جدوى للإستثمار
Jadwa Investment

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Monthly Bulletin

Banks lead fourth quarter profits

Profits of listed companies in the fourth quarter of 2010 were much better than in the same period of 2009, but down on those of the third quarter of last year. The year-on-year gain was due to an almost doubling of profits by banks and stronger performance from the petrochemicals sector. Profits were generally in line with expectations and as a result the TASI was broadly flat over the period of earnings releases. Profits for the whole of 2010 were 35 percent up on their level in 2009.

In the fourth quarter net income of listed companies was SR19.2 billion, up by 37 percent in year-on-year terms, but down by 9.7 percent on the previous quarter. Despite the strong year-on-year growth, earnings were lower for six of the 15 sectors. This was because the bulk of the gains were concentrated in the two largest sectors, petrochemicals and banks.

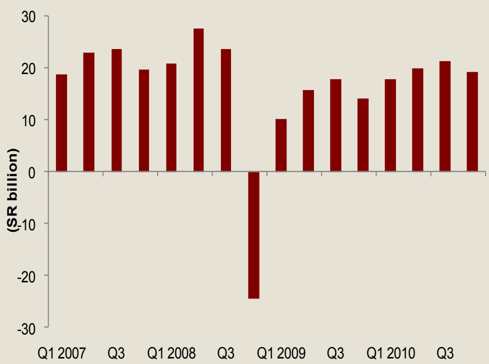
Profits of the banking sector were up by 91 percent year-on-year. A detailed breakdown of bank results is not yet available, but it is clear that the improvement is due to much lower provisioning for bad debts. Banks generally concentrate their provisioning into the final quarter in order to start a new year on a sounder footing. However, in response to guidance from SAMA, it seems that the bulk of provisioning occurred in the third quarter of 2010. As a result, bank profits rose in the fourth quarter for the first time since 2005, though the growth was small, at 5 percent, reflecting subdued lending and very low interest rates.

Petrochemicals posted 64 percent growth in earnings, in large part because of a sharp rise in product prices, but also because of the greater use of new capacity and new players entering production. Thirteen of the 14 petrochemical companies were profitable during the quarter, compared to nine in the corresponding quarter of 2009.

The hotels sector recorded the second largest growth in profits, of 85 percent, though this came from a very low base. Multi-investment rose by 54 percent largely because of the recovery of global stock markets. Earnings from insurance also rose strongly, by 43 percent, though this is down on the growth in the two previous quarters. Earnings of the largest player (Tawuniya) declined, but several others in the sector recorded healthy growth. Nonetheless around half of the listed insurance companies recorded losses in the fourth quarter, reflecting difficulties in ramping-up operations.

In year-on-year terms, building and construction was the worst performing sector, recording a quarterly loss for the first time in at least seven years, owing to one-time adjustments by two companies in the sector; in addition, tougher competition has impacted across

Profits of listed companies



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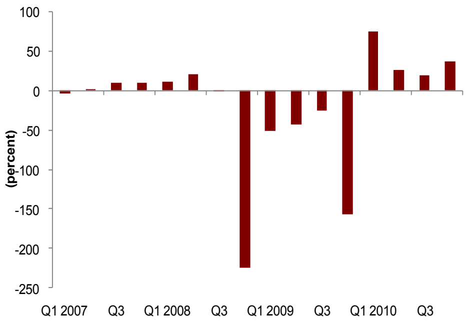
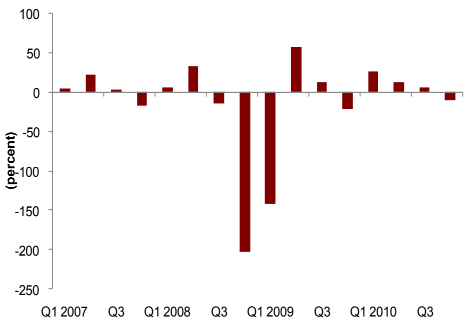
Year-on-year change in profits



Quarter-on-quarter change in profits



the sector. Electricity also recorded a loss in the fourth quarter, though this is in line with the seasonal norm and reflects lower use during the cooler months of the year. Agricultural earnings fell by 27 percent and were dented by one-time provisions by Savola for asset write-downs and losses on foreign subsidiaries and investments.

In quarter-on-quarter terms, total profits declined by 9.5 percent, with nine of the 15 sectors recording falls. This is consistent with the seasonal trend, with earnings falling in the fourth quarter in each of the last six years. It is caused by companies making one-time adjustments in order to clear their books for the new year, as was the case in 2010. Nonetheless, with the banks taking more of their provisions in the third quarter, the drop in the fourth quarter was the smallest since the fourth quarter of 2004.

Annual earnings of all listed companies in the Kingdom totaled SR78.2 billion in 2010, the highest since 2006 and 35 percent above that in 2009. All sectors were profitable last year, with profits rising in eleven. The gain is almost entirely due to the petrochemicals sector. Petrochemicals profits rose by 182 percent and accounted for 94 percent of the increase in total listed company profits in 2010. This was the result of higher production and product prices.

Listed company performance

	2010		Fourth quarter 2010	
Sector	**Net income (SR million)**	**Annual change (%)**	**Year-on-year change (%)**	**Quarter-on-quarter change (%)**
Petrochemicals	29,630	182.0	64.0	23.8
Banks	21,983	0.7	90.6	4.5
Telecoms	10,843	1.0	-7.6	-18.1
Cement	3,637	1.0	14.4	6.2
Agriculture & food	2,605	22.1	-27.1	-53.3
Energy & utilities	2,411	97.4	-	-
Real estate	1,466	-36.5	-32.1	25.0
Industrial inv.	1,399	-11.5	-54.0	-7.3
Retail	1,139	30.0	6.7	-33.4
Building & cons.	827	-38.0	-	-
Multi investment	752	45.0	54.2	65.0
Insurance	682	483.2	43.3	-26.8
Transport	549	13.1	4.1	-14.1
Media & publishing	156	18.3	14.7	94.1
Hotel & tourism	125	-67.1	85.4	-1.8
Market	**78,203**	**35.3**	**36.7**	**-9.7**

The other sectors that recorded high gains were also driven by industry-specific factors. Both insurance and multi-investment are small and their profits came from a low base; they resulted from expansion after recent liberalization and improved returns from foreign investments, respectively. For energy, the jump was due to an increase in tariffs. Nonetheless, double-digit growth for retail, agriculture and food, media and transport are all indicative of improved economic conditions.

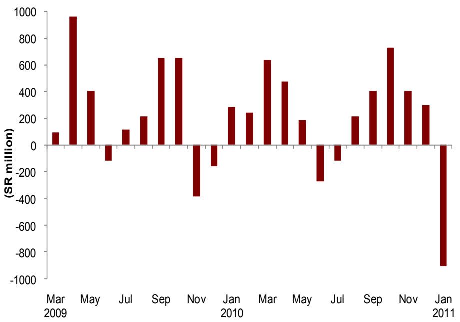
Three of the largest four sectors barely recorded any growth, with earnings from banks, telecoms and cement all up by 1 percent or less. For banks, this reflected high provisioning for bad loans, weak lending growth and very low interest rates. In the case of telecoms and cement, it was due to an intensification of competition. One cement company began production last year and other recent arrivals increased production, while the two newest telecoms operators both recorded losses.

In brief: Stock market

TASI

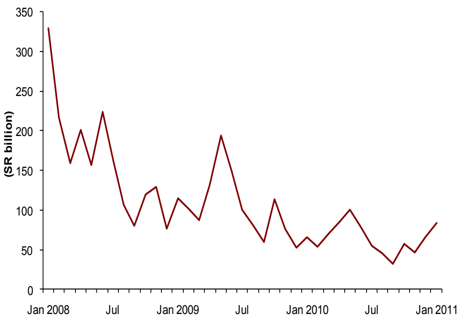
The unrest in Egypt pushed the TASI down to its low-point since late-November. It rebounded slightly after plunging by 6.4 percent on January 29, but remains well down on its level at the start of the year. The TASI had maintained its positive run in December through the first half of January as investors became increasing optimistic about the year ahead, before stabilizing around the middle of the month after the Sabic earnings were announced. While Sabic's earnings, the most-watched in the Kingdom, were in line with consensus forecasts, after the buoyancy of previous weeks and strong results announced earlier by some affiliates they appeared to temper investor enthusiasm. At the same time, the political situations in Tunisia, Lebanon and Egypt were increasingly weighing on investor sentiment.

Net purchases through the swap agreement



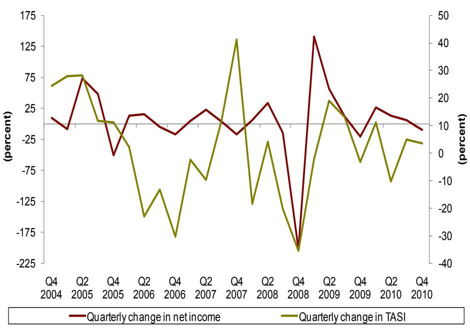
It appears that foreign investors responded to the troubles in Egypt by making large withdrawals of funds from the Saudi market. Net sales through the swap agreement were SR905 million in January 2011. As it is probable that foreign investors were buyers for most of the month in line with the generally upbeat sentiment (Saudi Arabia is one of foreign investors' favored regional markets), this suggests that over SR1 billion was withdrawn in the final three trading days of the month. This is by far the largest monthly withdrawal by foreign investors since the data was first issued in March 2009 and total sales were almost three times the monthly average for 2010. The extent of the outflow illustrates the speed in which foreign investors act at times when they become concerned about risk.

Monthly turnover



As a result of the wave of selling on January 29, daily stock market volumes surged, exceeding SR6 billion for the first time since April 2010. They fell back over subsequent days, but remained over SR4 billion. Volumes had already picked up in January, initially because of investor confidence about the outlook for 2011. The jump in the final few days of the month lifted the total value of shares traded to SR83.8 billion, the highest since May 2010. This was 32 percent higher than the 2010 monthly average. While the peak in volumes was driven by sellers, there were sufficient buyers in the market to match the orders, which shows the capacity for volumes to partially reverse their long-term downward trend when market conditions improve.

Company profits and the TASI



Results for the fourth quarter suggest that investors have become better at predicting company performance and that these expectations are playing a bigger role in moves in the stock market. The graph to the left shows that since the middle of 2008 there has been a fairly close relationship between moves in the TASI and in listed company net income. The increasing availability of equity research is clearly helping to shape expectations and the greater role of institutional investors may well be making the market less prone to sharp divergences from the fundamentals.

Oil market watch

Oil prices touch $100 per barrel

Oil prices touched their highest levels since October 2008 during January, reflecting both growing physical demand, rising stock markets and concerns about events in Egypt. Even though there has been a notable divergence in prices between two benchmark blends, prices are above the ceiling of the Kingdom's comfort zone. There has been mixed evidence on supply response from Opec producers so far, nonetheless we expect a gradual increase in supply this year and with the immediate tensions in Egypt likely to ease we maintain our projection for WTI to average of $83 per barrel in 2011.

Oil prices reached two-year highs in January, though the extent of their rise varies depending on the blend of crude. WTI peaked at $91.9 per barrel on January 11 and at its current level of $91 per barrel is up 8.2 percent from its end-November level. In contrast, Brent peaked at its current level of $100.5 per barrel, 16.1 percent higher than at the end of November.

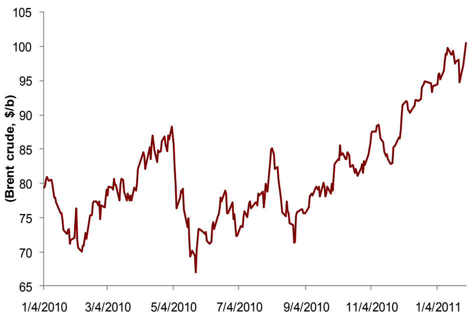
The size of this divergence in pricing is unusual. In absolute and percentage terms the monthly average premium of Brent over WTI in January was the highest since at least 1991. The price of WTI is determined at a specific delivery point in the US and can therefore be distorted by local factors. This currently appears to be the case, with high inventories reported. The susceptibility of WTI to local factors was one of the main reasons why Saudi Arabia stopped using it in its pricing formula for oil deliveries to North America. The Kingdom now uses the Argus Sour Crude Index, which is currently $97.8 per barrel, up by 17.2 percent from the end-November level.

Whichever price is considered, the upward movement is clear. It reflects growing confidence about the health of the global economy, the role of financial investors (as the correlation between oil prices and the stock market remains tight even though oil prices are approaching a level at which they would potentially damage corporate performance) and the unrest in Egypt. Prices are above our estimate of the ceiling of the Kingdom's comfort zone of $70-90 per barrel and several other Opec members have recently stated that they consider around $100 per barrel a more appropriate level (these prices do not relate to any specific blend of crude).

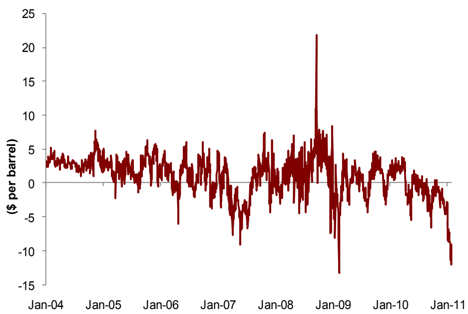
In response, it appears that the Kingdom began to raise production in December, though the picture is not consistent across all sources. According to Middle East Economic Survey data, Saudi oil output climbed to a two-year high of 8.35 million barrels per day, up over 100,000 barrels per day from the November level. The International Energy Agency also estimates a 100,000 barrels per day increase. Conversely, Bloomberg shows only a 15,000 barrels per day increase and Reuters estimates that production was unchanged. According to January data from Reuters, the Kingdom's output rose by 80,000 barrels per day during the month.

We expect a continued gradual rise in monthly oil production. Opec has indicated that it would increase output if tensions in the Middle East (or any other events) lead to an oil shortage, but it is unlikely to formally respond to any short-term price pressure. This means that oil prices have the potential to spike up if regional political conditions deteriorate sharply.

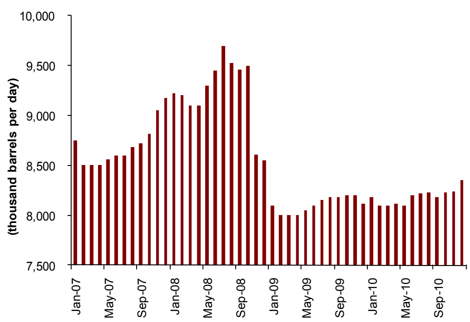
Oil price



Differential between Brent and WTI



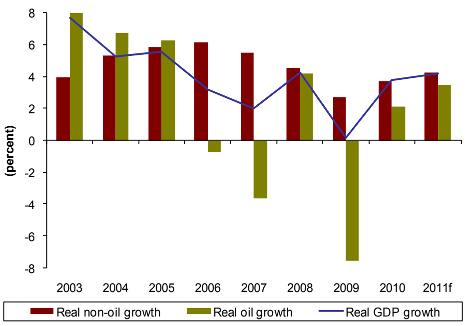
Saudi oil production



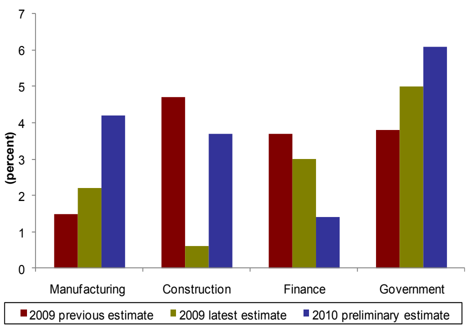
Economy watch

Economic growth data revised

Real GDP growth



Main revisions to real GDP growth



Newly published preliminary data on economic growth for 2010 is in line with that revealed in the budget. The economy grew by 3.8 percent in real terms last year and 16.6 percent in nominal terms. There were some significant revisions in the 2009 data, with growth that year lowered back down to just 0.2 percent, from an earlier estimate of 0.6 percent. It is normal for the government to revise its growth data several times and further revisions appear likely.

The new data for 2010 restate the estimates from the budget, with growth in the oil sector of 2.1 percent, non-oil private sector growth of 3.7 percent and non-oil government growth of 5.9 percent (see our *Saudi Arabia's 2011 budget* report). Of more interest are the changes to the 2009 data. Total real GDP growth for 2009 was put at 0.2 percent. This was the same level as contained in the preliminary data released alongside the 2010 budget, but down from the revised figure of 0.6 percent issued part way through last year.

Oil sector growth in 2009 was cut to -7.6 percent, from -7.1 percent. The new figure is closer to the 12 percent fall in oil production that year (output from the sector is usually greater than oil production due to gas output and some project work in the sector). The figure for non-oil private sector growth was cut to 2.7 percent from 3.5 percent. This means that the improvement in growth in 2010 was more encouraging, but emphasizes the difficulty the private sector faced in 2009 despite then record government spending. Growth of 2.7 percent was the lowest for the non-oil private sector since 1995 and last year's 3.7 percent was the second lowest.

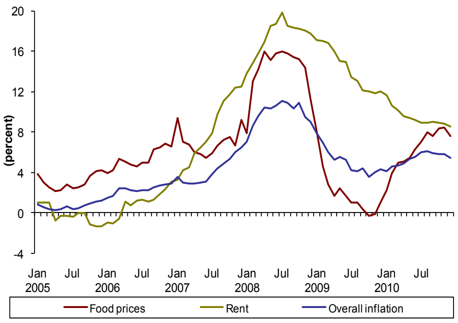
The revised breakdown shows that after agriculture, construction and manufacturing were the two worst performing sectors. Growth in the construction sector was slashed to just 0.6 percent from 4.7 percent. This seems inconsistent with the volume of work that took place and with the increase in cement sales that year, which was 11 percent according to the data produced by SAMA or 23 percent according to the cement companies.

Manufacturing growth was cut to 1.5 percent from 2.2 percent. This was due to a revision to the petroleum refining subsector (manufacturing is broken into petroleum refining, which accounts for 35 percent, and "other"), which now shrank by 3.3 percent compared to growth of 0.1 percent. The other fall was in the finance, insurance, real estate and business services sector. This sector is broken into ownership of dwellings (which accounts for 52 of the total) and "other". It was in the latter where the fall occurred, which may reflect difficulties in measuring output from these areas. Although growth was revised down to 4.8 percent from 6.3 percent, it is still difficult to explain the fall in growth in the subsector to just 1.1 percent in 2010.

The sole upward revision was for the government sector. Growth in non-oil government services was revised up to 5.2 percent from 4.4 percent and total government services up to 5 percent from 3.8 percent. This improvement is encouraging as there has been very high investment in the government sector and earlier rates of growth were little different to the growth in public-sector employment, imply no gains in productivity. Average growth in government services over 2009 and 2010 was the highest since 1984 and 1985.

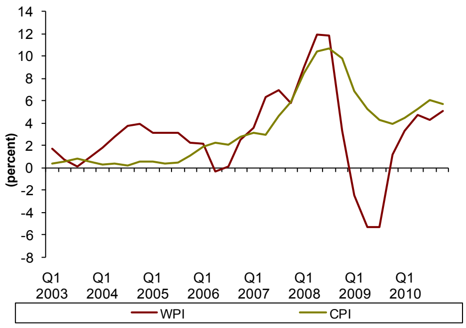
In brief: Economy

Inflation



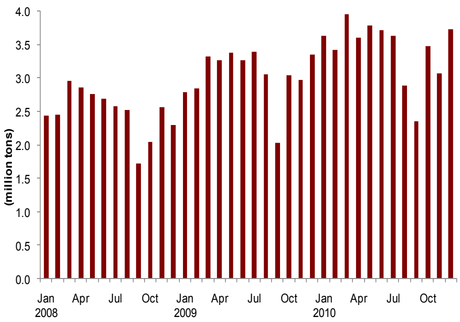
Inflation fell to an eight-month low in December of 5.4 percent, down from 5.8 percent in November. Both food price and rental inflation eased, with the latter at its lowest since November 2008. Rental inflation tends to be higher in the first half of the year, so it is possible that the downward trend will be reversed partially in the coming months, though we do not think any return to double digits will be for a sustained period. In month-on-month terms, total inflation was just 0.1 percent, also the smallest since November 2008. There remains little sign of domestically-driven inflation and it is likely that global price trends will play the major role in determining moves in inflation in the Kingdom over 2011.

Wholesale and consumer price inflation



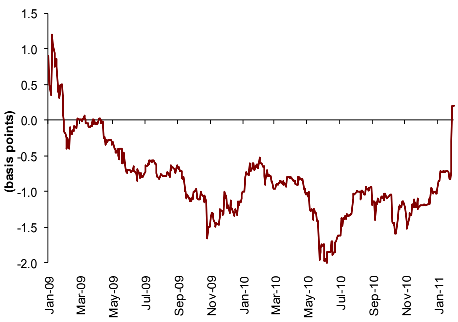
Wholesale price inflation reached its highest level in over two years in the final quarter of 2010, at 5.1 percent. Higher prices of chemicals and fertilizers are the main source of the rise. It is common for trends in wholesale prices to lead those of consumer prices as it takes some time for the costs of raw materials to be reflected in the price of final goods. However, the pass-through process in the Kingdom appears to be much quicker, so wholesale prices move in line with, rather than ahead of, consumer prices. Prospects for wholesale price inflation in 2011 are mixed; food prices have risen so far this year, but prices of raw materials are generally down. Wholesale food price inflation was 6.3 percent in the fourth quarter, compared to consumer food price inflation of 8.1 percent, suggesting that retailers are increasing profit margins.

Cement sales



Cement sales in December were at their highest level since May and 12 percent greater than in December 2009. For the whole of 2010, cement sales were up by 12 percent, less than the growth in 2009, but quicker than that in any of the previous six years. Those companies recording the strongest growth were Saudi Cement, which serves the Eastern Province, Arabian Cement, which operates in the west, and Najran Cement. Stocks of clinker (the raw material for cement) were down slightly from their end-2009 level, but have been on an upward trend since the middle of the year and at the end of the year were 27 percent above their end-June level.

One-year riyal forwards



One-year exchange rate forwards for the riyal against the dollar, which measure what investors expect the exchange rate to be in 12 months, have moved significantly in response to heightened perceptions of risk across the region stemming from the unrest in Egypt. Usually, exchange rate forwards suggest an appreciation of the riyal over the next year, but currently they are indicating a depreciation. This does not indicate any serious expectation of an exchange rate change; instead, foreign investors are using the forwards as a proxy for sovereign risk. We do not expect any serious pressure on the currency peg (the forward rate is currently closer to the actual rate than it has been since April 2009) and certainly do not think that the current move will have any impact on official exchange rate policy.

Key data

	2004	2005	2006	2007	2008	2009	2010E	2011F	2012F
Nominal GDP									
(SR billion)	938.8	1182.5	1335.6	1442.6	1786.1	1397.5	1630.0	1737.4	1864.8
($ billion)	250.3	315.3	356.2	384.7	476.3	372.7	434.7	463.3	497.3
(% change)	16.7	26.0	12.9	8.0	23.8	-21.8	16.6	6.6	7.3
Real GDP (% change)									
Oil	6.7	6.2	-0.8	-3.6	4.2	-7.6	2.1	3.5	4.3
Non-oil private sector	5.3	5.8	6.1	5.5	4.6	2.7	3.7	4.2	4.6
Government	3.1	4.0	3.1	3.0	3.7	5.2	5.9	5.0	5.0
Total	5.3	5.6	3.2	2.0	4.2	0.2	3.8	4.2	4.5
Oil indicators (average)									
WTI ($/b)	41.5	56.6	66.1	72.3	99.7	62.0	79.5	83.0	85.0
Saudi ($/b)	34.7	49.5	60.5	68.1	93.4	60.5	77.7	78.4	80.3
Production (million b/d)	9.0	9.5	9.2	8.7	9.2	8.1	8.2	8.3	8.6
Budgetary indicators (SR billion)									
Government revenue	392	564	674	643	1101	510	735	737	762
Government expenditure	285	346	393	466	520	596	627	658	682
Budget balance	107	218	280	177	581	-87	109	79	80
(% GDP)	11.4	18.4	21.0	12.2	32.5	-6.2	6.7	4.6	4.3
Domestic debt	614	475	366	267	237	225	167	160	160
(% GDP)	65.4	40.2	27.4	18.5	13.3	16.1	10.2	9.2	8.6
Monetary indicators (average)									
Inflation (% change)	0.3	0.7	2.3	4.1	9.9	5.1	5.3	5.3	4.4
SAMA base lending rate (%, year end)	2.50	4.75	5.20	5.50	2.50	2.00	2.00	2.25	2.75
External trade indicators ($ billion)									
Oil export revenues	110.4	161.6	188.2	205.3	281.0	163.1	203.2	204.0	200.3
Total export revenues	125.7	180.4	210.9	233.1	313.4	192.2	236.3	239.7	239.6
Imports	41.1	53.8	63.0	81.5	100.6	86.4	87.0	94.0	103.4
Trade balance	84.6	126.6	147.8	151.6	212.7	105.8	149.3	145.8	136.2
Current account balance	51.9	90.0	98.9	93.3	132.3	22.8	69.6	61.0	50.7
(% GDP)	20.7	28.5	27.8	24.3	27.8	6.1	16.0	13.2	10.2
Official foreign assets	127.9	195.5	273.4	359.8	502.0	474.2	519.9	567.4	607.8
Social and demographic indicators									
Population (million)	22.7	23.4	24.1	24.8	25.5	26.3	27.1	27.9	28.8
Unemployment (male, 15+, %)	11.0	11.5	12.0	11.0	9.8	10.5	10.2	9.8	9.6
GDP per capita ($)	11039	13503	14806	15523	18651	14158	16017	16587	17293

Sources: Jadwa forecasts for 2011 to 2012. Saudi Arabian Monetary Agency for GDP, monetary and external trade indicators. Ministry of Finance for budgetary indicators. Central Department of Statistics and Jadwa estimates for oil, social and demographic indicators.

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