Saudi Arabia budget report 2022

Review of the 2022 budget in the context of recent economic developments

December 2021

KPMG in Saudi Arabia

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Foreword

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As 2021 concludes, the global economy has been through another year of challenges, including affected supply chains, inflationary pressures, and new Covid-19 variants that have continued to threaten economic recovery. In Saudi Arabia, an effective vaccine rollout and other containment measures have allowed the economy to open, while higher international oil prices have supported a broader recovery.

I am pleased to present the annual KPMG budget report for Saudi Arabia, providing our view on the government's announced expenditures and revenues. The presented figures are based on the Ministry of Finance's (MoF) Budget Statement for FY 2022, as approved by the government on 12 December 2021, with our views supported by internal analysis and other sources.

As per the MoF, real GDP growth is estimated to expand by 2.9% in fiscal year 2021, supported largely by a broad pick-up in non-oil economic activity. Most components of non-oil GDP have continued to expand amid an easing of domestic pandemic-related containment measures and as consumer and business confidence have rebounded, owing to the aforementioned high international oil prices.

The continuation of the recovery in the domestic non-oil sector, combined with an expected increase in domestic oil production, should support robust real GDP growth in 2022. Such a broad-based pick-up in the non-oil sector should support tax receipts, most notably value added tax (VAT), and other non-oil revenues. A recovery in oil production will, in turn, benefit the oil sector even as oil prices remain elevated – this will support oil-related public sector revenues. These revenues, combined with fiscal prudence, are consistent with the fiscal sustainability program and will improve public finances.

Economic stability and expansion are also expected to be supported by conducive government policies, including Vision 2030 as the central agenda for economic diversification. The 2022 budget indicates economic recovery as the key pillar underpinning the improving fiscal outlook. The economic expansion should also help to support the budget position and debt levels as a proportion of GDP.

"The continuation of the broad-based recovery in the domestic non-oil sector, combined with an expected increase in domestic oil production, should support robust real GDP growth in 2022."

Planned expenditure for fiscal year 2022 stands at SAR955 billion, with a continued focus on promoting economic growth, improving spending efficiency and generating employment. The government also remains committed to spending on education, healthcare and social development, again as part of its mission to fulfil Vision 2030 objectives of promoting a better quality of life and a diversified economy.

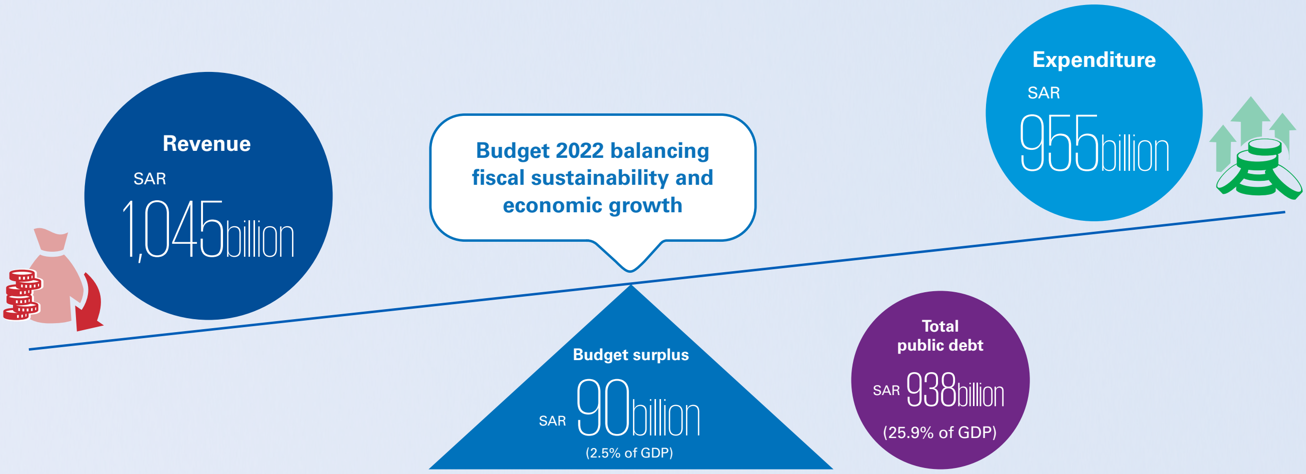
Total public revenues are forecast to reach SAR1,045 billion in 2022, on the back of the domestic economic recovery and higher oil prices. Tax revenues are expected to represent 27% of total revenues in 2022. The budget surplus in 2022 is expected to be SAR90 billion: the surplus of 2.5% of GDP is substantially better than than the 2.7% budget deficit in 2021. It is expected that public debt will stand at SAR938 billion in 2022, or 25.9% of GDP.

As the public balance sheet is currently reaping the benefits of high oil prices, any sudden change in the energy outlook could weaken this positive view. The energy outlook remains the largest challenge in the risk landscape, along with (related) uncertainty around new Covid-19 variants impacting the global economy and supply chains.

I hope you find our analysis and insights relevant for your business or organization, and our team is ready is respond to any inquiries you may have.

Budget summary

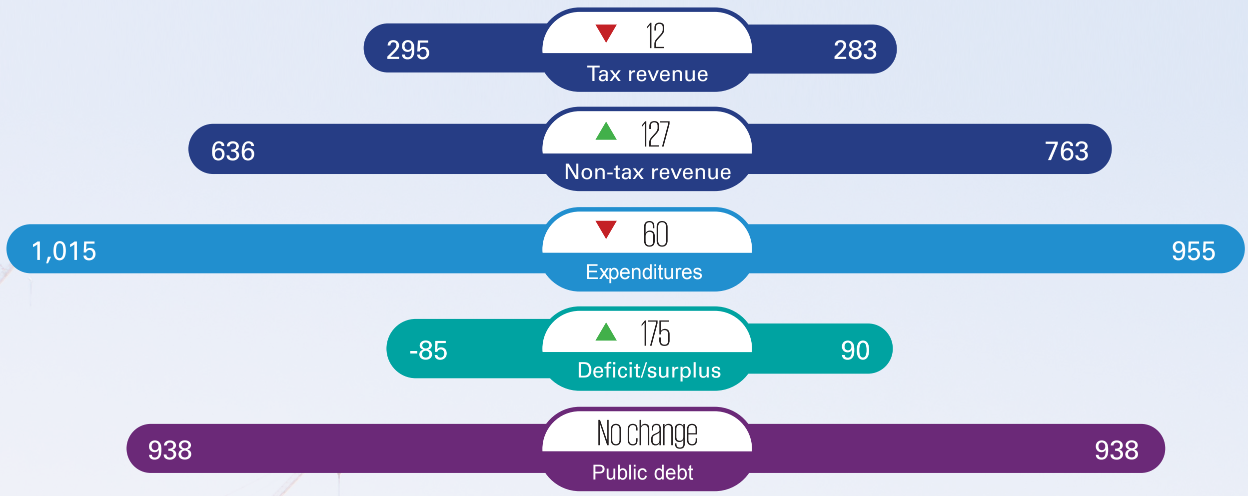
Budget 2022



Source: **MoF, Budget Statement 2022**

Changes in budget 2021-2022

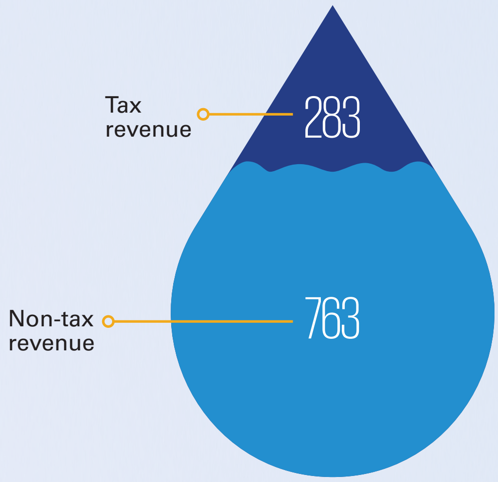
Estimated in 2021E (SAR billion) | Budgeted in 2022B (SAR billion)



Source: **MoF, Budget Statement 2022**

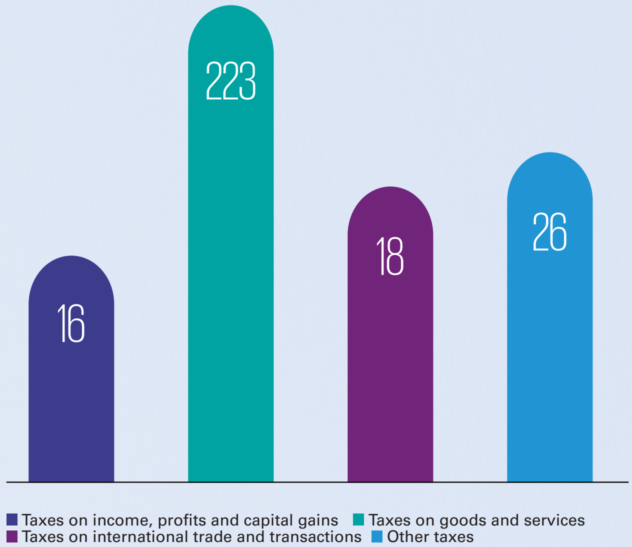
Total revenues 2022

Total revenue, SAR1,045 billion



Source: **MoF, Budget Statement 2022**

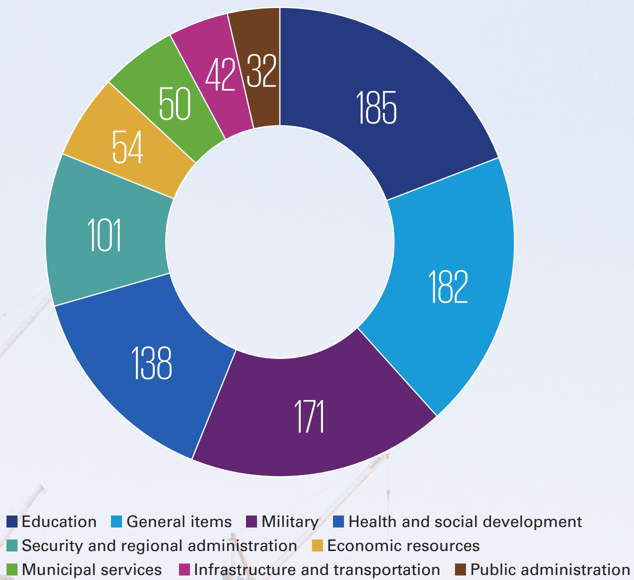
Tax revenue, SAR283 billion



Source: **MoF, Budget Statement 2022**

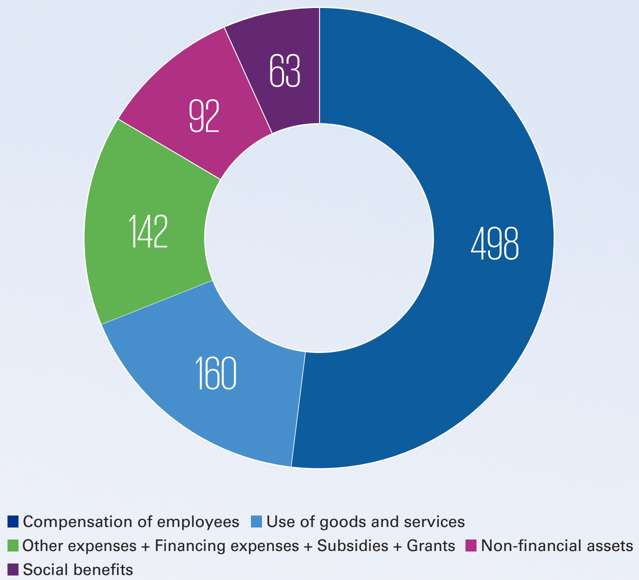
Total expenditures 2022

Expenditure by sectors, SAR955 billion



Source: **MoF, Budget Statement 2022**

Expenditure by components, SAR955 billion



Source: **MoF, Budget Statement 2022**

Key takeaways

Government finances are benefitting from significant tailwinds

Accelerating and broad-based domestic economic growth, combined with robust international oil demand, will boost the public finances. This will be through increasing revenues, reduced need for stimulus spending and as an expanding economy supports a range of indicators measured as a proportion of GDP.

Improving public sector finance metrics

Projections of a budget surplus in 2022 reflect a combination of improving revenues and the government's commitment to fiscal sustainability. The budget statement highlights efforts to contain public spending and the use of conservative assumptions in relation to expected government income.

Encouraging private sector development and investment

As part of Vision 2030 objectives that include the expansion of the private sector's role in the economy, the authorities will continue to pursue policies that encourage private investment and reforms designed to improve the business environment, while anticipating an active role from the National Development Fund (NDF) and its subsidiaries.

Priority spending categories remain unchanged

Healthcare and social development, Defense, Education and Infrastructure and transportation remain among the largest categories of public expenditure, reflecting long-standing trends and the fact these spending items are central to supporting a number of Vision 2030 initiatives.

Covid-19 mutations and rising policy rates remain key risks in creating new economic shocks

Global concerns over the spread of the Omicron-variant highlight the risks that mutations could negate the efficacy of Covid-19 vaccines and treatments, a scenario that could result in renewed business disruptions, even as rising global price pressures raise the specter of major central banks increasing policy rates sharply – both scenarios leave open the possibility of renewed global economic shocks.

Economic growth assumptions

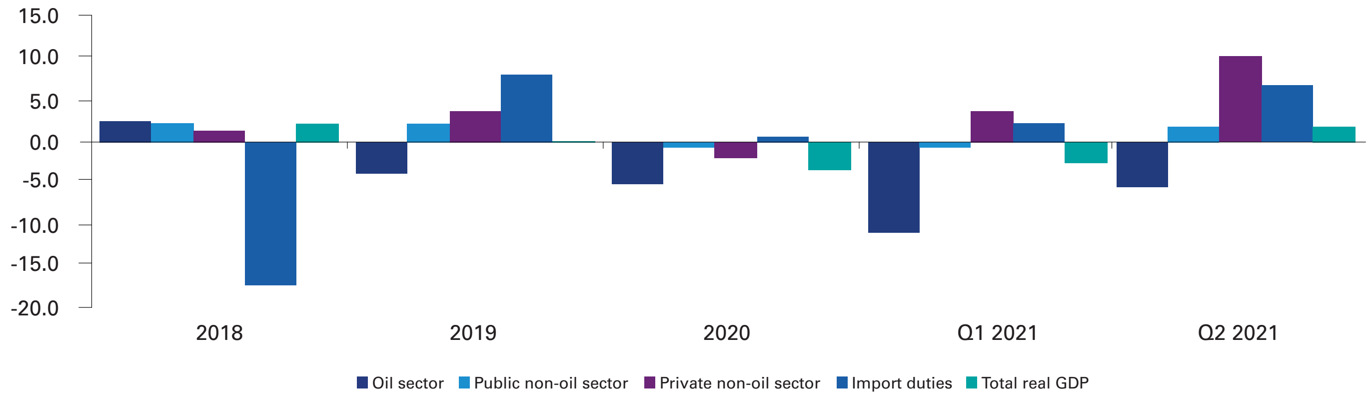
According to the MoF, real GDP growth is estimated to expand by 2.9% year-on-year (YoY) in fiscal year 2021, supported largely by a broad-based pick-up in non-oil economic activity. Most components of non-oil GDP have continued to expand amid an easing of domestic pandemic-related containment measures and as consumer and business confidence have been boosted by high international oil prices.

International oil prices have remained buoyant during much of 2021 as the OPEC+ plus agreements and a pick-up in global economic activity have improved the supply-demand balance in favor of oil producers. According to the Energy Information Administration (EIA), oil demand is estimated at an average of 96.9 million barrels per day (mb/d) in 2021, 5.1 million mb/d higher than in in 2020.[1] The EIA expects oil demand to rise to an average of 100.5 mb/d in 2022, with prices remaining buoyant even as OPEC+ production constraints are eased. Indeed, according to the International Monetary Fund's (IMF) October 2021 World Economic Outlook, oil prices are expected to average an elevated US$64.52 pb in 2022, compared with an annual average of US$65.68 pb in 2021.[2]

A number of government policies will bolster domestic economic stability and expansion next year. The Saudi Central Bank (SAMA) will continue to provide broad liquidity funding as well as specific support policies, such as the guaranteed financing program that is designed to contribute to funding stability for small- and medium-sized enterprises (SMEs).

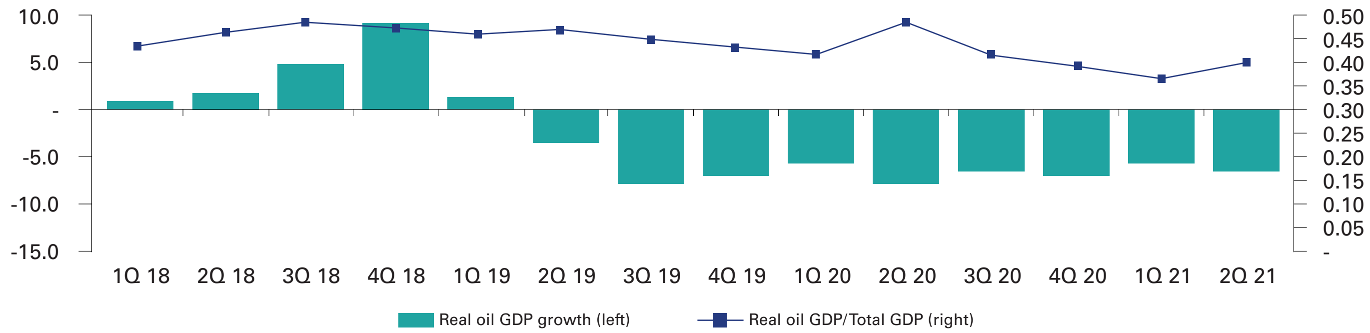
The ongoing implementation of Vision 2030 initiatives, mega projects and domestic spending by the Public Investment Fund (PIF) will boost investment and combine with higher oil production to support a broad-based recovery in the domestic non-oil sector (given the oil sector's role in impacting confidence and money flows into the broader economy). On balance, these trends are the main drivers behind the MoF's expectations that real GDP will accelerate to 7.4% in 2022.

Figure 1: **Real GDP growth breakdown (% change YoY)**



Source: **General Authority for Statistics (GaStat)**

Figure 2: **Real oil GDP growth and oil sector contribution to GDP**



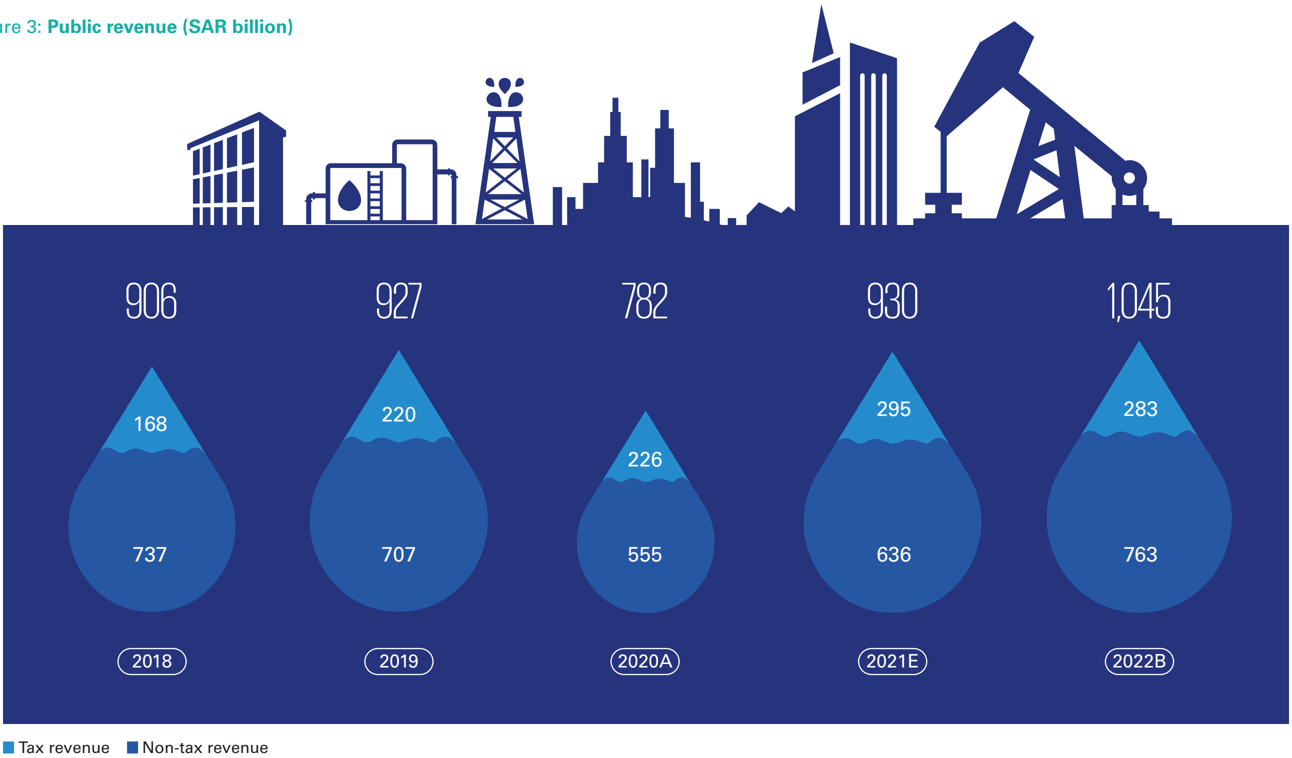
Source: **GaStat**

Budget 2022

Budget

The cabinet approved the budget for fiscal year 2022 on 12 December 2021. Saudi Arabia's government enters 2022 benefiting from economic tailwinds centered on an ongoing recovery in domestic non-oil GDP, high international oil prices and expectations of a rise in domestic oil production, reflecting an easing of OPEC+ oil production limits. These factors will together support both public non-oil and oil revenues. The government's commitment to containing spending even as the need for fiscal stimulus falls – containment measures related to Covid-19 in either Saudi Arabia or its main trading partners are not expected to return to the levels seen in 2020 – will help to limit public expenditure.

Figure 3: **Public revenue (SAR billion)**



Source: **MoF, Budget Statement 2022**

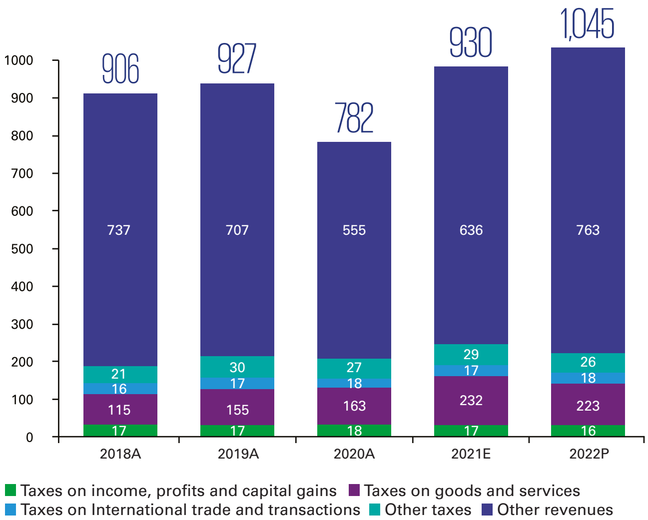
Revenues

The 2022 fiscal year budget statement indicates that the domestic economic recovery and rising international oil prices are estimated to have increased total revenues in fiscal year 2021 to SAR930 billion, 9.5% higher than was forecast in the original 2021 fiscal year budget statement and 18.9% higher than the 2020 outcome (see figure 3).

Two factors have largely driven the estimated revenue increase in 2021. First, higher international oil prices resulted in the oil component of public revenues rising by 35.2% YoY, to SAR558 billion, representing 60% of total revenue in 2021, compared with 52.8% of the total in 2020. Second, ongoing government efforts to diversify public revenues away from oil combined with a pick-up in economic activity have provided further support. In particular, an increase in the VAT rate of 10 percentage points to 15% in July 2020 supported revenues from this consumption-based tax rising by 41.8% YoY in 2021.

Total revenues are expected to stand at SAR1,045 billion in 2022 (see figure 4). Revenue support will reflect several trends that center on high international oil prices, rising oil production and accelerating domestic economic growth – the latter supporting consumption-linked and corporate tax revenues. High international oil prices and production will result in oil revenues remaining a key source of government income next year, although the authorities' efforts to diversify income sources are likely to gradually reduce the current reliance on hydrocarbon receipts over the coming years.

Figure 4: **Revenue components (SAR billion)**



Source: **MoF, Budget Statement 2022**

Expenditures

Actual government spending in fiscal year 2021 is estimated at SAR1,015 billion, compared with originally planned spending of SAR990 billion (see figure 5). The overshoot reflects in part pandemic-related spending such as overtime compensation for healthcare workers and the related implementation of the country's Covid-19 vaccination program. Other areas where actual spending in 2021 is estimated to be above planned spending include Use of goods and services and capital expenditure (CAPEX).

The estimated expenditure in 2021 was nevertheless lower than the actual outturn recorded in 2020, when total spending stood at SAR1,076 billion. CAPEX has led the decline – this component fell by an estimated 27.7% YoY in 2021, reflecting factors that include the completion of a wide range of infrastructure projects and the government's success in enhancing the role of the private sector and development funds in financing CAPEX. Of the three largest spending components on a sector basis – Defense, Education and Healthcare and social development – only the latter saw an increase in 2021, rising by a marginal 0.2% YoY. Health and social development would have supported the implementation of policies relating to offsetting the negative impacts of the pandemic and related containment measures.

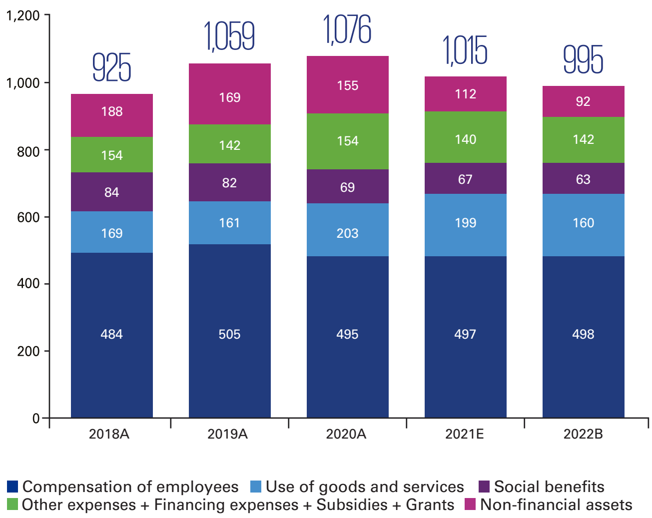
Planned total expenditure in 2022 is set to fall to SAR955 billion, which is down 5.9% versus the estimated figure for 2021. According to the MoF, the main drivers of this decline will be reduced spending on Use of goods and services – reflecting a reduced need for special spending as a result of the pandemic and as the government continues to pursue policies designed to improve spending efficiency – and CAPEX.

The government will maintain its spending commitments in relation to Vision 2030 goals, for example on mega projects and vision realization programs that encompass the creation of residential cities and tourism destinations, housing development and broader infrastructure investment. However, public spending will be curtailed for the reasons witnessed in 2021. Several existing capital projects have been concluded. At the same time, financing via the private sector, NDF and PIF are reducing pressure on public spending requirements in this category. The net result of these CAPEX trends is that this category of spending will reduce from an estimated SAR112 billion in 2021 to a planned SAR92 billion in 2022.

Budget deficit and public debt

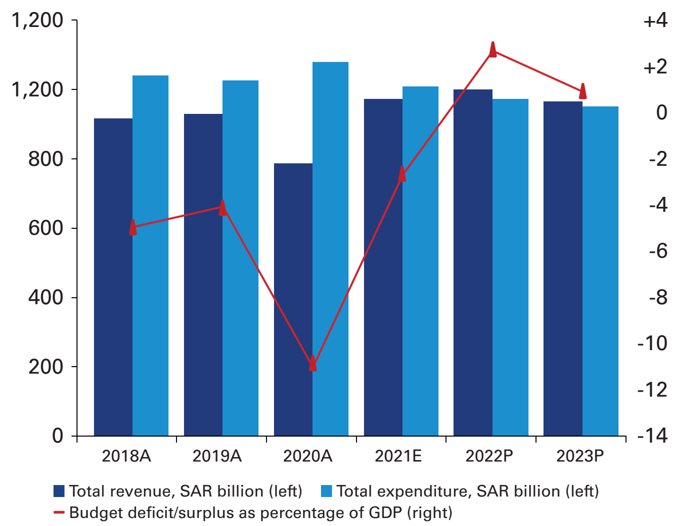
Relative to the 2020 fiscal year, the budget deficit estimate for 2021 indicates a marked improvement in both nominal terms and as a percentage of GDP, a positive trend that is being driven by a rapid expansion in revenues and the denominator (the latter reflecting the ongoing economic recovery following the economic contraction witnessed in 2020). The budget deficit decreased from SAR294 billion in 2020 (11.2% of GDP) to an estimated SAR85 billion in 2021 (2.7% of GDP) – the 2021 budget statement had envisaged a deficit of SAR141 billion, equivalent to 4.9% of GDP (see figure 6).

Figure 5: **Expenditure components (SAR billion)**



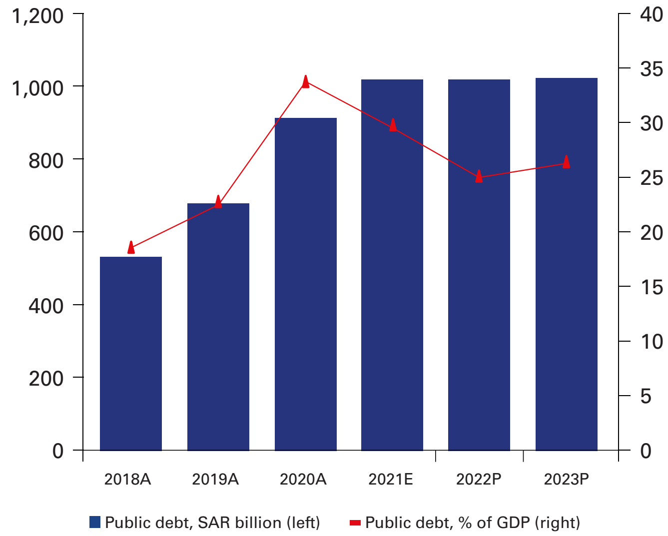
Source: **MoF, Budget Statement 2022**

Figure 6: **Fiscal position**



Source: **MoF, Budget Statement 2022**

Figure 7: **Public debt**



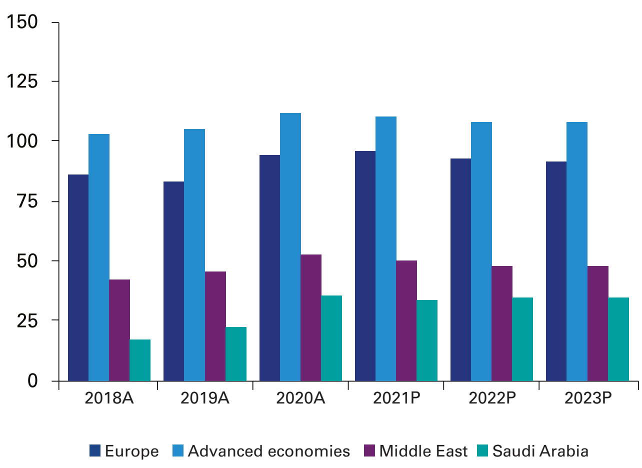
Source: **MoF, Budget Statement 2022**

A continued recovery in revenues, expenditure containment efforts and a rise in nominal GDP will combine to shift the 2022 budget into a surplus of SAR90 billion (2.5% of GDP). Although downside risks remain, the government's commitment to fiscal sustainability through Vision 2030's Fiscal Sustainability Program that includes, for example, the adoption of conservative assumptions in relation to future oil prices, should limit deviations between forecasts contained in the budget statement and final outcomes.

A narrowing budget deficit and nominal GDP expansion helped to reduce the public debt stock to GDP ratio from 32.5% in 2020 to an estimated 29.2% in 2021 (see figure 7). This estimate is in sharp contrast to the 32.7% public debt to GDP ratio envisaged in the original budget statement for 2021, although we note that in nominal terms the public debt stock rose from SAR854 billion to an estimated SAR938 billion over the same period. This reflects the fact that, despite narrowing, the budget remained in deficit as government expenditure was greater than government income.

In 2022, the expected budget surplus combined with robust, and related, economic growth will help to drive a substantial drop in the public debt to GDP ratio, to 25.9%. The expected stability of the public debt stock in nominal terms next year – it is expected to remain unchanged, at around SAR938 billion – reflects largely the government's intention to divert the income from the budget surplus to its reserves, as well to supporting development funds. The expected rate of improvement in Saudi Arabia's public debt metrics is in sharp contrast to many of its peers. Indeed, we note that the country's public debt-to-GDP ratio has traditionally remained significantly lower than that of these peers, a position that we expect to remain unchanged, on current trends (see figure 8).

Figure 8: **Public debt as percentage of GDP**



Source: **IMF**

Expenditure by sector

Healthcare and social development, Defense, Education, and Infrastructure and transportation remain among the largest categories of public expenditure, reflecting long-standing trends and the fact these spending items are central to supporting a number of Vision 2030 initiatives.

Education

Education spending reduced from SAR205 billion in 2020 to an estimated SAR191 billion in 2021, representing a 6.8% YoY decline. We note that the 2021 estimate is SAR5 billion higher than was originally set out in the 2021 budget statement. In 2020 and 2021, Covid-19 increased requirements for investment in online infrastructure. Conversely, the completion of such investment and a return to classroom-based learning will enable the government to contain Education expenditure at SAR185 billion in 2022, even as it resumes spending in line with longer term planning that is aligned with Vision 2030 goals. The focus will as a result move towards expanding apprenticeship programs and enhancing research capabilities in higher education, initiatives that are designed to boost the inclusivity of women, employability of the workforce, and the broader agenda of enhancing the value-added potential of the domestic economy. That also includes investments in pre-schooling as part of Vision 2030's Human Capital Development Program.

Healthcare and social development

Spending on Healthcare and social development is estimated at SAR191 billion in 2021, up a modest 0.2% YoY but significantly higher than the planned spending of SAR175 billion announced in the 2021 budget statement. The deviation from planned spending reflects in part the impact of the Covid-19 outbreak on demand for testing, vaccines and treatments. Moreover, the government maintained its spending commitments on non-pandemic related activities, for example, the inauguration of hospitals designed to expand and upgrade access to healthcare. As the pandemic eases into 2022, the authorities' focus will shift away from the pandemic to long-standing reform efforts that have been delayed by the outbreak. The budget for Healthcare and social development in 2022 is set to decrease by 27.6% to SAR138 billion in line with expectations that Covid-19-related spending will fall. Key objectives in 2022 include the expansion of centers providing a comprehensive range of specialist medical services across the country and the provision of training opportunities to enhance the country's human resources capabilities more generally.

Infrastructure and transportation

CAPEX in 2021 is estimated to fall by 27.7% YoY, to SAR112 billion, owing to the completion of a range of projects that include infrastructure development for industrial cities and the construction of roads and networks. Pressure on the public finances has been further eased by increased infrastructure spending by the private sector and development funds. These drivers have resulted in estimated spending on the Infrastructure and transportation sector declining by 19.9%, to SAR48 billion. CAPEX is projected to decline by a further 18.2% YoY in 2022 (versus 2021 estimates) to SAR92 billion, again as several large-scale public sector projects wind down and as alternative funding sources, including from the private sector and development funds, reduce pressure on the need for public infrastructure spending. Nevertheless, public CAPEX will continue to support development that includes transportation, housing and communications, as well as a range of projects designed to support the Vision 2030 agenda.

Defense

The estimate for Defense spending indicates a reduction from SAR204 billion in 2020 to SAR190 billion in 2021, and is expected to reduce further, to SAR171 billion, in 2022. The government is continuing on the path of long-term defense spending plans, focusing on renovation of capability in relation to equipment and enabling functions. These trends are primarily being driven by relevant national level strategies and capability priorities. There is more focus on alignment to ensure that defense spending achieves an appropriate balance between capability building and sustainability. That includes a central focus on capacity-building of service personnel, the workforce and the local supply chain, and for this to be achieved in a way that ties in the broader defense and security entities effectively. There are increasing examples that demonstrate large new capability decisions are being specifically targeted to expand the local defense industry, including encouraging new entrants – both local companies, and international original equipment manufacturers (OEMs) – to invest in the Saudi market for the long-term.

Risks and challenges

Covid-19 mutations lead to further lockdowns in Saudi Arabia's key trading partners

The optimistic outlook for Saudi Arabia's public finances rests in part on a continued economic recovery in the country's main trading partners, given that economic activity is a key driver of international oil demand, and thus oil prices.. While the rapid vaccination rollouts seen across major emerging and advanced economies have resulted in immunity rising to levels that suggest there will not be a repeat of the types of lockdowns witnessed at the height of the pandemic, the Omicron variant highlights ongoing concerns that mutant strains of Covid-19 could undermine the efficacy of vaccines and existing therapies. In such a scenario, assumptions that economic conditions will continue to normalize in a sustained manner would have to be adjusted, with the corresponding uncertainty undermining consumer and business confidence and posing risks of further economic shocks that would undermine oil consumption.

Tightening of monetary policy brings an increase in the severity and frequency of economic shocks

Covid-19 and related supply chain disruptions have been pivotal in increasing inflationary pressures across the world during 2021. Upward price pressures combined with the uncertainty caused by the path of the Covid-19 pandemic – a key factor in determining the extent of the current global economic recovery – have transmitted volatility into global capital markets. Such volatility reflects the fact that uncertainty over the path of inflation is in turn complicating policy-making and brings with it risks that monetary policy tightening could be mistimed. A policy failure, whether because of monetary tightening coming too late or too early, could transmit shocks into emerging markets in various way, including exchange rate weakness and rising interest payments on both private and public sector external debt. In a scenario of high inflation and/or a rapid tightening of monetary policy by major central banks, global economic growth and related import demand, including for oil, would be curtailed.

For more economic insights, addressing the risks and challenges on a global scale, see our latest edition of the **Global Economic Outlook**.

Economic indicators

Key indicators	2017A	2018A	2019A	2020A	2021E	2022P
Economic output						
Nominal GDP (SAR billion)	2,582	2,949	2,974	2,625	3,207	3,615
Nominal GDP (% change YoY)	6.7	14.2	0.8	-11.7	22.2	12.7
Real GDP (% change YoY)	-0.7	2.4	0.3	-4.1	2.9	7.4
Budget						
SAR billion						
Total revenue	692	906	927	782	930	1,045
Oil revenue	436	611	594	413	558	-
Non-oil revenue	256	294	332	369	372	-
Expenditure	930	1,079	1,059	1,076	1,015	955
Budget balance	-238	-173	-133	-294	-85	90
Gross public debt	443	560	678	854	938	938
% of GDP						
Total revenue	26.8	30.7	31.2	29.8	29.0	28.9
Oil revenue	16.9	20.7	20.0	15.7	17.4	-
Non-oil revenue	9.9	10.0	11.2	14.1	11.6	-
Expenditure	36.0	36.6	35.6	41.0	31.6	26.4
Budget balance	-9.2	-5.9	-4.5	-11.2	-2.7	2.5
Gross public debt	17.2	19.0	22.8	32.5	29.2	25.9
Trade and external sector						
Export (SAR billion)	832	1,104	981	652	935	956
of which oil exports	796	868	752	448	693	715
Current account balance (SAR billion)	29	271	143	-73	121	126
Current account balance (% of GDP)	1.5	9.2	4.8	-2.8	3.8	3.5

A | Actual **E** | Estimated **P** | Projected **-** | N/A

Source: IMF, MoF

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[1]https://www.eia.gov/outlooks/steo/
[2]https://www.imf.org/en/Publications/WEO/Issues/2021/10/12/world-economic-outlook-october-2021

Disclaimer: figures are rounded up to the nearest billion throughout the report. Some figures may not add up to 100 percent due to rounding.