November 2019

Q3 2019 Budget Statement

Non-oil revenue rises in Q3

- Government revenue totaled SR207 billion in Q3 2019, down 7 percent, or SR16 billion, year-on-year. Declines were seen only in oil revenue, whilst non-oil revenue rose by 9 percent.

- Government oil revenue declined by 14 percent, to SR132 billion year-on-year, in Q3, despite a rise by 5.3 percent in the year-to-September, compared with the same period last year.

- Meanwhile, total tax revenue, was up 18 percent on a yearly basis, as Q3 saw an increase in expat dependency fees, which significantly contributed to pushing up non-oil revenue as a whole in Q3.

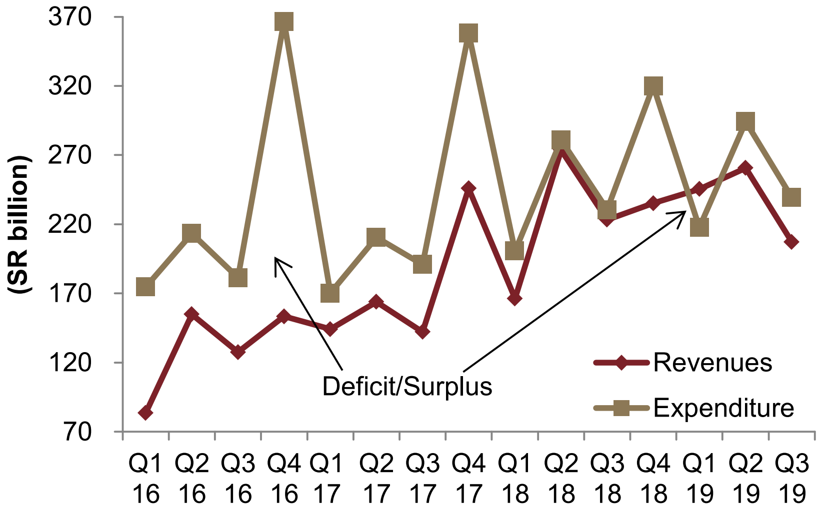
- Looking ahead, due to overall 2019 revenue expected to be lower than originally budgeted, as per the recently released 2020 preliminary budget, and the continued yearly rises in non-oil revenue on the back of higher expat dependency fees, we expect oil revenue to drop sizably in the last quarter of this year.

- Government expenses rose by 4 percent year-on-year in Q3 2019, to a total of SR239 billion, mainly as a result of higher spending on 'Compensation of Employees', which was up 10 percent in Q3 2019, on a year-on-year basis. Meanwhile, capital spending declined by 13 percent year-on-year.

- On the current expenditure side, 'Goods and Services' showed a yearly rise, but 'Subsidies' and 'Social Benefits' were down.

- A fiscal deficit of SR32.2 billion during Q3 (Figure 1), pushed total deficits to SR37.8 billion in the year-to-September. The Ministry of Finance (MoF) recently announced that the fiscal deficit for the whole of 2019 is expected to total SR131 billion, meaning Q4 will see a sizable deficit of SR93 billion.

Figure 1: Fiscal balance moves into deficit in Q3 2019



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Declines were seen only in oil revenue, as non-oil revenue rose by 9 percent during the quarter.

Government oil revenue declined by 14 percent, to SR132 billion year-on-year, despite a rise by 5.3 percent in the year-to-September.

The main driver of non-oil revenue in Q3 was tax revenue, which was up 18 percent on a yearly basis.

<u>Revenue:</u>

Table 1: Government Revenue (SR million)

Revenues	**Q3 2018**	**Q3 2019**	**Change (%)**
Oil revenue	153,950	131,843	-14
Non-oil revenues, of which;	69,312	75,366	9
-Taxes on income, profits and capital gains	3,645	4,822	32
-Taxes on goods and services (including petroleum product charges and harmful product tax)	30,895	37,596	22
-Taxes on trade and transactions (customs duties)	4,444	4,342	-2
-Other Taxes (including Zakat)	3,156	3,130	-1
-Other revenues	27,172	25,475	-6
Total	**223,262**	**207,208**	**-7**

Government revenue totaled SR207 billion in Q3 2019, down 7 percent, or SR16 billion, year-on-year (Table 1). Declines were seen only in oil revenue, as non-oil revenue rose by 9 percent during the quarter. Government **oil revenue** declined by 14 percent, to SR132 billion year-on-year (Figure 2), despite a rise by 5.3 percent in the year-to-September, compared with the same period last year.

The main driver of non-oil revenue in Q3 was tax revenue, which was up 18 percent on a yearly basis. More specifically, the ‘Taxes on Goods and Services’ segment was up by 22 percent, as expat dependency fees rose from SR200 to SR300 per dependent per month from mid-2019 onwards (Figure 3).

Looking ahead, due to overall 2019 revenue expected to be lower than originally budgeted, as per the recently released 2020 preliminary budget, and the continued yearly rises in non-oil revenue on the back of higher expat dependency fees, we expect oil revenue to drop sizably in the last quarter of this year.

Figure 2: Quarterly government oil revenue

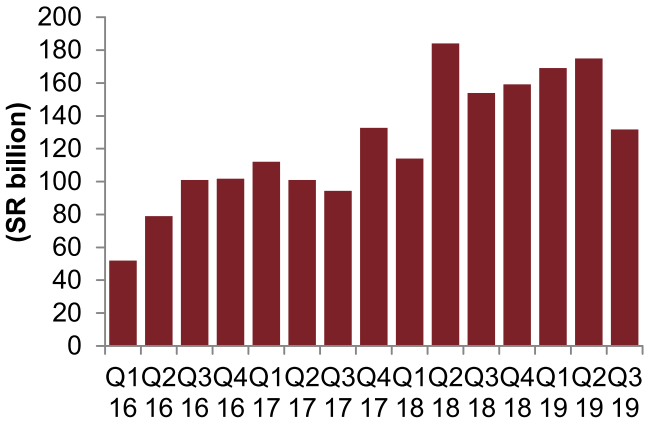
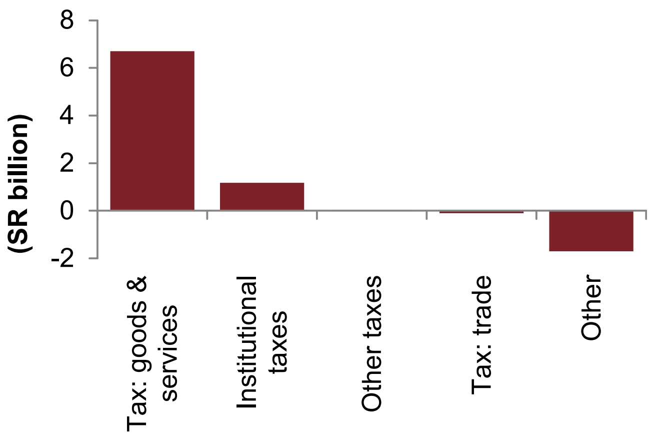


Figure 3: Non-oil revenue in Q3 supported by a rise in ‘Taxes on Goods and Services’



Other taxes = ‘Other Taxes (including Zakat)’
Tax: trade = 'Taxes on trade and transactions (customs duties)’
Institutional taxes = 'Taxes on income, profits and capital gains’
Other = ‘Other revenues (including returns from SAMA and PIF)’

Government expenses rose by 4 percent year-on-year in Q3 2019 to a total of SR239 billion.

On the current expenditure side, the largest component of this segment, 'Compensation of Employees', showed a rise by 10 percent year-on-year.

Capital spending saw a rise of 4.6 percent in the year-to-September, despite a decline by 13 percent in Q3 2019, year-on-year.

Expenditures:

Table 2: Government Expenditure (SR million)

Expenses	Q3 2018	Q3 2019	Change (%)
Compensation of Employees	109,752	121,276	11
Goods & Services	28,580	40,543	42
Financing Expenses	4,557	5,879	29
Subsidies	3,566	2,602	-27
Grants	66	274	>100
Social Benefits	19,387	16,756	-14
Other Expenses	28,380	20,632	-27
Non-Financial Assets (Capital)	36,261	31,415	-13
Total	**230,549**	**239,376**	**4**

Government expenses rose by 4 percent year-on-year in Q3 2019 to a total of SR239 billion (Table 2). **Current expenditure**, the lower economic growth enhancing element of government spending, was up 7 percent on a year-on-year basis as the largest component of this segment, 'Compensation of Employees', also showed a rise by 10 percent year-on-year. Meanwhile, 'Grants', 'Goods and Services' and 'Financing Expenses' showed the largest yearly rises (Figure 5).

The compensation of employees (wage bill) still constitutes a substantial level of total expenditure. In the year-to-September 2019, the wage bill constituted 50 percent of total expenditure and grew by 5.7 percent over the same period last year, making the projected 6 percent year-on-year reduction for the full year difficult to achieve. At the same time, however, combined level of social benefit and subsidies expenditure rose by 8 percent year-on-year till Q3 2019, underlining the government's commitment to improving the quality of life and raising the standard of living for citizens.

As we outlined in our previous [Budget update](), outlays on development projects related to Vision Realization Programs (VRP), would push up capital spending ('Non-Financial Assets-Capital'). In line with this, a rise of 4.6 percent was seen in the year-to-September 2019, despite a decline by 13 percent in Q3 2019, on a

Figure 4: Breakdown in non-oil revenue

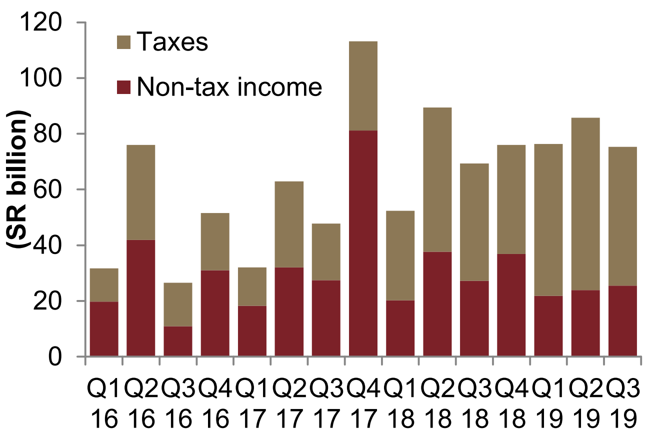
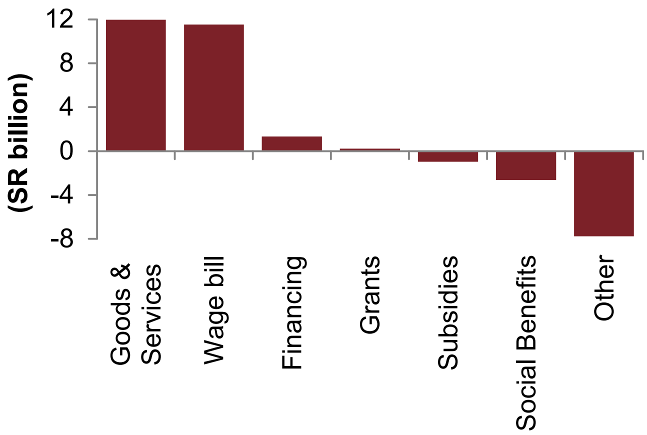


Figure 5: Year-on-year change in Q3 2019 current expenditure



year-on-year basis. We see this elevated level of capital spending as having directly contributed to lifting non-oil economic activity within the Kingdom. As Q2 2019 GDP data showed, non-oil private sector GDP was up 3.4 percent year-on-year, whilst our non-oil private sector composite index shows that economic activity has remained at elevated levels during Q3 2019 (Figure 6).

Capital spending related to the PIF and the NDF are also likely have contributed to lifting economic activity.

That said, it is important to highlight that capital spending related to the Public Investment Fund (PIF) and the National Development Fund (NDF), which are not funded through the central government budget, are also likely have contributed to lifting economic activity. So, for instance, the PIF spent SR32 billion in the domestic economy between 2018 and Q1 2019, and we expect the level of expenditure to have accelerated since then as progress continues on various mega-projects.

Public Debt:

The government had issued a total SR96 billion in bonds/sukuks in the year-to-September.

According to the Debt Management Office's 2019 borrowing plan, net debt issuance will total SR118 billion, (plus SR2 billion in refinancing) with a split of 55 percent in domestic debt and 45 percent in international debt. As the Q3 budget performance report showed, the government had issued a total SR96 billion in bonds/sukuks in the year-to-September. Since then, the MoF announced the issuance of $2.5 billion international sukuk (SR9 billion), as well as a domestic sukuk issuance totaling SR7.3 billion. As a result, the Kingdom's year-to-date debt issuance stands at SR115 billion, with a domestic/international split of 56/44 percent. Looking ahead, on the domestic side, we expect an additional SR4 billion in issuances, with any issuances above the planned SR118 billion for the remaining months of 2019 coming from domestic rather international issuances.

Deficit:

Total deficits was SR37.8 billion in the year-to-September.

A fiscal deficit of SR32.2 billion during Q3 pushed total deficits to SR37.8 billion in the year-to-September. The MoF recently announced that the fiscal deficit for the whole of 2019 is expected to total SR131 billion, meaning Q4 will see a sizable deficit of SR93 billion (Figure 7).

Figure 6: Jadwa's non-oil private sector composite index shows a pick-up in activity

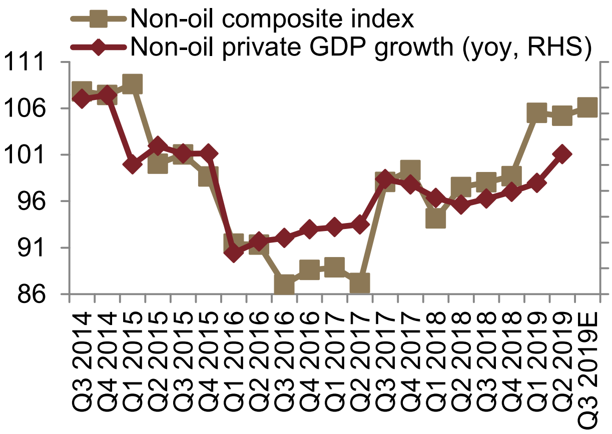
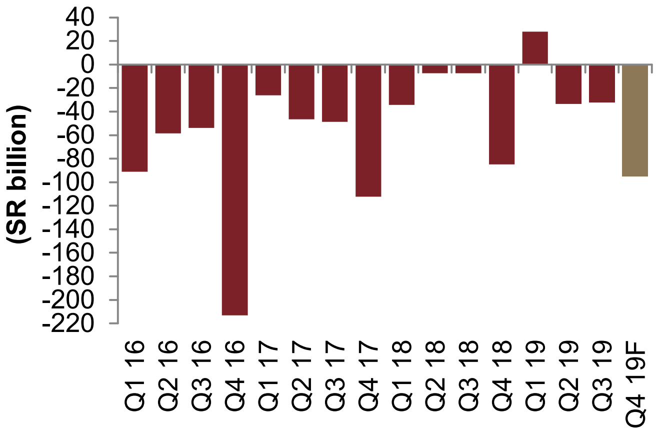


Figure 7: We expect to see a sizable deficit in Q4



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