supply of expatriate workers and increased labor force participation.

CPI Inflation
(Y-o-y percent change or contribution)



Sources: World Economic Outlook, GASTAT, country authorities and IMF staff calculations.

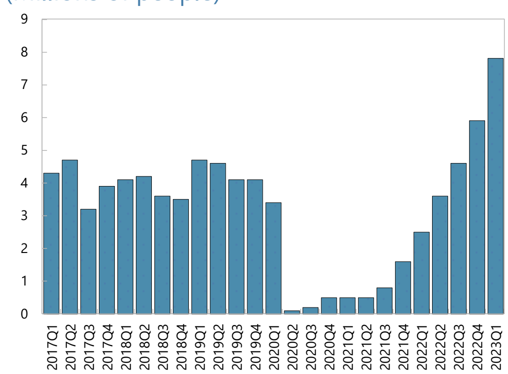
Average Monthly Wages
(Riyals)



Note: Unskilled labor is defined as workers with no schooling, else is defined as skilled.

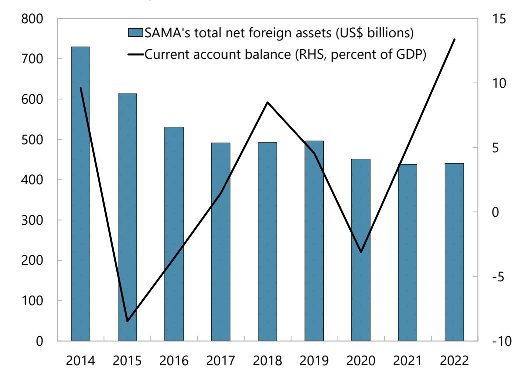
6. Higher oil prices/production improved the current account to a 10-year high surplus last year. Higher exports—primarily from oil and accompanied by a record level of non-oil exports (a fifth of total exports) and strong tourism inflows—continue to surpass the strong import growth and large remittance outflows although marginally lower than the level observed in 2021. The 13.6 percent of GDP surplus in 2022—equivalent to $150.8 billion—only led to a $4.5 billion increase in reserves over 2021, although net foreign assets stood at about 19.4 months import cover and were comfortably above the ARA metric (Annex V). This muted increase in reserves is mostly explained by a large accumulation of assets abroad, including by the Public Investment Fund (PIF) and the Saudi national oil company (Aramco).[1] More recently, reserves have further declined by about $17.7 billion in May 2023 relative to 2022, primarily due to large amortizations.

Number of Tourists, Overnight Visitors
(Millions of people)



Sources: Ministry of Tourism
*2022 and 2023 estimates are preliminary.

International Reserves and Current Account
(USD billion, percent of GDP)

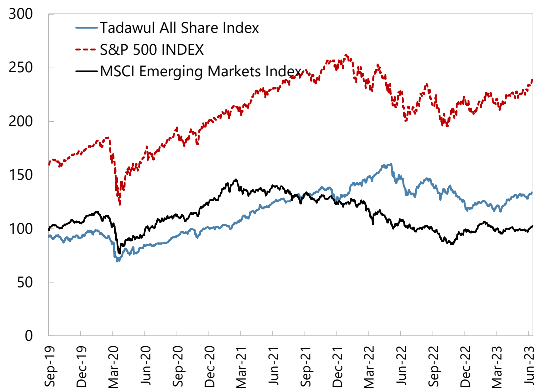


Sources: Country authorities and IMF staff estimates.

7. Capital market deepening is continuing. Reflecting global trends and rising global interest rates, the Tadawul All Share Index fell by 7.1 percent in 2022, although sovereign spreads have remained low (72 bps of daily average in 2022). An expanding market capitalization (the 9th largest in the world for equity), and Saudi Arabia's increased weights in the MSCI emerging market index (also due to the exclusion of Russia) attracted more foreign investors. Debt-raising activities—such as a $10 billion sovereign issuance, $6 billion sukuk issuance and the green bonds by the PIF ($3 billion in October 2022, and $5.5 billion in February 2023)—are helping diversify Saudi Arabia's long-term funding options, though still relying on international markets while local debt markets are gradually deepening. Rating agencies have upgraded Saudi Arabia's sovereign credit ratings in recognition of the sustained reform momentum, which will further facilitate Saudi Arabia's market access.

[1] Aramco for instance had US$135 billion in cash and short-term investments at the end of 2022 (equivalent to 12 percent of GDP), mostly abroad.

Stock Market Indices
(Index; Jan 1, 2014=100)



Sovereign Credit Ratings
(Long term rating outlook, foreign currency)

Date	Fitch	S&P	Moodys
Apr-23	A+ (Stable)	A (Stable)	A1 (Positive)
Mar-23	A	A (Stable)	A1 (Positive)
Mar-22	A	A- (Positive)	A1 (Positive)
Nov-21	A	A- (Positive)	A1 (Stable)
May-20	A	A- (Positive)	A1 (Negative)
Apr-20	A	A- (Positive)	A1 (Stable)
Sep-19	A (Stable)	A- (Positive)	A1 (Stable)
Apr-19	A+	A- (Positive)	A1 (Stable)
Jun-18	A+ (Stable)	A- (Positive)	A1 (Stable)
Apr-18	A+ (Stable)	A- (Positive)	A1 (Stable)

Sources: World Economic Outlook, S&P. Fitch, Moody's, country authorities and IMF staff calculations.

OUTLOOK, RISKS, AND SPILLOVERS

8. **The outlook is strong despite an uncertain external environment**. Under the current baseline, international oil prices are expected to average $78 per barrel in 2023 (a 21 percent decrease over the average 2022 WEO oil price). Possible revisions in global demand and further shifts in international commodity prices bring additional uncertainty to staff's baseline scenario:

- **Non-oil and overall GDP**. Leading indicators and staff's nowcasting analysis continue to show strong non-oil growth momentum early in the year, with non-oil real GDP growth expected to average 4.9 percent in 2023 as accelerated project implementation boosts demand. In line with the recent OPEC+ agreement (June 2023), oil GDP growth is expected to decline by 2.5 percent in 2023, despite increasing refining production. As a result, overall real GDP is projected to grow by 1.9 percent in 2023. Non-oil growth will continue its momentum in 2024 before returning to its medium-term potential of 4 percent as the

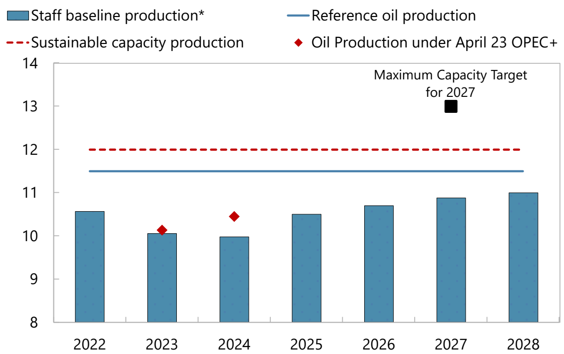
Nowcasting Analysis
(Y-o-y percent)

Leading Nowcasting Indicators (Monthly)		
Consumer Price Index (2018=100)		
4 Week Treasury Bill (Average, %)		
Stock Market: Number of Transactions (Number)		
Stock Market: Number of Shares Traded (Mil)		
Non-oil Exports (Mil. Riyals)		
Tadawul All Share Index (EOP, 1985=1000)		
Global Manufacturing PMI using Markit Mfg for U.S.		
3 Month SAIBOR (Average, %)		
Cement Deliveries (Thous. Ton)		
Foreign Reserves: Investment in Foreign Securities (EOP, Mil. Riyals)		
Crude Oil: Saudi Arabia (Thous. Barrels per Day)		
Saudi Arabian Light: Spot Crude Price ($/BBL)		
Nowcasting Results	**Q1-2023**	**Q2-2023**
Non-oil Activity		
GASTAT Flash Estimate (May 2023)	5.8	
GASTAT Actual (June 2023)	5.4	
IMF staff estimate (May 2023)	5.4	5.3

Sources: Haver Analytics and IMF staff calculations.
Note: The IMF staff's nowcasting framework is based on a non-parametric approach that iterates over 19 models and considers a pool of 130 variables of mixed frequency. The best model was selected based on out-of-sample performance (e.g., RMSE)—Q1 and Q2 nowcasts were estimated by stochastic gradient boosting trees and support vector machine RBF one-SE, respectively. Non-oil activities represent GASTAT new presentation which excludes government activities.

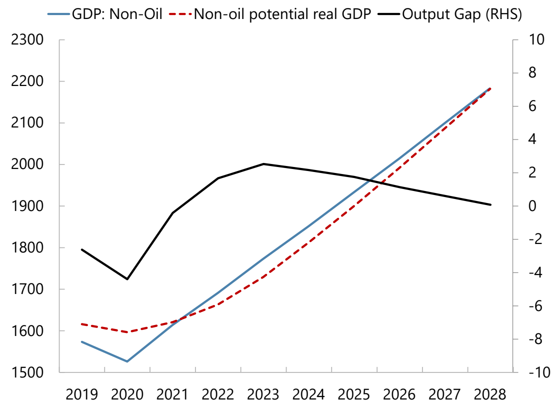
positive output gap closes, investment projects mature, and reforms increase productivity and yield dividends. Non-Oil GDP is expected to represent 71 percent of the economy by 2028 (from about 56 percent in 2022).

Oil Production Schedule
(Millions of barrels per day)



*Baseline shows June 2023 OPEC+ agreement and assumes a drop to 9 mbpd for July 2023 and production of 10 mbpd in 2024.

Non-Oil GDP and Output Gap
(SAR billion, percent)



Sources: World Economic Outlook, OPEC, country authorities and IMF staff calculations.
Note: Potential real GDP was estimated based on a production function using one-sided HP filter.

- **Headline inflation** is expected to remain contained despite an upward revision reflecting the impact of a sustained rise in rent prices, the latest increase in diesel prices, and with a one-year lag, of global inflation. This is moderated by subsidies, price caps on certain products, and a slowdown in the real estate market (due to higher financing costs). While diminishing labor market slack and demand from a booming economy could increase inflationary pressures over the short term, inflation over the longer term is expected to return to 2 percent—the long-term U.S. average.

- The significant improvement in the **external position** is expected to abate. The current account surplus would decline over the medium term as oil prices stabilize and imports pick up. With the ambitious Vision 2030 reform agenda underway and supported by sizeable investments—imports of both intermediate and final goods are expected to pick up. As the diversification strategy bears fruit over the medium term, non-oil exports are expected to increase although not at the same pace as imports. Net foreign assets—which exclude holdings of the PIF or Aramco—are expected to stabilize at a lower level, reaching a cover of around 13.8 months of imports or the equivalent of 36 percent of GDP by 2028.

Selected Economic Indicators, 2022–28

	Est. 2022	Proj. 2023	Proj. 2024	Proj. 2025	Proj. 2026	Proj. 2027	Proj. 2028
Real GDP	8.7	1.9	2.8	4.2	3.3	3.3	3.1
Non-oil real GDP	4.8	4.9	4.4	4.4	4.2	4.2	4.0
Consumer price index (average)	2.5	2.8	2.3	2.0	2.0	2.0	2.0
Current account balance (percent of GDP)	13.6	6.5	3.5	2.7	1.7	0.6	-0.3
SAMA's total net foreign assets (US$ billions)	440.5	427.8	413.1	412.1	422.7	438.8	459.2
In months of imports of goods and services [1]	19.4	17.5	15.7	14.6	14.0	13.9	13.8

Sources: Country authorities; and IMF staff estimates and projections.

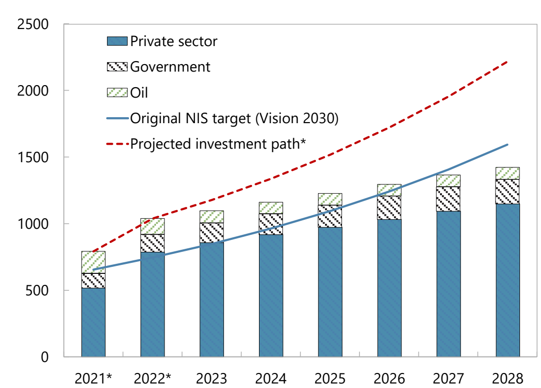
[1] Next 12 months.

9. Risks to the outlook are balanced (Annex II):

- On the **upside**, higher than expected oil production should OPEC+ production cuts be reversed, higher oil prices if expectations of a supply shortfall persist for the second half of 2023, and accelerated structural reforms supported by the full implementation of the NIS under Saudi Arabia's Vision 2030 (staff's implementation assumes half of the planned year-on-year increase), could improve growth and the outlook. Further sales by the government of Aramco shares as envisaged would ease further financing, potentially allowing for increased spending.

Gross Fixed Capital Formation

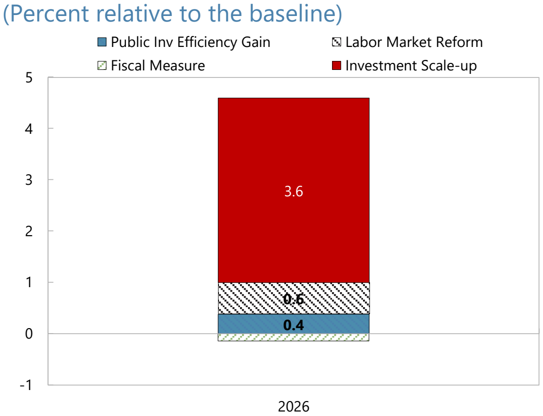
(Current Prices)



Source: NIS and IMF staff calculations.
Note: *The projected investment path takes realized values in 2021/22 and applies the original y-o-y growth planned under the NIS in Vision 2030 (13.5 percent nominal y-o-y growth vs. an average of 5 percent for 2023-28 in the baseline).

Gain of Real Non-Oil GDP Growth from Investment Scaling-Up and Reforms

(Percent relative to the baseline)

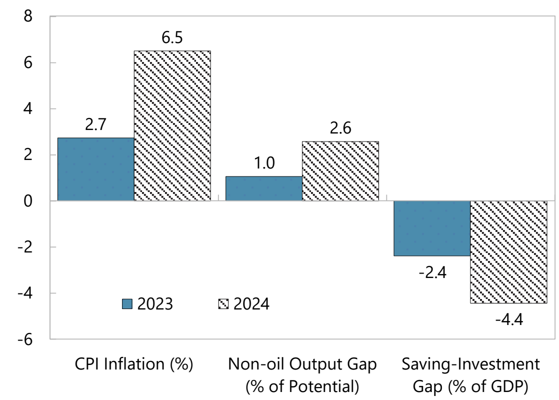


Source: Country authorities and IMF staff calculations.
Note: The scale-up scenario considers 2022 realized values and applies the original y-o-y growth planned under Vision 2030 (13.5 percent nominal y-o-y growth). Simulations were conducted using the IMF's DIGNAR-19 model (see [Saudi Arabia: Selected Issues 2022 (imf.org)])

- On the **downside**, lower oil prices due to subdued global activity (in the short term) and a quicker shift in demand for fossil fuels (medium- to long-term), pressures to spend higher oil revenue and deviate from fiscal prudence, a slowdown in the implementation of the reform agenda, and overheating represent key risks. In addition to fluctuating oil prices that will affect macroeconomic outcomes directly (Figure 9), two scenarios illustrate potential near-term and long-term risks:

- **Investment scaling up leading to an "overheating" scenario.** As giga projects implementation increases, and project acceleration is being considered, demand pressures on the economy could rise, widening further the output gap and inflationary pressures. Higher associated import growth would impact the savings investment balance, worsening the current account and funding requirements needed. In this situation, a flexible labor market—including through expatriate labor as seen during Covid—could help mitigate risks. Contingency measures—such as a tighter monetary and fiscal policy, including through reprioritization of capital projects—should be considered if such demand pressures manifest themselves.

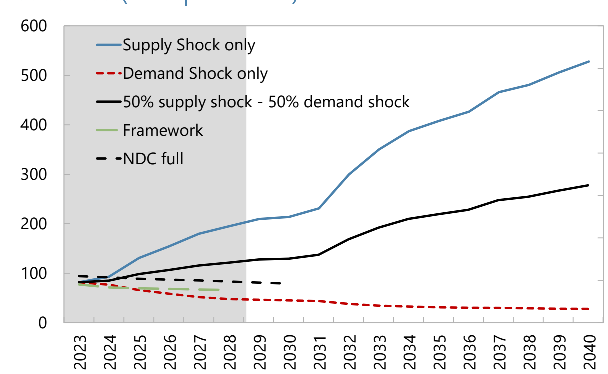
Overheating Scenario
(Percentage points change relative to baseline)



Sources: IMF staff calculations.
Note: This scenario assumes a 24 percent y-o-y growth of real gross fixed capital formation in 2022 persisting over the next two years (vs. average 6 percent for 2023-24 in the baseline). Non-oil potential output is assumed to remain unchanged from the baseline over the near-term.

- **Climate change**. Saudi Arabia faces energy transition risks as the world shifts towards achieving a net zero emissions target, which would require continuing to build buffers in the context of high uncertainty and in the event of a potential long-term decline in oil prices. Depending on the relative magnitude of supply effects (e.g., underinvestment in oil) and demand effects (e.g., shift to low-carbon consumption), the oil price could move to allow more or less fiscal space. Nevertheless, even in a transition scenario where all countries implement their National Determined Contributions (NDC) and where Saudi Arabia implements its NDC commitment to reduce emissions by 278Mt of CO_2eq per annum by 2030, the impact on the economy is expected to be limited as the oil price reduction is contained.

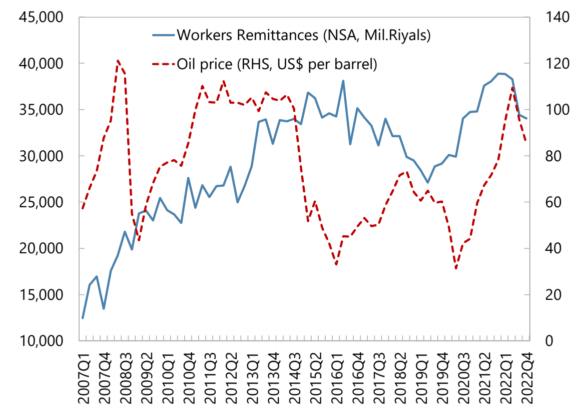
Nominal Oil Price Projections under Net-zero Scenarios (USD per barrel)



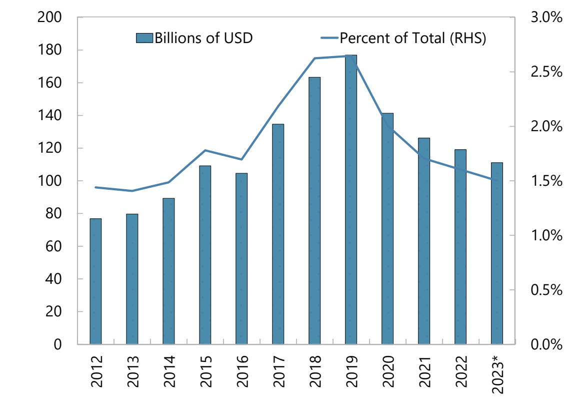
Sources: IMF staff calculations.

10. Potential inward and outward spillovers from recent developments appear limited. The impact of financial tensions in the U.S. and Europe, notably as both Saudi Arabia's public and private sectors have large investments abroad, is limited so far. In the case of U.S. Treasury bills and bonds holdings, Saudi exposure has declined in the recent period though they still represent the equivalent of 10 percent of GDP. Positive spillovers from increased outward remittances are expected in view of stronger growth in the Kingdom and the post-Covid return of expatriate workers. Support to vulnerable countries has also risen, with Saudi Arabia providing US$28 billion since October 2021, including to help mitigate the impact of the food security crisis.

Worker Remittances and Oil Price
(SAR Million and USD per barrel)



Holdings of U.S. Treasuries
(Billions of USD and percent of total)



Sources: Haver Analytics, U.S. Treasury, and IMF staff calculations.
*2023 data represents latest available monthly.

Authorities' Views

The authorities agreed with staff's 2023 growth projection, with near-term growth to remain above potential as strong consumption spending and accelerated project implementation boost demand. Over the medium term, while the authorities agree on the need to use prudent forecasts, they are confident that strong reforms and implementation of Vision Realization Programs, sectoral strategies, regional strategies and giga projects will continue raising non-oil growth and potential growth above staff's baseline.

The authorities recognize that large structural transformation reforms will always have risks, and opportunities. They noted that they are constantly assessing these risks while exploring venues to seize the opportunities, including by reviewing funding requirements and capacity needed to meet their Vision 2030 reform agenda. They pointed out that a flexible labor market and existing cap on gasoline prices represent mitigating factors limiting inflationary pressures while continuous monitoring and evaluation will help them reprioritize projects and limit spending to avoid an overheating scenario. They underscored their strong resolve to pursue structural reforms under Vision 2030, which they expect to have positive spillovers regionally and globally.

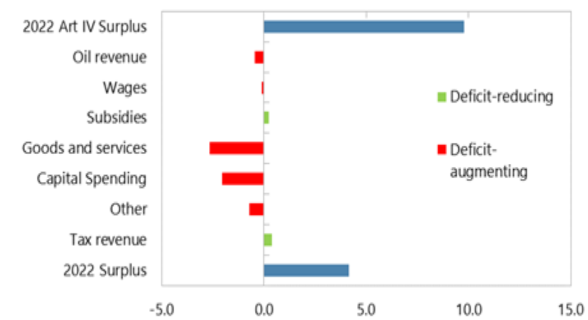
POLICIES FOR GROWTH AND STABILITY IN A HIGH OIL PRICE AND FRAGMENTED WORLD ECONOMY

11. Policy discussions focused on managing the oil revenue windfalls in a sustainable way, including to mitigate risks from a rapid ramp up in investment and fluctuations in international oil prices. Priorities include: (i) maintaining fiscal discipline through broad-based fiscal consolidation; (ii) ensuring financial stability in a turbulent world; and (iii) continuing to implement structural reforms to support strong, sustainable, and inclusive growth.

A. Fiscal Policy

12. Favorable oil market dynamics strengthened the fiscal position, which also created room for additional spending. The fiscal surplus for 2022—the first since 2013—has been halved relative to staff's initial projection of 5½ percent of GDP. This mostly reflects increases in goods and services and capital spending, including additional military expenditures of 2 percent of GDP. Close to 3 percent of GDP were, in the authorities' latest estimates, one-off non-recurrent spending (of which, half is in goods and services). Fiscal space is assessed as substantial, with no significant constraint to undertaking temporary fiscal measures, if there is an economic case.

Contribution to Surplus Reduction
(Percent of GDP)



Sources: Country Authorities IMF staff estimates.

Budget and IMF Staff Central Government Operations Projections
(Billions of Riyals)

	2022	Budget 2023	IMF 2023
Revenues			
Revenues	1,277	1,130	1,137
Non oil tax revenues	333	322	371
Other revenues	944	808	766
Expenditures	1,173	1,114	1,185
Expenses	1,030	957	1,026
Of which:			
Employee compensation	513	514	520
Use of goods and services	258	218	239
Support (subsidies)	30	22	28
Social benefits	79	67	85
Net acquisition of non-financial assets	143	157	159
Net lending (+)/borrowing (-)	104	16	-48
Net lending (+)/borrowing (-) (in percent of GDP)	2.5	0.2	-1.2

Sources: IMF staff calculations.

13. With this upward shift in total spending in 2022—about 18 percent relative to the 2022 Article IV baseline—fiscal accounts are projected to stay close to balance in the medium term. Taking into account higher expenditures—including the estimated non-recurrent one-off spending made in 2022—staff estimates a deficit of 1.2 percent of GDP in 2023. Potential additional dividends from Aramco could allow for an upside in revenues. While the non-oil primary balance is expected to improve in tandem by a cumulative 10 percent of non-oil GDP by 2028, overall surpluses appear small and remain contingent on any shift in the oil price. This trend reflects prudent forecasts under the baseline, which keeps non-oil revenue constant as percent of non-oil GDP in the absence of new revenue measures presented by the authorities.

14. The medium-term fiscal stance should remain consistent with stabilizing the Central Government Net Financial Assets (CGNFA) ratio and intergenerational equity. Staff's updated analysis shows that higher spending (until 2030) would prolong the transition phase required to achieve the fiscal stance that is consistent with stabilizing the CGNFA ratio and intergenerational equity as applied with the Permanent Income Hypothesis (PIH) over the medium term. Under current policies, the non-oil primary deficit would reach about 20.5 percent of non-oil GDP by 2028 and with almost no accumulated fiscal surpluses over the medium term, the CGNFA (which does not include inter alia the PIF) would not improve by 2028, while remaining at a negative level. Reaching the PIH norm (computed as an annuity constant in real terms)[2] would now require new measures over the baseline transition period of close to 2 percent of non-oil GDP by 2028, which could be achieved through:

- **Non-oil tax revenue** has doubled over the past four years to reach 10.6 percent of GDP and 14 percent of non-oil GDP in 2022, still below the G20 average, while the tax gap with Saudi Arabia's estimated tax capacity reduced to around 10 percent of non-oil GDP in 2022 (from 15 percent in 2019). This was achieved with a good performance in terms of compliance in particular for VAT, with the simple VAT structure (few exemptions) and sound regulatory compliance helping slightly outperforming the G20 both in terms of revenue yield and C-efficiency. Ongoing efforts to develop a comprehensive revenue strategy could help narrow the tax gap by:

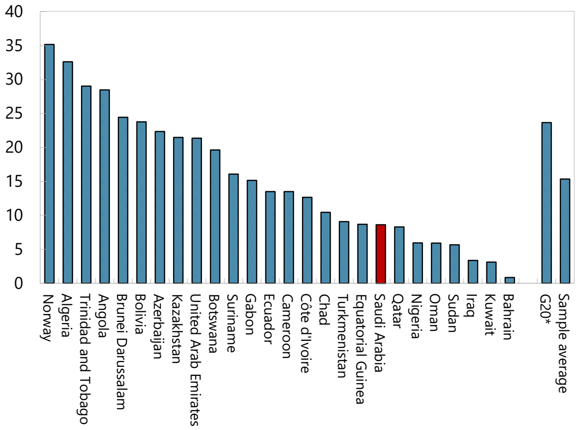
    - at least maintaining the VAT rate (which was tripled during Covid) at 15 percent, widening the base through reduced tax expenditures, and considering plans for reforming excises/customs duties, corporate income taxation, expat levies and property taxation (the latter non-existent in Saudi Arabia during a period of property boom, while property taxes represent on average 1.8 percent of GDP in the G20 and emerging economies and up to 4 percent in some advanced economies).

    - accelerating ongoing efforts to remedy tax administration gaps identified through an internal TADAT assessment, which should be part of a comprehensive medium-term revenue strategy.

[2] For a discussion of the preferred fiscal anchor see Saudi Arabia: Selected Issues (imf.org)

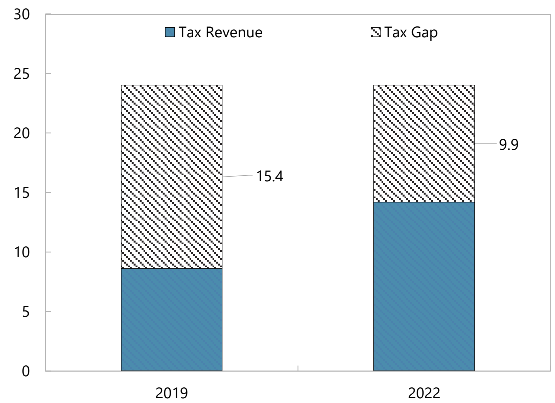
Tax Gap: An International Comparison

Non-oil Tax Revenue in Saudi Arabia and Comparable Economies
(Percent of non-oil GDP)



Source: IMF staff estimates.

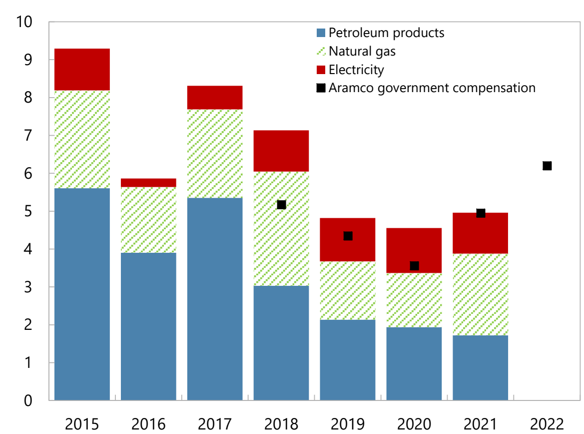
Saudi Arabia: Tax Capacity and Tax Gap
(Percent of non-oil GDP)



*Tax capacity is defined as the maximum level of tax revenues observed in similar countries with the same set of economic characteristics and measured using the stochastic frontier analysis model

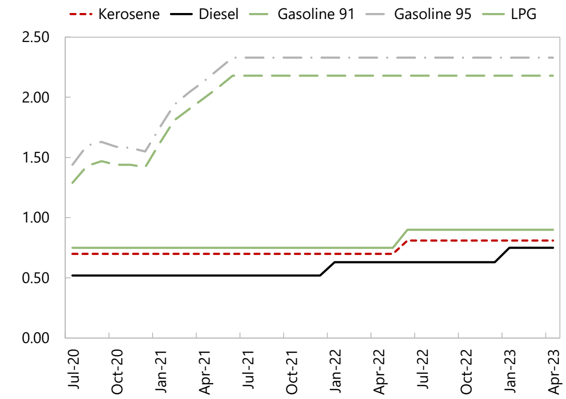
- **Energy price reforms** implemented in 2016 and 2018 have played an important role in halving subsidies between 2010 and 2020. Measures taken at the end of 2021, such as increasing prices for heavily subsidized diesel and asphalt, and increases made on four products in 2022, are welcome, but not enough to reduce subsidies on liquid fuels, which have reached 6.2 percent of GDP in 2022 through foregone revenue for the government from Aramco sales. In addition to the 25 percent increase in diesel prices at the end of 2022, staff supports the authorities' plans to gradually eliminate fuel subsidies by 2030. To that end, lifting the cap on gasoline prices would help further reduce subsidies, which are expected to decline in view of weaker oil prices in 2023 than 2022, and encourage energy conservation. Adjusting the current formula to allow faster increases for other fuel prices and electricity would also help contain the rise in energy subsidies seen recently. Moreover, this would support Saudi Arabia's efforts to reach its mitigation targets.

Energy Subsidies
(Percent of GDP)

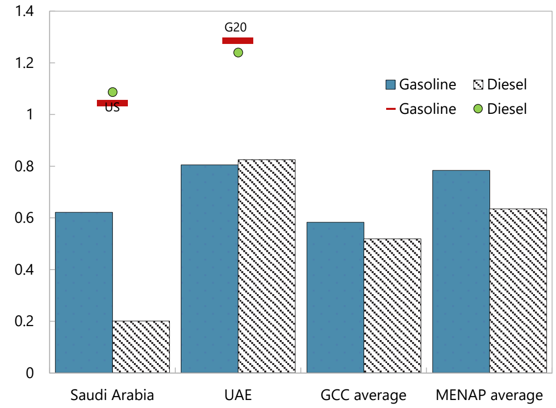


Sources: ARAMCO audited financial statements (since 2019), Fossil Fuel Subsidies (imf.org) and IMF staff calculations.
Note: Data is latest available.

Fuel Retail Prices
(SAR per liter)



Retail Sales Prices of Gasoline and Diesel
(USD equivalent, including taxes April 2023)



Sources: CEIC, Global Petrol Prices and IMF staff estimates.

- **Rationalizing expenditures**. Partial cuts planned in the budget in goods and services following the large one-off increases of 2022 and in social benefits/subsidies are leading to a 1¼ percent of GDP savings in the 2023 budget. Implementing those cuts will be challenging for most expenditure items, including social benefits. Sustaining them over the medium term will require continued rationalization of subsidies and the high wage bill, including through strategic workforce planning and review, greater medium-term planning and efficiency in public investment and spending (see below), regular spending reviews, and full utilization of the digitalized expenditure chain platform (Etimad).

- **Strengthening the social safety net.** Staff welcomes the elaboration of a new social protection strategy, which has been submitted for legislative approval. To support energy subsidy reforms, staff recommends scaling up well-targeted and means-tested social programs—such as the needs-based Damaan program—which could also be enhanced by narrowing the existing "untargeted" coverage in the Citizens' account program. The setup of a single registry is welcome and should be accelerated to ensure that benefits remain well-targeted, and leakages reduced. A new household living standards survey—being conducted with the World Bank—will further help underpin the level of social spending while using a means-tested approach.

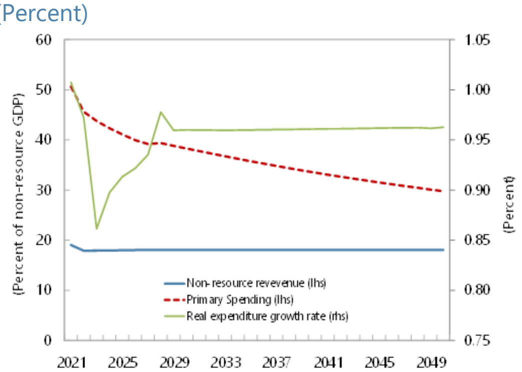
Budgetary Central Government Operations, 2020–28
(Percent of non-oil GDP unless otherwise indicated)

	2020	2021	2022	2023	2024	2025	2026	2027	2028
Revenue	38.6	45.3	54.9	45.1	43.0	43.0	42.5	41.8	40.0
Oil	20.4	26.4	36.8	26.2	24.1	24.1	23.6	22.9	21.1
Non-oil	18.2	18.9	18.1	18.9	18.9	18.9	18.9	18.9	18.9
Tax revenues	9.4	13.3	14.3	14.7	14.7	14.8	14.8	14.8	14.9
Non-oil non-tax revenues	8.9	5.6	3.8	4.2	4.1	4.1	4.1	4.1	4.1
Expenditure	53.2	48.8	50.4	47.0	45.4	44.1	42.7	41.5	40.0
Expenses	45.5	43.3	44.3	40.7	39.1	37.8	36.4	35.3	34.1
Employee compensation [1]	24.4	23.3	22.0	20.6	19.6	18.7	17.9	17.2	16.6
Use of goods and services	10.0	9.6	11.1	9.5	9.0	8.7	8.4	8.0	7.8
Support (subsidies)	1.4	1.4	1.3	1.1	1.1	1.0	1.0	0.9	0.9
Social benefits [2]	3.4	3.3	3.4	3.4	3.4	3.4	3.4	3.4	3.4
Net acquisition of non-financial assets	7.7	5.5	6.1	6.3	6.3	6.3	6.3	6.2	5.9
Net lending (+)/borrowing (-) (percent of GDP)	**-10.7**	**-2.3**	**2.5**	**-1.2**	**-1.6**	**-0.7**	**-0.2**	**0.2**	**0.0**
Non-exported oil primary balance/non-oil GDP	-35.4	-27.2	-29.6	-23.7	-21.4	-19.6	-17.9	-16.2	-15.3

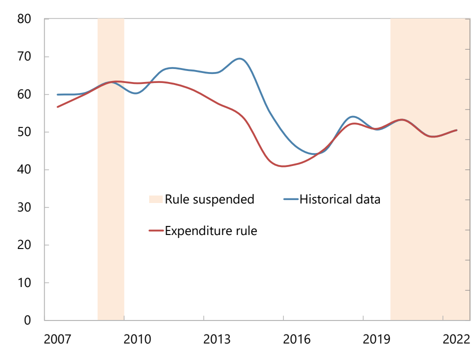
- Sources: Country authorities and IMF staff calculations.

15. **An expenditure rule based on a fiscal anchor derived from the PIH, with a norm based on prudent assumptions, may best serve Saudi Arabia in its growth and stabilization objectives.** Staff welcomes the important reforms being made under the fiscal sustainability program—including ongoing work and experimentation with a structural fiscal rule expected to be implemented in 2024—which aims at avoiding procyclicality and is based on a 50-year smoothing of oil prices in real terms. However, the recent increases in spending calls for a quick application of a fiscal rule that clearly delinks spending decisions from higher oil prices. Staff reiterated its past advice favoring a spending ceiling with a simple rule, based on the PIH.[3] Staff also estimates that an expenditure rule setting 1½-2 percent real growth in spending would have performed well in view of developments in oil prices in the past few years (this rule would have set spending ceilings that were close to actuals and would prevent pro-cyclical expenditure growth during high oil price years).

Decomposing the Adjustment
(Percent)



Total Spending
(Percent of non-resource GDP)



Sources: Saudi Arabian Authorities and IMF staff estimates.

[3] Under the PIH, the total financial wealth (current wealth and the net present value of future oil revenue) is used to finance either a constant flow of revenue in real term or in real term per capita, with a modified PIH allowing for a transition period (this can also enable countries to factor the positive growth impact of the transition, if, for example, it is used to scale up investment to buttress growth prospects). Compared to other approaches (such as" spend-as-you-go") this would help reconcile Saudi Arabia's growth and stabilization objectives, and better account for intergenerational equity needs while maintaining budget credibility.

16. Staff's longstanding advice to accelerate the authorities' ongoing work towards developing a Sovereign Asset-Liability Management (SALM) framework is even more relevant. Staff welcomes ongoing work towards developing a SALM framework—which has commenced with a first phase focusing on quantifying financial assets and liabilities. However, given the increasing role of the PIF, NDF, and other entities in capital expenditures and borrowing, quickly moving to a SALM approach is critical to monitor sovereign balance sheet exposures in an integrated manner; thus, enabling the authorities to assess future investment commitments and their funding in a comprehensive manner and implement a more cost-effective management of public-sector debt and assets. Such an analysis should not infringe on institutional independence. A preliminary assessment of the public sector balance sheet and information on the PIF/NDF spending plans (and sources of financing) suggest that balance sheets are healthy with significant assets and limited leverage though any significant ramp up in investment would require further capital (e.g., for NDF).

Saudi Arabia's Public Sector Balance Sheet 1/
(2021 or latest available, percent of GDP)

	General Government					
	Budgetary Central Government	Social Security Funds	Oil company	SWF	Central Bank	Public Sector (total)
Assets	**150.2**	**28.9**	**660.9**	**81.2**		**921.2**
Non-Financial Assets	133.0		648.7			781.6
Fixed assets 2/	133.0		39.3			
Hydrocarbon 3/			609.3			
Financial Assets	17.2		12.2		52.8	82.2
liquid assets	17.2				52.7	69.9
other assets					n.a.	n.a.
Liabilities	**28.2**		**11.6**	**33.1**	**32.7**	**107.4**
Domestic	19.2					
External	9.0					
Net Assets	**120.2**		**649.2**	**48.1**	**20.1**	**813.7**
Net Financial Assets	**-12.8**		**0.6**	**n.a.**	**20.1**	**n.a**
Net Liquid Financial Assets	**-12.8**		**-**	**n.a.**	**20.1**	**n.a**

1/ A simplified balance sheet. It notably does not incorporate all SOEs and refers to different years depending on the available data. For social security funds (pension fund) it does not incorporate liabilities and in particular actuarial liabilities as the information is not available.

2/ IMF staff estimate using the perpetual inventory method of the capital stock. For the oil company (Aramco) based on audited financial statements.

3/ NPV oil wealth in the ground (based on estimates of proved reserves as of 2021)

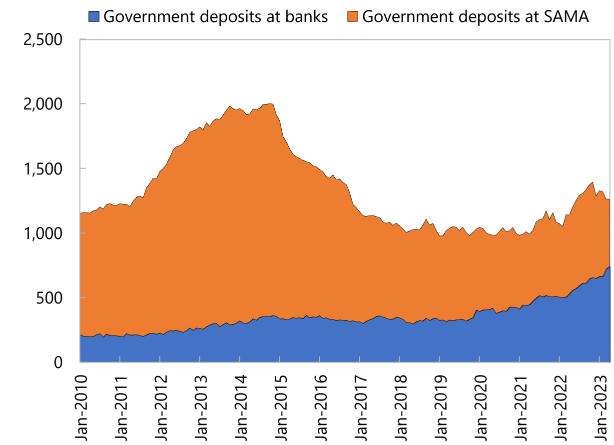
Sources: IMF staff calculations and estimates.

17. Ensuring a sustained fiscal position and fiscal rule will require the continued strengthening of fiscal frameworks. These include:

- **Anchoring fiscal policy in a medium-term fiscal framework (MTFF)**, which is even more of a priority in the wake of the spending increases in 2022 and implementation of the giga projects. A proper MTFF should incorporate the multi-year revenue initiatives currently planned and spending priorities to ensure it remains a credible framework. Planning purposes would also be helped by moving quickly from the current 3-year MTFF to a 5-year one. Progress in establishing a medium-term expenditure framework (currently a pilot in 6 ministries) and the forthcoming move to accrual accounting are important steps towards improving expenditure prioritization and moving towards performance-based budgeting as planned by the authorities for 2027.

- **Enhancing cash management**. The implementation of the Treasury Single Account (TSA) is progressing well, with more than ten thousand government accounts rationalized since its operationalization. Further progress is expected this year, with 3000 accounts expected to be left once the transfer of the 188 entities is completed this year (so far 160 have transferred). The rationalization of the remaining accounts—which have large amounts—should be carefully coordinated with the central bank (SAMA), including through provision of treasury cash flows to help improve liquidity forecasting.

Government Deposits at SAMA vs. Banks
(SAR Billion)



Sources: Country authorities and IMF staff estimates.
Note: Government deposits refers to the total deposits from central government, quasi-government, and government institutions.

- **Strengthening budget execution.** The use of the Etimad platform has greatly improved budget execution and tracking of "disputed payments", with suppliers now directly entering their bills in the Etimad platform when due. Speeding the payment to suppliers—which has improved considerably over the past three years—is helping enhance transparency, provide a clearer view of the status of actual budget execution as well as have a positive impact on the business environment. The proposed transition to accrual budgeting, which will account for eventual payment delays, will allow for an accurate assessment of the fiscal position (as would a move to accounting on a general government basis). Similarly, the settlement of previous obligations with SOEs should be more properly disclosed and accounted for.

- **Accounting for fiscal risks.** The authorities' work on quarterly and annual internal reports on macro-fiscal risks facilitates risk monitoring. In line with best international practices, such reports—which already evaluate various risk scenarios—should assess contingent liabilities from Public Private partnerships (PPPs) and credit guarantees and be made public to enhance transparency. The authorities' ongoing work on improving fiscal risks tools (e.g., developing a risk assessment matrix and criteria, improving the risk register, and increasing coverage to analyze risks from PPPs) is encouraging in this regard.

- **Enhancing fiscal transparency.** Significant progress has been made in fiscal transparency through the expanded Budget Statement and higher frequency reports. The authorities also launched a Community Participation in the Budget Process survey at the end of 2022. The mission encourages the authorities to continue these efforts, including by providing additional details on revenue and expenditure items and continuing to gradually extend institutional coverage, and reporting systemic explanation of the deviations between budget outcomes and plans, which would be further reduced through more realistic revenue and expenditure forecasts during the budget preparation phase. The important efforts made to increase the transparency of PIF operations—including the forthcoming publication of its financial statements— will help determine an accurate state of public finances. In line with best international practices, and in view of the numerous exemptions/incentive schemes currently existing or under discussion, all tax expenditures should be quantified and reported as well. This would help provide more clarity and transparency, as well as guide policy decisions.

18. Sound debt management should continue to support fiscal policy and mitigate risks. At close to 24 percent of GDP, public debt remains low and is assessed to be sustainable (Annex III). Results from stress scenarios suggest low overall risk of sovereign stress, with existing buffers that can support periods of fiscal deficits (reinforcing the importance of a comprehensive view of sovereign assets and liabilities). The borrowing strategy is set to remain agile and innovative to lengthen debt maturities, further improve interest risk management, reduce refinancing costs, build a yield curve in domestic and international markets, develop green issuance, and further deepen the local debt market (e.g., with the introduction of international primary dealers). Government guarantees appear limited to debt issuances by the Saudi Refinancing Company (0.3 percent of GDP), albeit fiscal risks would be further mitigated by assessing and disclosing all potential contingent liabilities linked to increased private sector participation, including from PPP, and debt issuances by the PIF.

Authorities' Views

The authorities emphasized that fiscal sustainability and discipline based on a medium-term fiscal anchor remains their priority. They argued that generating wealth now—including through increased capital expenditures and by accelerating investments when possible—would benefit future generations and justify slight deviations from the expenditure ceilings previously set, which could generate a small deficit for this fiscal year. Relatedly, they highlighted the significant improvements in enhancing fiscal transparency since the Vision 2030 was launched, which will bring about more information on the fiscal policymaking.

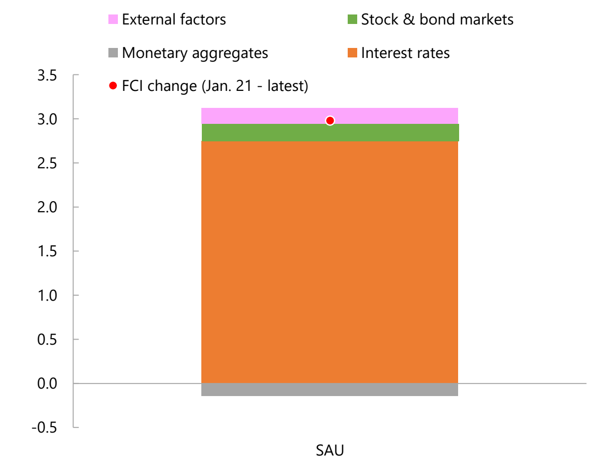
They noted that they are currently considering transitioning to a fiscal rule that establishes expenditure ceilings delinked from oil prices and with clear criteria for surplus allocation. They expect fiscal consolidation to be expenditure-driven, mostly through spending efficiency, and the continuation of implementing energy price reforms. Despite having well-targeted social safety net schemes in place, the authorities argued that the cap on gasoline prices is still necessary, indicating that the cost of subsidies will fall this year in line with lower global commodity prices. They reiterated that non-oil revenue mobilization remains a key anchor of their fiscal sustainability strategy, with an immediate priority on broadening the base and growth in the economy, and not on new tax policy measures.

They agreed on accelerating the work on an asset liability management framework. They emphasized the important reforms already initiated to enhance budget disclosure, coverage of fiscal risks and *progress towards an MTFF, which they plan to pursue further in line with international best practices. On cash management, the authorities stressed the progress made and increased communication with the monetary authorities to limit risks to liquidity management as the authorities continue moving towards a Treasury Single Account.*

B. Monetary and Exchange Rate Policies

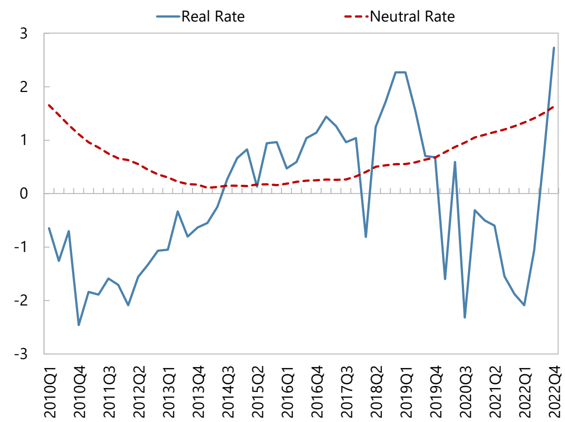
19. Monetary expansion has continued despite a tighter policy stance. SAMA raised its policy rate by 475 basis points since early 2022, in line with the U.S. monetary tightening cycle, with the real interest rate fast becoming positive in support of the pegged exchange rate regime. However, broad money (M3) growth remained robust at 8 percent in 2022, supported by expansion of time and savings deposits, which increased by 32 percent as depositors sought to benefit from higher interest rates and shifted away from unremunerated demand deposits (a 2 percent y-o-y decline, also helped by higher consumption opportunities for households post-Covid). This trend appears to be continuing in Q1 2023 as total bank deposits have grown by 10.8 percent y-o-y, mainly supported by time and savings deposits (38 percent y-o-y increase).

Change in Financial Conditions Index
(January 2021 to latest)



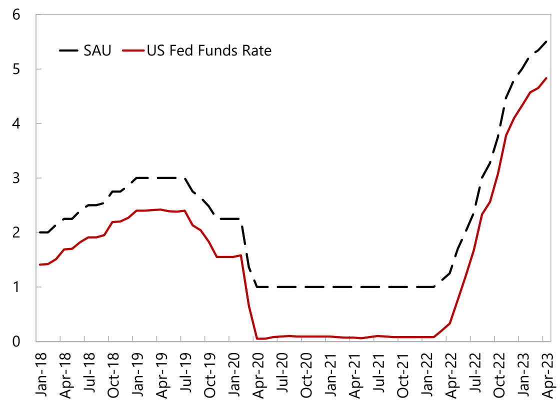
Sources: April 2023 MCD REO
Note: The FCI is constructed by extracting the common source of variation for a set of financial indicators, as represented by the principal component, computed using monthly data. A larger number indicates tighter financial conditions.

Real and Neutral Rate
(Percent)



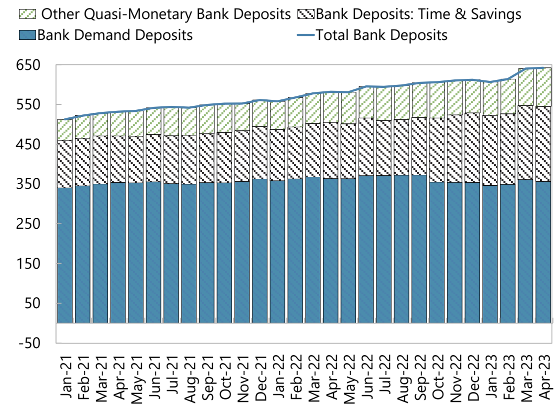
Sources: April 2023 MCD REO
Note: The parameters and trends in the model above are estimated using quarterly data from 2000Q1 to 2022Q4 with the Kalman filter and Bayesian methods.

Policy Rates
(Average, percent)



Sources: Haver Analytics and IMF staff calculations.

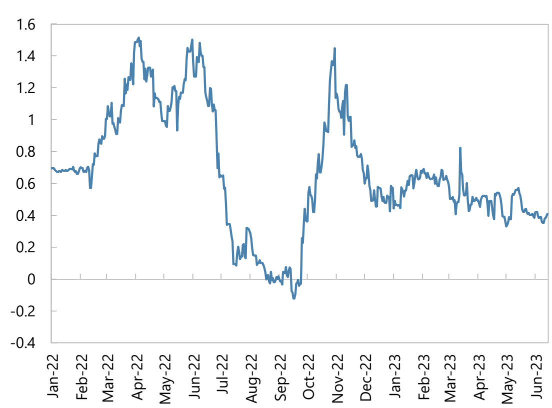
Bank Deposits
(USD Billion)



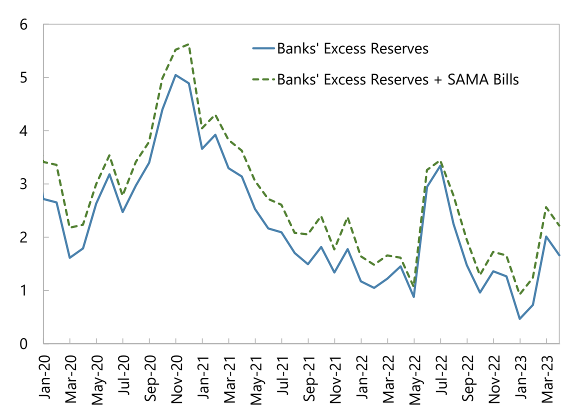
Sources: Haver Analytics and IMF staff calculations.

20. Systemic liquidity pressures emerged twice in 2022 but were eased through a speedy and resolute action by SAMA, partly through using deposit injections (Annex IV). With high credit expansion outpacing deposit growth and non-oil tax revenue increasing, tight liquidity across the banking system emerged in June 2022 and then again in October 2022, as reflected in a significant widening of the three-month SAIBOR-LIBOR spreads to over 150 basis points (more than double the 60 basis points historical average). SAMA responded by injecting liquidity through its standard facilities (open market operations) as well as placement of SAMA's deposits with banks. The swift and comprehensive response by SAMA proved to be effective in calming down the market as interest rate spreads have normalized to their historical averages.

SAIBOR and LIBOR Spreads
(Three-month difference)



Excess Liquidity in Banking Sector
(Percent of bank assets)



Sources: Saudi Arabia Central Bank, Haver Analytics, and IMF staff calculations.

21. Monetary policy should continue to support the exchange rate peg. With an open capital account, policy rates should move in line with the Fed policy rate, with risk premia ensuring the interest rate differential remains consistent with the exchange rate peg. To that end, the monetary policy operational framework (i.e., the instruments used to manage liquidity) should aim at keeping the interbank rate in line with the announced policy rate, while supporting the development of money markets. With those principles in mind, liquidity management operations could be further strengthened through:

- **Market-based monetary policy instruments**. SAMA's interventions should continue to primarily rely on open market operations (SAMA bills, repos/reverse repos) to manage aggregate liquidity in the system. Any other type of injection—including deposits—should be market-based and avoid unnecessary risks to SAMA's balance sheet.

- **Strengthening liquidity forecasting**. Accurate forecasting is essential for effective liquidity management. SAMA's reforms in this area over the past few years, including the establishment of a dedicated liquidity forecasting team and enhanced cooperation with the MoF through regular meetings—are welcome. More accurate liquidity forecasts would require daily data to better calibrate SAMA's interventions, appropriate government forecasts on revenue and expenditure (including ex-post reviews to assess reasons for deviations), and regular exchange of information with the PIF/NDF in view of the large impact of their interventions on the economy.

- **Enhancing the communication on the operational framework.** Effective communication on SAMA's framework—including the modalities with which it pursues its operational target—would improve public understanding of monetary developments and enhance banks' willingness to engage in different market segments.

22. Efforts to create the emergency liquidity assistance (ELA) framework should be accelerated. In line with longstanding FSAP advice, formulating and developing a formal ELA framework is an important component of any central bank toolkit to address temporarily illiquid but solvent banks. SAMA has established an ad-hoc term repo facility, which aims to provide emergency liquidity to local banks, should the existing overnight repo and term repo facilities fail to address banks' liquidity. Staff recommends that a clear criterion as to when and why to provide an ELA should be set—with the ELA provided only as long as the liquidity shortage persists and against a broader set of collateral at a penalty rate to viable banks. This should be separated from standard monetary policy operations because of its focus on individual institutions rather than the entire banking system.

23. The pegged exchange rate regime has been serving Saudi Arabia well in supporting monetary stability. Over the longer term, the peg should continue to be reviewed periodically to ensure it remains appropriate. Reforms to deepen money and capital markets and further strengthen the monetary policy framework should continue to ensure institutions are in place to support a more independent monetary policy in the future if this becomes appropriate. Saudi Arabia's external position is substantially stronger than that implied by medium-term fundamentals, with the buffers well above the minimum level defined under the ARA metric (Annex V). Competitiveness-enhancing reforms and a sizeable investment program, including by PIF, will help align the external position in the medium term, while implementing a medium-term fiscal framework will support fiscal consolidation.

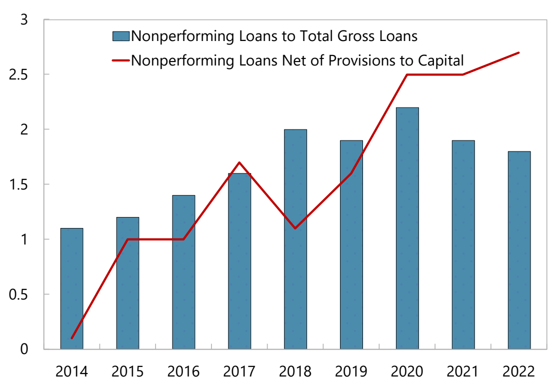
Authorities' Views

The authorities agreed that monetary policy should continue to support the peg and ensuring that liquidity levels in the banking system remains adequate. They highlighted that the temporary liquidity pressures have been eased due to their timely and resolute action. Going forward, they will continue to primarily use market-based methods (e.g., open market operations). They welcomed forthcoming Fund technical assistance on liquidity forecasting and agreed on the importance of finalizing a formal emergency liquidity assistance framework.

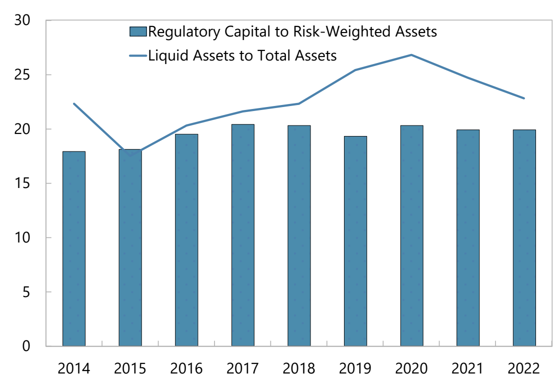
C. Financial Sector Policies

24. The banking system remains on a solid footing. The aggregate capital adequacy ratio is strong (well above the regulatory minimum), profitability is high and above pre-pandemic levels, and the NPL ratio is low and declining. While growth in mortgages has recently moderated, demand for project-related and consumer loans is expected to remain strong, helping offset the impact on profitability from rising funding costs linked to higher policy rates and shift in banks' liabilities towards more time and saving deposits. Spillovers from the collapse of Credit Suisse and several mid-sized U.S. banks have been limited.

Asset Quality
(Percent)



Capital Adequacy and Liquidity
(Percent)



Sources: Haver Analytics and IMF staff calculations

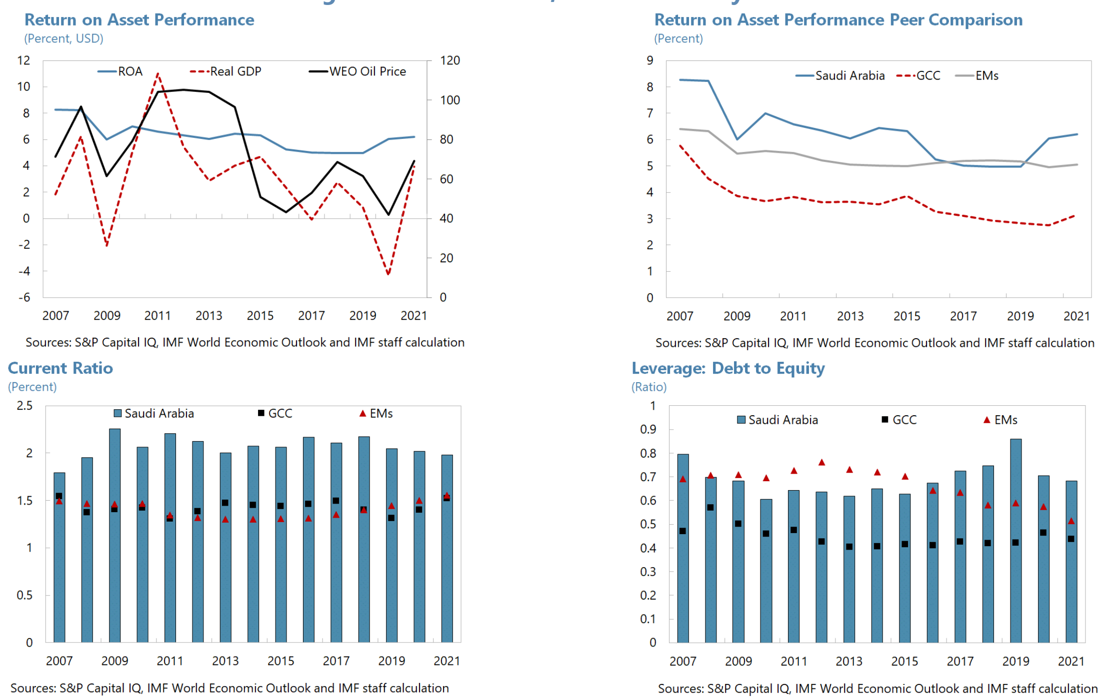
25. The impact on banks of tighter monetary policy conditions has been muted. While banks suffered some losses on their marked-to-market portfolios in 2022, net interest margins have been increasing given that the vast majority of deposits are unremunerated. According to SAMA calculations using end-December 2022 data, the repricing of all bonds classified as held-to-maturity to reflect the increase in interest rates would lower the capital adequacy ratio by less than a percentage point. Staff and the authorities considered capital buffers—which already include a capital conservation buffer—to be adequate to withstand these effects. Furthermore, the assessment of corporate vulnerabilities suggests that despite declining profitability, the corporate sector remains resilient to macroeconomic shocks (Box 1).

Box 1. Saudi Corporate Performance and Resilience to Shocks

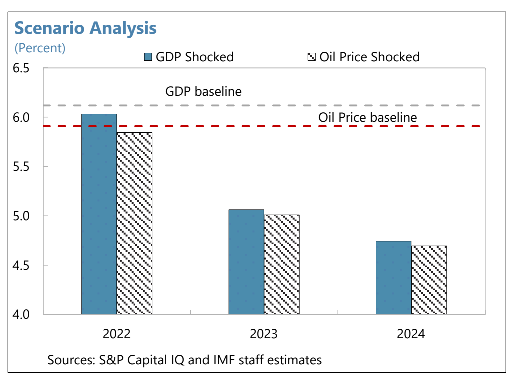
Company coverage
200+ yearly companies
19 major sectors
42 subsectors
560,375 SAR median total assets
288,650 SAR median total revenue

Corporate profitability in Saudi Arabia had been on a declining trend but remains high and above peers. Using a sample of 200+ companies, return on asset declined from 8 percent in 2007 to about 6 percent in 2021—a trend influenced by global market developments and that reflects fluctuations in oil prices that impacted the economy. However, Saudi Arabia has consistently outperformed peers in the GCC and EMs, while maintaining consistently high liquidity (Figure 1). While the leverage ratio is still low and allows for some room, it is higher than comparators in the region and caution should still be exercised in the period ahead in view of higher interest rates and the large funding needs expected from forthcoming large investment programs (including through Shareek).

Figure 1. Saudi Arabia, GCC and EM Stylized Facts



Firms' profitability remains resilient to shocks. Performing a panel data analysis using firm-level data drawn from S&P Capital IQ (CompStat) database (2007-2021), and data collected from the IMF World Economic Outlook, staff estimated[1] that profitability is largely persistent and positively associated with real GDP growth and oil price. A two standard deviation decline in real GDP (about 7 percent decline), or a two-standard deviation decline in oil prices (about a 50 percent) would keep return on assets above 4 percent even two years after the shock.



[1] Return on assets was dynamically projected utilizing a generalized method of moments approach with a two-step robust estimation method. The model examined the relationship between average firms' Return on Assets (ROA) and various lagged independent variables (IVs), including lagged values of ROA, Total Assets, Capital Ratio, Asset Turnover, Debt-to-Equity Ratio, and macro variables (GDP and WEO Oil Price).

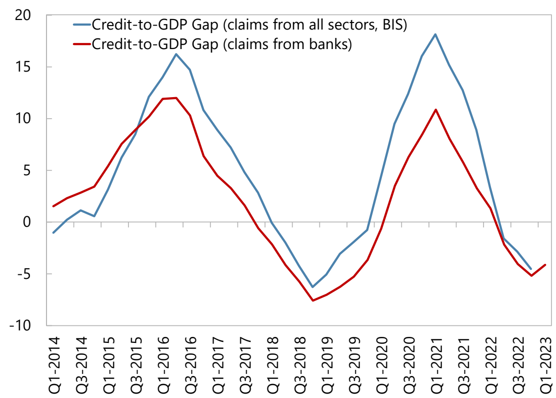
26. Despite the mortgage boom in recent years, banking sector risks from the housing sector are assessed to be low. Driven by the initiatives under the Saudi Housing Program, mortgages have expanded since 2018 becoming an important part of bank portfolios. However, the risks emanating from mortgage lending are relatively contained (see Annex VI for more details). Although house prices have been growing fast in a few specific areas, there are no signs of over-heating and house prices in Saudi Arabia remain moderate compared to other GCC countries as demand (even incentivized) has not significantly outpaced the supply of dwellings. Most mortgages are subsidized, issued at a fixed interest rate, with a full recourse, and repayments made by salary assignments from public sector employees, which contribute to repayment discipline.

27. Strong bank performance is underpinned by ongoing efforts to modernize the regulatory and supervisory frameworks. Most of the 2017 FSAP recommendations have been implemented, including the roll-out of the risk-based bank supervision framework, and adoption of IFRS9 requirements for banks (Annex VII). As of January 1, 2023, SAMA implemented Basel III final reforms with regards to capital requirements, which included refinements to risk-weighted assets and a revised leverage framework. The temporary regulatory measures introduced in 2020 in response to the COVID-19 pandemic were phased out in 2022 and early 2023 (these included loan deferral and guaranteed lending programs) with limited or no impact so far on asset quality. Work is currently under way on the finalization of the draft Banking Law, which will seek to strengthen the framework for bank licensing, regulation, and supervision—including removing the provision allowing individual exemptions from regulation. Ongoing work to strengthen the regulatory framework for Islamic banks and to issue implementing regulations for the Resolution Law is welcome.

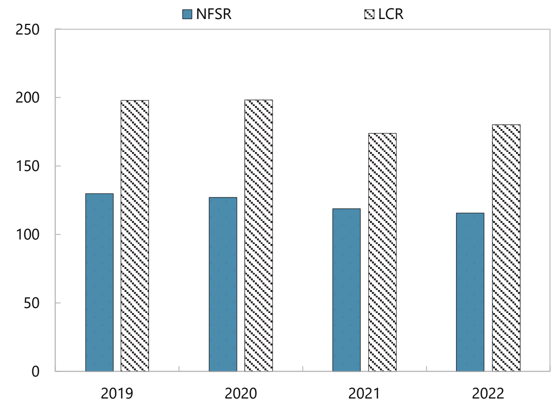
28. Nevertheless, the authorities should remain vigilant. Rapid credit growth, especially of mortgages, calls for closely monitoring credit underwriting and credit management practices in banks. Early detection of debtors and exposures in distress, timely recognition of loan delinquencies, and adequate provisioning are very important. In this regard, the thematic onsite inspections by SAMA of banks focusing on review of corporate loan portfolios or evaluation of mortgage portfolios are welcome. Regular implementation of ICAAP and ILAAP helps improve risk management, while the ongoing SAMA's annual assessment of the countercyclical capital buffer is very timely. More generally, SAMA's efforts to enhance systemic financial risk analysis by reviewing the National Financial Stability Index are commendable.

29. In case of persistently elevated credit growth, staff recommends gradually tightening macroprudential measures. Despite rapid credit growth, a negative credit-to-GDP gap suggests that systemic risks are currently low and there are no signs of overheating. Liquidity indicators of the banking sector, such as the liquidity coverage ratio (LCR) and the net stable funding ratio (NSFR), remained well above 100 percent. If elevated credit growth persists, a tightening of macroprudential measures will be needed, including by reducing the loan-to-value ratio for first-time home buyers, tightening the guideline on the loan-to-deposit ratio, and lowering the debt service-to-income ratio. Phasing out fiscal incentives provided for house mortgages should also be considered. Also, the composition of banks' liabilities should be carefully monitored with a view to avoid creating vulnerabilities relating to wholesale or foreign funding.

Credit-to-GDP Gap
(Percent)



LCR and NSFR of Banking Sector
(Percent)



Sources: Saudi Central Bank and IMF staff calculations.

30. SAMA's efforts to promote the Kingdom as a fintech hub are welcome. The Fintech Strategy was approved in May 2022, building on SAMA's ongoing efforts to foster the fintech ecosystem, with financial inclusion and fintech activity diversity continuing to improve. Since the regulatory sandbox was established in 2018 to help gain insights and assess the impact of emerging technologies, the number of fintech in operation has increased to 147 by December 2022—with 89 companies licensed or authorized by SAMA, which is spearheading the issuance of forward-looking regulations and frameworks. In April 2022, SAMA initiated a public consultation on implementing a law to regulate payments and payment services (which constitute 30 percent of fintech companies' registered activities). In addition, SAMA is implementing Cyber Resilience Fundamental Requirements, which should help Saudi financial institutions manage and mitigate a wide range of cyber risks.

31. SAMA is building on existing expertise to explore further Central Bank Digital Currency (CBDC) use. Through its Aber CBDC project, SAMA was one of the first central bank in the world to experiment with domestic and cross-border wholesale CBDC. Leveraging the lessons of the experiment, SAMA is continuing to explore CBDC use cases with a focus on evaluating the domestic wholesale design. SAMA is undertaking a three-phased approach (evaluation, testing, implementation), allowing for ongoing assessment at each stage, against which the future roadmap will continue to evolve.

32. Efforts to improve the effectiveness of Anti-Money Laundering/Combatting the Financing of Terrorism (AML/CFT) framework should continue. The National Risk Assessment is being finalized and its findings should then serve as the basis to further improve the prioritization of mitigation measures. Saudi Arabia continues to enhance coordination on AML/CFT between the competent authorities. Strengthening the framework for confiscation of major proceeds of crime is also ongoing, including through raising the capacity of various AML/CFT stakeholders. SAMA continues to enhance AML/CFT supervision, including monitoring risks associated with fintech.

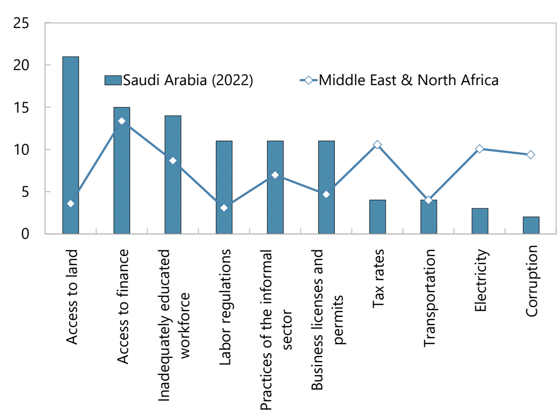
Authorities' Views

The authorities shared staff's views about the strong performance of the banking sector, highlighting that risks from higher credit growth (including mortgages) or global spillovers are relatively contained. They noted that their move to Basel III reforms and full IFRS 9 implementation ensures adequate capital buffers in case of risks, which are further minimized through regular thematic inspections and rigorous monitoring. They project that credit growth will remain in single digits, lessening the need to tighten macroprudential tools in the near term. They noted plans to continue enhancing the regulatory framework, including by adopting the recently revised Banking Law, implementing regulations to the resolution law, and on AML/CFT (including monitoring cyber risks). They highlighted that SAMA remains on top of financial innovation, while work on CBDC is still exploratory in nature at this stage.

D. Structural Reforms for Strong, Sustained, and Inclusive Growth

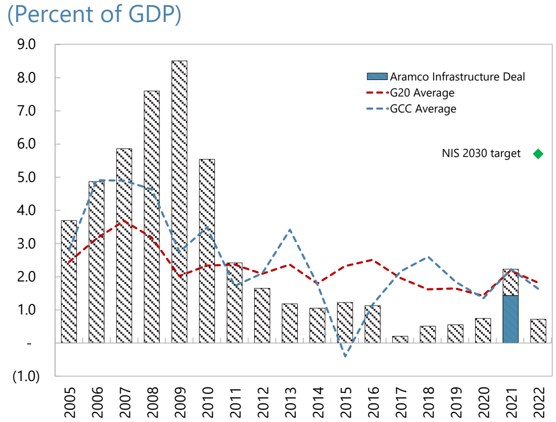
33. Saudi Arabia's structural reform agenda under Vision 2030 is aimed at diversifying its economy and boosting growth. A mid-way stocktaking of the objectives set under Vision 2030 has identified important progress in improving the regulatory and business environment, reducing costs to setting up a business, enhancing digitalization and further reforming labor markets—in some cases with targets set for 2030 already surpassed (Annex VIII). The PIF is expected to catalyze private investment by providing seed money in strategic areas and in industries where the private sector presence has been limited (e.g., electric vehicle production). It is also taking an increasing role in restructuring some sectors (e.g., aerospace). During 2022, new investment deals have increased by 95 percent in 2022 while new investment licenses grew by 267.4 percent, mostly in construction and

Top Ten Business Environment Constraints
(Percent of firms)



Source: World Bank Enterprise Surveys 2022

Foreign Direct Investment
(Percent of GDP)



Sources: Haver Analytics; Authorities data; and IMF staff calculations
Note: The sharp increase in net FDI inflows in 2021 is attributable to a $12.4 billion infrastructure deal by Aramco with a global investor consortium.

manufacturing. However, total factor productivity needs to be enhanced and FDI inflows remain low while diversification into sophisticated products—i.e., those that boost overall economic complexity—is limited. The latest World Bank Enterprise Survey points to access to land, access to finance, and education of the workforce as the main constraints to investment.

34. Decisive progress in the following areas will help enhance private sector development and sustain growth:

- **Improvements in the regulatory environment**. The implementation of recent laws (e.g., on commercial courts and insolvency framework) have helped protect investors' rights, including by expediting court cases facilitated by an extensive digitalization effort. The new Investment Law currently shared for public consultation will help create a level playing field for Saudi and non-Saudi investors by protecting investors' rights and upholding transparency. The creation of the Saudi Center for Commercial Arbitration is anticipated to notably decrease the time and expenses associated with dispute resolution. An effective communication strategy to announce forthcoming policy changes will help ensure policy certainty, anchor investors' expectations, and reduce any investors' wait-and-see attitude.

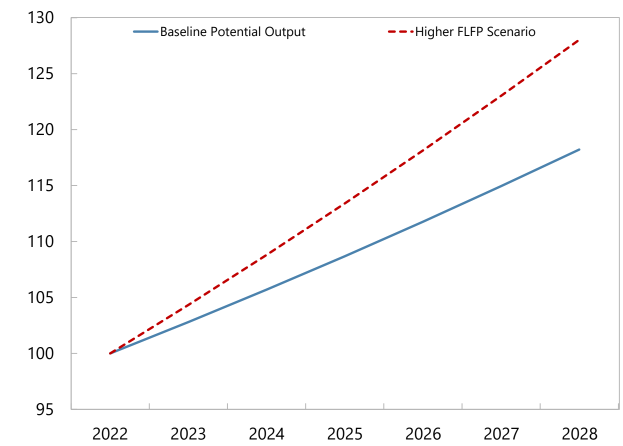
Law/Regulation	Objective	Status
Commercial Courts Law	Efficient resolution of commercial disputes in KSA, including through expedited procedures, and mandatory mediation.	✓
Mining Investment Law	Accelerate foreign investment in the mining sector including by facilitating investor access to financing and supports exploration and geological survey activities.	✓
Anti-concealment Law	Prohibit concealment of ownership and beneficiary.	✓
Competition Law	Prohibits anti-competitive practices and agreements.	✓
Foreign Investment Law	Permit foreign investors to wholly own companies in most economic sectors, removing the requirement for a Saudi partner. It safeguards investors against expropriation and allows profit transfers abroad.	✓
Amending the List of Activities Excluded from Foreign Investment	Amendment allows foreign investment in the following services: domestic labor; audio and visual; land transport services; and home brokerage services.	✓
Anti-fraud and Breach of Trust Law.	Foster transparency and accountability, effective governance and responsible enablement through detailed punitive action for fraud.	✓
Companies Law	Simplifying the management of companies, thereby encouraging investment.	✓
New investment Law	Encouraging investment through incentives and fair treatment between local and foreign investors. Promoting investors rights, including through fair competition, dispute settlement.	In progress
Consumer protection Law	Safeguard the rights of consumers by preventing deceptive and unfair business practices. Ensure fair trade, competition and accurate information in the marketplace.	In progress

Sources: Authorities and IMF staff.

- **Streamlining fees**. The proliferation of fees, although serving to mobilize revenues at the local and municipality level, also distort the playing field as these tend to be regressive and are a key constraint to operating a business for SMEs and micro enterprises. Staff welcomes the ongoing work by the Non-Oil Revenue Center to streamline and standardize the numerous fees faced by businesses in Saudi Arabia. Such an exercise should also be conducted holistically so that it takes into account tax policy reforms envisaged by the Kingdom.

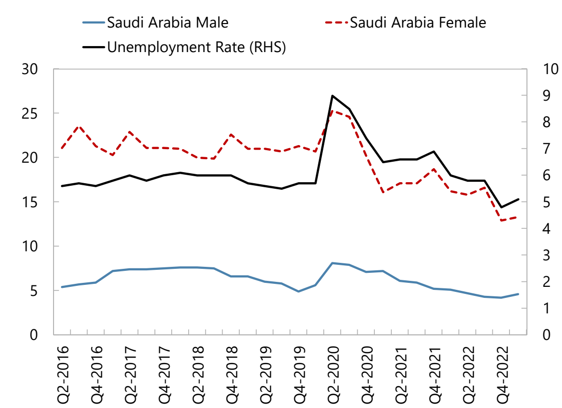
- **Labor market reform**. The rapid growth in the economy—and its ambitious transformation goals—will require a larger pool of highly skilled labor force, both Saudi and non-Saudi. The capacity of Saudi Arabia to scale up and reduce the wage premium will be supported by the recently launched Human Capital Development Program and the Labor Demand Foresight Unit. The authorities have made strides in promoting gender equality, which resulted in a doubling of the Saudi female labor force participation since 2017, facilitated by the removal of formal restrictions in the legal code, employer incentive schemes, childcare assistance, and training and scholarships. The much faster-than-anticipated progress should be sustained, with a new target being established while considering additional initiatives and ensuring alignment of female human capital with sectoral and diversification initiatives. Potential growth gains from increasing female participation to the OECD or G20 average are estimated at 1.6 percent per annum. The launch of the Women Empowerment initiative will support the momentum, notably through the authorities' gender budgeting program in the annual budget process.

Potential Output Gains from Higher Female Force Participation
(Projected potential Output, 2022=100)

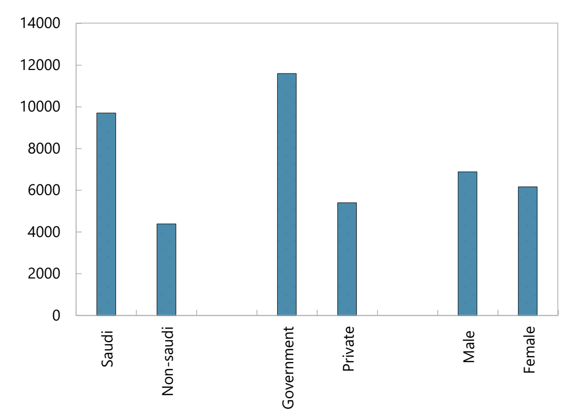


Sources: GaStat, Haver, World Bank, ILO and IMF staff calculations.
Note: Using a production function approach, we decompose the level of income into productivity, stock of physical capital, and human capital components. We assume that male and female labor are additively separable.

Unemployment Rates
(Percent)



Average Monthly Wages
(SAR, latest available)

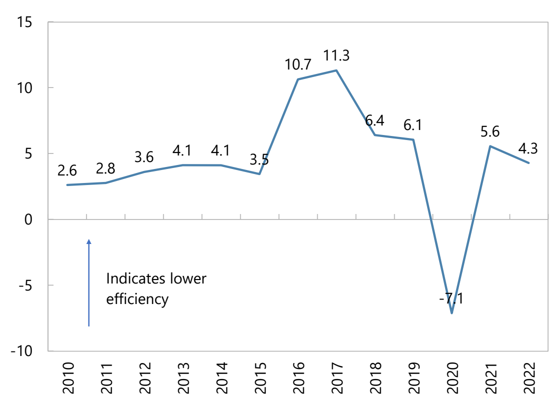


Sources: GASTAT, country authorities, World Bank, and IMF staff calculations.

- **PIF interventions**. PIF's policy to undergo a rigorous cost-benefit analysis of its projects, including through a systematic analysis of exit and divestment options for any new deal— as well as a regular monitoring of risks and reprioritizing projects to ensure high risk-adjusted returns—is welcome. It will be important to ensure that private sector investments are not crowded out, with PIF clearly communicating its exit strategy—i.e., through IPOs, as was the case for Tadawul—to help clarify policy intentions and avoid persistent perceptions of crowding out, as currently communicated notably through increased engagement with the private sector.

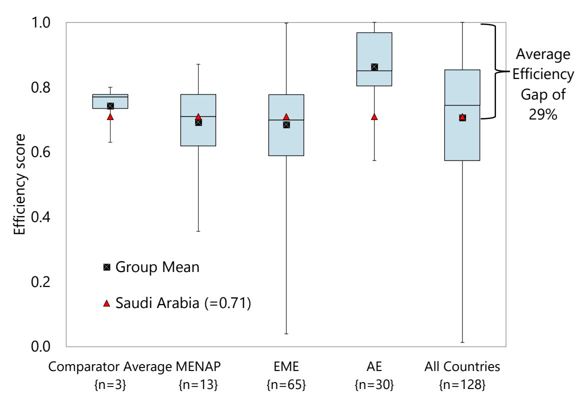
- **Increasing investment efficiency,** including through effective project selection and appraisal, feasibility, and governance framework, in particular as investments are mobilized through PPPs and avenues that fall outside the traditional budget process. Staff welcomes efforts made to address these weaknesses at the government level—including through better prioritization, monitoring and evaluation. With efficiency scores still showing some gaps, this will be increasingly important as public led investment projects are being ramped up. To that end, a unified public investment management system would be critical to ensure that the same rigorous standards are used across the country (whether it is for Vision Realization Programs, Giga projects, or PPPs). Proper guidelines should also be applied to projects where the PIF or NDF participate and that benefit from government guarantees. A Public Investment Management Assessment (PIMA) could help better benchmark the current framework and identify priorities ahead.

Non-Oil Sector Incremental Capital Output Ratio (ICOR)
(Ratio)



Sources: IMF staff calculations.

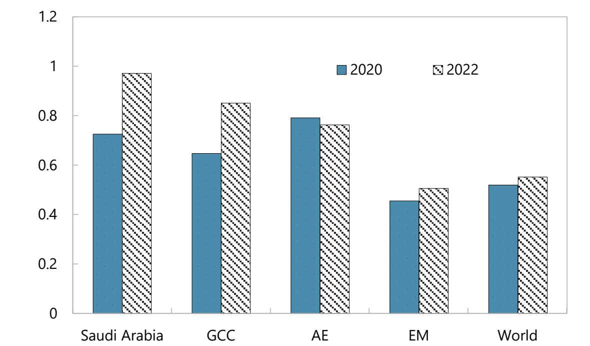
Public Investment Efficiency, 2000-2019
(Efficiency score 0-1)



Source: IMF Tool for Investment and Efficiency (2021)
Note: Comparator average takes the average of UAE, Bahrain, and Oman.

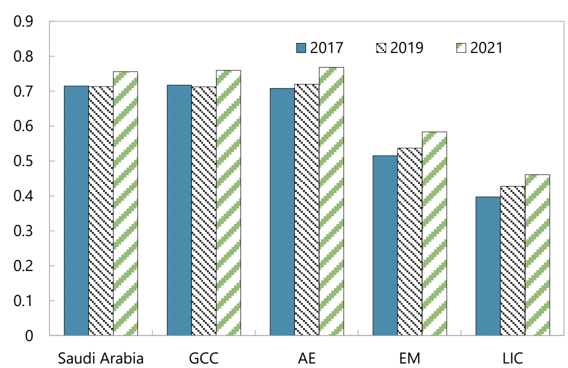
- **Digital Transformation**. Since the launch of the ICT sector strategy in 2019, the digital economy has already surpassed its key 2023 targets and ranks high globally on digital infrastructure and the maturity of digital government transformation. Staff's estimates show that strong digital development in Saudi Arabia has improved financial inclusion, the resilience of the financial sector, and enhanced government effectiveness. However, Saudi Arabia still lags high-income countries on some measures of financial inclusion and usage of digital financial services. Further progress in improving digital literacy and skills, deploying high-speed internet access, cyber security measures, and activating e-participation for all segments of the population remain key priorities to further boost growth.

GovTech Maturity Index (GTMI)
(Index: 0-1, 1=highest maturity of digital government)

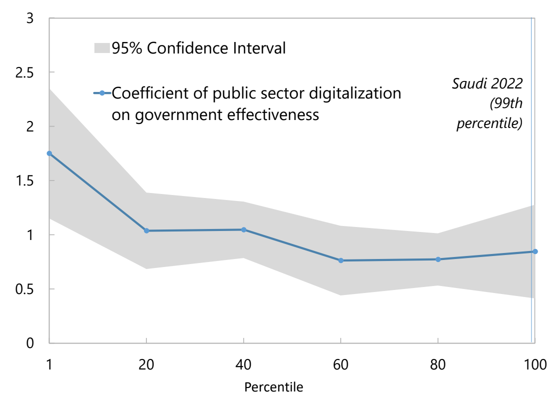


Sources: World Bank.

Enhanced Digital Access Index (EDAI)
(Index: 0-1, 1=highest level of digitalization)



Impact of Public Sector Digitalization
(100 percentile = highest level of public sector digitalization)



Sources: World Bank and IMF staff calculations.
Note: The impact of public sector digitalization is assessed in a quantile regression by regressing a government effectiveness index on a measure of public sector digitalization (i.e., GTMI) with additional control variables.

35. Strengthening governance is an important priority. The implementation of past governance and anti-corruption advice is ongoing, with progress currently being made in finalizing the anti-corruption strategy and measures to strengthen the transparency of public procurement—including to collect information on beneficial ownership. The approval of the anti-corruption agency (Nazaha)'s by-laws should be accelerated to allow it to fully and independently exert its mandate and prepare important milestones, which include an asset declaration framework and an enhanced framework for prosecuting illegal enrichment. A whistleblower protection law has also been pending approval.

36. As part of the voluntary assessment of transnational aspects of corruption, staff discussed steps taken to prevent the laundering of foreign proceeds of corruption and the payments of bribes to foreign public officials. Good progress has been made regarding controls on foreign ownership of companies to mitigate the risk of misuse of legal persons and arrangements, effective AML/CFT preventive measures implemented by larger financial institutions, and measures to strengthen ML investigations and prosecutions. Saudi Arabia also made progress regarding the criminalization of the bribery of foreign public officials. However, further improvements are necessary for a more effective prevention and disruption of transnational aspects of corruption (Annex IX).

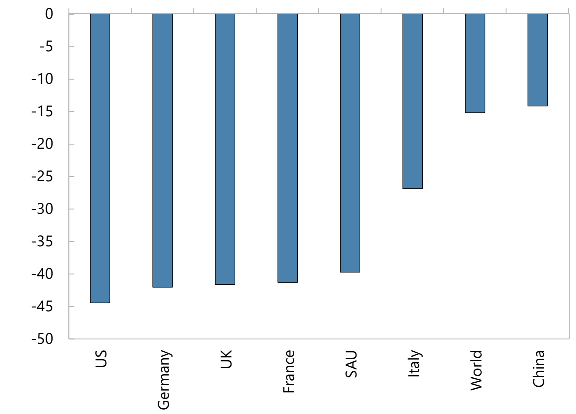
37. While supporting the impressive structural reform efforts, guardrails are needed to minimize inefficiencies associated with industrial policy (Annex X). Saudi Arabia's Industrial Policy (IP) aims to reduce the Kingdom's reliance on oil through targeted interventions, incentives, and the establishment of Special Economic Zones (SEZ). Risks associated with such interventions should be minimized by ensuring they target and rectify market failures, optimizing the allocation of resources. Staff welcomed the ongoing efforts to conduct a cost-benefit analysis on each new IP measure before it is approved and supports the authorities' plans to monitor incentives whose design includes a strict exit criteria, claw-back mechanisms, sunset clauses, and time-bound measures. Moreover, the authorities' intentions to ensure such policies are integrated into the broader reform agenda—fostering backward and forward linkages—and with a special emphasis on export orientation—are welcome. Staff also welcomed the authorities' commitment to remain WTO compliant despite the increasingly protectionist measures rising across the world. However, discriminatory provisions included in the authorities' plans—such as local content requirements in government contracts—should be avoided as they could create distortions in the allocation of production and elicit retaliatory actions by trade partners.

38. Reaching Saudi Arabia's 2030 emissions reduction target hinges on the implementation of the Green Initiative. Saudi Arabia has among the world's largest 's emissions per capita, mainly driven by the energy sector, though the country has the second lowest emissions globally per unit produced, with the reduction in flaring intensity helping it reduce upstream carbon intensity despite higher oil production. Staff welcomes ongoing plans to increase renewable energy by an additional 2.1 GW capacity by 2024, generate savings through efficiency programs, deployment of the Circular Carbon Economy (CCE) technologies (including Carbon Capture Utilization and Storage (CCUS), and becoming the world's clean hydrogen producer. Staff welcomes the roadmap laid out by the authorities to reach net zero emissions scenario, with staff analysis showing that their targets (which were revised up in 2021) can be reached with minimal GDP losses, including after eliminating fuel subsidies (Box). Assessing progress and adjustment necessary to attain Saudi Arabia's emissions target will also require:

- **Additional costing and detailing of specific initiatives** linked to each target and associated emissions reduction—including from afforestation or hydrogen. When included, it is possible that reliance on carbon capture would be less than currently envisaged as necessary to reach the target.

- **Accounting for specific cost uncertainty**. For example, uncertainty about technology and ambiguity about scaling up could impact the GDP loss linked to carbon capture. Albeit, even if the costs were to double from \$50/ton of CO_2eq to US\$100/ton of CO_2eq, mitigation loss is expected to remain in line with mitigations losses identified in the literature (Box 2).

Total GHG Emissions for NDC Scenarios in Different G20 Countries in 2030
(Percent change w.r.t. baseline values)



Sources: Climate Watch and IMF staff calculations.

- **Green finance initiatives**, including through PIF's impulse, and climate adaptation efforts (considering potential risks stemming from increased water demand for agriculture, coastal flooding and soil degradation), such as water and waste management, which are also important priorities.

Saudi Arabia's Green Initiative

	Targets by 2030	Selected initiatives
Reducing emissions	Reducing carbon emissions by 278 mtpa Through more than 5 initiatives	Enhance Energy Efficiency Program Change the energy mix: Increase domestic capacity from renewable energy to around 50 percent, with the remaining majority from gas. Expansion of the master gas system, capitalizing on Circular Carbon Economy framework to increase supply capacity by more than 40 percent (2027). Use captured carbon to produce chemicals and synthetic fuels (2030) Become the world's leading hydrogen producer and exporter (2030)
Greening Saudi Arabia	Plant 10 billion trees across Saudi Arabia Through 24 initiatives	Study on 10 billion trees program Green Mosques Mangrove Plantation pilot at Jeddah Port
Protecting land and sea	Raise protected areas to more than 30 percent of terrestrial and marine areas Through at least 4 initiatives	Establish nature reserves Desert Preservation Initiative Designate 10 biodiversity protection areas of 977 sq.km

Source: Saudi Green Initiative

39. Data provision to the Fund is adequate for Fund surveillance, but further improvements are needed (Informational Annex). Positive developments include a new census published in June 2023, improvements to the labor force survey being completed, a household survey to be ready in Q3 2023, and a chain-linked volume estimation of GDP rebased to a more recent year and planned for Q1 2024. Staff welcomes ongoing plans to refine FDI data compilation based on recent statistical manuals and guides, with help from Fund TA. Staff also welcomed the planned outreach and extensive comprehensive public communication to explain methodological changes when publishing revised data, which would help preserve data credibility. Work on national accounts, price statistics, and external sector statistics as well as government finance statistics should continue, including to classify one-off revenues and expenditures and to move towards a general government concept.

Box 2. From Oil Wells to Solar Cells: Saudi Arabia's Climate Transition

Under the Nationally Determined Contributions (NDC) to the United Nations Framework Convention of Climate Change (UNFCCC), Saudi Arabia has committed to an objective of reducing, capturing, and removing emissions by 278Mt of CO_2eq per annum by 2030, an upward revision in 2021 from the previous 2016 pledge of 130Mt CO_2eq reductions. Saudi Arabia's Green Initiative also includes plans to achieve net zero emissions by 2060, and net zero emissions through Saudi Aramco by 2050.

Scenario	Domestic policies
1. **NDC**	○ No further action
2. FFSR: Fossil Fuel Subsidy removal	○ Subsidies on fossils are phased out by 2030. ○ We assume that the savings from the subsidy elimination are used as follows: One-fifth is redistributed to households (SSN) and the rest is used to increase overall investment.
3. NDC Partial: FFSR + Renewable	○ Subsidies on fossils are phased out by 2030 ○ Subsidies and production taxes to increase solar electricity capacity and natural gas capacity to 50 percent each.
4. **NDC Full:** FFSR + Renewable + CCUS	○ Subsidies on fossils are phased out by 2030 ○ Subsidies and taxes to increase to increase solar electricity generation and natural gas capacity to 50 percent each ○ CCUS abatement costed at US$50/ton CO2 in energy and industry sectors

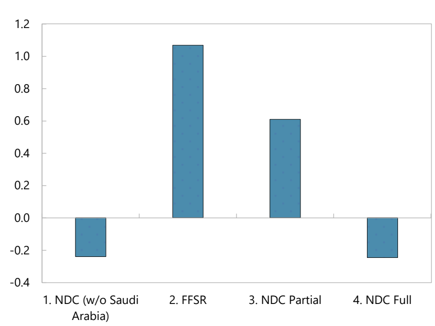
Using the IMF-ENV model, a dynamic CGE model, staff quantified the economic and CO_2 emission impacts of Saudi Arabia's climate transition policies. After calibrating the baseline to staff's current macro-economic framework, four incremental scenarios were considered, starting with no further action then considering a phaseout of fossil fuel subsidies. The subsequent incremental scenarios consider measures to boost renewable energy generation capacity to 50 percent, with the gap being closed by carbon capture at a cost of US$50/ton. In all scenarios, other countries undertake policies aligned with their Nationally Determined Contributions (NDC).

The analysis shows that eliminating fossil fuel subsidies yields a reduction of about 100 million MTCO_2eq (about a third of the reduction target planned for 2030). Adding renewable energy will generate an additional 56 million MTCO_2eq emission reduction, requiring that CCUS be used to reach the 2030 target. At the same time, the GDP loss will be limited to 0.2 percent—a loss smaller than country GDP losses estimated in the literature for global mitigation scenarios which range between 0.4 – 0.7 percent of GDP. Doubling the costs of carbon capture to $100/ton will almost double losses to 0.4 percent, which is still within the estimated range in the literature.

Results—including needed contributions from CCUS—could be further refined once details are available on policy plans considered by the authorities on each of the pillars underpinning their climate strategy. For example, details on afforestation, CCUS, hydrogen—including on financing and investment needs—may help reassess needed contributions from CCUS to reach the authorities' emissions target.

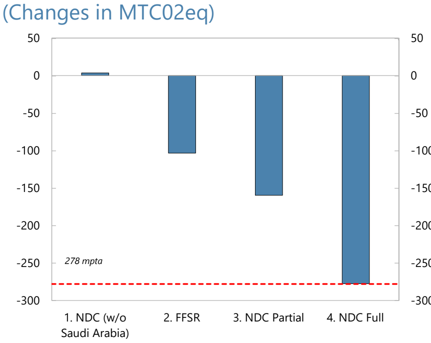
Real GDP Effects for Different Policy Scenarios in 2030

(Change w.r.t. baseline values)



Total GHG Emission Levels for Different Policy Scenarios in 2030

(Changes in MTC02eq)



Sources: IMF staff estimates.

Note: Global mitigation in all scenarios. 1. NDC= Saudi Arabia does not adopt NDC; 2. FFSR= Gradual phaseout of subsidies by end-2030, partially recycled toward social safety net; 3. NDC Partial=FFSR and measures to enhance renewable energy generation; NDC Full = NDC Partial combined with CCUS deployment to close the mitigation gap.

Authorities' Views

The authorities welcomed staff findings acknowledging that the reform momentum has been sustained. They noted that their reform strategy—as outlined in Vision 2030, Vision Realization Programs, sectoral strategies and regional strategies— relies on enhancing private sector role, highlighting the significant progress made in removing legal impediments, enhancing digitalization and reforming labor markets. They emphasized that they have now completed a mid-way stock-taking of Vision 2030, which is leading them to set up more ambitious targets than initially planned given performance so far. They highlighted that the public investment management program is being implemented to improve investment efficiency.

The authorities noted that SEZs and other Industrial policies are being put in place to accelerate the economic transformation in certain areas, with care being taken to ensure these do not undermine the important structural reforms taken. They also stressed that they remain committed to a rules-based global trade system, with great efforts being made to ensure new policies remain WTO compliant.

On climate change, they welcomed staff's results highlighting that implementation of the Saudi Green initiative can deliver on its emissions target reduction. They emphasized that Circular Carbon Economy (CCE) is a balanced, comprehensive, and holistic approach to managing emissions with technologies supported under four principles (Reduce, Reuse, Recycle, and Remove), and they expected that resources spent on R&D will help scale it up significantly.

STAFF APPRAISAL

40. Saudi Arabia's economic transformation is progressing well. Helped by reforms under the Vision 2030 agenda and higher oil prices, Saudi Arabia's economy is booming, the output gap is closed, inflation is contained, unemployment is at a record low, external and fiscal buffers have been rebuilt, and oil contribution to various sectors of the economy is diminishing.

41. The near-term outlook is strong, with risks broadly balanced. Possible revisions in global demand and further shifts in international commodity prices or in OPEC+ oil production schedules bring additional uncertainty to the outlook. Contingency measures—such as tighter fiscal policy and careful calibration of investment spending—should be considered if demand pressures from a rapid ramp up in investment manifest themselves.

42. Additional fiscal adjustment over the medium term would allow Saudi Arabia to maintain stronger buffers and meet intergenerational needs while mitigating risks from oil price volatility. Such a strategy would build on the impressive non-oil revenue mobilization efforts already initiated by maintaining the current VAT rate, reforming corporate income and property taxation, and strengthening revenue administration. Actions taken to reduce energy subsidies are welcome but faster increases in energy prices—including by lifting the cap on gasoline prices—are important as it would help create additional fiscal space and would be critical for long-term fiscal sustainability and the authorities' climate change agenda. This should be accompanied by scaling up well-targeted social programs to limit the impact on the most vulnerable. Continuing to rationalize the public sector wage bill, greater efficiency in public investment, and full utilization of the expenditure chain are also welcome parts of this strategy.

43. Sustaining medium-term fiscal consolidation will be necessary to ensure intergenerational equity. A strict application of a fiscal rule—preferably based on a simple expenditure rule—would help support the authorities' plans to delink spending decisions from oil price fluctuations. Moves taken to develop an MTFF, improve budget forecasting, strengthen disclosure, monitor fiscal risks, and broaden public sector coverage—are welcome and would be important pre-requisites for an effective fiscal rule. Moves towards a treasury single account should be continued while quantifying and reporting tax expenditures would help guide policy decisions.

44. Sound debt management continues to support fiscal policy and mitigate risks. Public debt remains sustainable and low, with ample fiscal space. The authorities' borrowing strategy appropriately aims at lengthening maturities, reducing refinancing costs and building a yield curve. Careful monitoring and disclosure of guarantees and contingent liabilities, including from PPPs, would further help reduce risks.

45. Progress towards developing a sovereign asset-liability management (SALM) framework is welcome and should be accelerated. Establishing a SALM framework is critical to allow the authorities to monitor sovereign balance sheet exposures in an integrated manner and allow the authorities to assess future investment commitments and their funding in a comprehensive manner.

46. The exchange rate peg continues to serve Saudi Arabia well given the current economic structure. Saudi Arabia's external position is substantially stronger than that implied by medium-term fundamentals, with the buffers well above the minimum level defined under the ARA metric. The projected normalization of oil exports together with competitiveness-enhancing reforms and a sizeable investment program, including by PIF, will help align the external position in the medium term.

47. A tight monetary policy should continue to support the exchange rate peg. In view of an open capital account, policy rates should continue to move in line with the Fed's interest rates, with risk premia ensuring an appropriate interest rate differential to support the exchange rate peg. To that end, the monetary policy framework should continue to aim at an interbank rate in line with the policy rate through continued use of market-based instruments, which should be assisted through improved liquidity forecasting and enhanced communication of the operational framework. Establishing the emergency liquidity assistance framework is an important priority.

48. The banking system remains on a strong footing, underpinned by ongoing efforts to modernize the regulatory and supervisory frameworks. The aggregate capital adequacy ratio is strong, profitability is high, and the NPL ratio is low. Despite the mortgage boom in recent years, banking sector risks from the housing sector are assessed to be limited so far. Staff welcomes the roll out of a comprehensive risk-based supervisory framework, the adoption of IFRS9 requirements for banks, the full implementation of Basel III final reforms, and regular implementation of ICAAP and ILAAP. It commends the authorities on the progress made in revising the Banking Control Law, encourages further adjustments in line with international best practices and urges its swift adoption.

49. Rapid credit growth—including mortgages—calls for closely monitoring credit underwriting and management practices in banks. Early detection of borrowers and exposures in distress, timely recognition of loan delinquencies, and adequate provisioning are very important. Staff welcomes SAMA's thematic onsite inspections of corporate and mortgage loan portfolios. Gradually tightening macroprudential guidelines/regulations and phasing out fiscal incentives should be considered in case of persistently elevated credit growth. In this regard, SAMA's ongoing annual assessment of the countercyclical capital buffer is very timely.

50. Progress on implementing the Vision 2030 reform agenda towards a productive and green economy is encouraging. The impressive pace of digitalization, increasing female labor force participation, improvements in regulatory and business environment—along with a new set of laws to promote entrepreneurship and reduce the costs of doing business—have contributed to higher private sector investment. Ongoing measures to boost human capital, streamline multiple fees, expand access to finance, and enact a new investment law would further boost productivity and growth. Careful calibration of the various investment programs—including PIF interventions—would be needed to ensure catalytic effects are in place and avoid private sector crowding out and overheating risks.

51. Ongoing actions to strengthen governance are welcome and should be accelerated. The finalization of an anti-corruption strategy, the adoption of the Oversight and anti-corruption authority (Nazaha) by-laws and of a whistleblowers' protection law are urgently needed. Progress taken to prevent transnational aspects of corruption are encouraging, but further improvements will help ensure a more rapid disruption of the laundering of proceeds of foreign corruption.

52. The authorities' industrial policy agenda should be supporting the impressive structural reform efforts while minimizing associated risks. The authorities' plans to include a cost-benefit analysis, impact evaluation, strict exit criteria, claw-back mechanisms, sunset clauses and time-bound incentives are welcome as they would help minimize risks and phase out policies as needed. Such targeted interventions should not be a substitute for broad-based structural reforms, which should continue to be rolled out. While the authorities' commitment to remain WTO compliant is welcome, preferential policies, such as local procurement for government contracts, are discriminatory and should be avoided, including because they could trigger retaliatory actions by trading partners.

53. The Kingdom's efforts on climate policies are welcome, with the implementation of the Green Initiative essential to meet Saudi Arabia's net emissions reduction plans. Staff welcomes ongoing plans to increase renewable energy, generate savings through efficiency programs, deploy carbon capture, and develop hydrogen production and exports. Pursuing this strategy—along with removing fuel subsidies—will help the authorities achieve their 2030 net emissions target with minimal losses. Going forward, elaborating on specific programs and investments related to each goal will facilitate the evaluation of progress made and the necessary modifications to achieve the emissions reduction objective.

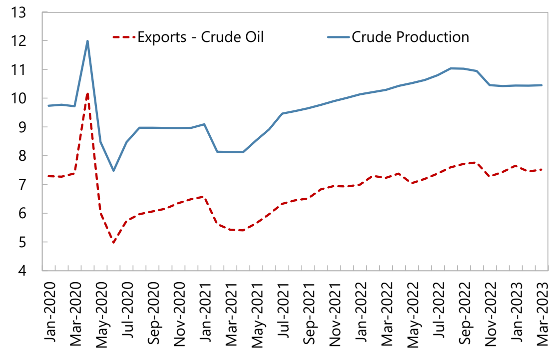
54. Improvements in economic data are welcome and should be sustained. Continued improvements in national accounts, monetary and external statistics and GFS compilation remain priorities.

55. It is recommended that the next Article IV takes place on the standard 12-month cycle.

Figure 1. Saudi Arabia: Real Sector Developments

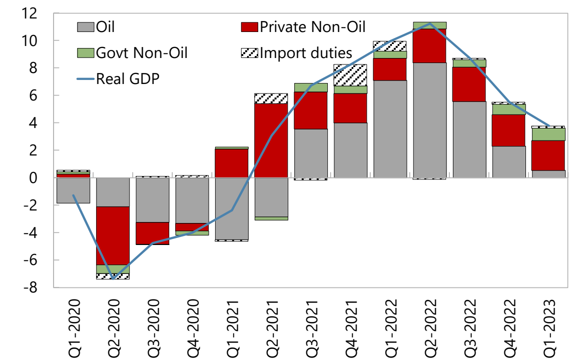
Oil production has trended upwards, but declined recently following OPEC+ production cuts…

Oil Production and Exports
(Million barrels per day)



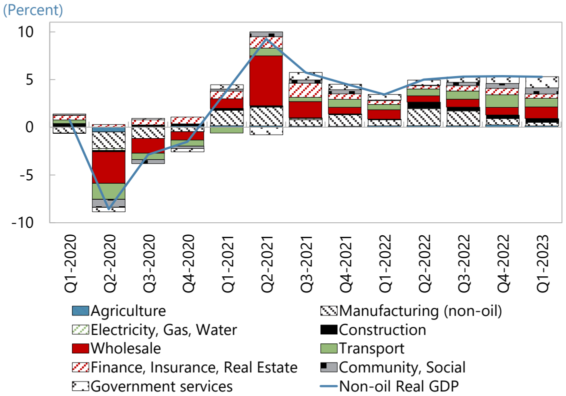
…leading to non-oil GDP representing a larger contribution to Real GDP growth.

Contribution to Real GDP Growth
(Percent)



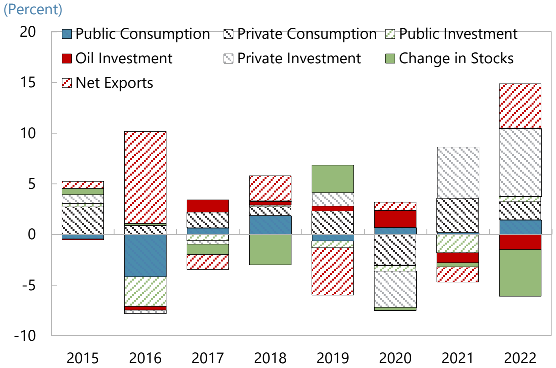
Non-oil growth is driven by retail and construction…

Non-Oil Real GDP Decomposition
(Percent)



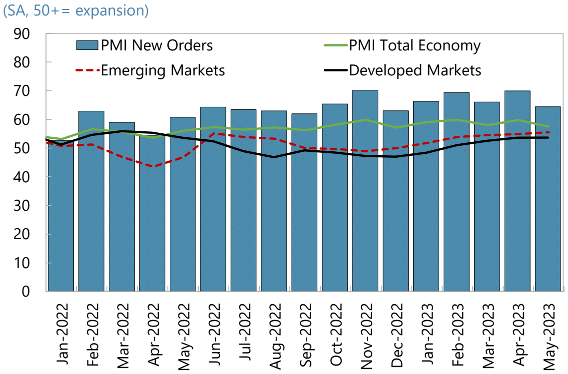
…while private investment drives real growth on the demand side.

Real Demand Side Decomposition
(Percent)



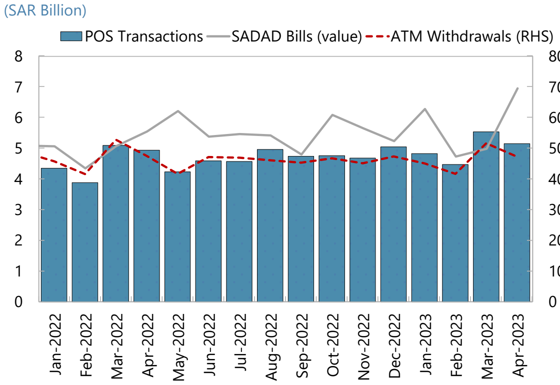
Outlook is positive as PMI remains strong…

Purchasing Managers Index
(SA, 50+= expansion)



…with consumption spending strong as indicated by POS transactions and ATM withdrawals.

POS Transactions and ATM Withdrawals
(SAR Billion)



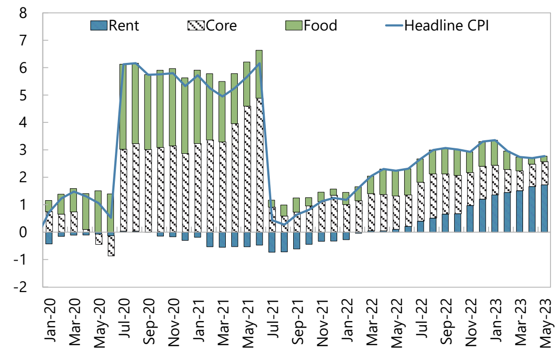
Sources: Haver Analytics, World Economic Outlook, Country Authorities and IMF staff calculations.

Figure 2. Saudi Arabia: Inflation Developments

Headline and core inflation have declined…

CPI Inflation

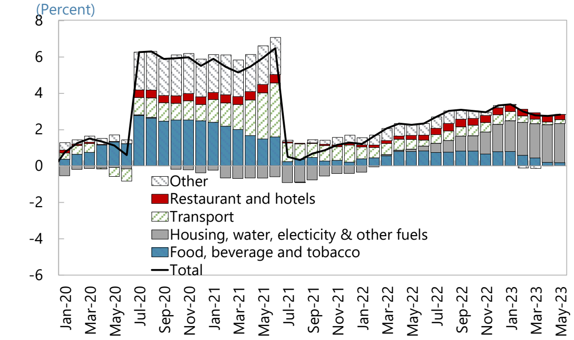
(Y-o-y percent change or contribution)



… with transports and food showing the largest declines.

Contributions to Inflation

(Percent)

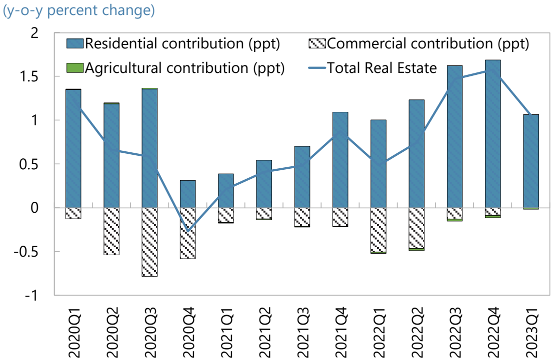


Other includes: clothing and footwear, furnishings, houshold equipment & maintenance, health, communication, recreation, culture, education, miscelaneous.

The real estate sector shows signs of slowdown after a two-year strong growth…

Real Estate Index

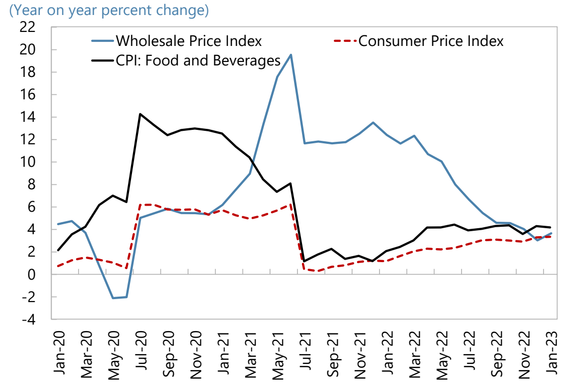
(y-o-y percent change)



… with pressures from wholesale prices subsiding.

Inflation and Wholesale Price Index

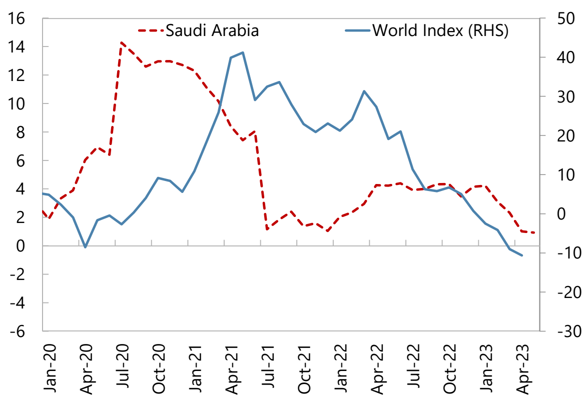
(Year on year percent change)



Food price indices have declined in line with world prices….

Food Price Indices

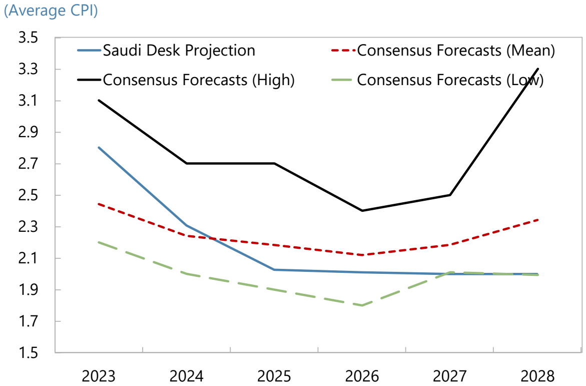
(y-o-y percent change)



…and projections suggest contained inflation.

Consensus Forecasts April 2023

(Average CPI)

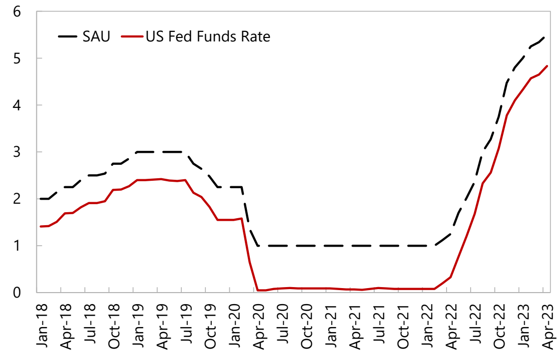


Sources: Haver Analytics, World Economic Outlook, Country Authorities and IMF staff calculations.

Figure 3. Saudi Arabia: Monetary and Financial Sector Developments

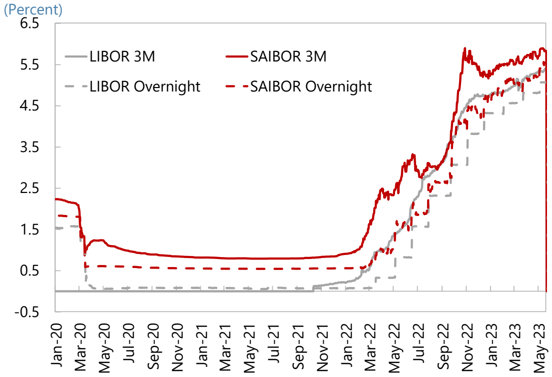
Monetary policy remains aligned with the U.S. tightening cycle…

Policy Rates
(Average, percent)



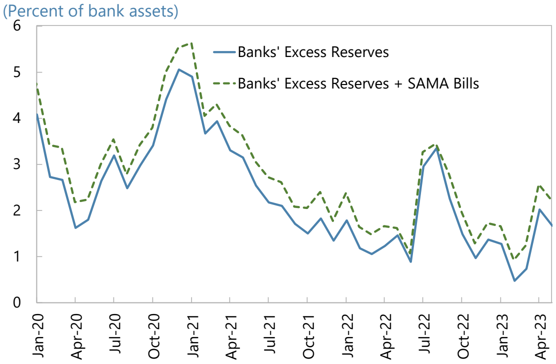
…with SAIBOR/LIBOR spreads recently stabilizing after two episodes of stress in the last year.

SAIBOR and LIBOR
(Percent)



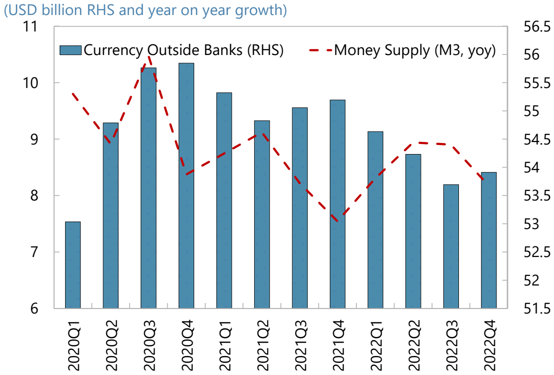
Excess liquidity has now reverted to more normal levels.

Excess Liquidity in Banking Sector
(Percent of bank assets)



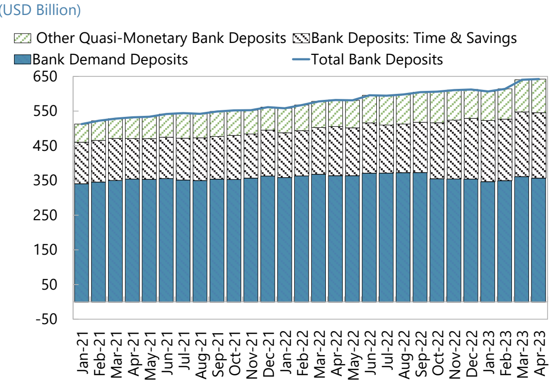
Monetary growth remains robust…

Money Supply
(USD billion RHS and year on year growth)



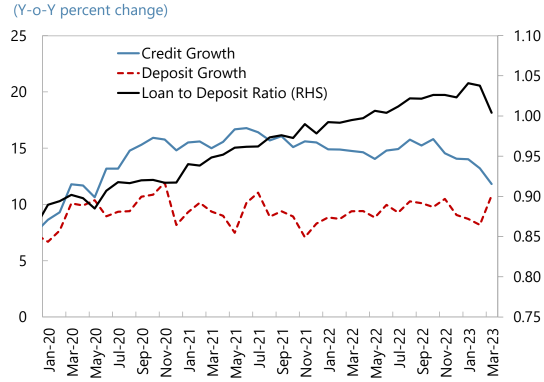
…through deposits, with a shift to time deposits…

Bank Deposits
(USD Billion)



…while credit growth remains high but moderating from recent highs

Private Sector Credit and Deposit Growth
(Y-o-Y percent change)

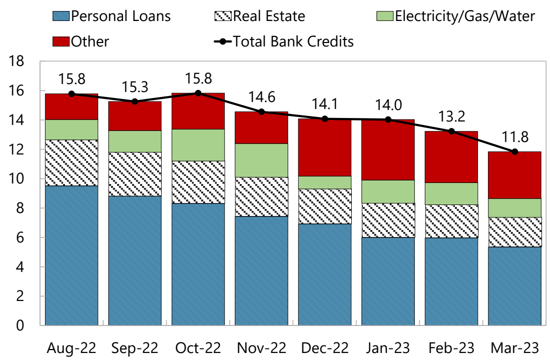


Sources: Haver Analytics, World Economic Outlook, Country Authorities and IMF staff calculations.

Figure 4. Saudi Arabia: Banking and Financial Sector Developments

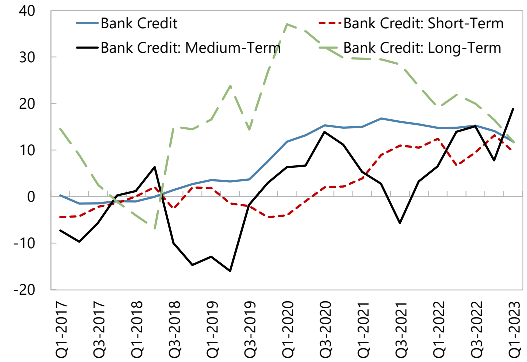
Bank credit growth is slightly declining, driven by personal loans and real estate activities…

Contribution to Bank Credits by Economic Activity
(y-o-y percent change of contribution)



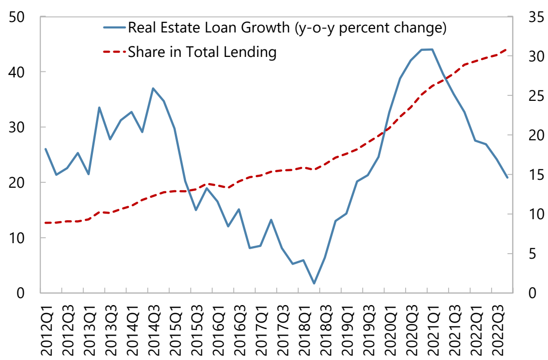
…with growth in long-term credit tapering off more recently

Bank Claims by Maturity
(Y-o-Y percent change)



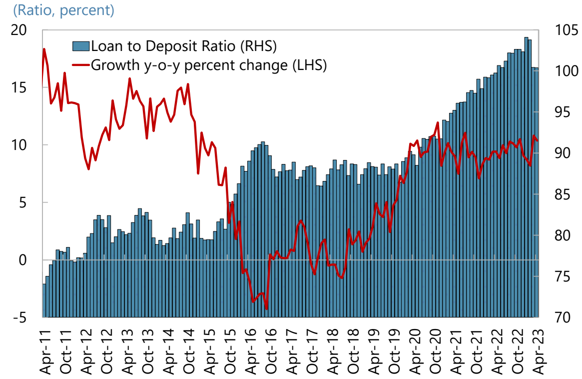
The share of mortgage loans now surpasses 30 percent of all bank loans…

Mortage Loans
(Percent)



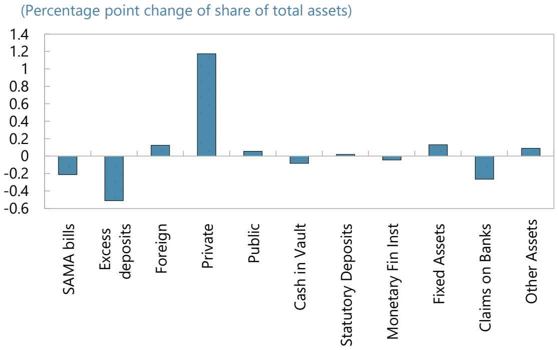
and commercial bank deposit growth remains robust.

Commercial Bank Deposits
(Ratio, percent)



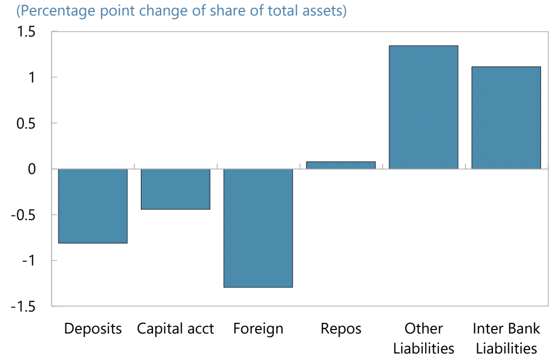
The composition of balance sheets confirms an increase in private assets…

Change in Banking System Balance Sheet Composition, Assets, 2021-2020
(Percentage point change of share of total assets)



…and a decrease in foreign liabilities.

Change in Banking System Balance Sheet Composition, Liabilities, 2021-2022
(Percentage point change of share of total assets)

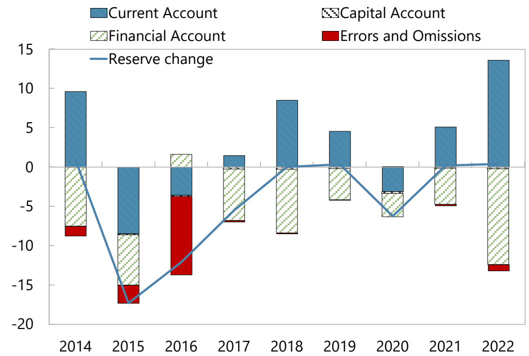


Sources: Haver Analytics, World Economic Outlook, Country Authorities and IMF staff calculations.

Figure 5. Saudi Arabia: External Sector Developments

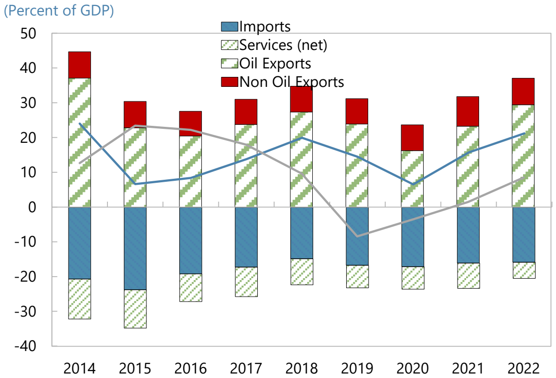
Higher oil prices improved the current account…

Current and Financial Account Balance
(Percent of GDP)



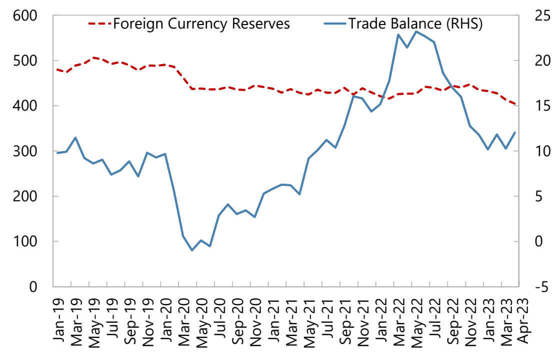
…driven by oil, but also ongoing diversification suggested by a lower services deficit.

Trade Balance
(Percent of GDP)



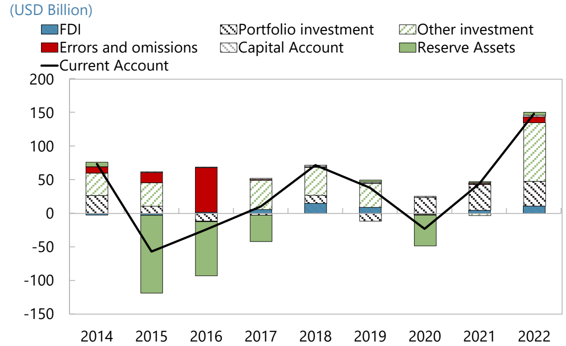
However, reserve accumulation has been tepid

Foreign Reserves and Trade Balance
(EOP, USD Billion)



…driven by sizeable foreign assets acquisition abroad, including by PIF and Aramco.

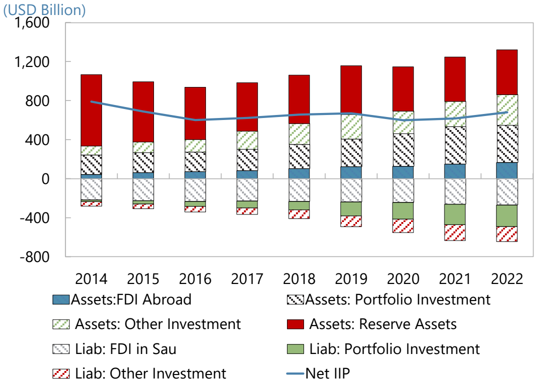
Balance of Payments
(USD Billion)



Note: Net flows shown.

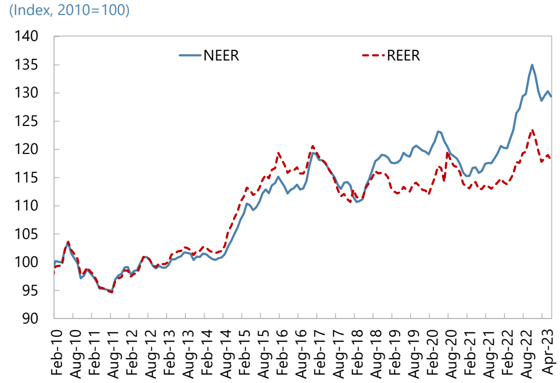
That said, the external balance sheet remains robust, including with reserves exceeding ARA metrics.

International Investment Position
(USD Billion)



NEER appreciation driven by the dollar and with inflation less than in trading partners, the REER appreciated less.

Real and Nominal Effective Exchange Rate
(Index, 2010=100)

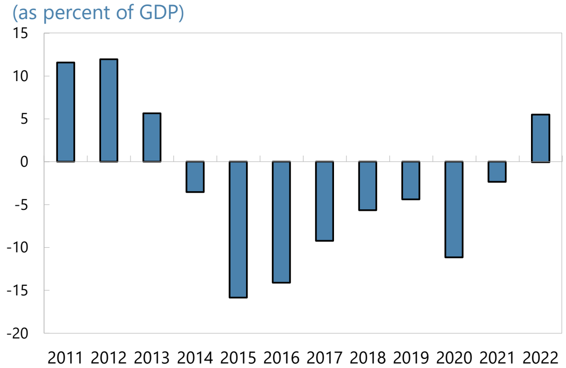


Sources: Haver Analytics, World Economic Outlook, Country Authorities and IMF staff calculations.

Figure 6. Saudi Arabia: Fiscal Developments

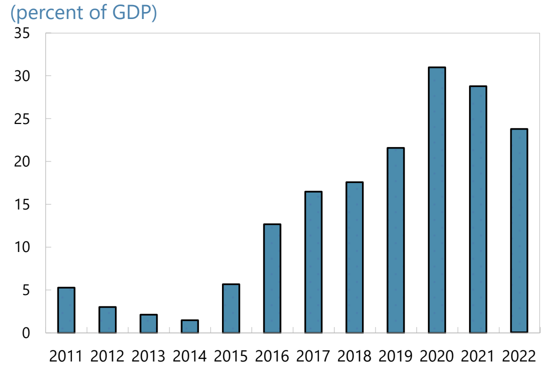
Fiscal performance has improved with the return to a surplus in 2022…

Fiscal Performance
(as percent of GDP)



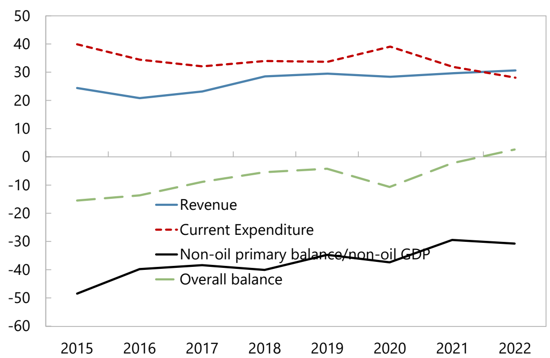
…with debt levels improving and remaining low

Central Government Gross Debt
(percent of GDP)



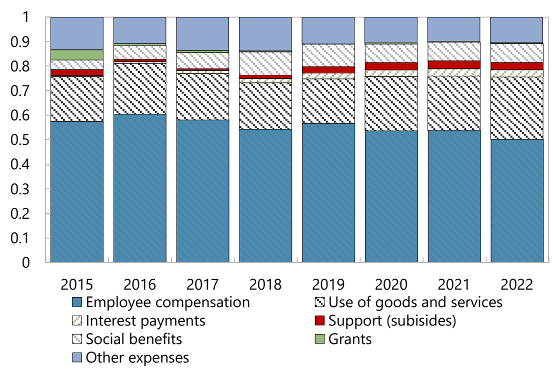
Current expenditures have been contained…

Spending, Revenue and Overall Balance
(Percent of GDP)



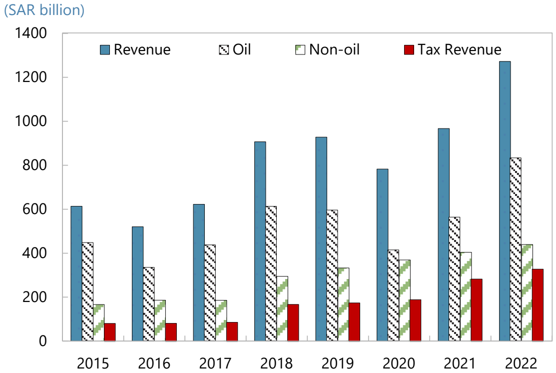
…with employee compensation slightly decreasing as a share of expenditures

Expenses
(Percent of total)



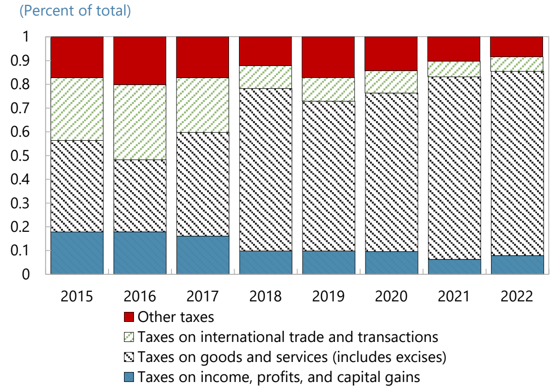
Revenue increased because of sizable oil windfalls….

Government Revenues
(SAR billion)



…and a strong pick-up in non-oil revenue from goods and services taxation

Tax Revenue
(Percent of total)



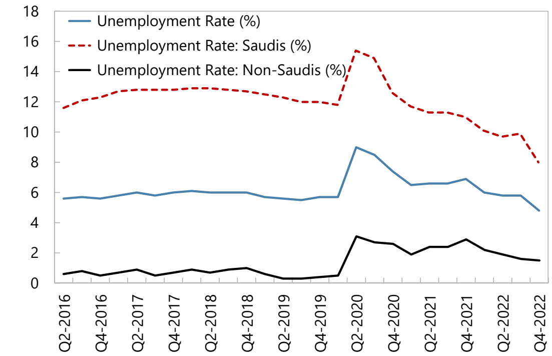
Sources: Haver Analytics, World Economic Outlook, Country Authorities and IMF staff calculations.

Figure 7. Saudi Arabia: Labor Market Developments

The total unemployment rate is trending downward driven by Saudi nationals and expatriates.

Unemployment Rates and Labor Participation

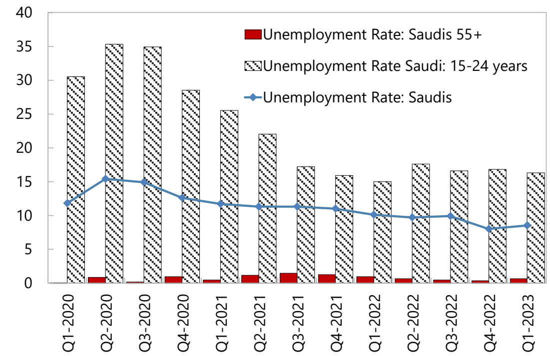
(Percent)



Saudi national employment improved and has been halved for youth.

Saudi National Unemployment Rate by Age

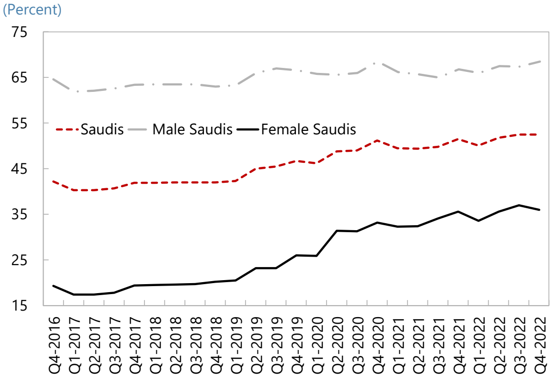
(Percent)



Labor force participation improved, particularly for females.

Labor Force Participation Rate

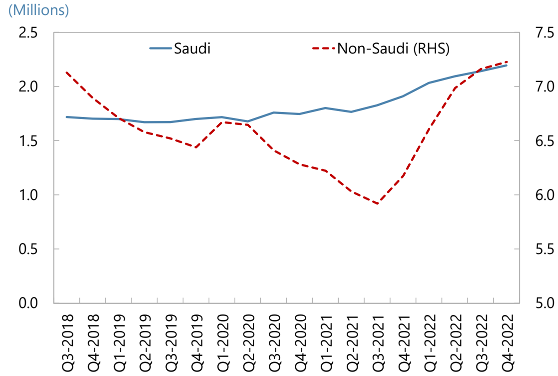
(Percent)



...while private sector employment continues to rise.

Private Sector Employment

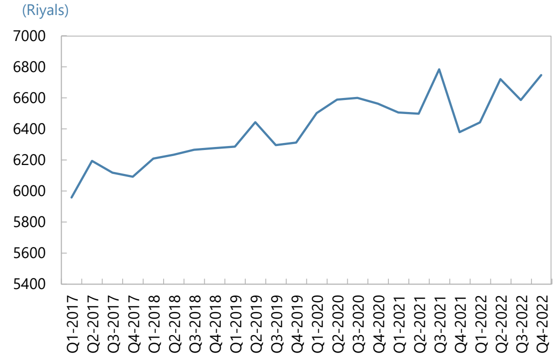
(Millions)



Average monthly wages remain contained, despite a slight increase over the past year...

Average Monthly Wages

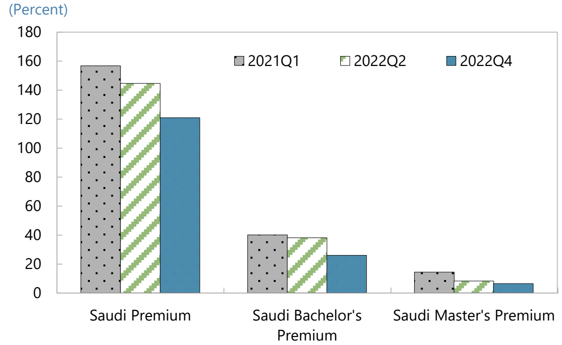
(Riyals)



...but premia remain between Saudi and non-Saudi, also in education.

Wage Premium

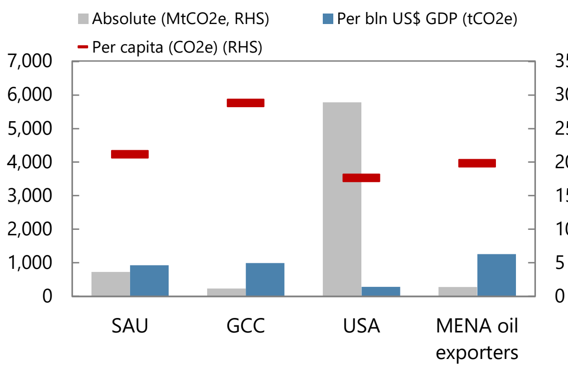
(Percent)



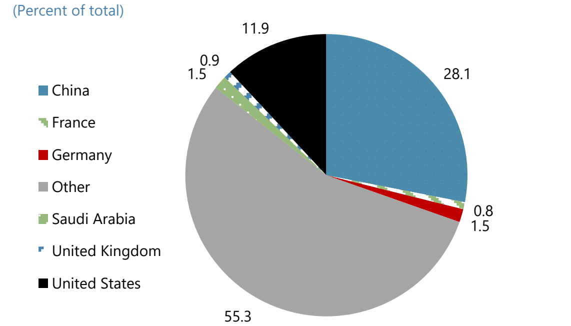
Sources: Haver Analytics, World Economic Outlook, Country Authorities and IMF staff calculations.

Figure 8. Saudi Arabia: Climate Change (2019 or Latest Available)

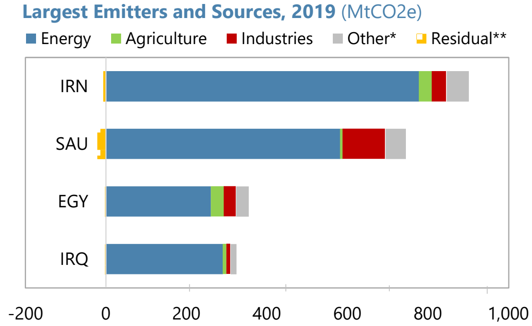
While Saudi Arabia's absolute levels of GHG emissions are low, in per capita terms they are sizeable…



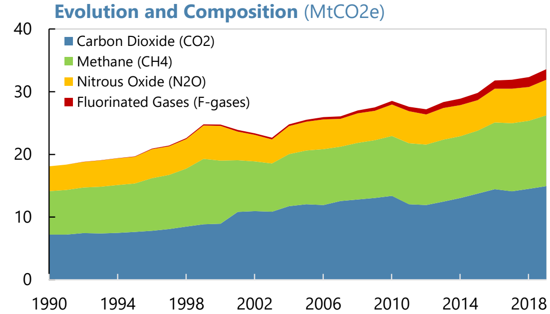
… as well as in terms of shares of global emissions.



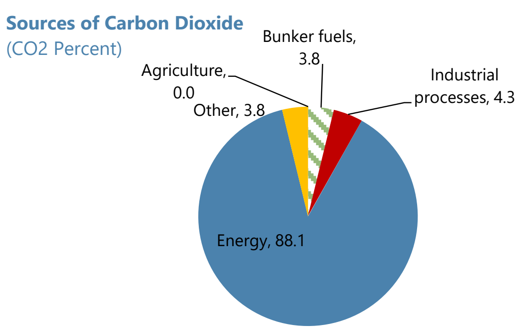
It is also one of the largest emitters in the region, although trailing Iran.



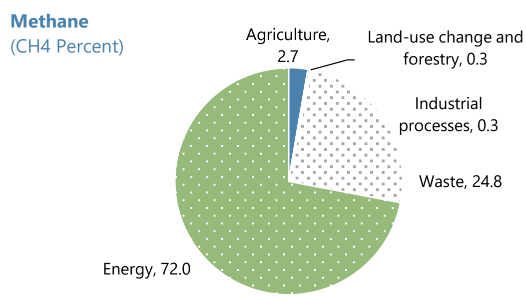
Saudi Arabia's GHG emissions mainly consist of CO_2 and Methane.



The CO_2 emissions are largely driven by the energy sector…

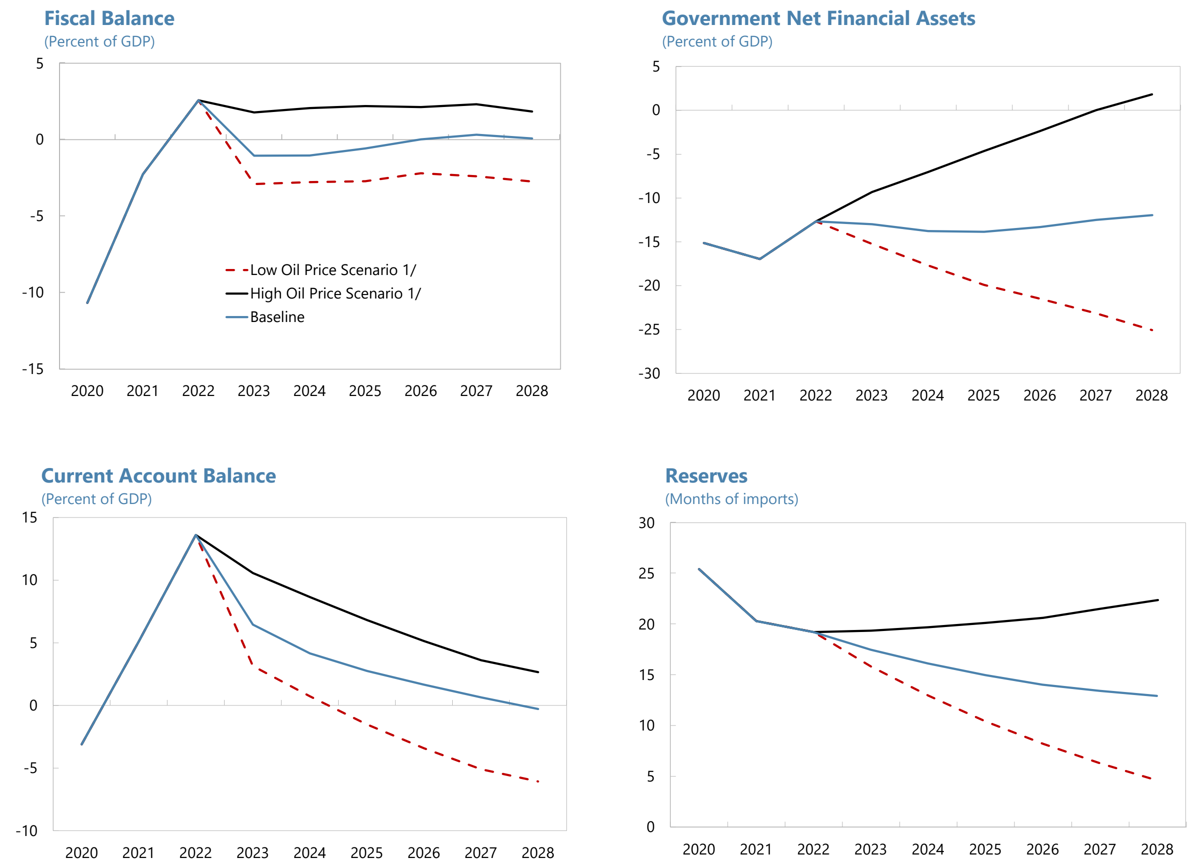


… as is the case for Methane, with waste contributing to these emissions as well.



Sources: CAIT, Climate Watch, IMF WEO and staff calculations.

Figure 9. Saudi Arabia: Upside/Downside Oil Price Scenarios



Source: IMF staff calculations.

1/The low/high oil price scenario assumes the oil price is two standard deviations for period 2023-2028 below/above the WEO adjusted oil price throughout the projection years. Both scenarios assume no change in government spending, non-oil revenue collections, or external borrowing relative to baseline.

Table 1. Saudi Arabia: Selected Economic Indicators, 2019–2028

	2019	2020	2021	Est. 2022	Proj. 2023	Proj. 2024	Proj. 2025	Proj. 2026	Proj. 2027	Proj. 2028
	(Percent change; unless otherwise indicated)									
National income and prices										
Crude oil production (million of barrels per day)	9.8	9.2	9.1	10.6	10.1	10.0	10.5	10.7	10.9	11.0
Average oil export price (U.S. dollars per barrel)[1]	65.9	42.7	73.2	102.0	80.4	73.6	70.9	68.9	67.2	65.9
Nominal GDP (SAR billions)	3,145	2,754	3,257	4,156	3,997	4,055	4,223	4,383	4,558	4,746
Nominal GDP (US$ billions)	839	734	869	1,108	1,066	1,081	1,126	1,169	1,216	1,266
Nominal non-oil GDP (SAR billions)	2,094	2,024	2,131	2,327	2,522	2,681	2,843	3,010	3,189	3,375
Nominal GDP per capita (US$)	27,893	23,271	28,215	34,441	32,474	32,300	32,985	33,558	34,219	34,930
Real GDP	0.8	-4.3	3.9	8.7	1.9	2.8	4.2	3.3	3.3	3.1
Oil	-3.3	-6.6	0.2	15.3	-2.5	0.1	4.1	1.9	1.9	1.6
Non-oil [2]	3.5	-3.0	5.7	4.8	4.9	4.4	4.4	4.2	4.2	4.0
Consumer price index (avg)	-2.1	3.4	3.1	2.5	2.8	2.3	2.0	2.0	2.0	2.0
External sector										
Exports f.o.b.	-11.1	-33.5	58.9	48.7	-19.8	-5.5	4.0	2.1	2.8	2.4
Oil	-13.4	-40.5	69.4	61.4	-25.4	-9.7	2.2	-0.9	-1.2	-1.6
Imports f.o.b.	11.7	-10.2	11.0	25.9	7.1	9.7	10.4	9.0	8.8	7.7
Current account balance (percent of GDP)	4.6	-3.1	5.1	13.6	6.5	3.5	2.7	1.7	0.6	-0.3
Export volume	-6.4	-5.2	5.2	9.2	0.6	3.3	7.7	5.9	6.8	5.7
Import volume	10.0	-9.6	0.1	14.5	8.2	8.7	9.4	8.1	7.6	5.9
Terms of trade	-5.6	-34.1	46.2	32.0	-22.1	-10.6	-4.9	-4.6	-4.9	-4.9
Money and credit										
Net foreign assets	-1.7	-8.9	-4.5	3.8	-2.2	-2.7	0.3	3.0	4.1	4.9
Net domestic assets	17.8	26.0	20.7	10.8	10.0	10.4	8.0	6.6	6.3	5.9
Of which: claims on private sector	7.0	14.0	15.4	12.6	9.6	9.5	8.5	8.3	7.6	6.7
Money and quasi-money (M3)	7.1	8.3	7.4	8.1	8.0	6.3	6.1	5.9	5.9	5.9
3-month Interbank rate (percent p.a.) [3]	2.3	0.8	0.9	5.3	...	...	...	...	...	...
Central government finances	(Percent of GDP)									
Revenue	29.5	28.4	29.6	30.7	28.4	28.4	29.0	29.2	29.3	28.5
Expenditure	33.7	39.1	31.9	28.2	29.7	30.0	29.7	29.4	29.0	28.4
Expense	28.3	33.4	28.3	24.8	25.7	25.9	25.5	25.0	24.7	24.2
Net acquisition of non-financial assets	5.4	5.6	3.6	3.4	4.0	4.2	4.2	4.3	4.3	4.2
Net lending (+)/borrowing (-)	-4.2	-10.7	-2.3	2.5	-1.2	-1.6	-0.7	-0.2	0.2	0.0
Excluding oil revenue	-23.1	-25.7	-19.5	-18.1	-17.7	-17.6	-17.0	-16.4	-15.8	-15.0
Non-oil primary balance/non-oil GDP	-34.7	-37.4	-29.5	-32.4	-27.4	-25.8	-24.4	-23.2	-22.0	-20.5
Non-exported oil primary balance/non-oil GDP	-32.4	-35.4	-27.2	-29.6	-23.7	-21.4	-19.6	-17.9	-16.2	-15.3
Central government deposits at SAMA	16.8	15.9	11.8	11.1	10.6	9.0	8.0	7.5	7.4	7.1
Central government gross debt	21.6	31.0	28.8	23.8	25.1	25.8	25.1	24.2	23.3	22.7
Central government net financial assets	-4.7	-15.1	-17.0	-12.7	-14.5	-16.8	-17.1	-16.7	-15.8	-15.6
Memorandum items:										
SAMA's total net foreign assets (US$ billions)	494.0	449.2	438.2	440.5	427.8	413.1	412.1	422.7	438.8	459.2
In months of imports of goods and services [3]	32.5	25.3	20.3	19.4	17.5	15.7	14.6	14.0	13.9	13.8
Imports goods & services/GDP	26.1	24.8	24.5	23.4	25.6	27.1	28.1	29.0	29.8	30.4
Real effective exchange rate (2010=100, end of period) [3]	114.0	113.9	114.7	119.6	118.1	...	...	...	...	...
Average exchange rate Saudi riyal/U.S. dollar	3.75	3.75	3.75	3.75	...	...	...	...	...	...
Population (millions)	30.1	31.6	30.8	32.2	32.8	33.5	34.1	34.8	35.5	36.2
Unemployment rate (nationals)	12.2	13.7	11.3	9.4	...	...	...	...	...	...
Unemployment rate (overall)	5.6	7.7	6.6	5.6	...	...	...	...	...	...
All-Shares Price Index (TASI)	8,389	8,760	11,282	10,478	...	...	...	...	...	...

Sources: Saudi Arabian authorities; and IMF staff estimates and projections.

[1] Includes refined products.

[2] Recent reclassification of national accounts is not yet fully reflected.

[3] Latest observation

Table 2. Saudi Arabia: Budgetary Central Government Operations, 2019–28

	2019	2020	2021	Est. 2022	Budget 2023	Proj. 2023	Proj. 2024	Proj. 2025	Proj. 2026	Proj. 2027	Proj. 2028
	(Billions of Saudi Arabian riyals)										
Revenue	927	782	965	1,277	1,130	1,137	1,152	1,223	1,280	1,333	1,350
Oil	594	413	562	857		661	646	686	711	730	712
Non-oil	332	369	403	420		476	506	537	569	603	639
Tax revenues	175	189	283	333	322	371	395	420	446	473	502
Taxes on income, profits, and capital gains	17	18	18	24	22	28	30	32	33	35	37
Taxes on goods and services (includes excises)	110	126	217	261	254	283	301	319	338	358	379
Taxes on international trade and transactions	17	18	19	19	18	25	28	31	33	36	39
Other taxes	30	27	29	28	28	35	37	39	41	44	46
Non-oil non-tax revenues	157	179	120	88		105	111	117	123	130	137
Property income (excluding oil)	22	74	20	32		20	20	20	20	20	20
Sales of goods and services	33	26	30	36		30	32	34	36	38	41
Fines, penalties, and forfeits	10	9	11	13		14	15	16	17	18	19
Other revenues	92	70	59	7		40	43	47	50	54	57
Expenditure	1,059	1,076	1,039	1,173	1,114	1,185	1,218	1,255	1,286	1,324	1,349
Expense	890	921	922	1,030	957	1,026	1,049	1,076	1,097	1,126	1,151
Employee compensation [1]	505	495	496	513	514	520	526	533	539	550	561
Use of goods and services	161	203	205	258	218	239	242	246	251	256	262
Interest payments	21	24	27	30	39	39	40	43	40	40	40
Domestic	11	13	15	16		26	28	30	26	26	26
Foreign	10	11	13	14		13	12	13	14	14	14
Support (subsidies)	23	28	30	30	22	28	30	30	29	29	29
Social benefits [2]	82	69	70	79	67	85	90	95	101	107	113
Grants	1	4	3	3	2	3	3	3	3	4	4
Other expenses	97	97	91	117	96	113	118	125	132	140	143
Net acquisition of non-financial assets	169	155	117	143	157	159	169	179	190	198	199
Net lending (+)/borrowing (-)	**-132.6**	**-294**	**-73**	**104**	**16**	**-48**	**-67**	**-32**	**-7**	**9**	**1**
	(In percent of GDP)										
Revenue	29.5	28.4	29.6	30.7	29.2	28.4	28.4	29.0	29.2	29.3	28.5
Oil	18.9	15.0	17.3	20.6		16.5	15.9	16.2	16.2	16.0	15.0
Non-oil	10.6	13.4	12.4	10.1		11.9	12.5	12.7	13.0	13.2	13.5
Tax revenues	5.6	6.9	8.7	8.0	8.3	9.3	9.7	10.0	10.2	10.4	10.6
Taxes on income, profits, and capital gains	0.5	0.7	0.5	0.6	0.6	0.7	0.7	0.7	0.8	0.8	0.8
Taxes on goods and services (includes excises)	3.5	4.6	6.7	6.3	6.6	7.1	7.4	7.6	7.7	7.9	8.0
Taxes on international trade and transactions	0.6	0.6	0.6	0.5	0.5	0.6	0.7	0.7	0.8	0.8	0.8
Other taxes	1.0	1.0	0.9	0.7	0.7	0.9	0.9	0.9	0.9	1.0	1.0
Non-oil non-tax revenues	5.0	6.5	3.7	2.1		2.6	2.7	2.8	2.8	2.8	2.9
Property income (excluding oil)	0.7	2.7	0.6	0.8		0.5	0.5	0.5	0.5	0.4	0.4
Sales of goods and services	1.0	0.9	0.9	0.9		0.8	0.8	0.8	0.8	0.8	0.9
Fines, penalties, and forfeits	0.3	0.3	0.3	0.3		0.4	0.4	0.4	0.4	0.4	0.4
Other revenues	2.9	2.6	1.8	0.2		1.0	1.1	1.1	1.1	1.2	1.2
Expenditure	33.7	39.1	31.9	28.2	28.8	29.7	30.0	29.7	29.4	29.0	28.4
Expenses	28.3	33.4	28.3	24.8	24.7	25.7	25.9	25.5	25.0	24.7	24.2
Employee compensation [1]	16.1	18.0	15.2	12.3	13.3	13.0	13.0	12.6	12.3	12.1	11.8
Use of goods and services	5.1	7.4	6.3	6.2	5.6	6.0	6.0	5.8	5.7	5.6	5.5
Interest payments	0.7	0.9	0.8	0.7	1.0	1.0	1.0	1.0	0.9	0.9	0.8
Domestic	0.3	0.5	0.4	0.4		0.6	0.7	0.7	0.6	0.6	0.6
Foreign	0.3	0.4	0.4	0.3		0.3	0.3	0.3	0.3	0.3	0.3
Support (subsidies)	0.7	1.0	0.9	0.7	0.6	0.7	0.8	0.7	0.7	0.6	0.6
Social benefits [2]	2.6	2.5	2.1	1.9	1.7	2.1	2.2	2.3	2.3	2.3	2.4
Grants	0.0	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other expenses	3.1	3.5	2.8	2.8	2.5	2.8	2.9	3.0	3.0	3.1	3.0
Net acquisition of non-financial assets	5.4	5.6	3.6	3.4	4.1	4.0	4.2	4.2	4.3	4.3	4.2
Net lending (+)/borrowing (-)	**-4.2**	**-10.7**	**-2.3**	**2.5**		**-1.2**	**-1.6**	**-0.7**	**-0.2**	**0.2**	**0.0**
Non-exported oil primary balance/non-oil GDP	-32.4	-35.4	-27.2	-29.6		-23.7	-21.4	-19.6	-17.9	-16.2	-15.3

Sources: Ministry of Finance; and IMF staff projections.

[1] Including the extra month salary according to Hijri calendar in 2016.

[2] Zakat charity transfers, social welfare payments and Hafiz Job-seekers allowance.

Table 3. Saudi Arabia: Budgetary Central Government Operations, 2019–28 (concluded)

	2019	2020	2021	Est. 2022	Proj. 2023	Proj. 2024	Proj. 2025	Proj. 2026	Proj. 2027	Proj. 2028
	(Billions of Saudi Arabian riyals)									
Net lending (+)/borrowing (-)	**-133**	**-294**	**-73**	**104**	**-48**	**-67**	**-32**	**-7**	**9**	**1**
Financing	**143**	**271**	**172**	**-104**	**48**	**67**	**32**	**7**	**-9**	**-1**
Net acquisition of financial assets	-25	-96	-54	187	-39	-59	-28	-7	9	1
Domestic	-27	-96	-54	187	-39	-59	-28	-7	8	-1
Deposits at SAMA (+, buildup)	-33	-93	-51	187	-39	-59	-28	-7	8	-1
Loans and equity	6	-3	-3	0	0	0	0	0	0	0
Foreign	2	0	0	0	0	0	0	0	1	2
Net incurrence of liabilities (- = repayment)	118	176	118	83	9	8	4	0	0	0
Domestic	70	174	109	107	50	8	41	85	41	39
Banks	0	78	0	0	0	0	0	0	0	0
Nonbanks	70	96	109	107	50	8	41	85	41	39
Foreign	50	46	49	19	52	40	35	21	27	41
Amortization	-2	-44	-40	-43	-93	-40	-72	-106	-68	-80
Domestic	-2	-44	-20	-24	-23	-34	-46	-85	-41	-39
Foreign	0	0	-21	-18	-70	-6	-26	-21	-27	-41
Residual/ Gap (+ve = overfinancing)	**11**	**-23**	**98**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
	(In percent of GDP)									
Net lending (+)/borrowing (-)	**-4.2**	**-10.7**	**-2.3**	**2.5**	**-1.2**	**-1.6**	**-0.7**	**-0.2**	**0.2**	**0.0**
Financing	**4.5**	**9.9**	**5.3**	**-2.5**	**1.2**	**1.6**	**0.7**	**0.2**	**-0.2**	**0.0**
Net acquisition of financial assets	-0.8	-3.5	-1.7	4.5	-1.0	-1.4	-0.7	-0.2	0.2	0.0
Domestic	-0.9	-3.5	-1.7	4.5	-1.0	-1.4	-0.7	-0.2	0.2	0.0
Deposits at SAMA (+, buildup)	-1.1	-3.4	-1.6	4.5	-1.0	-1.4	-0.7	-0.2	0.2	0.0
Loans and equity	0.2	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities (- = repayment)	3.8	6.4	3.6	2.0	0.2	0.2	0.1	0.0	0.0	0.0
Domestic	2.2	6.3	3.3	2.6	1.3	0.2	1.0	1.9	0.9	0.8
Banks	0.0	2.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Nonbanks	2.2	3.5	3.3	2.6	1.3	0.2	1.0	1.9	0.9	0.8
Foreign	1.6	1.7	1.5	0.5	1.3	1.0	0.8	0.5	0.6	0.9
Amortization	-0.1	-1.6	-1.2	-1.0	-2.3	-1.0	-1.7	-2.4	-1.5	-1.7
Domestic	-0.1	-1.6	-0.6	-0.6	-0.6	-0.8	-1.1	-1.9	-0.9	-0.8
Foreign	0.0	0.0	-0.6	-0.4	-1.8	-0.1	-0.6	-0.5	-0.6	-0.9
Residual/ Gap (+ve = overfinancing)	**0.3**	**-0.8**	**3.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum items:										
Non-oil overall balance	-727	-707	-636	-753	-709	-712	-718	-717	-721	-711
Non-oil primary balance	-728	-757	-628	-755	-690	-692	-695	-697	-701	-691
Non-oil revenue/non-oil GDP	15.9	18.2	18.9	18.1	18.9	18.9	18.9	18.9	18.9	18.9
Tax revenue/non-oil GDP	8.4	9.4	13.3	14.3	14.7	14.7	14.8	14.8	14.8	14.9
Current balance	37	-139	44	247	111	102	148	183	207	200
Non-oil primary balance/non-oil GDP	-34.7	-37.4	-29.5	-32.4	-27.4	-25.8	-24.4	-23.2	-22.0	-20.5
Government gross domestic debt/GDP	11.8	18.3	17.2	14.8	15.2	14.4	13.7	13.2	12.7	12.2
Government foreign issued debt/GDP	9.7	12.7	11.6	9.0	8.6	9.3	9.1	8.8	8.4	8.1
Government gross debt/GDP	21.6	31.0	28.8	23.8	23.8	23.6	22.8	21.9	21.1	20.3
Government deposits at SAMA/GDP	16.8	15.9	11.8	11.1	10.6	9.0	8.0	7.5	7.4	7.1
Government net financial assets/GDP	-4.7	-15.1	-17.0	-12.7	-13.2	-14.6	-14.8	-14.4	-13.7	-13.1
Government Deposits at SAMA (SAR billions)	529	437	385	463	424	365	338	331	339	338
GDP market prices (SAR billions)	3,145	2,754	3,257	4,156	3,997	4,055	4,223	4,383	4,558	4,746
Non-oil GDP (SAR billions)	2,094	2,024	2,131	2,327	2,522	2,681	2,843	3,010	3,189	3,375
Average oil export price	65.9	42.7	73.2	102.0	80.4	73.6	70.9	68.9	67.2	65.9

Sources: Ministry of Finance; and IMF staff projections.

Table 4. Saudi Arabia: Balance of Payments, 2019–28
(USD Billion)

	2019	2020	2021	Est. 2022	Proj. 2023	Proj. 2024	Proj. 2025	Proj. 2026	Proj. 2027	Proj. 2028
Current account	38.2	-22.8	44.3	150.8	68.8	37.8	30.9	19.3	7.8	-3.5
(Percent of GDP)	4.6	-3.1	5.1	13.6	6.5	3.5	2.7	1.7	0.6	-0.3
Trade balance	121.3	47.9	136.5	234.7	140.7	104.1	95.0	81.3	68.5	55.7
Exports	261.6	173.9	276.2	410.7	329.2	311.0	323.4	330.2	339.4	347.4
Oil exports	200.5	119.4	202.2	326.3	243.5	219.8	224.7	222.8	220.1	216.5
Other exports	61.1	54.5	74.0	84.4	85.7	91.2	98.6	107.5	119.3	131.0
Imports (f.o.b.)	-140.3	-125.9	-139.7	-176.0	-188.5	-206.8	-228.4	-248.9	-270.9	-291.7
Services	-54.4	-47.3	-63.0	-50.9	-42.7	-37.4	-34.8	-32.1	-29.9	-27.1
Transportation	-12.9	-12.9	-14.1	-18.4	-16.4	-15.0	-14.6	-14.1	-13.7	-13.1
Travel	1.3	-4.8	-8.4	7.6	10.8	12.9	13.9	15.0	16.1	17.3
Other services	-42.8	-29.6	-40.5	-40.1	-37.1	-35.3	-34.1	-33.0	-32.3	-31.3
Income	7.9	13.9	15.2	11.1	15.2	16.9	17.9	18.6	19.0	19.2
Of which: Investment income [1]	8.5	13.9	15.8	11.3	15.5	17.2	18.1	18.9	19.3	19.4
Current transfers	-36.6	-37.4	-44.4	-44.1	-44.5	-45.8	-47.2	-48.5	-49.9	-51.2
Of which : Workers' remittances	-30.3	-34.3	-39.8	-38.8	-39.1	-40.5	-41.9	-43.2	-44.6	-45.9
Capital Account	-1.7	-1.8	-1.3	-2.5	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	-33.2	-21.9	-39.9	-135.1	-81.5	-52.5	-31.9	-8.8	8.3	23.9
Direct Investment	-9.0	0.5	-4.6	-10.9	-7.5	-4.8	-1.8	2.2	6.7	11.6
Abroad	-13.5	-4.9	-23.9	-18.8	-15.3	-13.2	-11.1	-8.8	-6.5	-4.5
In Saudi economy	4.6	5.4	19.3	7.9	7.8	8.4	9.3	11.0	13.2	16.1
Portfolio investments	11.5	-23.7	-38.5	-36.9	-20.4	-16.1	-14.7	-9.7	-0.1	9.0
Assets	-34.6	-53.6	-55.6	-49.7	-42.1	-39.8	-35.8	-28.6	-21.6	-16.9
Liabilities	46.1	29.9	17.1	12.8	21.6	23.8	21.1	18.9	21.5	26.0
Other investments	-35.7	1.3	3.2	-87.2	-53.6	-31.7	-15.4	-1.3	1.7	3.2
Assets	-55.7	-4.9	-22.3	-77.5	-48.1	-43.3	-30.3	-18.2	-16.4	-15.5
Liabilities	20.0	6.2	25.5	-9.7	-5.5	11.6	14.9	16.9	18.1	18.7
Net errors and omissions	-0.3	0.6	-1.4	-8.7	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	3.0	-45.9	1.7	4.5	-12.7	-14.7	-1.0	10.5	16.2	20.4
Financing	-3.0	45.9	-1.7	-4.5	12.7	14.7	1.0	-10.5	-16.2	-20.4
Change in SAMA's NFA (- increase)	-4.5	44.9	11.0	-2.3	12.7	14.7	1.0	-10.5	-16.2	-20.4
SAMA's total net foreign assets	494.0	449.2	438.2	440.5	427.8	413.1	412.1	422.7	438.8	459.2
(In months of imports) [2]	32.5	25.3	20.3	19.4	17.5	15.7	14.6	14.0	13.9	13.8
Net International Investment Position (% GDP)	80.0	81.6	71.4	64.4	73.4	75.9	75.6	74.5	72.3	69.1
Non-oil current account(% GDP)	-19.3	-19.4	-18.2	-15.8	-16.4	-16.8	-17.2	-17.4	-17.5	-17.4
External debt (% GDP)	22.2	32.4	31.7	23.9	24.9	26.1	26.4	26.5	26.6	27.1
Oil price (US$/barrel)	64.2	43.3	70.8	99.0	78.4	73.6	70.9	68.9	67.2	65.9
Average Saudi oil export price (US$/barrel)	65.9	42.7	73.2	102.0	80.4	73.6	70.9	68.9	67.2	65.9
Oil production (mbd)	9.8	9.2	9.1	10.6	10.1	10.0	10.5	10.7	10.9	11.0
Oil exports (mbd)	8.3	7.7	7.6	8.8	8.3	8.2	8.7	8.9	9.0	9.0
Oil exports/total exports	76.6	68.7	73.2	79.5	74.0	70.7	69.5	67.5	64.8	62.3
Imports of goods/GDP	16.7	17.1	16.1	15.9	17.7	19.1	20.3	21.3	22.3	23.0
GDP (US$ billion)	838.6	734.3	868.6	1,108.1	1,065.7	1,081.3	1,126.2	1,168.7	1,215.6	1,265.7
Government foreign issued debt (US$ billion)	81.4	93.6	101.1	100.0	91.2	100.3	102.7	102.7	102.7	102.7
US 6-month LIBOR (Percent)	2.3	0.7	0.2	2.9	5.6	5.8	4.7	3.6	2.8	2.8

Sources: Saudi Central Bank (SAMA), and IMF staff estimates and projections.

[1] Represents the return on NFA of SAMA, AGIs, and private sector.

[2] Imports of goods and services over the next 12 months excluding imports for transit trade.

Table 5. Saudi Arabia: Monetary Survey, 2019–28

(Percent)

	2019	2020	2021	Est. 2022	Proj. 2023	Proj. 2024	Proj. 2025	Proj. 2026	Proj. 2027	Proj. 2028
(Billions of Saudi Arabian riyals)										
Foreign assets (net)	1,923	1,752	1,673	1,736	1,697	1,651	1,656	1,705	1,776	1,862
SAMA	1,853	1,684	1,643	1,652	1,604	1,549	1,545	1,585	1,646	1,722
Commercial banks	70	68	30	84	93	102	111	120	130	140
Domestic credit (net)	1,463	1,843	2,225	2,465	2,711	2,992	3,232	3,444	3,661	3,876
Net claims on government	-146	2	95	47	75	116	121	85	57	38
Claims on government	384	438	481	510	499	482	459	416	396	376
Government deposits with SAMA	-529	-437	-385	-463	-424	-365	-338	-331	-339	-338
Claims on state enterprises	62	79	95	128	128	128	128	128	128	128
Claims on private sector	1,547	1,762	2,034	2,290	2,508	2,748	2,983	3,230	3,477	3,710
Money and quasi-money (M3)	1,985	2,149	2,309	2,495	2,695	2,864	3,038	3,216	3,407	3,606
Money (M1)	1,288	1,489	1,564	1,528	1,645	1,742	1,842	1,943	2,052	2,165
Currency outside banks	189	206	204	200	241	256	270	285	301	318
Demand deposits	1,099	1,283	1,360	1,328	1,403	1,487	1,572	1,658	1,751	1,847
Quasi-money	697	660	744	967	1,050	1,122	1,196	1,272	1,355	1,441
Other quasi-money deposits	195	186	249	312	339	362	386	411	438	466
Other items (net liabilities)	1,401	1,445	1,589	1,705	1,714	1,779	1,850	1,933	2,030	2,132
(Changes in percent of beginning broad money stock)										
Foreign assets (net)	-1.8	-8.6	-3.7	2.7	-1.6	-1.7	0.2	1.6	2.2	2.5
Domestic credit (net)	11.9	19.2	17.7	10.4	9.9	10.4	8.4	7.0	6.8	6.3
Net claims on government	6.0	7.4	4.4	-2.1	1.1	1.5	0.2	-1.2	-0.9	-0.5
Claims on government	4.2	2.8	2.0	1.3	-0.5	-0.6	-0.8	-1.4	-0.6	-0.6
Government deposits (increase -)	1.8	4.7	2.4	-3.4	1.6	2.2	1.0	0.2	-0.3	0.0
Claims on state enterprises	0.4	0.9	0.7	1.4	0.0	0.0	0.0	0.0	0.0	0.0
Claims on private sector	5.5	10.9	12.6	11.1	8.8	8.9	8.2	8.2	7.7	6.8
(Percent change; unless otherwise indicated)										
Foreign assets (net)	-1.7	-8.9	-4.5	3.8	-2.2	-2.7	0.3	3.0	4.1	4.9
Domestic credit (net)	17.8	26.0	20.7	10.8	10.0	10.4	8.0	6.6	6.3	5.9
Of which: claims on private sector	7.0	14.0	15.4	12.6	9.6	9.5	8.5	8.3	7.6	6.7
Money and quasi-money	7.1	8.3	7.4	8.1	8.0	6.3	6.1	5.9	5.9	5.9
(Percent; unless otherwise indicated)										
Memorandum items:										
Specialized Credit Institutions credit (SAR billions)[1]	236.4	237.4	…	…	…	…	…	…	…	…
Ratio of M3-to-GDP	63.1	78.1	70.9	60.0	67.4	70.6	71.9	73.4	74.7	76.0
Ratio of Claims on private sector-to-non-oil GDP	73.8	87.1	95.5	98.4	99.5	102.5	104.9	107.3	109.0	109.9

Sources: Saudi Central Bank (SAMA); and IMF staff estimates.

[1] For 2020, data is latest available.

Table 6. Saudi Arabia: Financial Soundness Indicators, 2016-2022

	2016	2017	2018	2019	2020	2021	2022
Banking sector							
Structure of the banking sector							
Number of licensed banks	24	25	29	25	25	26	27
Number of banks accounting for:							
25 percent of total assets	2	2	2	2	2	1	1
75 percent of total assets	6	6	6	6	6	5	5
Total assets (percent of GDP)	93.3	89.3	80.1	81.6	104.9	97.2	84.3
Of which: Foreign currency-denominated (as percent of total	10.0	10.5	9.4	9.5	8.7	8.1	8.2
Total loans (percent of GDP)	57.9	53.7	48.3	51.8	67.6	65.4	58.5
Credit to private sector (percent of GDP)	55.9	51.9	46.7	47.4	61.9	60.3	53.5
Total deposits, excluding interbank (as percent of GDP)	66.9	62.7	56.3	57.1	70.6	64.6	55.2
Capital adequacy							
Regulatory capital to risk-weighted assets	19.5	20.4	20.3	19.3	20.3	19.9	19.9
Tier-1 capital to risk-weighted assets	17.5	18.3	18.5	18.0	18.7	18.2	18.4
Asset quality							
Net loans to total assets	62.8	62.2	62.6	63.5	64.4	67.3	69.3
Gross NPLs to gross loans	1.4	1.6	2.0	1.9	2.2	1.9	1.8
Total provisions to gross NPLs	177.0	151.9	157.2	148.1	134.7	147.7	124.5
Net NPLs to total capital	1.0	1.7	1.1	1.6	2.5	2.5	2.7
Total provisions for loan losses (as percent of total loans)	2.6	2.6	3.2	2.8	2.9	2.7	2.2
Loans to property and construction sector to total loans	-	-	-	-	-	-	-
Loans to domestic manufacturing sector to total loans	-	-	-	-	-	-	-
Contingent and off-balance sheet accounts to total assets	84.2	76.2	71.3	73.9	69.0	63.3	65.6
Profitability							
Profits (percent change)	-4.8	8.6	9.8	4.5	-24.0	42.9	28.5
Average pretax return on assets	1.8	2.0	2.1	2.0	1.4	1.8	2.1
Return on equity	12.6	12.9	13.8	12.1	8.6	10.8	12.5
Noninterest expenses to total income [1]	38.0	36.6	36.3	35.9	36.2	36.1	34.0
Average lending spread	3.5	3.5	3.9	3.9	3.5	3.2	2.4
Liquidity							
Liquid assets to total assets	20.3	21.6	22.3	25.4	26.8	24.7	22.8
Liquid assets to short-term liabilities [2]	31.8	34.6	35.5	41.3	43.8	41.3	39.7
Customer deposits to net loans	115.7	117.9	115.6	115.0	109.6	102.6	97.5
Demand deposits to total deposits	59.9	61.4	62.2	61.2	66.0	64.6	57.9
Sensitivity to market risk							
Foreign currency-denominated deposits to total deposits	7.6	8.6	8.7	8.6	7.4	9.5	11.9
Foreign currency-denominated loans to total loans	8.2	8.0	8.4	8.9	8.6	7.5	7.5
Foreign currency-denominated contingent and off-balance sheet accounts to total assets	28.3	27.1	27.1	27.5	28.0	27.1	31.2
Net open foreign currency position to capital	2.6	4.0	6.4	6.7	7.3	0.0	-2.4
Stock market							
Stock market capitalization (percent of GDP)	69.5	65.4	63.0	287.0	330.6	307.3	237.7
Overall stock market price index (change in percent)	4.3	0.2	8.3	7.2	3.6	29.8	-7.1
Bank stock price index (change in percent)	-67.4	8.2	31.1	12.4	-6.4	61.0	-5.6

Source: Saudi Central Bank (SAMA).

[1] Total income includes net interest income and gross noninterest income.

[2] Short-term liabilities include demand deposits maturing in 90 days or less. Liquid assets include cash, gold, Saudi government bonds and treasury bills and interbank deposits maturing within 30 days.

Annex I. Status of Staff Recommendations Made During the 2022 Article IV Consultation

Recommendation	Status
Support fiscal consolidation by stepping up efforts on non-oil revenue mobilization, energy price reforms and strengthening social safety net.	Though no new tax measures were in place, non-oil tax revenue has remained strong and increased with good compliance. Prices of four energy products were increased in 2022, including for diesel (the most subsidized item) but not enough to reduce subsidies on liquid fuels, which have now reached 6.2 percent of GDP in 2022 in the wake of increased oil prices through foregone government revenue from ARAMCO.
Maintain fiscal discipline by adhering to the 2022 budget ceilings	The fiscal balance improved by close to 5 percent of GDP in 2022, but by less than expected in the 2022 Article IV. Over the medium term, the fiscal consolidation path appears more challenging than projected because of higher spending and lower oil revenues.
Increases necessary social safety nets targets or food subsidies to support low-income households in 2022	Spending on social benefits in 2022 was increased during the year, including with a special package of measures to deal with high food prices. A new household living standards survey (conducted by the World Bank) will help underpin the level of social spending.
Develop a sovereign asset-liability management framework remain a high priority to support fiscal sustainability	The work towards developing a sovereign asset liability management framework is ongoing, starting with a first phase on financial assets and liabilities and aiming at a comprehensive coverage.
Strengthen public financial management reforms	Continued improvements are made as more accounts are streamlined within the TSA, Preparations are made towards medium term budgeting, budget disclosure is improving through regular reporting, and a statement of fiscal risks is being developed. The ongoing framework to assess PPP risks is being finalized.
Continue sound public debt management to support fiscal policy and capital market development.	Public debt remains low, has decreased by 5 percent of GDP in 2022 and is sustainable. The borrowing strategy is set to remain agile to lengthen debt maturities and would help deepen the local debt market
Enhance supervisory scrutiny of credit risks and implementation of Basel III framework.	Gross NPLs to total loans remain low. An enhanced monitoring of risks is ongoing, various thematic bank inspections are completed, including IFRS 9 model review, mortgage portfolio review, targeted inspections of banks' corporate loan portfolios. The Banking Control Law is being finalized. Basel III frameworks for leverage, operational risks, and market risks are being applied.
Rationalize and unify initiatives to support SMEs	Initiatives to support SMEs have been unified and rationalized in the SME Bank. To support SMEs, much remains to be done, including streamlining the numerous fees faced by SMEs (a key constraint to Doing Business).
Facilitate investment efficiency and catalyze private investment	Non-oil private investment increased by 45 percent in real terms and is notably driven by the increasing pace of various giga projects. The efficiency of private sector investment still needs to improve. Divestment of the PIF from Tadawul and Acwa power shows areas where it exited its earlier participations to favor an emerging private sector.
Continue Labor market reforms to boost productivity	The authorities have made strides in promoting gender equality, including by changing restrictions in the legal code, notably with an anti-discrimination regulation. Both Saudi nationals and expatriates are driving a downward trend in the national unemployment rate (5.6 percent overall unemployment rate in 2022). Overall female labor force participation remained high at 34.5 percent in 2022Q4, exceeding Vision 2030 targets.
Continue authorities' efforts on climate policies	A total of $186 billion has been announced for investment by the Saudi government through the Saudi Green Initiative (SGI). Progress in 2022 under the (SGI) include 18 million trees planted, and the launch of a $1.5 billion Sustainability Fund. A coherent National Hydrogen Strategy will be published in 2023.
Improve economic data	A new GDP series based on a new supply and use table (SUT) estimation has been published, and the transition to a chain-linked volume estimate is expected to be completed by early 2024. Input and output tables were published for the first time. A population census has been completed and a new household survey is being conducted.

Annex II. Risk Assessment Matrix[1]

Nature/ Source of Main Risks	Likeli-hood	Expected Impact on the Economy if Risk is Realized	Policy Response
		Global Risks (Conjunctural)	
Intensification of regional conflict(s). Escalation of Russia's war in Ukraine or other regional conflicts and resulting economic sanctions disrupt trade (e.g., energy, food, tourism, and/or critical supply chain components), remittances, refugee flows, FDI and financial flows, and payment systems.	**High**	**Medium** Direct spillover channels (trade, food prices, investments, financial sector) are limited for Saudi Arabia, and Saudi Arabia is mostly commodity exporting. Although not threatened at the moment (in particular due to the constitution of advance stocks), food security has always been the focus of the Saudi authorities. Tensions, geopolitical or financial, in Asia would be affecting Saudi Arabia more strongly as it is the main destination for its exports and economic ties have intensified recently (in particular with China).	The needed policy response would depend on the nature of the shock. Fiscal policy could respond, and the authorities would need to ensure adequate liquidity in the banking system.
Abrupt global slowdown or recession. Global and idiosyncratic risk factors combine to cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and markets fragmentation. In Europe, an intensifying fallout from the war in Ukraine, worsening energy crisis and supply disruptions, and monetary tightening could exacerbate economic downturns and housing market corrections.	**Medium**	**Medium** Main channel would be through lower commodity prices and demand for Saudi Arabia fuel, particularly as China is now Saudi Arabia's largest buyer of oil (with 26 percent of its oil exports), China is also a significant non-oil exporter to Saudi Arabia, while Chinese and Saudi companies have developed direct foreign investments, including a large oil refinery facility in China, and a number of joint projects.	Fiscal policy needs to be anchored in a medium-term framework to reduce the risks of procyclical fiscal policies. Existing buffers together with external borrowing could be used to smooth the fiscal adjustment in the short term in the event of a large shock, such as an abrupt growth slowdown that would significantly affect China's demand for Saudi oil exports. There should also be close monitoring of disruptions to banking system liquidity and signs of banking stress. Structural reforms should be accelerated to reduce the impact of oil price fluctuations on the economy over the longer term
Commodity price volatility. A succession of supply disruptions (e.g., due to conflicts and export restrictions) and demand fluctuations (e.g., reflecting China reopening) causes recurrent commodity price volatility, external and fiscal pressures, and social and economic instability.	**Medium**	**Medium** An increase/decrease in the global price of oil would raise/reduce growth and inflation in Saudi Arabia, while higher/lower oil export revenues would improve/worsen the fiscal and current account balances. Further disruptions to food supply and prices globally, as experienced during Covid and in the wake of the Russian invasion of Ukraine, would have a tamed impact given Saudi Arabia's policies to constitute food stocks and regulate some food prices on the domestic markets.	In response to a large increase/decrease in the global price of oil, use fiscal consolidation/stimulus to stabilize growth and inflation, given high fiscal space. Accelerate structural reforms to help diversify the export base away from oil.
Systemic financial instability. Sharp swings in real interest rates, risk premia, and assets repricing amid economic slowdowns and policy shifts trigger insolvencies in countries with weak banks or non-bank financial institutions, causing markets dislocations and adverse cross-border spillovers.	**Medium**	**Low** Saudi Arabia with a fixed exchange rate tied to the U.S. dollar and significant assets abroad (in bond and equity markets and bank deposits), is vulnerable to shifts in interest rates and abrupt shifts in international market sentiment. However, the country has large buffers, favorable market access with high and recently increasing credit ratings. It has been relatively affected by the increase in interest rates, in the context of high liquidity and growth in the wake of oil windfalls and a favorable balance sheet structure of banks,	Continue a prudent financial sector policy and keep closely monitoring exposures from banks and other financial institutions, including through stress testing and thematic inspections. Provide liquidity if needed, and with market-based mechanisms compatible with the exchange rate peg.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path. The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Nature/ Source of Main Risks	Likeli-hood	Expected Impact on the Economy if Risk is Realized	Policy Response
Monetary policy miscalibration. Amid high economic uncertainty and volatility, major central banks slow monetary policy tightening or pivot to loosen monetary policy stance prematurely, de-anchoring inflation expectations and triggering a wage-price spiral in tight labor markets.	Medium	**Low** Risk is low for Saudi Arabia, amid low inflationary pressures. Monetary policy would follow closely that of the U.S., but because of low inflationary pressures the risks associated with a de anchoring of inflation expectations and monetary policy miscalibration are limited.	Continued strong fundamentals would likely prevent excessive volatility in Saudi Arabian financial markets. Continue with monetary policies and liquidity management that are consistent with the exchange rate peg.
Global risks (structural)			
Deepening geo-economic fragmentation. Broader and deeper conflict(s) and weakened international cooperation lead to a more rapid reconfiguration of trade and FDI, supply disruptions, technological and payments systems fragmentation, rising input costs, financial instability, a fracturing of international monetary and financial systems, and lower potential growth.	High	**Medium** Given its prominent role in the Middle East and in the global oil market, Saudi Arabia could be drawn into contributing to geo-economic fragmentation or be affected by geo-economic fragmentation trends. Its geopolitical closeness and economic ties to China and Russia, notably through the oil market could be a contributing factor, while risks from geo-economic fragmentation would also affect Saudi Arabia through downward pressure on demand for Saudi exports, supply disruptions, technological and payments systems fragmentation, rising input costs, financial instability, a fracturing of international monetary and financial systems,	Saudi Arabia remains very engaged multilaterally notably as part of its active participation in the G20 and other international fora. Care should be on keeping open trade policies, including as part of the ambitious development goals of the Kingdom. Accelerate fiscal and structural reforms to boost potential growth, by incentivizing the diversification of the export base away from oil and enhancing the competitiveness of the non-oil export sector. Maintain strong capital adequacy requirements to absorb any increases in NPLs during the economic transition.
Domestic risks			
While there is a significant risk that reforms may slow including because of domestic inflationary pressures, the reforms implemented in recent years may support a stronger recovery. Slippages in the reform agenda, perhaps due to domestic risks or the impact of international shocks such as on prices, would reduce prospects for stronger growth and employment over the medium-term.	High	**Low** Staff projections may underestimate the impact of reforms and risks in this area may be tilted to the upside. The failure to continue to deliver on the planned fiscal consolidation and ambitious structural reforms would however adversely affect growth and employment. The failure to turn reforms into jobs for Saudis in the private sector will lead to pressures to increase public employment with negative implications for fiscal sustainability. Similarly, inflationary pressures should they materialize might lead to a slowing of reforms (e.g., on energy prices and subsidies, VAT)	Continue with structural reforms to boost non-oil growth and labor market reforms to increase the competitiveness of Saudi nationals in the private sector. Implement fiscal adjustment that balances the need to support recovery with the need to rebuild fiscal buffers.
Cyberthreats. Cyberattacks on critical domestic and/or international physical or digital infrastructure (including digital currency and crypto ecosystems) trigger financial and economic instability.	Medium	**Medium** Given the geopolitical tensions in the region, the prominent role of Saudi Arabia, and the rapid digitalization of its economy and society, Saudi Arabia is prone to a high density of cyberattacks. In 2012, 2015, 2017, 2019 and 2020 experienced serious attacks on its critical infrastructure, including targeting ARAMCO and its oil production facilities.	Saudi Arabia has expanded its capacity to react to cyberthreats notably through the creation of the National Cybersecurity Agency in 2017 that has developed a national cybersecurity strategy with 6 objectives to reach by 2030. It has also developed local capacity skills. Close monitoring and supervision including of the banking and payment system should continue.
Energy transition. A faster transition to lower fossil fuel consumption globally could lead to lower demand and oil prices and affect oil exporting economies.	Medium	**Medium** Despite recent achievements in diversification, Saudi Arabia remains very vulnerable to lower oil prices for its exports and public finances. However, it has shown resilience in the past in periods of low oil prices and the capacity to adjust with implementing new measures (e.g., tax measures). A more prolonged slump would exert more pressure though leaving some capacity for accelerated diversification. The Saudi authorities consider the risk of a prolonged	Saudi Arabia is already engaging in diversifying away from the use fossil fuels in its power generation with the buildup in its renewable energy capacity in line with Vision 2030. However, this would require also an accelerated phasing out of energy subsidies, enhanced economic and diversification efforts, a fiscal policy that follows rules

Nature/ Source of Main Risks	Likeli-hood	Expected Impact on the Economy if Risk is Realized	Policy Response
		slump as low in view of what they see as global energy security imperatives and a slow transition away from fossil fuels.	in line with the Permanent Income Hypothesis, and much more sustained non-oil revenue mobilization
Extreme climate events. Extreme climate events cause more severe than expected damage to infrastructure (especially in smaller vulnerable economies) and loss of human lives and livelihoods, amplifying supply chain disruptions and inflationary pressures, causing water and food shortages, and reducing growth.	**Medium**	**Low** Though Saudi Arabia is subject to some extreme events made more frequent and intense by climate change, such as sandstorms and floods, the impact of these events remains manageable. With limited water resources and increasing temperatures adaptation costs are likely to increase rapidly. And spillovers from extreme events in partner countries could also affect Saudi Arabia.	Continue with a policy seeking increased resilience to climate events and aimed addressing challenges related to climate change adaptation. The Saudi Green Initiative aims at planting 10 billion trees, and this should also made fully consistent with a strategy on water resources and policy.

Annex III. Fiscal and Debt Sustainability Assessment

Figure 1. Saudi Arabia: Risk of sovereign stress

Horizon	Mechanical signal	Final assessment	Comments
Overall	…	Low	The overall risk of sovereign stress is low, reflecting a low level of vulnerability in the near-term, driven solely by global conditions, and low levels of vulnerability in the medium-, and long-term horizons.
Near term 1/			
Medium term	Moderate	Low	Medium-term risks are assessed as low against a mechanical high signal as large financial asset buffers mitigate debt solvency risks. On the fanchart specifically, in the case of Saudi Arabia, assets exceed 75 percent of GDP and 100 percent of public debt, thus the mechanical signal from the debt fanchart module is adjusted to low, regardless of the DFI's level. In addition, the medium-term risk is assesed as low on the basis of the strength of institutions, the depth of the investor pool, low debt levels and substantial sovereign wealth fund.
Fanchart	High	…	
GFN	Moderate	…	
Stress test	Comm. Prices	…	
Long term	…	Low	Long-term risks are low given large asset buffers from the PIF if needed, and limited pass through of aging-related expenditures on health and social security fed into debt dynamics. Oil reserves remain strong and staff assess limited climate transition costs adding to the debt dynamics.
Sustainability assessment 2/	Not required for surveillance countries	Not required for surveillance countries	Not applicable
Debt stabilization in the baseline			Yes

DSA summary assessment

Commentary: Saudi's public debt is assessed to remain sustainable under the baseline scenario. Saudi Arabia has large buffers that can support periods of fiscal deficits. Some of the debt increases in the past were also driven by the need to develop local debt market and nurture access to international markets. The assessment of low debt and financing risks over the medium term and long term, together with the results from the stress scenarios, lead to the final assessment of low risk. Saudi Arabia is at a low overall risk of sovereign stress and debt is sustainable. Most indicators have started to normalize as the recovery from the COVID-19 shock has proceeded. Medium-term liquidity risks as analyzed by the GFN Financeability Module are low.

Source: Fund staff.

Note: The risk of sovereign stress is a broader concept than debt sustainability. Unsustainable debt can only be resolved through exceptional measures (such as debt restructuring). In contrast, a sovereign can face stress without its debt necessarily being unsustainable, and there can be various measures—that do not involve a debt restructuring—to remedy such a situation, such as fiscal adjustment and new financing.

1/ The near-term assessment is not applicable in cases where there is a disbursing IMF arrangement. In surveillance-only cases or in cases with precautionary IMF arrangements, the near-term assessment is performed but not published.

2/ A debt sustainability assessment is optional for surveillance-only cases and mandatory in cases where there is a Fund arrangement. The mechanical signal of the debt sustainability assessment is deleted before publication. In surveillance-only cases or cases with IMF arrangements with normal access, the qualifier indicating probability of sustainable debt ("with high probability" or "but not with high probability") is deleted before publication.

Figure 2. Saudi Arabia: Debt coverage and disclosures

1. Debt coverage in the DSA: 1/

CG	GG	NFPS	CPS	Other
CG [chosen]				

1a. If central government, are non-central government entities insignificant? 0

2. Subsectors included in the chosen coverage in (1) above:

CPS	NFPS	GG: expected	CG	#	Subsectors captured in the baseline	Inclusion	Comments
CPS	NFPS	GG: expected	CG	1	Budgetary central government	Yes	
				2	Extra budgetary funds (EBFs)	No	Not applicable
				3	Social security funds (SSFs)	Yes	
				4	State governments	Yes	
				5	Local governments	Yes	
				6	Public nonfinancial corporations	No	
				7	Central bank	No	
				8	Other public financial corporations	No	

3. Instrument coverage:

Currency & deposits	Loans	Debt securities	Oth acct. payable 2/	IPSGSs 3/
[Missing]	[Chosen]	[Chosen]	[Missing]	[Missing]

4. Accounting principles:

Basis of recording		Valuation of debt stock		
Non-cash basis 4/	Cash basis	Nominal value 5/	Face value 6/	Market value 7/
	[Chosen]	[Chosen]		

5. Debt consolidation across sectors:

Consolidated	Non-consolidated
	[Chosen]

Color code: chosen coverage; Missing from recommended coverage; Not applicable

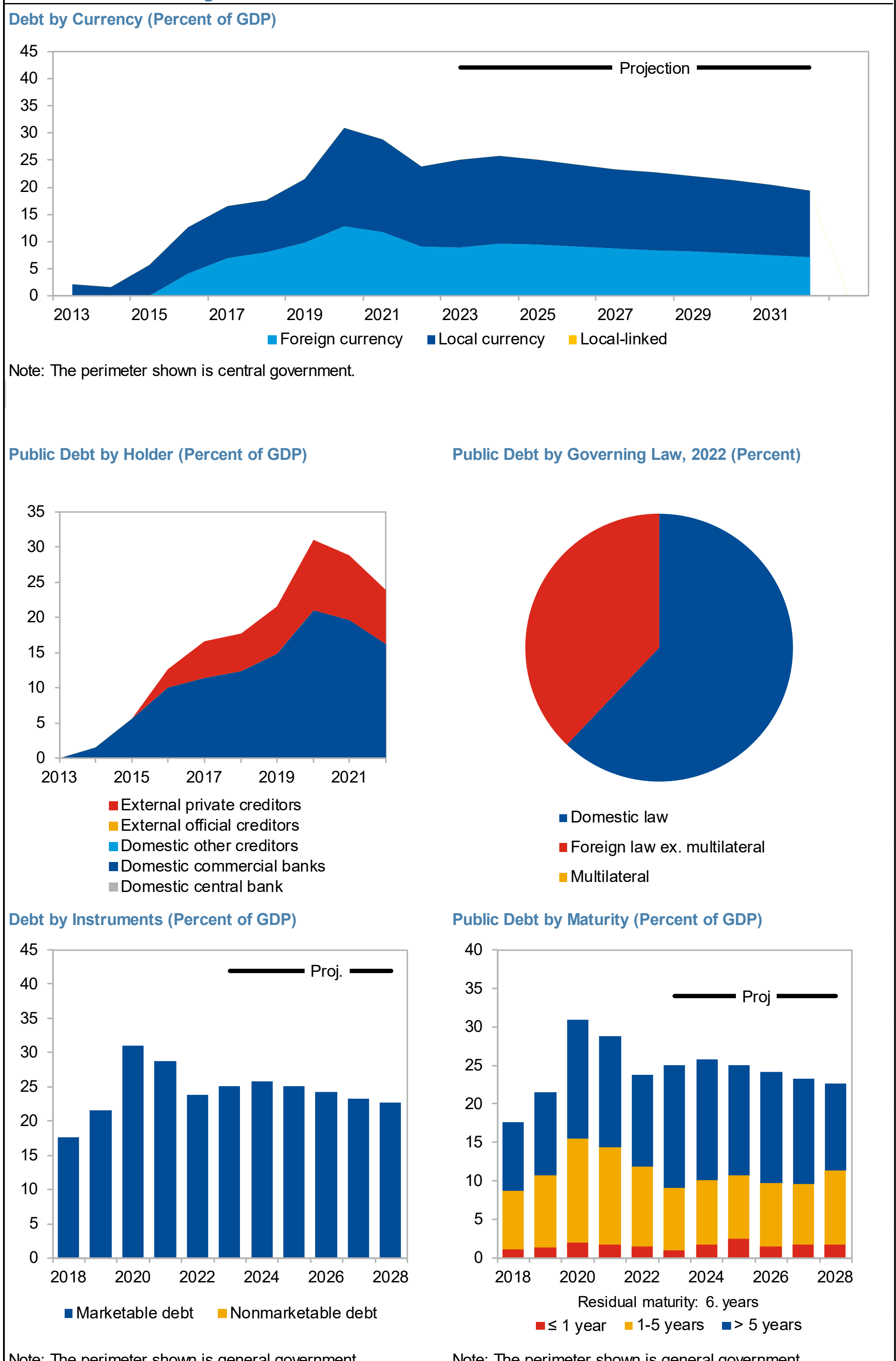
Reporting on intra-government debt holdings

Issuer \ Holder	Budget. central govt	Extra-budget. funds	Social security funds	State govt.	Local govt.	Nonfin. pub. corp.	Central bank	Oth. pub. fin corp	Total
1 Budget. central govt									0
2 Extra-budget. funds									0
3 Social security funds									0
4 State govt.									0
5 Local govt.									0
6 Nonfin pub. corp.									0
7 Central bank									0
8 Oth. pub. fin. corp									0
Total	0	0	0	0	0	0	0	0	0

1/ CG=Central government; GG=General government; NFPS=Nonfinancial public sector; PS=Public sector.
2/ Stock of arrears could be used as a proxy in the absence of accrual data on other accounts payable.
3/ Insurance, Pension, and Standardized Guarantee Schemes, typically including government employee pension liabilities.
4/ Includes accrual recording, commitment basis, due for payment, etc.
5/ Nominal value at any moment in time is the amount the debtor owes to the creditor. It reflects the value of the instrument at creation and subsequent economic flows (such as transactions, exchange rate, and other valuation changes other than market price changes, and other volume changes).
6/ The face value of a debt instrument is the undiscounted amount of principal to be paid at (or before) maturity.
7/ Market value of debt instruments is the value as if they were acquired in market transactions on the balance sheet reporting date (reference date). Only traded debt securities have observed market values.

Commentary: State and local governments in Saudi Arabia do not have their own separate debt issuance authority, and typically operate under the umbrella of the central government, including their borrowing requirements.

Figure 3. Saudi Arabia: Public Debt Structure Indicators



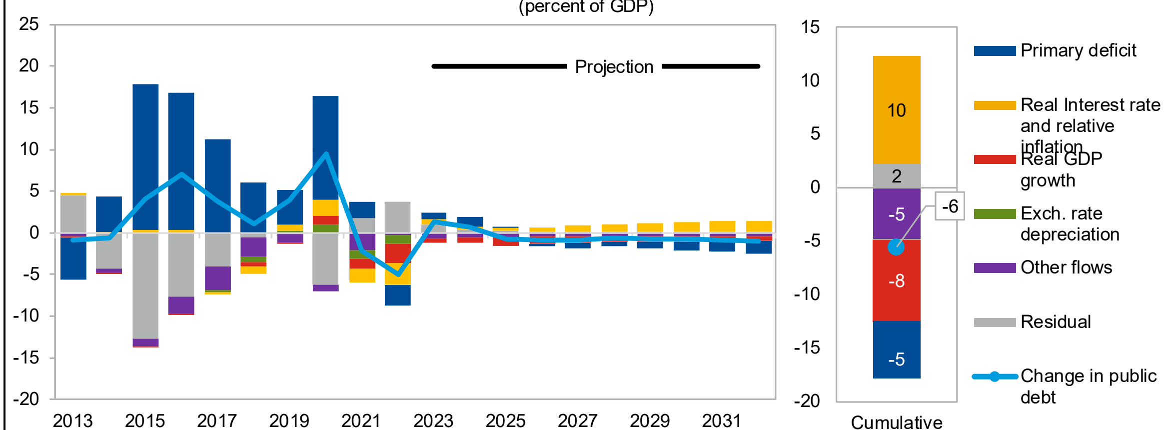
Commentary: Saudi Arabia continues to have space for external market access. The share of foreign currency debt slightly increases in the forecast horizon. Partial repurchasing of outstanding local and international debt bonds and securities maturing in the short term helped reduce future refinancing risk and slightly increased the average time to maturity.

Figure 4. Saudi Arabia: Baseline scenario

	Actual	Medium-term projection						Extended projection			
	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032
Public debt	23.8	25.1	25.8	25.1	24.2	23.3	22.7	22.1	21.3	20.4	19.4
Change in public debt	-5.0	1.3	0.7	-0.7	-0.9	-0.9	-0.6	-0.7	-0.8	-0.9	-1.0
Contribution of identified flows	-8.7	0.2	0.4	-0.9	-1.0	-1.0	-0.6	-0.8	-0.9	-1.0	-1.1
Primary deficit	-2.5	0.7	1.1	0.2	-0.3	-0.6	-0.4	-0.7	-1.0	-1.2	-1.5
Noninterest revenues	30.0	27.9	27.9	28.5	28.7	28.8	28.0	27.7	27.4	27.1	26.8
Noninterest expenditures	27.5	28.7	29.1	28.7	28.4	28.2	27.6	27.0	26.5	25.9	25.4
Automatic debt dynamics	-5.9	0.2	-0.2	-0.7	-0.3	0.1	0.2	0.4	0.5	0.6	0.8
Real interest rate and relative inflation	-2.6	0.7	0.4	0.4	0.5	0.8	0.9	1.1	1.2	1.3	1.4
Real interest rate	-3.9	1.4	0.8	0.6	0.7	0.9	1.0	1.1	1.2	1.4	1.5
Relative inflation	1.3	-0.7	-0.3	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Real growth rate	-2.3	-0.4	-0.7	-1.0	-0.8	-0.8	-0.7	-0.7	-0.7	-0.6	-0.6
Real exchange rate	-1.0	…	…	…	…	…	…	…	…	…	…
Other identified flows	-0.3	-0.7	-0.5	-0.5	-0.5	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Contingent liabilities	0.2	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other transactions	-0.5	-0.8	-0.5	-0.5	-0.5	-0.4	-0.4	-0.4	-0.4	-0.4	-0.4
Contribution of residual	3.7	1.0	0.3	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Gross financing needs	-2.0	2.7	2.1	2.0	2.6	1.7	2.3	2.1	2.0	1.8	1.6
of which: debt service	1.0	2.3	1.4	2.3	3.4	2.8	3.2	3.2	3.4	3.4	3.4
Local currency	0.6	0.6	1.1	1.4	2.6	1.8	1.9	1.9	2.1	2.0	2.1
Foreign currency	0.4	1.8	0.3	0.9	0.8	1.0	1.3	1.3	1.3	1.3	1.3
Memo:											
Real GDP growth (percent)	8.7	1.9	2.8	4.2	3.3	3.3	3.1	3.1	3.1	3.1	3.1
Inflation (GDP deflator; percent)	17.3	-5.6	-1.3	-0.1	0.5	0.7	1.0	1.0	1.0	1.0	1.0
Nominal GDP growth (percent)	27.6	-3.8	1.5	4.2	3.8	4.0	4.1	4.1	4.1	4.1	4.1
Effective interest rate (percent)	0.0	0.0	1.7	2.2	3.3	4.7	5.5	6.2	6.9	7.6	8.4

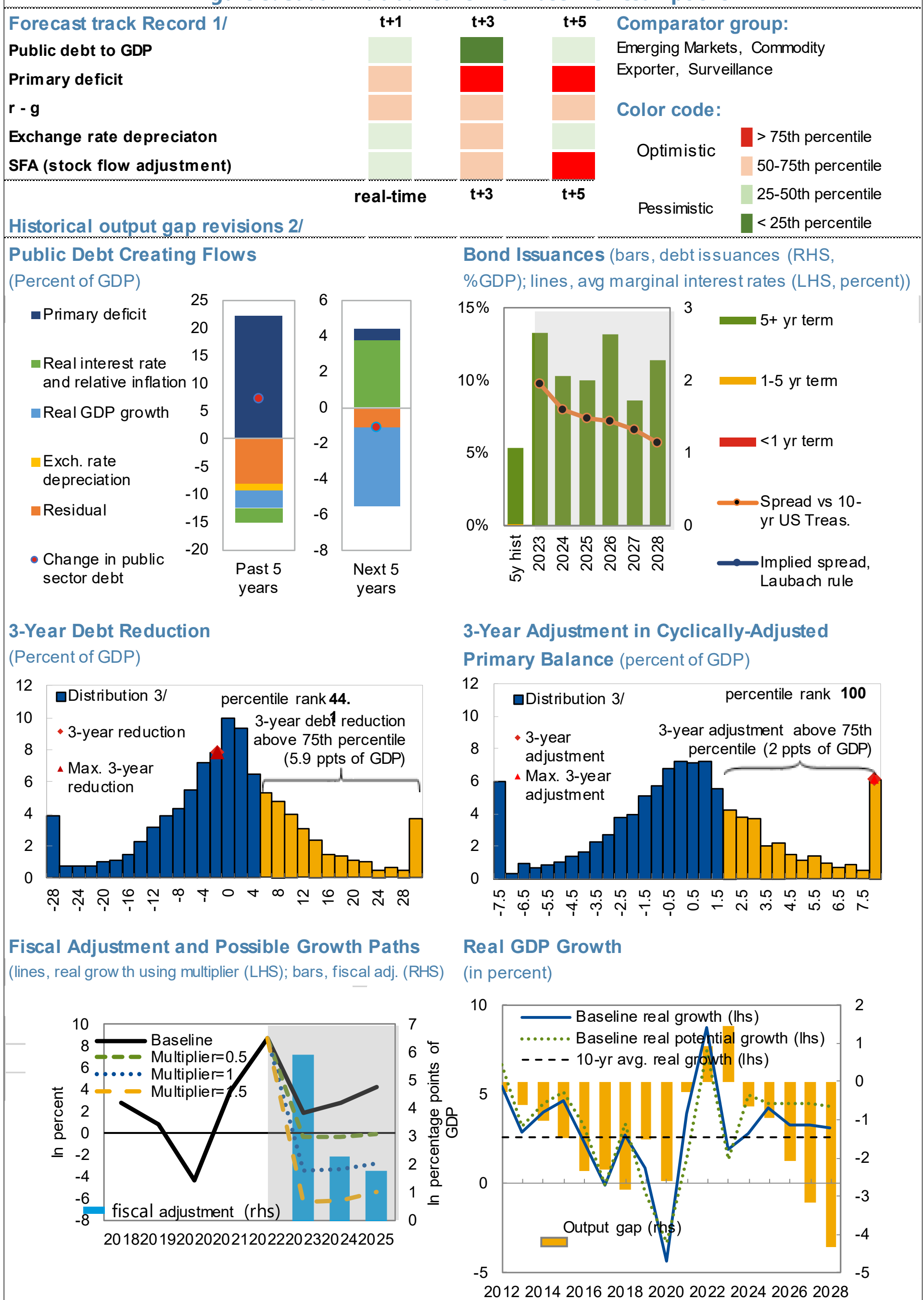
Contribution to change in public debt

(percent of GDP)



Commentary: Public debt reflects expectations of a narrowing of primary deficit and stable economic conditions in the short term, also due to improved fiscal position.

Figure 5. Saudi Arabia: Realism of Baseline Assumptions



1/ Projections made in the October and April WEO vintage.

2/ Calculated as the percentile rank of the country's output gap revisions (defined as the difference between real time/period ahead estimates and final estimates in the latest October WEO) in the total distribution of revisions across the data sample.

3/ Data cover annual observations from 1990 to 2019 for MAC advanced and emerging economies. Percent of sample on vertical axis.

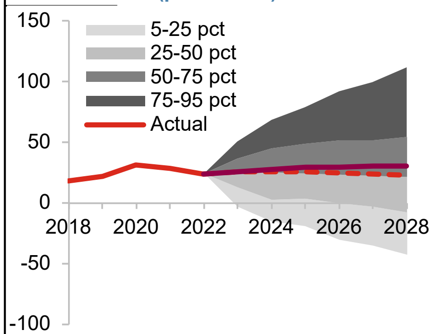
4/ The Laubach (2009) rule is a linear rule assuming bond spreads increase by about 4 bps in response to a 1 ppt increase in the projected debt-to-GDP ratio.

Commentary: The realism analysis does not point to major concerns and the projected fiscal adjustment and debt reduction are well within norms. The forecast of oil growth in the past few years appeared more optimistic with the introduction of the OPEC+ oil production quota in 2020 and the subsequent changes to the quota. The impact of fiscal adjustment on growth is only imperfectly apprehended in the context of an oil exporting economy as the assessment should be more finely focused on non oil growth.

Figure 6. Saudi Arabia: Medium-term Risk Assessment

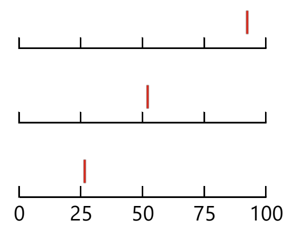
		Value	Contrib [1/]	Percentile in peer group [2/]

Final Fanchart (pct of GDP)

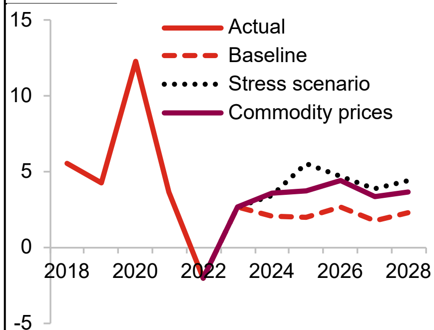


Debt fanchart module

	Value	Contrib	
Fanchart width *(percent of GDP)*	154.6	2.2	
Probability of debt non-stabilizaiton *(percent)*	46.1	0.4	
Terminal debt-to-GDP x institutions index	10.3	0.2	
Debt fanchart index (DFI)		2.9	
Risk signal: [3/]		**High**	

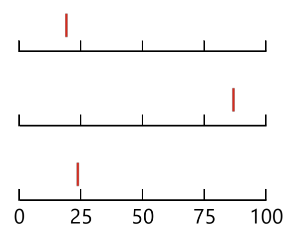


Gross Financing Needs (pct of GDP)

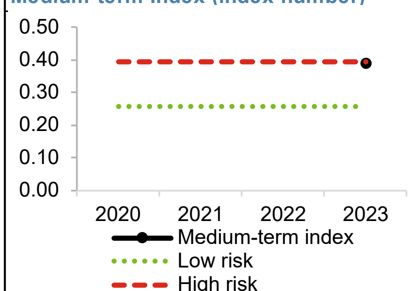


Gross financing needs (GFN) module

	Value	Contrib	
Average baseline GFN *(percent of GDP)*	2.2	0.8	
Banks' claims on the gen. govt *(pct bank assets)*	18.0	5.8	
Chg. In banks' claims in stress *(pct banks' assets)*	3.0	1.0	
GFN financeability index (GFI)		7.6	
Risk signal: [4/]		**Moderate**	



Medium-term Index (index number)



Medium-term risk analysis

	Value	Weight	Contribution
Debt fanchart index (normalized)	0.6	0.5	0.3
GFN finaceability index (normalized)	0.1	0.5	0.1
Medium-term index	0.4		
Risk signal: 5/	**Moderate**		
Final assessment:	**Low**		

Prob. of missed crisis, 2023-2028, if stress not predicted: 36.4 pct.

Prob. of false alarms, 2023-2028, if stress predicted: 10.2 pct.

Medium-term risks are assessed as low against a mechanical high signal as large financial asset buffers mitigate debt solvency risks. On the fanchart specifically, in the case of Saudi Arabia, assets exceed 75 percent of GDP and 100 percent of public debt, thus the mechanical signal from the debt fanchart module is adjusted to low, regardless of the DFI's level. Commodity price shock (lower prices) would slightly increase public debt (on average about 5 pp) and GFNs further (on average about 1.3 pp) in the medium term.

Source: IMF staff estimates and projections.

1/ See Annex IV of IMF, 2022, Staff Guidance Note on the Sovereign Risk and Debt Sustainability Framework for details on index calculation.

2/ The comparison group is emerging market, non-commodity exporting countries, with Fund-supported programs.

3/ The signal is low risk if the DFI is below 1.13; high risk if the DFI is above 2.08; and otherwise, it is moderate risk.

4/ The signal is low risk if the GFI is below 7.6; high risk if the DFI is above 17.9; and otherwise, it is moderate risk.

5/ The signal is low risk if the GFI is below 0.26; high risk if the DFI is above 0.40; and otherwise, it is moderate risk.

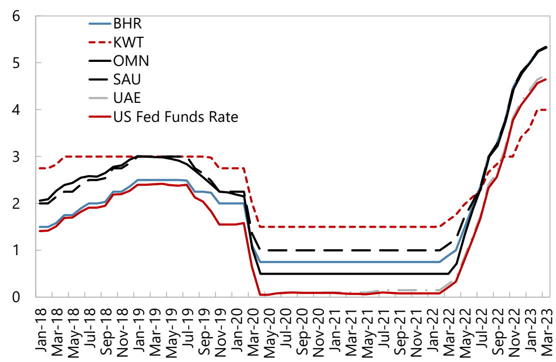
Annex IV. Liquidity Developments in the Banking Sector

Background

1. **Saudi Arabia has a fixed exchange rate regime, with a peg to the U.S. dollar**. Since 1986, the Saudi Riyal has been pegged to the U.S. dollar at a rate of 3.75 Saudi Riyal to the dollar. Saudi Arabia has a free capital account.

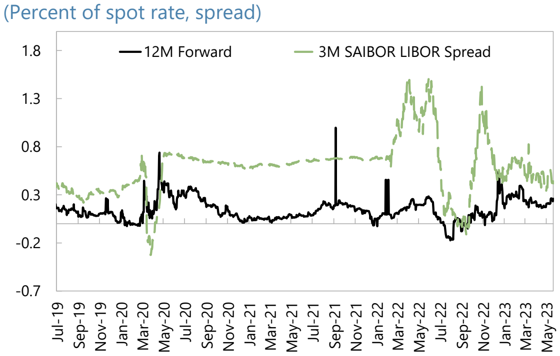
2. **The exchange rate peg is the intermediate target, meaning the interest tool is focused solely on supporting the exchange rate objective.** The Central Bank of Saudi Arabia (SAMA) keeps the exchange rate peg by using its interest rate instrument, or more precisely by managing the reverse repo and repo rates reflecting the changes in the U.S. dollar interest rate. As of end-April 2023, this corridor system had the upper bound and lower bound rates fixed at 5.75 percent and 5.25 percent respectively.

Policy Rates
(Average, percent)



Sources: Haver Analytics and IMF staff calculations.

Forward Premium Over Spot Exchange Rate and Interest Rate Differential
(Percent of spot rate, spread)



Sources: Bloomberg and IMF staff calculations.

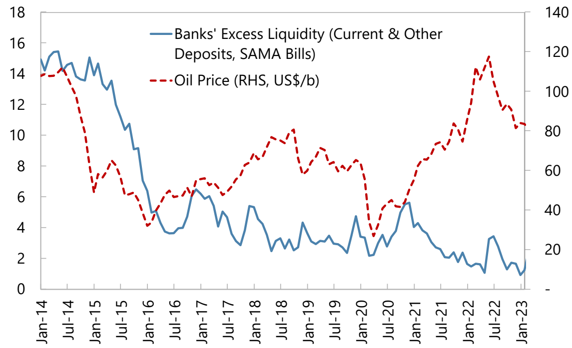
3. **SAMA utilizes a broad range of indicators to assess market developments**. These include measures of liquidity (e.g., bank's net liquidity position at the central bank) and trends in SAIBOR interest rates relative to their relevant U.S. LIBOR benchmark and the loan-to-deposit ratio.

Recent Developments

4. **Recent monetary policy tightening by SAMA was in line with the action by the Fed**. Since early 2022, SAMA raised its policy rate by 475 basis points, almost in line with the U.S. monetary policy tightening cycle, and in support of the exchange rate peg regime.

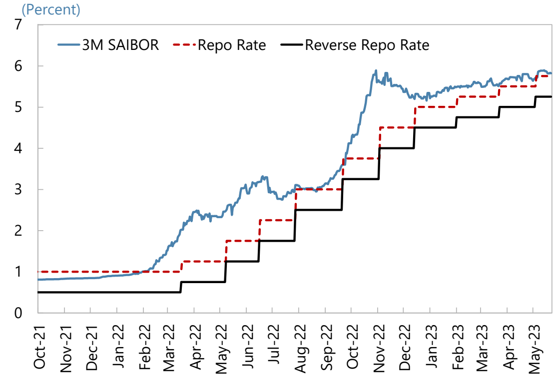
5. **Two liquidity squeezes in June and October 2022 caused interest rates to spike**. This materialized through a significant widening of the three-month SAIBOR-LIBOR spreads to over 150 basis points during June 2022 and then again in October 2022 (compared to the historical average of the past 3 years of around 60 basis points). Contrary to past episodes of funding squeezes that materialized when oil prices fell, this surprisingly occurred when oil prices were relatively high.

Excess Liquidity in Banking Sector
(Percent of bank assets)



Sources: Haver Analytics and IMF staff calculations.

Interest Rate Corridor
(Percent)

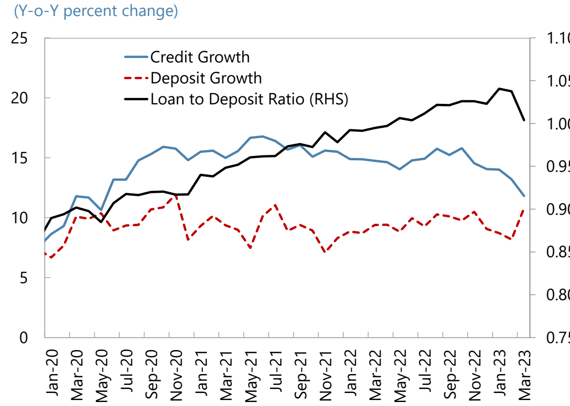


Sources: Bloomberg and IMF staff calculations.

6. **Several factors could explain these recent liquidity squeezes in a context of high oil prices**. These are:

- **Rapid credit growth**. Rapid credit growth continued to reduce excess liquidity. Bank credit to the economy increased by 12 percent in 2022, outpacing growth in bank deposits of only 9 percent. This resulted in a steady increase in the loan-to-deposit ratio, which reached 100 percent in early 2023. The loan-to-(weighted) deposit ratio defined by the SAMA's guidelines reached 82 percent in December 2022, approaching the prudential maximum of 90 percent. To fund the strong growth in lending—including to reach the authorities' 70 percent home ownership target (see below) and to participate in the funding of the lucrative giga-projects—banks had to price up their deposits (through increased recourse to time-savings deposits) and attract non-deposit sources of funding.

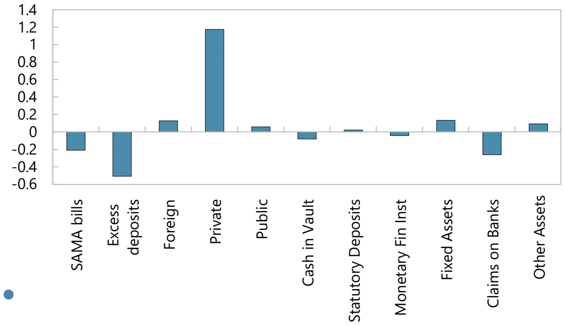
Private Sector Credit and Deposit Growth
(Y-o-Y percent change)



Sources: Haver Analytics and IMF staff calculations.

Change in Banking System Balance Sheet Composition, Assets, 2021-2020

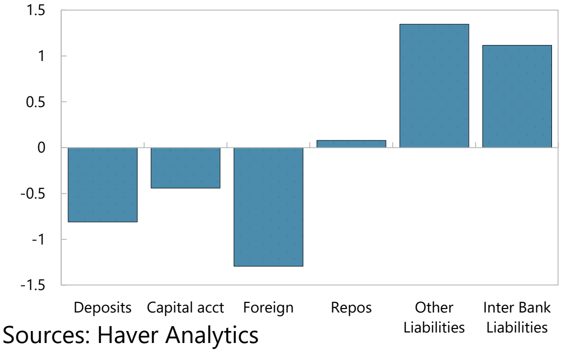
(Percentage point change of share of total assets)



Sources: Haver Analytics and IMF staff calculations.

Change in Banking System Balance Sheet Composition, Liabilities, 2021-2022

(Percentage point change of share of total assets)

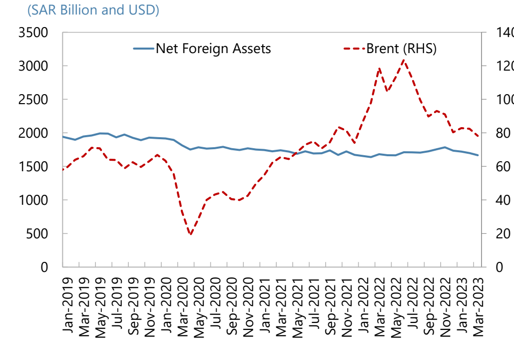


Sources: Haver Analytics and IMF staff calculations.

- **Delink of oil revenues and domestic liquidity**. SAMA's balance sheet and domestic liquidity have traditionally been strongly affected by oil revenues, with earnings generated by oil exports deposited with SAMA and spent. However, a significant share of oil revenues is now invested abroad rather than being used domestically. Stronger government fiscal discipline in a period of higher oil prices—a very welcome development—has weakened the link between excess domestic liquidity and higher oil prices. Foreign assets of Saudi residents (outward FDIs, portfolio investments, deposits with foreign banks, etc.) increased by around 14 percent of GDP in 2022, matching the amount of the current account surplus driven by oil proceeds.

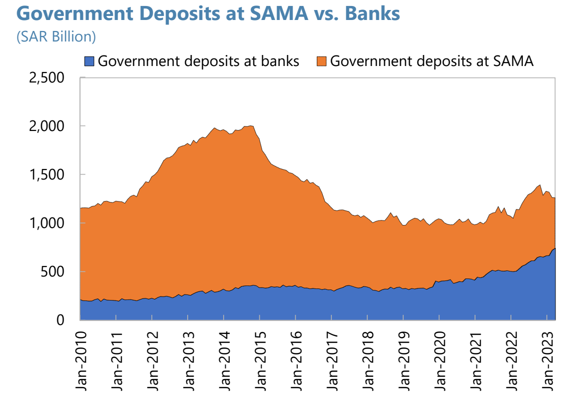
Net Foreign Assets and Oil Price

(SAR Billion and USD)



Sources: Haver Analytics and IMF staff calculations.

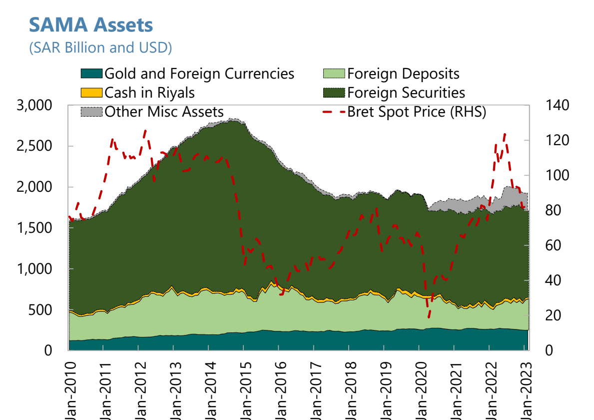
- **Establishment of the Treasury Single Account (TSA)**. The welcome establishment of the TSA at SAMA had transitory implications for liquidity management. Out of 188 government entities, 160 have been enrolled in the TSA, with the enrollment of the remaining 28 entities expected to be completed in 2023. The TSA—which rationalized more than 10,000 bank accounts by 2022—impacted liquidity even though the amount of government deposits in the banking system has been relatively stable or even increasing since 2017.



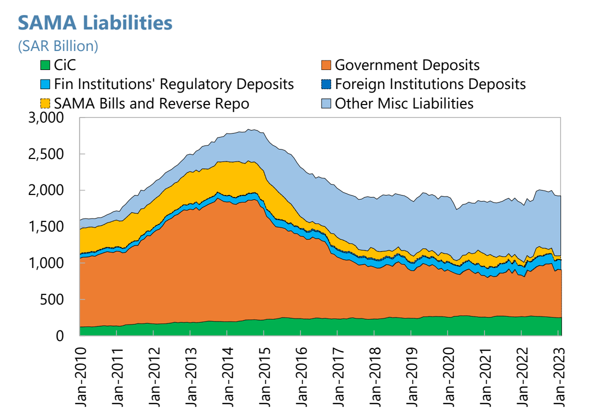
Sources: Haver Analytics and IMF staff calculations.

- **Increasing Non-Oil Revenue**. As a changing pattern from the past, non-oil revenue—which grew by 137 percent between 2016 (SAR 186 billion) and 2022 (SAR 440 billion), indicating that a greater amount of liquidity is taken out of the system than in the past.

7. **An assessment of SAMA's balance sheet further illustrates the points above.** In this case, looking at SAMA's assets, while investment in foreign securities and foreign deposits represent the main assets, these have not grown in line with higher oil revenue. As of February 2023, about 34 percent of SAMA's liabilities are government deposits—a declining trend as government reserves have declined.



Sources: Haver Analytics and IMF staff calculations.

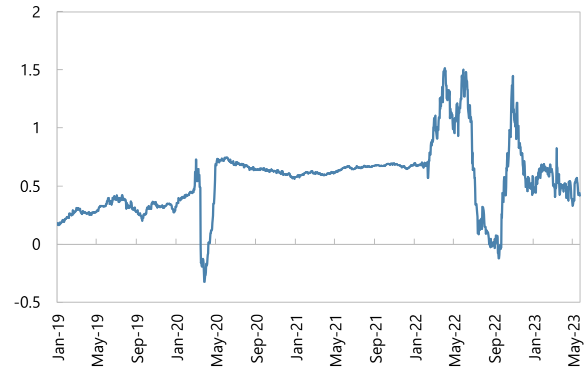


Sources: Haver Analytics and IMF staff calculations.

8. **Temporary liquidity pressures have been eased thanks to the authorities' timely and resolute action**. In June 2022, SAMA intervened with the injection of SAR 40 billion (US$10.7 billion) in the form of deposits. This quickly reassured market participants and resulted in a narrowing of the SAIBOR-LIBOR spreads. The re-emergence of liquidity pressures in October 2022 was handled using a newly developed framework that required interaction between SAMA and the Ministry of Finance as it involved the recycling of MoF funds in the banking system, with SAMA acting as the fiscal agent of the government (for about SAR 50 billion).

3M SAIBOR-LIBOR Spread

(Spread)



Sources: Haver Analytics and IMF staff calculations.

9. **Although SAMA has a range of indirect market-based monetary policy instruments in its toolkit, the recent episodes of liquidity squeeze were in part addressed by non-market tools**. SAMA uses overnight facilities and term repos/issuance of SAMA bills (open market operations), FX swaps, and reserve requirements. Yet, the authorities felt that the use of conventional monetary tools needed to be complemented by interventions in the form of direct placement of deposits in the banking system.

Annex V. External Sector Assessment[1]

<table>
<tr><td colspan="8">Overall Assessment: The external position in 2022 was substantially stronger than the level implied by medium-term fundamentals and desirable policies. The external balance sheet remains strong. Reserves remain adequate according to standard IMF metrics. Under the current fiscal balance path, the central government's non-oil primary balance is expected to be on an improving trend. Given the economy's structure, the pegged exchange rate continues to provide Saudi Arabia with a credible policy anchor.

Potential Policy Responses: With the projected normalization of oil exports, the gap is expected to diminish. The ambitious structural reform agenda, as part of Vision 2030, to help diversify the economy, lift productivity, and boost the non-oil tradable sector, will be accompanied by a sizeable investment program, including by the Public Investment Fund (PIF), Saudi Arabia's SWF. These factors will reduce the current gap and help align the external position in the medium term. Continued fiscal reforms to avoid procyclical fiscal policy amid high hydrocarbon windfalls will be important, which includes delinking spending decisions from international oil price fluctuations while implementing a medium-term fiscal framework. Important structural fiscal reforms have been initiated over the past few years, including non-oil revenue mobilization, broad-based improvement of public financial management, and energy price reform. Risks associated with industrial policies should be minimized, while discriminatory policies should be avoided as they could create distortions in the allocation of resources and elicit retaliatory actions by trade partners.</td></tr>
<tr><td>Foreign Asset and Liability Position and Trajectory</td><td colspan="7">Background. Net external assets are estimated at 64.4 percent of GDP at the end of 2022, down from 71.4 percent of GDP in 2021. While net external assets increased from US$620 billion to US$714 billion, nominal GDP expanded by a larger magnitude due to high oil prices. In the medium term, the NIIP is expected to stabilize at 69.1 percent of GDP. Only broad categories are available on the composition of external assets. Portfolio and other investments, reserves, and FDI, respectively, account for 54 percent, 34 percent, and 12 percent of total external assets.

Assessment. The external balance sheet remains very strong. Substantial accumulated assets represent both protection against vulnerabilities from oil price volatility and savings of exhaustible resource revenues for future generations.</td></tr>
<tr><td>2022 (% GDP)</td><td>NIIP: 64.4</td><td colspan="2">Gross Assets: 122.1</td><td colspan="2">Res. Assets: 41.5</td><td>Gross Liab.: 57.7</td><td>Debt Liab.: 23.9</td></tr>
<tr><td>Current Account</td><td colspan="7">Background. The CA balance registered a surplus of 13.6 percent of GDP in 2022, compared with a surplus of 5.1 percent in 2021. The trade balance improved by 9.1 percent of GDP as the price and volume of oil exports increased in 2022. The terms of trade improved by 28.9 percent during the year. For the projections, oil production is assumed to follow the OPEC+ (Organization of the Petroleum Exporting Countries, including Russia and other non-OPEC oil exporters) agreement, with a decline in 2023. The CA is expected to register a surplus in 2023 (around 6 percent of GDP) as oil export revenues decline relative to 2022, in part because of lower oil price projections (the terms of trade are projected to deteriorate by around 22 percent) in 2023.

Assessment. The IMF staff assesses a CA gap of 4.7 percent of GDP using the EBA-Lite CA model, although the overall assessment is subject to significant model uncertainty due to the idiosyncratic characteristics of the Saudi Arabian economy. Saudi Arabia's reliance on oil complicates the application of standard external assessment methodologies, given the wide swings of oil prices between 2020 and 2022. Oil prices increased substantially, in part due to the war in Ukraine, thus rendering a large surplus. This increase is partially captured in the cyclical adjustment component (1.1 percent of GDP). Additional cyclical considerations factoring in the transitory impacts of the COVID-19 pandemic on travel and transport services are assessed to be near 0. The Consumption Allocation Rules suggest a CA gap of 0.3 percent of GDP for constant real annuity rules and –2.6 percent of GDP for constant real per capita annuity allocation rules. The Investment Needs Model suggests a CA gap of 14.4 percent of GDP. The estimated CA gap of 4.7 percent of GDP has an estimated range from 2.2 to 7.2 percent of GDP.[2]</td></tr>
<tr><td>2022 (% GDP)</td><td>CA: 13.6</td><td>Cycl. Adj. CA: 12.5</td><td>EBA Norm: –</td><td>EBA Gap: –</td><td>COVID-19 Adj.:0.0</td><td>Other Adj.: –</td><td>Staff Gap:4.7</td></tr>
<tr><td>Real Exchange Rate</td><td colspan="7">Background. The riyal has been pegged to the US dollar at a rate of 3.75 since 1986. On average, the REER appreciated by 4.1 percent in 2022 and was 5 percent above its 10-year average, while the NEER appreciated by 8.7 percent in 2022. The NEER appreciation was mainly driven by the appreciation of the US dollar versus third currencies and with inflation less than in its trading partners, Saudi Arabia's REER appreciation was less than that of its NEER. As of April 2023, the REER was 0.2 percent below the 2022 average.

Assessment. Exchange rate movements have a limited impact on Saudi Arabia's competitiveness in the short term, as most of its exports are oil or oil-related products that are denominated in dollars. There is limited substitutability between imports and domestically produced products, which in turn have significant imported labor and intermediate-input content. The EBA-Lite REER model suggests an overvaluation of 11.2 percent. Consistent with the IMF staff CA gap and based on an elasticity of 0.2, the staff assesses the REER to be undervalued by 21.6 percent, with a range of –9.1 to –34.1 percent.</td></tr>
<tr><td>Capital and Financial Accounts: Flows and Policy Measures</td><td colspan="7">Background. Net financial outflows continued in 2022 as the PIF and other entities invested abroad.

Assessment. A lack of detailed information on the nature of financial flows in Saudi Arabia complicates analysis of its financial account. The strong reserves position, including the sizable assets of the PIF, limits risks and vulnerabilities to capital flows.</td></tr>
<tr><td>FX Intervention and Reserves Level</td><td colspan="7">Background. The PIF's investments abroad are increasing, although most of the government's foreign assets are still held at the central bank within international reserves. Net foreign assets increased to $440.5 billion (39.7 percent of GDP, 19.4 months of imports, and 231 percent of the ARA metric) at the end of 2022, down from $438.2 billion at the end of 2021 (and from $724 billion in 2014). This trend was, in part, driven by financial outflows. Reserves are expected to stabilize at about 14 months of imports in the medium term.

Assessment. Reserves play a dual role: they are savings for both precautionary motives and future generations. Reserves are adequate for precautionary purposes (measured by the IMF's metrics). Buffers are also provided by external assets held by the PIF and national oil company. Nevertheless, fiscal prudence is needed over the medium term to strengthen the CA and increase savings for future generations.</td></tr>
<tr><td colspan="8">[2] EBA models do not include Saudi Arabia. The IMF staff has considered three approaches in the EBA-Lite methodology, including two that incorporate the special intertemporal considerations that are dominant in economies in which exports of nonrenewable resources are a very high share of output and exports. Using the EBA-lite CA model, the cyclically adjusted CA norm is estimated at 7.7 percent of GDP (slightly higher than the CA norm of 7.5 percent of GDP in 2021). The Consumption Allocation Rules assume that the sustainability of the CA trajectory requires that the net present value (NPV) of all future oil and financial and investment income (wealth) be equal to the NPV of imports of goods and services net of non-oil exports. Estimated CA norms from the Consumption Allocation Rules were 13.3 percent of GDP and 16.2 percent of GDP for the constant real annuity and constant real per capita annuity allocation rules, respectively. The Investment Needs Model takes account of the possibility that it might be desirable to allocate part of the resource wealth to finance investment, which was not explicitly considered by the consumption-based model and produced a CA gap of 14.4 percent over the medium term. The reliance of the consumption and investment models on projected oil prices beyond the medium-term macro framework subjects the results to a high degree of uncertainty. The CA gap in 2022 of 4.7 percent of GDP represents the staff's overall assessment, which is anchored on the EBA-Lite CA model. The range for the gap is calculated using the estimates for Norway, a comparable oil-rich economy in the EBA sample.</td></tr>
</table>

[1] Prepared by Sidra Rehman.

Annex VI. Housing Market[1]

Context

1. **The housing market in Saudi Arabia is undergoing a dramatic transformation**. The Saudi Housing Program, which was launched in 2018 and is administered by the Ministry of Municipal and Rural Affairs and Housing (MOMRAH), is an important component of the Saudi Vision 2030.[2] Recognizing that "housing is the fundamental asset that is capable of shaping and influencing the vibrancy of the families, communities, and broader society," Vision 2030 aims at transforming the housing market and increasing investments in housing with a specific numerical target: the home ownership ratio is set to reach 70 percent by 2030, up from 47 percent in 2016.[3] Until reforms started, Saudi home buyers were largely reliant on the Real Estate Development Fund (REDF) to borrow funds, which sometimes took more than two decades for approval.

2. **Vision 2030 has also set several other strategic goals for Saudi cities**. These goals include: (i) becoming one of the top-15 world economies; (ii) recognition of Saudi cities in the top-ranked 100 livable cities in the world; and (iii) construction of 35+ megaprojects. As an example of these megaprojects, Saudi Arabia plans to build the world's tallest buildings in a mostly unpopulated area as part of a new development called Neom. Two twin skyscrapers about 500 meters high are planned to stretch for dozens of kilometers from the red sea into the desert hosting a mix of residential, retail, and office space.

3. **The Saudi Housing Program contains several specific initiatives which drive the current housing trends**. The initiatives include general tax incentives to purchase and own real estate, government programs for certain types of borrowers for house purchase, and liquidity support to the mortgage market by the Saudi Real Estate Refinancing Company (Box 1). The Program's introduction changed the game for all critical stakeholders: funders, builders, and beneficiaries. Moreover, MOMRAH has other initiatives to increase the housing units supply, namely through urban regeneration of districts within cities and modification of the building regulations.

4. **The Real Estate General Authority (REGA) was established in 2017 to regulate the real estate sector in Saudi Arabia, enhance its efficiency, and increase local as well as foreign investments**. REGA plays a key role in increasing the efficiency and professionalism within the real estate sector through several activities and programs. For example, REGA worked on increasing skills capacity in the sector by establishing the Saudi Real Estate Institute, which provides tailored training programs to different stakeholders, including real estate brokers. REGA also established the real estate arbitration center which reduces the burden on courts through an effective resolution of disputes arising from programs overseen by REGA.

[1] Prepared by Vassili Prokopenko.
[2] See https://www.vision2030.gov.sa/v2030/vrps/housing/
[3] The level of 70 percent of home ownership would be broadly similar to actual ratios in the U.S., UK, and EU.

Box 1. Key Initiatives Supporting Housing Market Developments in Saudi Arabia

Financial support to entitled beneficiaries. The subsidy program allows beneficiaries to construct their subsidies as they see fit using a real estate advisor platform. The average amount of subsidy is greater than SAR 150,000.

Interest rate subsidy. For mortgages to eligible low-income borrowers originated before February 2023, the REDF has committed to cover interest payments on up to SAR 500,000 of the principal balance of a loan; the borrowers pay interest on the principal balance exceeding SAR 500,000. This subsidy was modified in January 2023 due to a rapidly increasing interest rate. The new subsidy matrix is created based on the monthly income of beneficiaries. Beginning with a monthly salary of SAR 3,000, the subsidy is 45 percent of the beneficiary's income, and it is reduced for higher incomes.

Tax incentives for first-time property buyers. The first-time buyers of properties of up to SAR 1 million are exempt from the real estate disposal tax.

Program to facilitate housing loans to government employees. A joint MoF-MOMRAH program provides government guarantees for housing loans to employees from the public sector.

Housing support for military personnel. Until 2020, REDF provided an interest-free loan up to SAR 140,000 for the house purchase by active military personnel.

Mortgage guarantees. Until recently, REDF used to provide mortgage guarantees to some borrowers who were not considered creditworthy by banks.

Reduced down-payment. SAMA increased the regulatory threshold for the maximum loan-to-value ratio for the first-time home buyers from 70 percent to 85 percent in 2017 and then to 90 percent in 2018. For loans on properties valued under SAR 1 million and subject to specific eligibility criteria, the minimum down payment of 5 percent is permitted. The regulatory threshold for the maximum loan-to-value ratio for a second property is kept at 70 percent.

Provision of liquidity to the mortgage market. The Saudi Refinancing Company (SRC) was established in 2017 as a subsidiary of PIF to inject liquidity in the real estate market. The SRC provides liquidity to mortgage lenders through either portfolio acquisitions or direct short-term financing for subsequent mortgage on-lending. There are also plans to package loans into mortgage-backed securities by the SRC and sold to investors. Such a securitization has not yet taken place.

Outcome of the Program

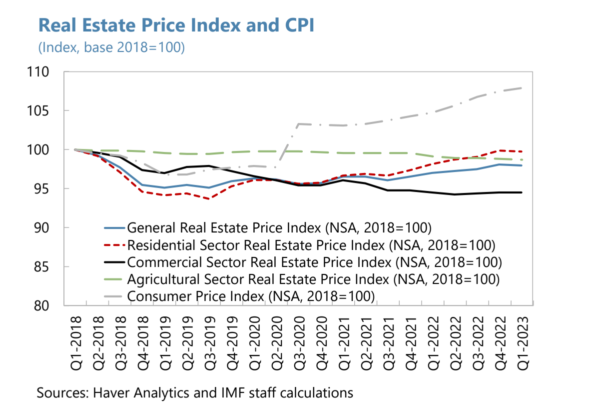
5. **As a result of the authorities' initiatives, Saudi Arabia started to experience a rapid growth in housing construction and mortgage issuance**. The number of real estate transactions has increased substantially since 2016, and more than 1.4 million Saudi families have benefited from the Program. Over 90 percent of signed mortgages are supported by the Saudi Housing Program. The home ownership ratio increased to 60.6 percent by 2022 (from 51.7 percent in 2018). The indicative target is to reach 65 percent home ownership by 2025.

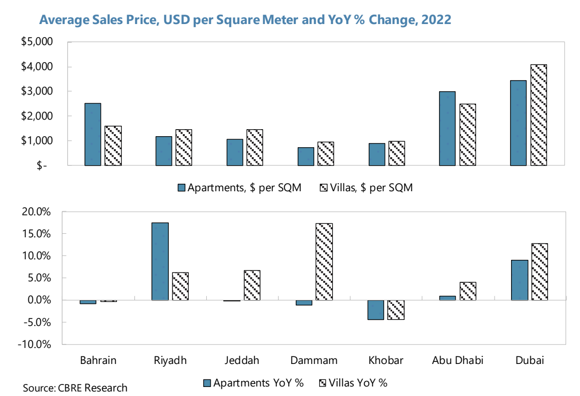
6. **The housing sector is now an important part of the Saudi economy**. The contribution of real estate activity to non-oil GDP was close to 13 percent in 2022, up from around 10 percent in

2021. As of February 2023, almost 5 million workers (17.5 percent are Saudis) were employed in various real estate activities and municipal sector.

7. The housing sector is now also strongly intertwined with the financial sector. Since 2017, real estate-related lending, particularly mortgages, has been growing very rapidly before moderating more recently. Residential mortgages increased from SAR 110 bn in 2016 to SAR 550 bn (US$144 bn) by end-2022, representing now approximately one quarter of bank claims on private sector (Charts). SRC provided refinancing to banks and real estate finance companies for the mortgage portfolio of SAR 19 billion (or 3.5 percent of total mortgages). This refinancing is expected to significantly increase in the next few years as SRC intends to refinance 20 percent of Saudi Arabia's total residential mortgages by 2026-27.

8. Despite the mortgage boom, there are no signs of over-heating in the Saudi real estate market. Demand for housing—emanating from low interest rate (until 2022), government subsidies, relaxed macroprudential policies, and provision of liquidity through SRC—has not significantly outpaced the supply of dwellings. As a result, property prices have been increasing less rapidly than CPI in recent years. Also, the average sales prices in Riyadh or Jeddah remain below those in Dubai, Abu Dhabi, or even Bahrain (charts).





Challenges

9. The Saudi Housing Program has a significant fiscal cost. Various subsidies, guarantees, and tax incentives have significant implications to the government budget. Around three quarters of mortgages are issued at subsidized interest rates. According to the REDF, the housing-related subsidies provided by REDF in 2022 were close to SAR 12 billion, and the outstanding amount of mortgage guarantees issued by the REDF was around SAR 50 billion. The budgeted costs for the housing program for 2023 amount to SAR 9 billion.

10. The situation in the housing market can now also impact the condition of banks. Mortgages have become a significant business for Saudi banks. Given the materiality of real estate loans in banks, an increase in default rates could create a challenge to banks, especially if combined with an abrupt decline in house prices. The probability of such a scenario is, however, relatively low. Until now, defaults on mortgages have been almost non-existent. This is supported by the fact that mortgages are often issued with a full recourse feature, debt service is limited to 65 percent of the borrowers' income, and most repayments are directly linked to salary assignments (and the majority of mortgage borrowers are public sector employees). Also, most mortgages are at fixed interest rate, which provides comfort even to those borrowers who received mortgage prior to the ongoing interest rate hiking cycle without any subsidies.

Conclusion

11. The ambitious agenda to transform the housing sector in Saudi Arabia has been successful. Since its inception in 2018, the Saudi Housing program successfully boosted access to adequate real estate and stimulated supply. Instead of the waiting time that could have lasted for over a decade in the past, the program facilitated procedures for almost immediate entitlement of qualified Saudi citizens to real estate. The ownership ratio has increased and is well on the way to reach the Vision 2030 70 percent target by 2030.

12. At present, risks in the rapid housing sector transformation are mitigated to a large extent. Although house prices have been growing fast in a few specific cities or areas, there are no signs of over-heating and house prices remain moderate compared to other GCC countries. Most mortgages are issued at a fixed interest rate and with a full recourse, which contribute to repayment discipline, while existing prudential ratios and the relatively high capitalization and solid profitability of banks create an extra cushion against unforeseen developments.

13. Nevertheless, the authorities should remain vigilant. While there are currently no signs of disequilibrium in the Saudi real estate market, the situation is fluid. As demand for labor increases and housing supply remains limited (particularly in some big cities), pressure on prices could intensify going forward, as recently seen through the double digit increase in rents driven by a massive return of expatriate workers. Demand for housing will be further boosted by the anticipated relaxation of regulations on real estate ownership by foreigners, which is linked to the intention of making Saudi Arabia a major international hub for various activities. The very rapid growth in mortgages calls for the need to closely monitor credit underwriting and credit management practices in banks. Early detection of debtors and exposures in distress, timely recognition of loan delinquencies, and adequate provisioning are very important.

14. Gradually phasing out various macroprudential and fiscal incentives should be considered if mortgage growth remains strong. Mortgages and other real estate-related lending have been the main contributor of rapid credit growth. Although the pace of mortgage lending started to moderate in late 2022, tightening the previously relaxed macroprudential measures as well as gradually exiting from various fiscal incentives (subsidies, tax exemptions, and guarantees) should be considered. Reducing the maximum loan-to-value ratios on mortgage lending and/or introducing a small countercyclical capital buffer could be among the first measures.

Annex VII. Status of Staff Recommendations Made During the 2017 FSAP

Recommendation	Current Status
Banking Oversight	
Update the Banking Charter and Banking Control Law to delete contradictory and redundant provisions and revoke Article 21 on the power of the Minister of Finance, under exceptional circumstances, to exempt any bank from regulation. Codify and publish all bank legislative circulars and eliminate those superseded.	The amended central bank law was adopted in 2020. The amendments included creation of a direct reporting channel to the King and establishment of SAMA's authority over all covered financial institutions. A revised Banking Control Law was published for general comments and is expected to be submitted to the legislative body in late 2023. SAMA officially launched its Circulars Portal in December 2020.
Strengthen the supervisory approach by refining the determination of banks' risk and control ratings, aligning the supervisory planning with banks' risk profiles, and enhancing the documentation relating to the loan examination process.	The new risk-based banking supervisory framework has been rolled out. A banks' risk rating is now based on a combination of its inherent risk rating and its control rating. The supervisory planning process for on and off-site supervision is now based on a bank's risk profile. In terms of loan examinations, documentation has been enhanced.
Develop a licensing manual for banks and publish guiding principles for bank licensing.	Revised licensing requirements and guidelines were developed and published on SAMA's website in January 2019. Also, SAMA updated Banking Licensing page by adding Banking Laws and Regulations, Banking Rules and Instructions, Circulars Issued to the Banking Sector, Banking Licensing Guidelines and Minimum Criteria, Additional Licensing Guidelines and Criteria for Digital-Only Banks, and the forms needed for banks to start their application process.
Provide guidance to banks on mapping the risk profiles of Islamic products to the Basel framework.	SAMA implemented IFSB banking standards including risk management related standards. Following regulations have been issued: - Shari'ah Governance Framework - Risk Management Framework - Credit Risk Management - Early Settlement Attributes - Related Party - Profit Sharing Investment Accounts (PSIAs) - Capital Adequacy (work in progress) The banks are identifying, measuring and monitoring risks in light of the above-mentioned standards in addition to risk management regulations applicable to conventional banking. Since relevant Shariah related risk standards are in place there is no need to map the Islamic banking risks with those of conventional banking.
Adopt the draft regulation on loan classification and ensure regular, comprehensive reporting on the size of rescheduled and restructured loans.	SAMA adopted IFRS9 requirements which address loans classification and provisioning from an accounting perspective and banks are compliant with these requirements since 2018. SAMA has also implemented BCBS Guidelines on "Prudential treatment of problem assets – definitions of non-performing exposures and forbearance". The central bank is now in the process of issuing its own prudential requirements with regards to loans classification and provisioning which will serve as additional requirements aiming to further

Recommendation	Current Status
	strengthen the existing framework. These requirements are expected to be adopted by the end of 2023.
Require banks to establish formal policies and procedures for loan rescheduling, refinancing, and restructuring and to submit prudential returns on such loans.	SAMA issued rules and guidelines on management of problem loans in January 2020 that requires banks to establish policies and procedures for rescheduling and restructuring of existing exposures.
Strengthen cross-border cooperation by entering into MoUs with foreign regulators.	SAMA has signed an MoU with the Korean Financial Services Commission and Financial Supervisory Service in the area of financial institutions supervision. Another MoU in the areas of financial services and market cooperation has been signed with the UAE. Moreover, SAMA signed an MoU with the Dubai Financial Services Authority to work in the area of financial services.
Liquidity Management	
Establish a liquidity-forecasting framework to guide money market operations.	A liquidity forecasting model has been developed. A new TA mission will assess and provide recommendations on the new model.
Financial Safety Nets	
Adopt and implement the Draft Resolution Law (DRL).	The law on resolution of systemically important financial institutions was issued in December 2020. Currently, SAMA is drafting regulations to implementing that law. SAMA aims to complete the drafting by end-2023.
Establish an Emergency Liquidity Assistance (ELA) framework.	SAMA started developing a general ELA framework.
Establish a timeframe for DPF deposit payouts and ensure a back-up funding line.	The draft law is under public consultation and soon will be approved and be issued.
Macroprudential Policy	
Broaden the definition of debt service to income in the regulations to include all types of debt and income.	The principles that set the debt service to income ratio were issued in May 2018 and implemented in August 2018.
Strengthen data collection and use for the household, corporate, and real estate sectors	Monthly data on new residential mortgages and SMEs finance are now published. Work is ongoing to further strengthen data collection.

Annex VIII. Vision 2030: Actuals vs Authorities Targets[1]

Vision Realization Program	Economic Goals	Select Macro Targets	Baseline[1]	Present	Target
Financial Sector Development Program	Developing the financial sector	SME loans as percentage of total bank loans	2%	7.7%	11%[2]
		Share of cashless operations	18%	62%	70%[2]
Fiscal Sustainability Program	Achieving a sustainable fiscal balance and reducing dependency on oil revenues	Increase non-oil government revenue	166 Billion SAR	410.9 Billion SAR	1 Trillion SAR
Health Sector Transformation Program	Enhancing healthcare services and accessibility.	Life expectancy (years)	77	78	80
		Inclusive healthcare coverage including rural areas	78%	94%	100%
	Developing healthcare infrastructure and technologies.	Number of ICU beds per 100k population.	12.5	15	14 [2]
	Improving healthcare quality and patient outcomes.	Percentage of population covered by the unified digital medical records system	13%[3]	89.6%	100%[2]
Housing Program	Increasing homeownership rates and improving housing affordability.	Homeownership rate	47%	64%	70%
	Developing sustainable and diverse housing options.	Citizen satisfaction index	80%[4]	90%	80%[2]
Human Capability Development Program	Developing a skilled and productive workforce.	Unemployment rate among Saudis	12%	8%	7%
	Enhance education and skills development	Increase Saudization in high skilled jobs	32%	42%	40%[2]
		Ranking in World Bank Human Capital Index	87th	77th	50th[2]
		Females' economic participation rate	22.8%	34.5%	30%
	Promoting entrepreneurship, innovation, and knowledge-based industries.	Percentage of unemployed graduates that find a job in less than 12 months	51%	60%	70%[2]

[1] Prepared by Greta Polo and Sidra Rehman.

Vision Realization Program	Economic Goals	Select Macro Targets	Baseline[1]	Present	Target
	Enhancing education and vocational training systems.	Percentage of technical and vocational education graduates enrolled in the labor market within 6 months of graduation	14%	42%	65%
National Industrial Development and Logistics Program	Enhancing the competitiveness of key industries.	Number of licenses issued in promising industries	169	721	1040 [2]
	Developing a robust logistics infrastructure and facilitating trade.	Logistics Performance Score	49	38	25
National Transformation Program	Serving as the overarching program coordinating and monitoring the implementation of Vision 2030.	Digital economy contribution to GDP	0.2%	15%	19.2%[2]
		Government Effectiveness Index Rank	78th	66th	20th
	Focusing on economic diversification, private sector growth, and job creation.	Increase SME contribution to GDP	20%	29%	35%
		Global Competitiveness Index	41st	36th	10th
	Implementing various initiatives across multiple sectors to achieve the vision's goals.	Ranking of the Kingdom in the United Nations e-Government Development Index	44th	31st	5th
Pilgrim Experience Program	Enhancing services, facilities, and infrastructure for pilgrims.	Increase the capacity to welcome Umrah visitors per year	6.2 million	8.4 million	30 million
Privatization Program	Promoting the privatization and private sector participation in key sectors.	Increase private sector contribution to GDP	40%	43%	65%
	Attracting local and foreign investments through privatization initiatives.	Increase FDI (percent of GDP)	1.2%	2.2%	5.7%
Public Investment Fund Program	Enhancing the role of the Public Investment Fund as a catalyst for economic growth.	Increase Public Investment Fund assets	600 Billion SAR	2.23 Trillion SAR	7 Trillion SAR

Vision Realization Program	Economic Goals	Select Macro Targets	Baseline[1]	Present	Target
Quality of Life Program	Developing the tourism sector, supporting cultural and entertainment initiatives, and facilitating private sector investments for sustained development and growth	Tourism sector contribution in GDP	3.6%	4.5%	10%

[1]Baseline is as of 2016 unless otherwise indicated. Target indicates latest available observation.
[2]2025 Target.
[3]Baseline is as of 2018.
[4]Indicates a threshold of 80% is to be maintained consistently throughout the year.

Annex IX. Saudi Arabia: Voluntary Assessment of the Transnational Aspects of Corruption

As part of its Framework for Enhanced Engagement on Governance (2018), the Fund urges all members to volunteer to have their own legal and institutional frameworks assessed in the context of bilateral surveillance and on transnational aspects of corruption, for purposes of determining whether: (a) they criminalize and prosecute the bribery of foreign public officials; and (b) they have an effective AML/CFT system that is designed to prevent foreign officials from concealing the proceeds of corruption. So far, 13 members have agreed to the voluntary assessment: G7 countries and Austria, Czech Republic, Netherlands, Norway, Saudi Arabia, and Switzerland.

Facilitation Issues

1. **Saudi Arabia has taken steps to strengthen the Anti-Money Laundering (AML) framework to mitigate the risks of the country being used to conceal the proceeds of foreign corruption or "facilitation issues."[1]** As noted in the MER, the country's national risk assessment (NRA) identifies corruption as one of the most significant domestic proceeds-generating crimes, however, Saudi Arabia is not considered an attractive location for laundering international proceeds.[2] Key findings from the MER and measures taken by the authorities include:

- **Controls on foreign ownership of companies to mitigate the risk of misuse of legal persons for money laundering (ML) purposes.** Competent authorities and the private sector can access information on beneficial ownership (BO) of legal persons through the corporate registry. As part of its efforts to enhance the registration of the BO information, Saudi Arabia issued the new company law in 2022 that explicitly provides the Ministry of Commerce with the authority to set the rules and procedures to ensure the BO information is updated and accurate. However, beneficial ownership information maintained by banks on their clients was not always up to date. Furthermore, the authorities have recently launched an electronic platform to increase access and update to beneficial ownership information of legal persons and issued circulars to enhance awareness of methods to conceal beneficial ownership.

- **Larger financial institutions have a good understanding of ML risks** and apply appropriate AML/CFT preventive measures including customer due diligence and identification of beneficial ownership. However, financial and non-financial institutions could improve the timeliness of their reporting of suspicious transactions, and the authorities have since issued guidance on preventive measures with a view to addressing this.

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[1] The Financial Action Task Force (FATF) and Middle East and North Africa Financial Action Task Force (MENAFATF) conducted a joint assessment of Saudi Arabia's AML/CFT framework and issued the relevant mutual evaluation report (MER) in 2018.

- **Supervisors of financial institutions** have a good understanding of ML/TF risks, conduct intensive supervision of higher-risk sectors, and have a high level of engagement with regulated entities.

- **The authorities have sought to improve ML investigations and prosecutions.** Recent efforts focused on capacity building and training on parallel financial investigations by the Oversight and Anti-Corruption Authority (Nazaha) on asset tracing and confiscation by the financial intelligence unit, and a manual on procedures for seizure and confiscation issued by the Public Prosecutor. Nazaha established an asset recovery department focusing on recovery of corruption proceeds and departments for asset tracing and confiscation were established at the Directorate of General Security. As part of its efforts to confiscate proceeds of corruption offenses, Saudi Arabia recently amended its anti-bribery legislation to provide a basis for confiscation of the proceeds of bribery and adopted the principle of non-conviction-based confiscation in 2019. Saudi Arabia also improved its case management system for mutual legal assistance and is increasing its cooperation with foreign counterparts on corruption investigations through formal and informal cooperation by increasing the number of memoranda of understanding with foreign counterparts and utilizing existing networks for multilateral cooperation.

2. **Further improvements are nevertheless needed to ensure that the laundering of the proceeds of foreign corruption is detected and disrupted more effectively.** These notably include: (i) enhance understanding of the risks and, to that effect, complete the process of updating the NRA to include an analysis of the inflows of proceeds of foreign crimes such as corruption being laundered in the country; (ii) ensure that accurate and up-to-date beneficial ownership information is maintained on all legal persons in Saudi Arabia; (iii) encouraging the authorities - while recognizing the notable steps that have been taken towards investigations into foreign predicate offenses and related money laundering - to continue the measures to further enhance effectiveness for confiscation of the instrumentalities and proceeds of crimes.

Supply Side Issues

3. **In recent years, Saudi Arabia made progress regarding the criminalization and prosecution of the bribery of foreign public officials or "supply-side issues."** In December 2021, the anti-bribery law was amended to extend the criminalization of corrupt acts to foreign government officials, as well as certain officials of international institutions and international organizations. Based on the amendments, Nazaha established the Department for Combating Foreign Bribery. The department's law enforcement officers are tasked with receiving, processing, and investigating all reports of foreign bribery, as well as following up on the Kingdom's implementation of commitments of international conventions such as the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (which the Kingdom is not party to yet). The department is authorized to initiate investigations into suspected cases of foreign bribery that are received through the department's reporting, as well as through a specialized reporting channel aimed at providing support to foreign investors known as "Investor

Care", and reports received via social media platforms. Furthermore, the department regularly conducts workshops aimed at raising awareness of the offense of foreign bribery and aims at including foreign bribery as a predicate offense to money laundering. Saudi Arabia also joined the OECD Working Group on Bribery in 2020 and its participant status has been extended.

Annex X. Industrial Policy in Saudi Arabia[1]

Industrial policy (IP) is an important component of Saudi Arabia's pursuit of structural transformation and diversification enshrined in its Vision 2030 reform program. This policy—guided by the National Industrial Strategy (NIS) and supported by other key initiatives and institutions—aims to achieve these objectives through targeted interventions, incentives, and the establishment of special economic zones (SEZs). However, to realize the full potential of the envisaged policies, it is important to minimize inefficiencies, including through guardrails that have been instituted, and ensure IP complements the ambitious structural reform agenda underway.

1. **As countries seek to deploy their own national programs to encourage investment and boost diversification, industrial policy is gaining renewed attention**. Industrial policy (IP)[2] can play a role in structural transformation and diversification under certain conditions. The literature suggests that it can be justified if there is a significant market failure or externality at the industry level and the government is able to identify these industries and has the ability to correct them through appropriate policies. These externalities can be classified as information externalities, which entails discovering the cost structure of an economy; coordination externalities in the presence of scale economies; or technological or environmental externalities where there are spillovers from firm-level training or R&D spending[3]. For instance, renewable energy represents an industry where government intervention could correct such market failures by encouraging investments in renewables. Interventions are justified if broad-based reforms are deemed insufficient, and these policies must pass a cost-benefit analysis, considering alternative uses of resources. Additionally, in formulating interventions, the risks of government failures should also be minimized. [4]

2. **Saudi Arabia considers IP to be a crucial component of the country's efforts to diversify its economy and reduce its reliance on oil.** Vision 2030's diversification agenda is supported by key pillars and initiatives, notably the National Industrial Strategy (NIS), Public Investment Fund (PIF) and the Green Initiative. The NIS is a strategic roadmap aimed at transforming the economy through a series of key entities and incentives, which falls under the direct purview of Kingdom's leadership (Figure 1). Based on detailed analysis of sub-sectors and value chain segments, the NIS has identified certain sectors as strategic and prioritized investments into these sectors. These include renewable energy, chemicals, metals, advanced manufacturing, food processing, automotive, defense, and pharmaceuticals.

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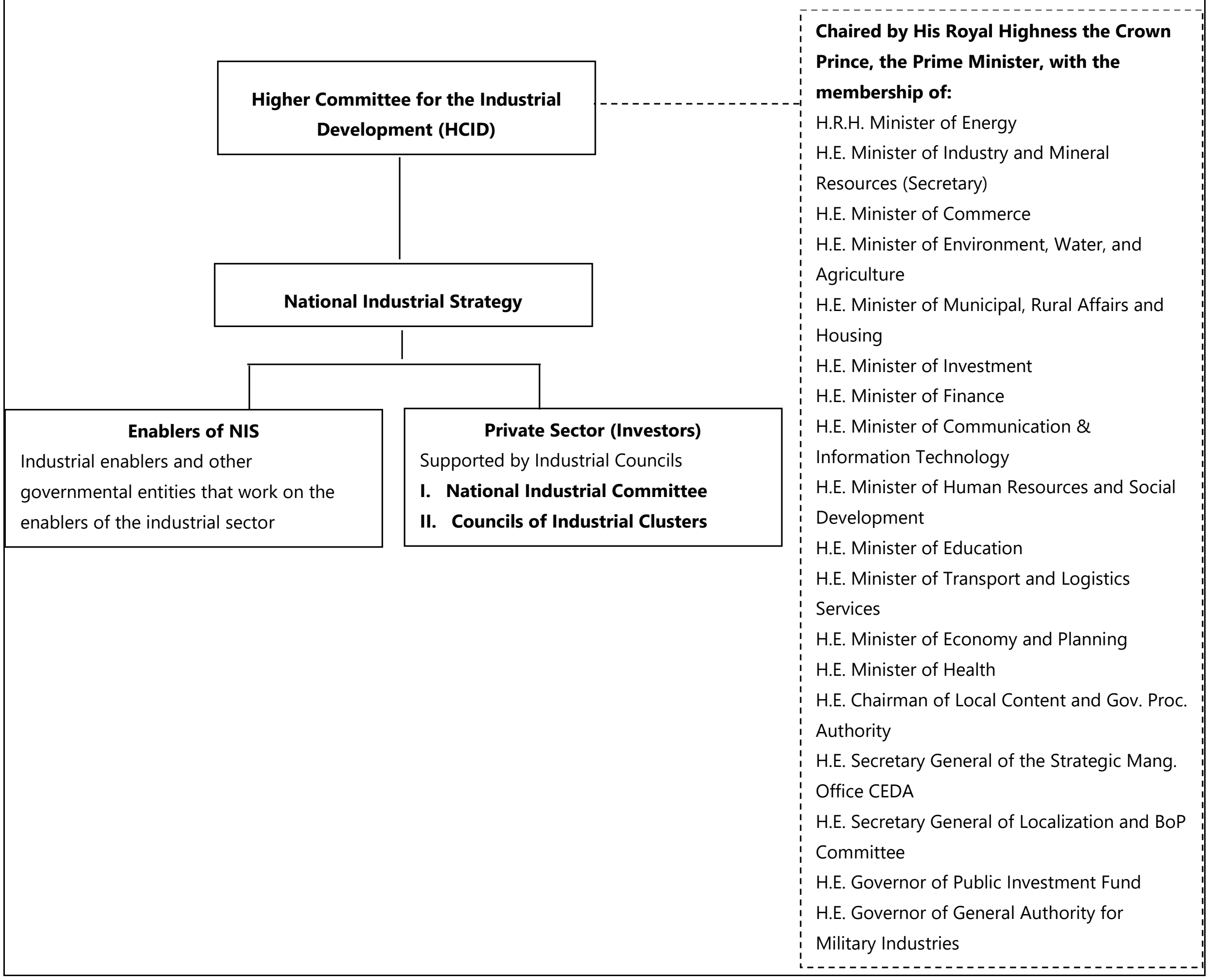
[1] Prepared by Sidra Rehman.
[2] Industrial policy refers to industry-specific interventions that may be temporary, such as fiscal incentives like tax credits and direct subsidies through loans, grants, or guaranteed loans. It is distinct from measures that enhance productivity in a more neutral or horizontal manner across sectors, such as public investment in infrastructure or basic research and development (R&D) initiatives.
[3] See Rodrik, 2004.
[4] See Cherif et. al, 2022.

Figure 1. The Governance of NIS



3. **The NIS focuses on three main objectives**: i) building industrial national resilience; ii) becoming an integrated regional manufacturing hub; and iii) expanding global leadership in selected segments. In the NIS, these objectives will hinge on four enabling conditions: i) building world-class supply chains; ii) growing the industrial business base; iii) unlocking international trade; and iv) cultivating innovation and know-how. Some of the key targets and KPIs are identified below (Figure 2, Table 1).

Figure 2. Key Targets

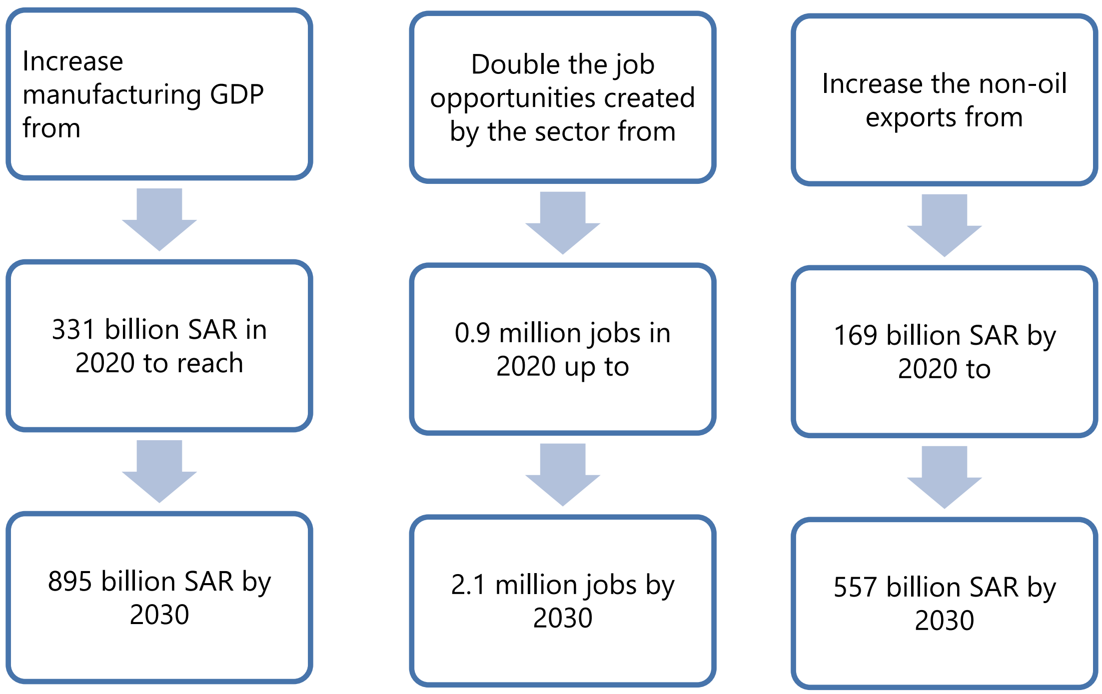


Table 1. Saudi Arabia: KPIs

Indicator Name	Baseline 2020	2030	2035	Clarification
Competitive Industrial Performance Index (CIP Rank) Economic Complexity Index (ECI Rank)	37 39	20 20	Top 15 Top 15	The Kingdom aspires to be among the top 15 countries in the world in the industrial sector competitiveness and the economic complexity index.
Manufacturing GDP (SAR Billion)	331	895	1,413	Increasing the GDP which would contribute to the advancement of the Kingdom's position within the G20.
Manufacturing exports (SAR Billion)	169	557	892	Increasing manufacturing exports as the Strategy is aiming to improve the competitiveness of local products, which will lead to improvement in the balance of trade.
Manufacturing sector employment (Thousands of jobs)	893	2,074	3,281	Creating new manufacturing jobs to reach almost 3 times comparison with 2020.
NIS Localization Ratio (percent)	41%	57%	64%	Growth in the percentage of local industries serving the local market by a multiple of 1.4.

4. The IP strategy, as envisaged by the Kingdom, will be shaped by a series of initiatives, such as the localization of specific services and inputs, providing incentive packages to attract global investors and the development of special economic zones (SEZs). Salient features include:

- **Building a world-class supply chain** by developing logistics and infrastructure where SEZs will play a key role. The **National Industrial Development and Logistics Program** (NIDLP), supported by the Saudi Industrial Development Fund (SIDF), aims to transform Saudi Arabia into a leading industrial powerhouse and a global logistics hub by maximizing the value of its mining and energy sectors as well as logistics, which will serve to support backward and forward linkages. The Kingdom views world-class SEZs as the next frontier for attracting investment and localizing business, as reflected in the 2021 National Investment Strategy commitment to developing SEZs with "game-changing regulatory and competitiveness offerings" by 2030 (see box 1).

Box Table 1. Special Economic Zones

Special Economic Zones (SEZs) are legal, logistical, and tax arrangements, typically intended to help attract foreign investment into export-oriented manufacturing. Through such zones, countries aim to overcome critical constraints related to service provision, infrastructure, land titling, and red tape. Indeed, their popularity has grown over time, with an estimated 4,300 zones around the world, although the definitions of SEZs differs substantially across countries (World Bank, 2017).

Box Figure 1. Location of Key SEZs

Source: Country Authorities.

By developing SEZs and other initiatives to attract foreign direct investment, Saudi Arabia seeks to accelerate its competitiveness in the global marketplace while recognizing that the impact of its structural reforms could take more time to materialize. Through the establishment of SEZs, the authorities aim to catalyze the formation of business clusters by concentrating similar industries in one area, thereby encouraging collaboration, competition, and information sharing. The target sectors range from light manufacturing, and logistics to cloud computing and the digital economy. Some examples of key SEZs ,including those launched by Economic Cities and Special Zones Authority (ECZA), are: the Special Economic Zone at King Abdullah Economic City (KAEC SEZ), located north of Jeddah, which is set to become a massive commercial and logistics hub; Special Integrated Logistics Zone ((SILZ); Ras Al Khair SEZ which includes the King Salman Global Maritime Industries Complex, and Jazan SEZ, all of which offer incentives beyond those in the base economy (Box Figure 1). NEOM, a futuristic smart city development, also aims to become a semi-independent free zone. Some anchor investors have already signed up including Lucid, Ceer, and Google Cloud, and a pipeline of investors have expressed a strong interest in target sectors including automotive components, tier 2 and 3 maritime components, and digital technologies.

SEZ authorities and sector regulators are entitled to develop a range of independent regulations and incentives that could potentially provide far more favorable treatment to investors in SEZs than is currently provided

Box Table 1. Special Economic Zones (concluded)

in the regular economy, including regulatory exemptions and tax breaks to companies, including generous fiscal exemptions such as the 50-year tax holiday in SILZ (Box Table 1). The SEZ regulatory authorities (Economic Cities and Special Zones Authority, in coordination with General Authority for Civil Aviation, and the recently established Center for Special Economic Zones in Riyadh City) oversee the network of SEZs. The National Incentives Committee, overseeing incentives across the economy, coordinates through a working group with ECZA, which is the umbrella regulator and the authority responsible to regulate, plan, and monitor SEZs across the Kingdom. This will ensure harmonization as regulations and incentives are devised. While General Authority of Civil Aviation (GACA) is currently responsible for SILZ, it is expected to fall under the umbrella of ECZA.

Table 1. Special Economic Zones Incentives

Instrument/Policy	
Corporate Income	5 percent for 20 years[1]
Withholding tax	0 percent permanently for repatriation of profits from SEZs into foreign countries.
Customs duties	0 percent deferral for goods coming into the SEZs
Expat levy	Fees exemptions
Saudization and local content requirements	0 percent from 1-5 years; 15 percent from 6-10 years; 11-15 will be supported by job replacement programs while maintaining flexibility with investors.

[1] 50 years for SILZ. The Cloud Computing SEZ does not have tax incentives.

- **Growing the industrial base** which, as envisaged in the NIS, will depend on a transparent and agile regulatory framework. Increasing local production and the proportion of locally produced goods and services will focus on developing local industries, supporting SMEs such as through SIDF's Afaq program, improving the business environment, and fostering partnerships between local and international companies. Saudi Arabia's IP considers local procurement to be a key lever of this effort, where incentives vary depending on the sector, and will be pursued through the following approaches:

    - **Government procurement,** guided by the Local Content Procurement Government Authority, aims to nurture local potential by creating the legislative environment, including regulations and policies, for the development of local content. Mandated thresholds and compliance requirements vary by sector and are typically set on a project-by-project basis, following a contract analysis. Key initiatives include issuing the mandatory list of national products for various sectors. This measure does not discriminate between local or foreign owners, as long as they are domiciled in Saudi Arabia. This extends to foreign firms who would not be excluded from the bid but would only win if the price is very competitive. Other waivers also exist, including if costs of locally sourced inputs are beyond prices considered appropriate, or if the quality is deemed suboptimal. Since the introduction of this measure in 2022, local content in government contracts increased to 40 percent (from 28.8 percent in 2018, and against a 70 percent target set for 2030).

- o **Made in Saudi** initiative, which is a NIDLP initiative led by the Saudi Export Development Authority, aims to help local businesses grow by encouraging local consumers to buy more locally made products, and helping businesses increase their exports to priority markets. Under one unified brand, where program beneficiaries use the Made in Saudi Logo, the initiative aims to bring significant opportunities for businesses to expand their reach and promote their products domestically and globally.

- o **In-Kingdom Total Value Add (IKTVA)** program, created by ARAMCO, has set a target of achieving a specific level of local content in the oil and gas sector by 2030. As of 2022, the program had already achieved a 63 percent local content level.[5]

- **The Regional Headquarters (RHQ) initiative** aims to incentivize multinational companies to establish their RHQs in Saudi Arabia and contribute to the country's economic diversification. In 2021, Saudi Arabia announced that starting 2024, the government would cease signing contracts with foreign companies that do not have their regional headquarters in the Kingdom. This is intended to stimulate foreign investment. Incentives include Saudization exemptions, visa limit exemptions, end-to-end business services, and government fee waivers, among others.

- **Other key pillars of Vision 2030 with IP policies include:**

  - o **The PIF**. Utilizing its strong asset base and strategic economic partnerships, the PIF is committed to unlocking new sectors in the Kingdom, and by utilizing its position as a leading global asset manager, it aims to play a key role in de-risking sectors, thereby catalyzing private investment in such sectors. It is also planning to introduce local content requirements, aligned with the overall direction of local content at the national level, although the requirements are independent of LC application of government procurement.

  - o The **Saudi Green Initiative** aims to reach net zero GHG emissions by 2060 with Saudi Aramco, the country's main oil producer, achieving net zero Scope 1 and Scope 2 emissions by 2050. The targets will be achieved through a wide range of policies, notably through enhanced energy efficiency, increased reliance on renewable energy and through the Circular Carbon Economy. These policies will be shaped by a series of incentives including subsidies and tax incentives as well as coupled with energy price reforms and climate friendly investment to boost the renewable sector. Additionally, other initiatives such as an increased penetration of electric vehicles through PIF's ownership of California-based electric vehicle company Lucid Motors will play a role, which again underscores PIF's position as a key stakeholder.

[5] See IKTVA and Saudi Arabia Vision 2030 by Raj Savio: SSRN and Signings worth $7.2bn at 7th IKTVA Forum as Aramco Digital Company launched | Aramco

5. Certain pitfalls can plague such targeted policies, including through distortions or limiting spillovers to the broader economy, which warrants a careful calibration of these policies.

- **Local procurement for government contracts** remains WTO compliant for Saudi Arabia due to its status as a non-signatory to the WTO Government Procurement Agreement (GPA). It is also benefiting from carve-outs for goods and services that are available to all WTO members. However, the emergence of local content provisions may pose a challenge to Saudi Arabia if it decides to transition from an observer to a full member of the GPA. Moreover, local procurement for government contracts could inadvertently create constraints in a rapidly growing economy and hinder competition thereby bidding up wages and prices of scarce local inputs.

- **Spillover outcomes from SEZs** remain uncertain as they depend on various factors, such as the characteristics and strategies of SEZ-based firms, local endowments, and the host country's institutional setting.[6] A World Bank study (2017) found no catalytic impact of SEZs on the countries they operate in, though a positive effect was observed within a 20 km perimeter. The empirical literature on Foreign Direct Investment (FDI) expresses skepticism regarding spillover benefits for developing countries, attributing it to constrained absorptive capacity.[7]

- **Fiscal incentives**—while not always the primary constraint to investments in Saudi Arabia and elsewhere—are frequently employed to attract firms to establish their operations in SEZs. By design, SEZs may entail tax expenditures, and more attractive incentives within these zones may lead to a cannibalization of the base economy and limit broader spillovers.

6. Successful industrial policies and targeted interventions hinge on broad-based structural reforms, while minimizing associated inefficiencies, including through guardrails already being considered by the Kingdom. Properly formulated industrial policies can play an important role in structural transformation and diversification. However, to maximize the benefits to economic growth and minimize the risks, incentives should be carefully designed with a focus on transparency and accountability to minimize governance risks, and with due consideration to the following basic principles that the literature generally agrees on:

- **Institutional set-up**. A strong governance framework is essential to prevent waste of public resources and government failure. Successful industrial policy episodes in East Asian economies share four common features in their planning agencies: *ambition, autonomy, accountability, and adaptability*. The state and firms need to collaborate closely, with the state setting ambitious goals and policies, giving firms autonomy to achieve them, and ensuring strict accountability through domestic and international competition, thus preventing patronage and capture. Finally, both the state and firms must adapt quickly to changing circumstances to achieve long-lasting success.[8]

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[6] See Farole and Winkler, 2014.
[7] See Duarte et al., 2014.
[8] See Cherif et. al 2021.

- o ***Staff views and authorities' actions****. On the institutional set-up, the authorities have a clear governance framework and a national incentives committee—which should govern all incentives (including through a working group with SEZs). For example, while the National Incentives Committee is responsible for deal-level incentives, such as the Apple deal within SILZ, the incentives scheme for each of the SEZs operating under ECZA is coordinated with NIC through a working group and is subject to a Council of Ministers decree/approval. Targets are set by KPIs.*

- **Rigorous evaluation of policy impact** ensures accountability, particularly by delineating clear lines of responsibility for both successes and failures in implementing industrial policy. This evaluation serves as vital input for informed decision-making. Monitoring and accountability could involve regular reporting on targets and achievements, accompanied by explanations for deviations from planned outcomes. Such monitoring can help identify successful policies and phase out others, including those that may have unintended consequences. Thus, resources can be more efficiently allocated, maximizing the investment impact.[9]

  - o ***Staff views and authorities' actions****. The authorities have a monitoring and evaluation mechanism in place, which would lead to regular reporting on targets and achievements. In this context, the authorities' monitoring efforts to conduct a cost-benefit analysis on each new IP measure before it is approved as well as regular assessment of the impact and effectiveness of IP—including local content requirements—will help mitigate risks, including by providing the flexibility to abandon, phase-out or modify policies as deemed necessary. On tax incentives:*

    - ✓ *Current initiatives are to assess the level of tax expenditures and economic activity in SEZs to determine if the benefits awarded to firms are justified by increased employment or positive spillovers to the rest of the economy and ensuring the stringent application of selection criteria for benefiting industries to avoid past errors that have afflicted industrial policy implementation. This should be accompanied by making sure there is a level playing field between firms in SEZs and the broader economy by reevaluating the tax burden on firms operating outside the zones, addressing regressive taxes, and fostering SME development.*

    - ✓ *Ongoing work by the authorities to inventory and keep track of a database of all incentives will help better identify costs and identify inconsistencies is welcome. Fiscal risks will also be reduced through strict exit criteria, sunset clauses and time bound nature of incentives granted. Notwithstanding these efforts, fiscal exemptions, in particular the 50-year tax holiday at SILZ, may become a burden.*

- **Special emphasis on export orientation** with a focus on technology and innovation rather than import substitution, and holding firms accountable for the support received, such as on the basis of strict performance criteria. In the "Asian miracle economies", the government intervened

[9] See Rodrik, 2008, and OECD 2013.

early on to support domestic firms in sophisticated sectors while ensuring fierce competition (Cherif et al, 2021). While import tariffs can protect nascent sectors ("infant industry argument"), they can also lead to misallocation of resources, rent seeking and lack of competition.

- ***Staff views and authorities' actions***. *The authorities are aware that global trading regime restricts the use of import tariffs which can be distortionary or elicit retaliation from trading partners. Hence, their commitment to ensure consistency with WTO legal obligations. To ensure focus remains on export-oriented activities, the authorities could consider additional targets to ensure that their export goals are met—for example, through monitoring export shares and not just manufacturing production. Due to the potential pitfalls from local content provisions, it is important that such preferential practices, which are discriminatory, be avoided because they can distort local production and could risk triggering retaliatory actions by trading partners and disrupt balanced growth.*

- **Well-coordinated policies to foster backward linkages**, such as through high domestic value added, and forward linkages with a focus on downstream activities. High linkages and associated spillovers induce agglomeration effects and clusters which, through feeding back into productivity gains, can support sustained employment. For example, SEZs can contribute to growth and development by helping to attract investment, create jobs and boost exports – both directly and indirectly when they succeed in building linkages with the broader economy and when accompanied by an integrated strategy, including a conducive business environment, technology upgrading and skills training.

  - ***Staff views and authorities' actions***. *The authorities have instituted substance requirements, including related to minimum capital requirements, which can help stimulate activity rather than just reshuffling existing economic activity. Regular economic impact assessment can also introduce important guardrails. Furthermore, industrial policy instruments need to be developed jointly with other policies while continuing to ensure there is no hindrance to foreign competition.*[10]

- **Upskilling and reskilling the current workforce** to remove skills gaps and mismatches and better aligning educational programs with employer needs.

  - ***Staff views and authorities' actions***. *Initiatives such as the Human Capital Development program and the Labor Demand Foresight Unit will serve to address these needs. Additionally, improving the quantity and quality of education at all levels, including vocational training for middle-aged workers, will create a more productive workforce. Furthermore, reducing the public-private wage gap will boost employment in the private sector, while addressing the productivity-wage gap will ensure competitive wages.*

[10] See UNCTAD (2019) World Investment Report 2019: Special Economic Zones, UNIDO (2016) The Role of Local Content Policies in Manufacturing and Mining in low- and Middle-Income countries, Cherif and Hasanov (2019) The Return of the Policy That Shall Not Be Named: Principles of Industrial Policy and Cherif et al. (2022, forthcoming) Industrial Policy for Growth and Diversification: A Conceptual Framework, IMF Departmental Paper.

INTERNATIONAL MONETARY FUND

SAUDI ARABIA

STAFF REPORT FOR THE 2023 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

July 7, 2023

Prepared By	Middle East and Central Asia Department (In consultation with other departments)

CONTENTS

FUND RELATIONS

(As of May 31, 2023)

Membership Status: Joined August 26, 1957; Article VIII.

General Resources Account:	**SDR Million**	**Percent Quota**
Quota	9,992.60	100.00
Fund holdings of currency	7,056.45	70.62
Reserve tranche position	2,936.16	29.38
Lending to the Fund		
New Arrangement to Borrow	32.67	

SDR Department	**SDR Million**	**Percent Allocation**
Net cumulative allocation	16,259.95	100.00
Holdings	15,554.50	95.66

Outstanding Purchases and Loans: None

Latest Financial Arrangements: None

Projected Payments to the Fund

(SDR Million; based on existing use of resources and present holdings of SDRs)

	2023	2024	2025	2026	2027
Principal	0.00	0.00	0.00	0.00	0.00
Charges/interest	13.57	27.21	27.18	27.20	27.20
Total	13.57	27.21	27.18	27.20	27.20

Lending to the Fund and Grants:

Saudi Arabia is a participant in the New Arrangements to Borrow (NAB), whose credit arrangement under the NAB amounts to about SDR 11.31 billion. The outstanding amount under the credit arrangement as of May 31, 2023 is about SDR 32.67 million.

- ***PRGT loan resources**:* Saudi Arabia has provided four loans to the Poverty Reduction and Growth Trust (PRGT), totaling SDR 3.3 billion, through borrowing agreements with the Saudi Central Bank (SAMA). The first borrowing agreement (SDR 500 million) was effected in May 2011 and the other three agreements—provided in the context of the 2021 loan fundraising round and totaling SDR 2.8 billion—were effected in November 2022 (SDR 550 million), April 2023 (SDR 225 million), and May 2023 (SDR 2,025 million). In addition, in 1989, the Saudi Fund for Development ("SFD") provided SDR 49.5 million in concessional loans made at an interest rate of 0.5 percent per annum through an Associated Agreement with the PRGT.

- ***PRGT subsidy resources**:* As of end-April 2023, Saudi Arabia's total subsidy contributions to the PRGT, including interest earned on outstanding balance of the Trust, was estimated at

SDR 122.3 million, with the remaining balance amounting to SDR 99.7 million. These contributions include:

- ***Implicit subsidy*** earned on the balances of the 1989 loan above and which was estimated at SDR 14.7 million (as of 2005).

- ***Subsidy resources generated from deposits***. In March 2001, Saudi Arabia agreed to support the PRG-HIPC Trust with deposit contributions totaling SDR 94.4 million, of which SDR 16.71 million was contributed by the Kingdom of Saudi Arabia ("Saudi Arabia") and SDR 77.67 million by SFD. In April 2006, these deposits were extended to end-December 2021 with an additional deposit of SDR 38.2 million from SFD, to provide SDR 40 million (end-2005 NPV terms) in subsidy resources to support the Exogenous Shocks Facility. Saudi Arabia's deposit of SDR 16.71 million that matured on December 31, 2021, was transferred as grant contribution to the PRGT General Subsidy Account. SFD's aggregate deposit amount of SDR 115.87 million made at interest rate of 0.5 percent was most recently extended to mature on September 25, 2023 (effective on June 29, 2023, and after completion of internal formalities).

- ***Subsidy resources from other contributions***. In April 2005, Saudi Arabia agreed to provide a grant contribution of $4 million (equivalent to SDR 2.7 million) to subsidize Emergency Natural Disaster Assistance to low income countries, of which SDR 0.15 million was transferred to the PRGT General Subsidy Account upon termination of the EPCA/ENDA Administered Subsidy Account in February 2014. In October 2012 and October 2013, Saudi Arabia provided subsidy resources to the PRGT through the transfer of its full share in the distributions of the general reserve attributed to windfall gold sale profits, totaling SDR 71.87 million.

- ***Other initiatives***: In February 2018, Saudi Arabia pledged to contribute $2 million (equivalent to SDR 2.8 million) to the Financial Sector Stability Fund, supporting financial sector stability, inclusion, and deepening, focused on low- and lower-middle income countries.

Exchange Rate Arrangement

The Saudi Arabian Riyal was formally pegged to the U.S. dollar, effective January 2003 and the exchange arrangement is classified as a conventional peg. Prior to that, it was officially pegged to the SDR at the rate of SAR 5.2625=SDR 1, with margins of 7.25 percent even though in practice it has been pegged to the U.S. dollar since 1986, with a middle rate of SAR 3.7450=$1. Saudi Arabia maintains security-related exchange restrictions pursuant to UN Security Council resolutions 1267 and 1373.

Saudi Arabia has accepted the obligations of Article VIII, Sections 2(a), 3, and 4, and maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions and multiple currency practices

Last Article IV Consultation

Saudi Arabia is on the standard 12-month consultation cycle. The last Article IV consultation was held in person during May 23-June 8, 2022. The staff report was considered by the Executive Board on July 27, 2022 and published on August 17, 2022.

(https://www.imf.org/en/Publications/CR/Issues/2022/08/11/Saudi-Arabia-2022-Article-IV-Consultation-Press-Release-and-Staff-Report-522189).

Resident Representative

No resident representative is stationed in Saudi Arabia.

RELATIONS WITH THE WORLD BANK GROUP

(As of June 30, 2023)

World Bank Country Page:

https://www.worldbank.org/en/country/saudiarabia

STATISTICAL ISSUES

(As of June 30, 2023)

I. Assessment of Data Adequacy for Surveillance
General: Data provision to the Fund has some shortcomings but is broadly adequate for surveillance. Progress has accelerated on national accounts, census, and monetary statistics but there are areas for improvements in prices, monetary, and external sector statistics. As a G20 country, the authorities participated in multiple data initiatives and are committed to the transparent and timely dissemination of statistics for policy use.
Real sector statistics: • **National accounts:** The General Authority for Statistics (GASTAT) compiles annual and quarterly production and expenditure-based GDP estimates with 2010 as base year. New GDP series, which backcast current price and volume series for 1970-2017, were published in March 2023 based on new and more detailed supply and use tables. The transition to a chain-linked volume estimation of GDP as well as the rebasing of GDP to a more recent year, are expected to be completed by Q1 2024. A new methodology of classifying the activities in national accounts was adopted in 2021 to reflect a more accurate representation of oil, non-oil, and government activities. GASTAT also compiles and publishes an industrial production index with improved periodicity (from quarterly in 2016 to monthly since January 2019). • **Census statistics:** Saudi Census 2022 was published in June 2023, covering population, households, and dwellings of housing. The census data is expected to assist in updating socioeconomic indicators and rebasing the CPI basket using more updated weights. • **Price statistics:** CPI data is published monthly using a fixed basket of goods and services consisting of 490 items based on the 2018 expenditure and income survey. To improve the quality of the CPI, GASTAT is currently revising the CPI basket using updated weights. The weight reference period for the wholesale price index is 2014, covering purchaser's prices of expenditures made by businesses, and sample coverage remains limited to three main cities. Real estate price index is published quarterly, covering residential, commercial, and agricultural properties. A new producer price index will be published by end 2023, which will allow improved deflation techniques. • **Labor market statistics:** Data providing a breakdown of employment between the private and public sector is available from 2017. GASTAT discontinued publishing absolute employment numbers in the Labor Force Survey (LFS) in Q4 2022, but continues to provide unemployment rates summary by age, nationality, gender, and education status. Absolute employment numbers, available from Q3 2016, are published based on administrative data from the Ministry of Human Resources and Social Development (HRSD), the General Organization for Social Insurance (GOSI), and the National Information Center. Efforts are currently underway to further improve the LFS based on the census data, with the aim to improve its quality and align it with best practices. In addition, the extent of the informal economy is currently being assessed.
Government finance statistics: The authorities have reclassified the budget mostly in line with GFSM 2014. The GFSM 2014 framework is being used to report and publish some of the fiscal data. Work on accrual data statistics is ongoing. Current coverage of fiscal data is adequate for Fund surveillance but work on government finance statistics should continue, including to classify one-off revenues and expenditures and to move towards a general government concept.
Monetary and financial statistics: The quality of monetary data has improved and information is made available in the Saudi Central Bank (SAMA) Monthly Statistical Bulletin. Detailed data providing a breakdown of

corporate and household deposits is not available. SAMA submitted to STA the preliminary monetary and financial statistics based on the IMF's Standardized Report Forms (SRFs) which are under review. SAMA reports several series and indicators of the Financial Access Survey (FAS), including mobile and internet banking, gender-disaggregated data, and the two indicators adopted by the UN to monitor Target 8.10 of the Sustainable Development Goals (commercial bank branches per 100,000 adults and ATMs per 100,000 adults).
Financial sector surveillance: SAMA reports quarterly financial soundness indicators (FSIs) to the IMF, which are published on the IMF's FSI website (https://data.imf.org/FSI). The reported FSIs comprising all 12 core FSIs and 8 encouraged FSIs for deposit takers.
External sector statistics: Quarterly balance of payments (BOP) and international investment position (IIP) data are published according to the latest international standard (the sixth edition of the *Balance of Payments and International Investment Position Manual*). SAMA compiles external debt statistics quarterly and the Reserves Data Template monthly. The financial account of BOP and IIP are highly aggregated, and more granular data breakdown by institutional sectors will be beneficial for surveillance. At the same time the sectoral breakdown is available in the external debt publication. The coverage for the private sector needs to be improved. SAMA participates in the IMF's Coordinated Portfolio Investment Survey (CPIS). Direct investment data in external sector statistics needs improvements, and there are ongoing efforts to improve the data collection and compilation system under the leadership of GASTAT, with coordination from the Ministry of Investment and SAMA. The successful completion of these efforts will allow the country authorities to participate in the IMF's Coordinated Direct investment Survey (CDIS) and will ensure consistency between BOP and CDIS datasets.

II. Data Standards and Quality	
Saudi Arabia subscribed to the Special Data Dissemination Standard (SDDS) on September 18, 2019.	No data ROSC is available.

Table of Common Indicators Required for Surveillance

(As of June 30, 2023)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]
Exchange rates	6/30/2023	6/30/2023	D	D	D
International reserve assets and reserve liabilities of the monetary authorities[1]	5/2023	6/28/2023	M	M	M
Reserve/base money	5/2023	6/28/2023	M	M	M
Broad Money	5/2023	6/28/2023	M	M	M
Central Bank balance sheet	5/2023	6/28/2023	M	M	M
Consolidated balance sheet of the banking system	5/2023	6/28/2023	M	M	M
Interest rates[2]	6/30/2023	6/30/2023	D	D	D
Consumer price index	5/2023	6/15/2023	M	M	M
Revenue, expenditure, balance and composition of financing[3]—Central Government	Q1 2023	5/23/2023	Q	Q	Q
Revenue, expenditure, balance and composition of financing[3]—General Government	2022	12/13/2022	A	A	A
Stocks of central government and central government-guaranteed debt[4]	Q1 2023	5/14/2023	Q	Q	Q
External current account balance	Q1 2023	6/28/2023	Q	Q	Q
Exports and imports of goods	4/2023	6/22/2023	M	M	M
GDP	Q1 2023	6/08/2023	Q	Q	Q
Gross external debt	Q1 2023	6/28/2023	Q	Q	Q
International investment position[5]	Q1 2023	6/28/2023	Q	Q	Q

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by means as well as the notional values of derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[3] Foreign, domestic bank and domestic nonbank financing.

[4] Including currency composition.

[5] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[6] Daily (D), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).