Saudi Arabia budget report 2023

Review of the 2023 budget in the context of recent economic developments

December 2022
KPMG Professional Services

Content

Foreword

The global economy in 2022 has been facing several headwinds centered on high inflation that has seen major central banks pursue aggressive monetary policy tightening. Amid this growing external instability, Saudi Arabia's domestic economy showed resilience, with high international oil prices supporting an economic recovery across both the oil and non-oil sectors.

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 2023, as approved by the government on 7 December 2022, with our views supported by internal analysis and other sources.

As per the MoF, real GDP growth is estimated to expand by a robust 8.5% in fiscal year 2022, supported largely by a sharp rise in oil production as well as an uptick in non-oil economic activity. Most components of non-oil GDP have continued to expand amid a rebound in consumer and business confidence, supported by the aforementioned high international oil prices and oil production.

Growth in the domestic non-oil sector and still high oil income should support robust real GDP growth in 2023. A broad-based pick-up in the non-oil sector should support tax receipts, including through value added tax (VAT) as consumer spending remains healthy, and as healthy corporate profits are expected to translate into higher government revenues. These revenues, combined with fiscal prudence, are consistent with the government's fiscal sustainability program and will improve public finance metrics – Saudi Arabia's public debt stock is significantly lower than that of its advanced economy peers, for example.

Longer-term economic stability is also expected to be supported by conducive government policies, including Vision 2030 as the central agenda for economic diversification. Nevertheless, the 2023 budget indicates that the ongoing cyclical economic recovery remains a key pillar underpinning a short-term strengthening of the public balance sheet.

“A broad-based recovery in the domestic non-oil sector, alongside high international oil prices, will result in healthy real GDP growth in 2023.

Planned expenditure for fiscal year 2023 stands at SAR1,114 billion, with a continued focus on promoting economic growth and improving spending efficiency. The government also remains committed to spending on education, healthcare and social development. Reflecting its focus on Vision 2030 objectives; these spending components remain important in supporting objectives such as a better quality of life and a diversified economy.

Total public revenues are forecast to reach SAR1,130 billion in 2023, remaining high amid a healthy domestic economic expansion while also remaining high international energy prices. Tax revenues are expected to represent 28.5% of total revenues in 2023. The budget surplus in 2023 is expected to be SAR16 billion, equivalent to a surplus of 0.4% of GDP. It is expected that the public debt stock will stand at SAR951 billion in 2023, or 24.6% of GDP.

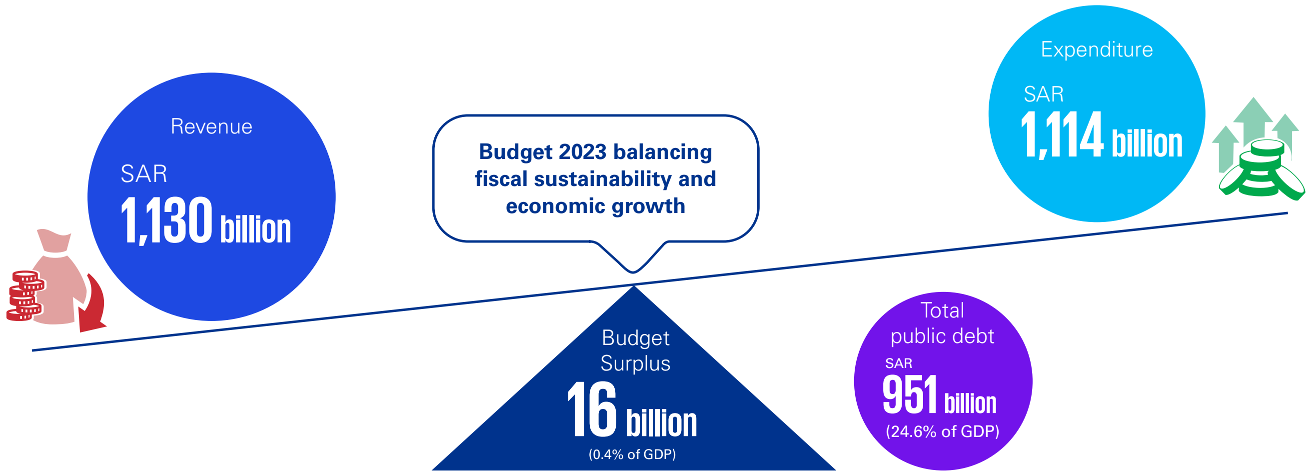
High energy prices are positive for both Saudi Arabia's sovereign balance sheet and the broader domestic economy. Conversely, any sudden change in the energy markets could weaken this outlook. Despite growing risks abroad, the government's balance sheet provides a cushion against external economic shocks.

Dr. Abdullah Hamad Al Fozan

Chairman & CEO
KPMG Professional Services

Budget summary

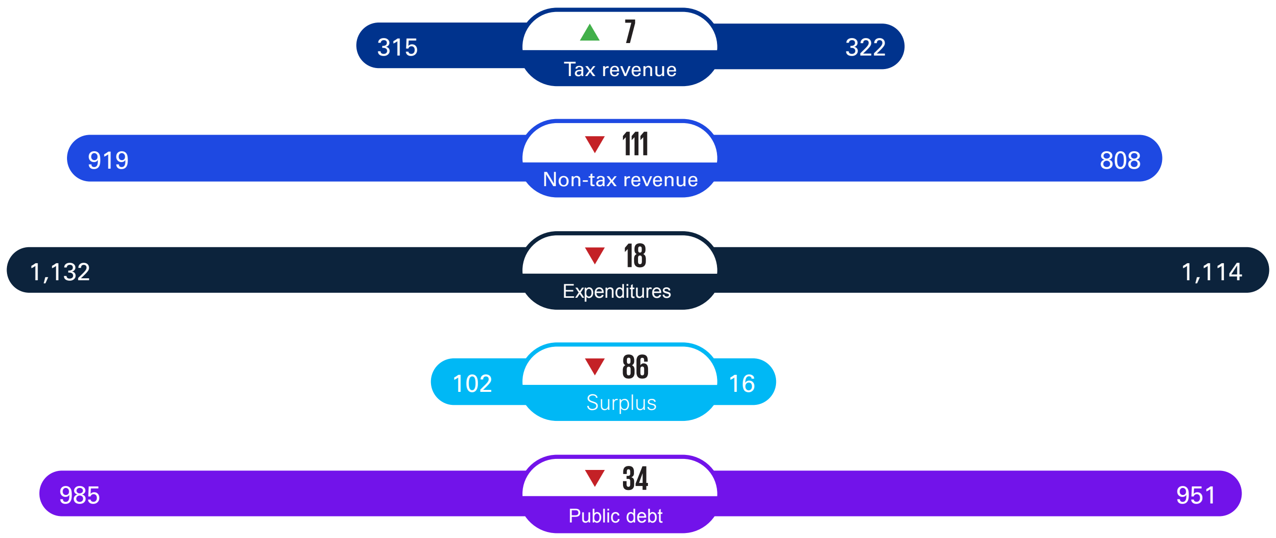
Budget 2023



Source: MoF, Budget Statement 2022

Changes in budget 2022-2023

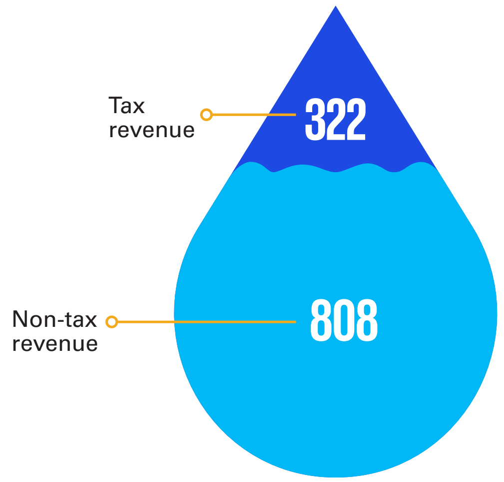
Estimated in 2022E (SAR billion) **Budgeted in 2023P (SAR billion)**



Source: MoF, Budget Statement 2023

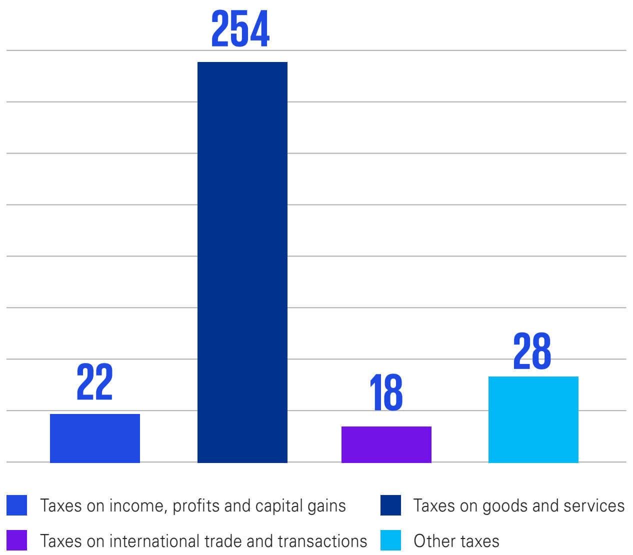
Total revenues 2023

Total revenue, SAR1,130 billion



Source: MoF, Budget Statement 2023

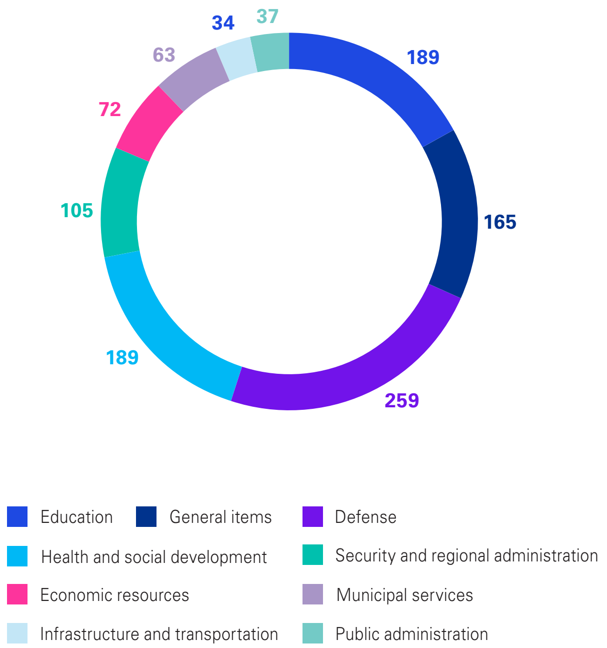
Tax revenue, SAR322 billion



Source: MoF, Budget Statement 2023

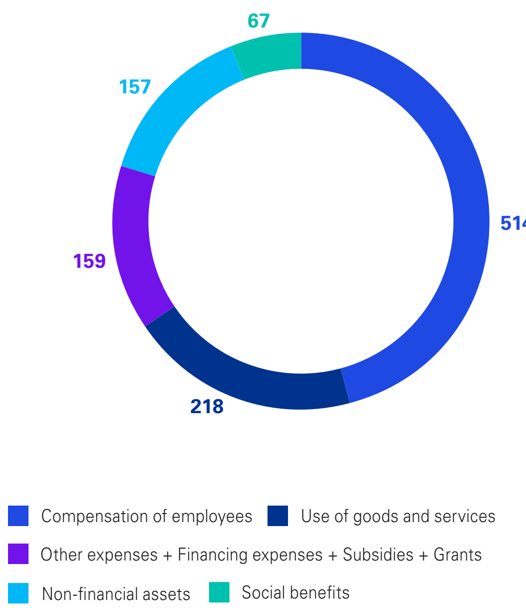
Total expenditures 2023

Expenditure by sectors, SAR1,114 billion



Source: MoF, Budget Statement 2023

Expenditure by components, SAR1,114 billion



Source: MoF, Budget Statement 2023

Key takeaways

Public finances are continuing to improve
Healthy domestic economic growth will support the public finances, as a combination of oil prices that are still high and an expansion in non-oil activity maintain a high level of revenues. At the same time, the authorities will contain spending at close to 2022 levels, in 2023.

Improving public sector balance sheet metrics
High public income levels and the government's commitment to fiscal sustainability will support confidence in Saudi Arabia's public finances. The 2023 budget statement once again involved the use of conservative assumptions in relation to expected government revenues.

Main spending components remain unchanged
Healthcare and Social Development, Defense, Education, and Infrastructure and Transportation are among the largest categories of public spending, reflecting long-term government commitments alongside the importance of these categories in supporting Vision 2030 initiatives.

High global inflation and related increases in policy interest rates have increased the risk of economic shocks
Rising global price pressures during 2022 have seen major central banks raising policy rates that have increased the risks of recession in Saudi Arabia's main trading partners. The potential for renewed economic shocks has therefore increased, with the specific risk for Saudi Arabia's global economic growth being slower, which reduces demand for oil (that would in turn undermine international oil prices and the government's oil income).

Supporting private sector investment
Government support for initiatives related to its Vision 2030 agenda will continue. The authorities will maintain a focus on spending that encourages an expansion in the private sector's role in the economy, including private investment that supports both product and regional development. The role of public development funds in nurturing the private sector will remain a key pillar of the government's Vision 2030 plans.

Economic growth assumptions

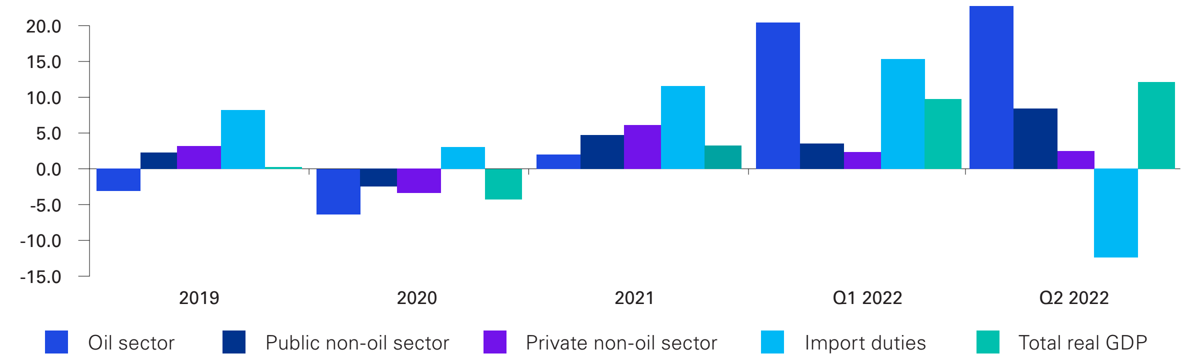
According to the Ministry of Finance, real GDP growth is estimated to grow by a robust annual average of 8.5% year-on-year (YoY) in fiscal year 2022, supported by a pick-up in both the oil and non-oil sectors. Non-oil GDP is being supported in particular by wholesale and retail trade, and restaurants and hotels components amid a reversal of pandemic-related restrictions. High international oil prices and domestic oil production have been supporting consumer and investor confidence more generally.

International oil prices have remained resilient during much of 2022 as a continued recovery in overseas economic activity, OPEC+ agreements and global supply disruptions have combined to improve the supply-demand balance in favour of Middle Eastern oil producers, in particular. According to the Energy Information Administration (EIA), oil consumption is estimated at an average of 99.9 million barrels per day (mb/d) in 2022, 2.3 million mb/d higher than in 2021. The EIA expects oil consumption to rise to an average of 101 mb/d in 2023, with prices remaining buoyant – the negative impact of weakening global economic conditions on oil prices is expected to be offset by supply disruptions outside the Middle East. Indeed, according to the International Monetary Fund's (IMF) October 2022 World Economic Outlook, oil prices are expected to remain elevated at an annual average of US$85.52 pb in 2023, compared with an annual average of US$98.12 pb in 2022.

A number of government policies will further support the domestic economy in 2023. A ceiling on gasoline prices and enhanced social protection programs (alongside a falling unemployment rate) will support private consumption, for example. Vision 2030 initiatives meanwhile will continue to provide a fillip to the broader economy.

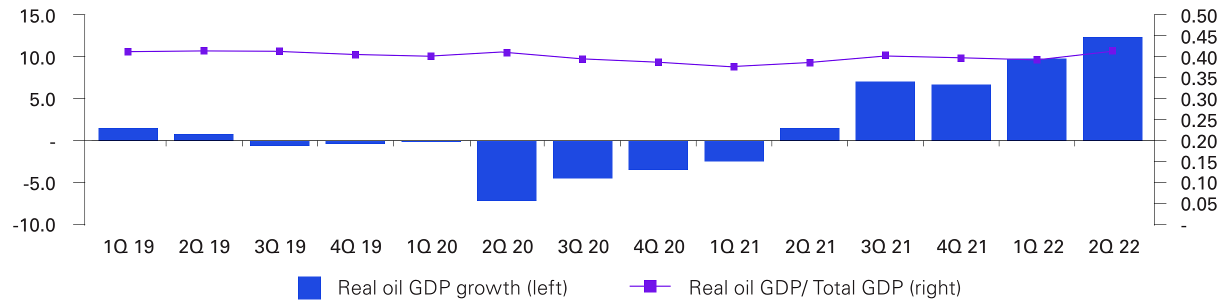
Vision 2030 initiatives and domestic spending by the the National Development Fund (NDF) and under that the Public Investment Fund (PIF) and sector-focused funds will boost investment which, along with a continued strong performance in the oil sector, will support activity in the domestic non-oil sector (reflecting the fact that oil sector trends impact confidence and money flows into the broader economy). Overall, these trends are the main drivers behind the MoF's expectations that real GDP will record respectable growth of 3.1% in 2023.

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 2023

Budget

Saudi Arabia's cabinet approved the budget for fiscal year 2023 on 7 December 2022. The government enters 2023 benefiting from several economic and fiscal headwinds. Positive drivers in 2022 have included respectable domestic non-oil GDP growth and high international oil prices – such trends have supported both public non-oil and oil revenues in 2022 – and these dynamics are expected to be maintained during 2023. The government's commitment to containing spending, even as it continues to support a range of initiatives designed to diversify the economy (thus supporting growth in non-oil revenues), will help to limit public expenditure in the next fiscal year.

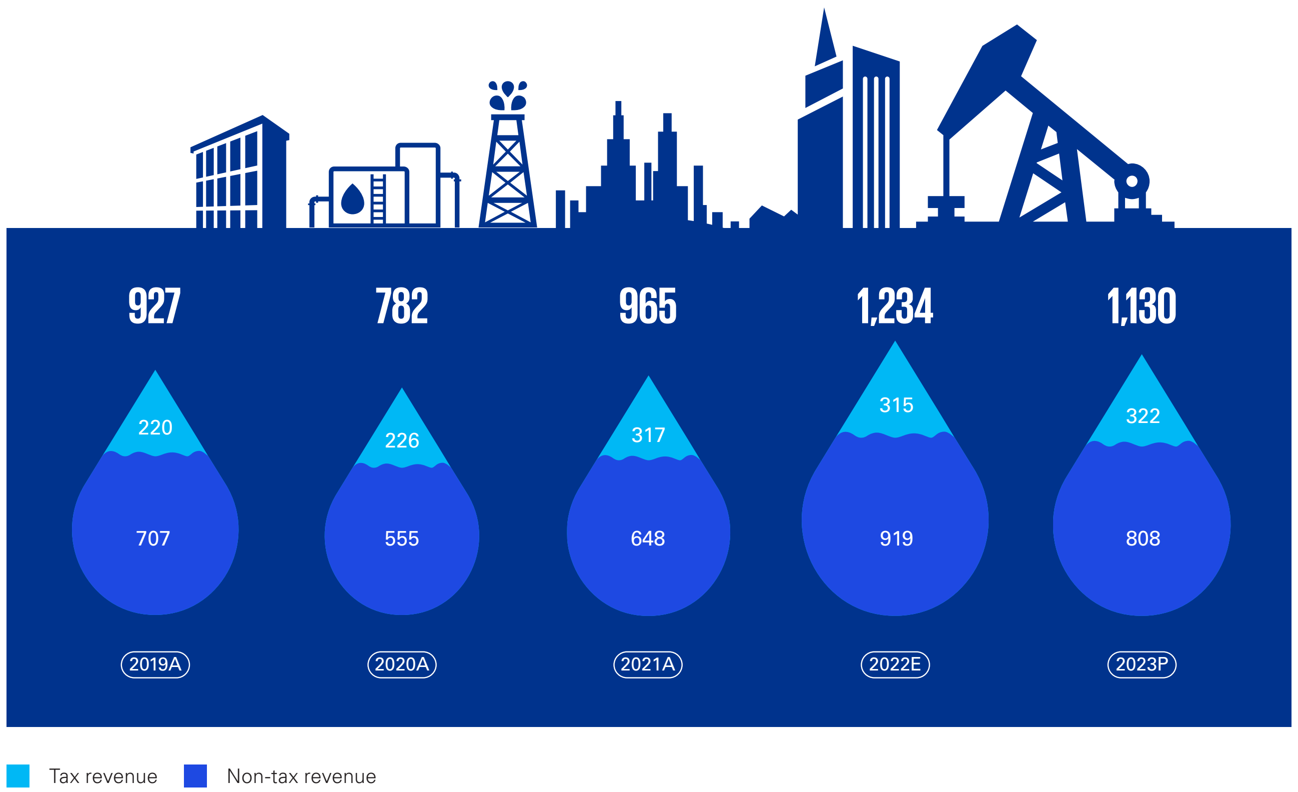
Revenues

The 2023 fiscal year budget statement reveals that robust domestic oil and non-oil economic growth and a rise in international oil prices are estimated to have increased total revenues in fiscal year 2022 to SAR1,234 billion, 18.1% higher than was forecast in the original 2022 fiscal year budget statement and 27.9% higher than the 2021 outcome.

The revenue increase in 2022 has largely been driven by several related factors. Higher international oil prices combined with a sharp rise in the country's oil production have resulted in the oil component of public revenues rising by an estimated 49.8% YoY, to SAR842 billion. This represents 68.2% of total revenues in 2022, compared with 58.2% of total public revenues in 2021. At the same time, strong non-oil GDP growth during 2022 (alongside government initiatives designed to diversify public revenue sources) have seen non-oil revenues stabilise, at around SAR400 billion.

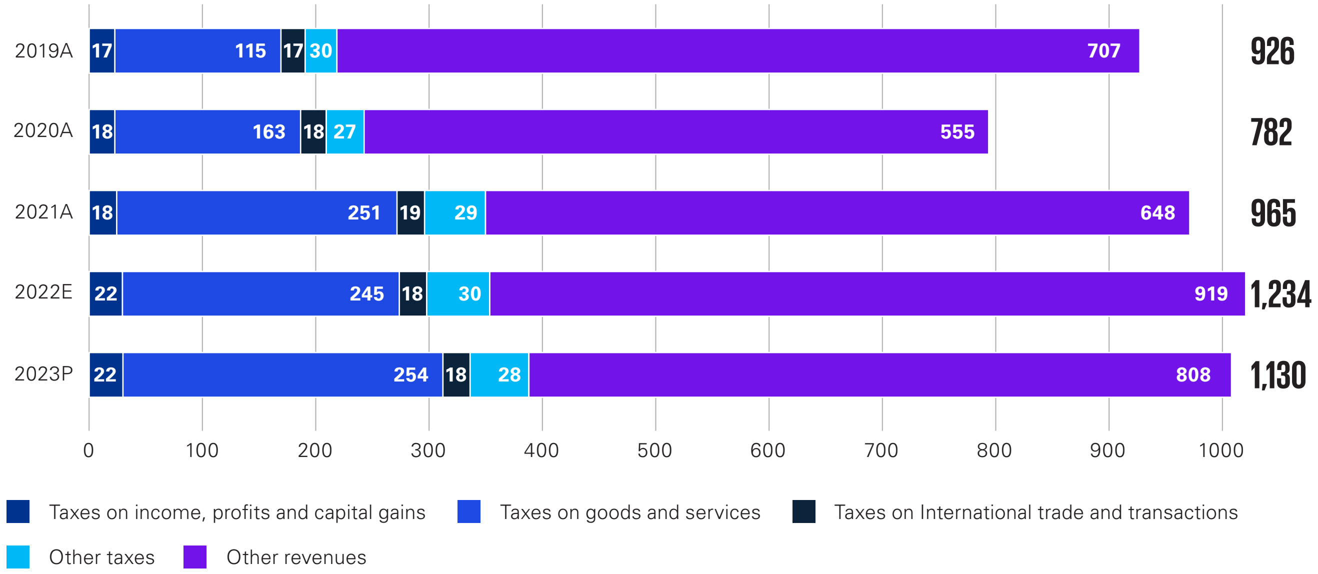
Total revenues are projected to stand at SAR1,130 billion in 2023. The budget for 2023 makes conservative assumptions, but the still-robust revenue projection reflects several factors. Economic growth will remain broad-based and continue to expand at a healthy rate. Continued high international oil prices and high oil production (albeit lower than 2022) will support oil revenues. Meanwhile, healthy non-oil GDP growth will continue to support tax revenues.

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



Source: MoF, Budget Statement 2023

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

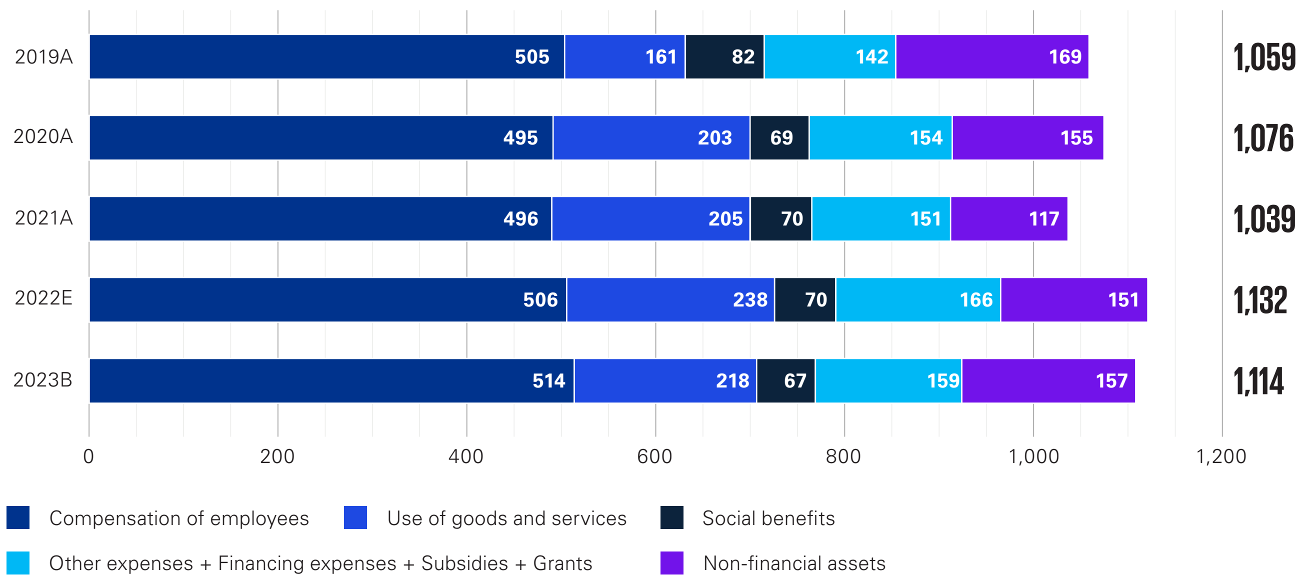


Source: MoF, Budget Statement 2023

Expenditures

Actual government spending in fiscal year 2022 is estimated at SAR1,132 billion, compared with originally planned spending of SAR995 billion (see figure 5). The overrun signals in part government initiatives designed to mitigate the impact of high global inflation on the domestic cost of living. Actual expenditure in 2022 is estimated to be above planned spending in several areas, including use of goods and services and capital expenditure (CAPEX), reflecting in part broader rising input costs in relation to public investment and consumption.

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



Source: MoF, Budget Statement 2023

The estimated expenditure in 2022 was higher than the actual outturn recorded in 2021, when total spending stood at SAR1,039 billion. CAPEX has led the increase – this component increased by an estimated 29.2% YoY in 2022, reflecting factors that include the continuation of a wide range of construction and related projects designed to enhance the quality of existing infrastructure and to develop new infrastructure as part of the government's continued strategy of developing new economic growth poles. That also includes accelerating CAPEX projects with high socio-economic impact that were slowed down during the pandemic. The four largest spending components on a sector basis – Defense, Health and Social Development, Education and General Items – all saw an increase in their budgets in 2022. Spending in the Health and Social Development component remained at elevated levels as the government continues to pursue a policy of improving the quality and quantity of healthcare services.

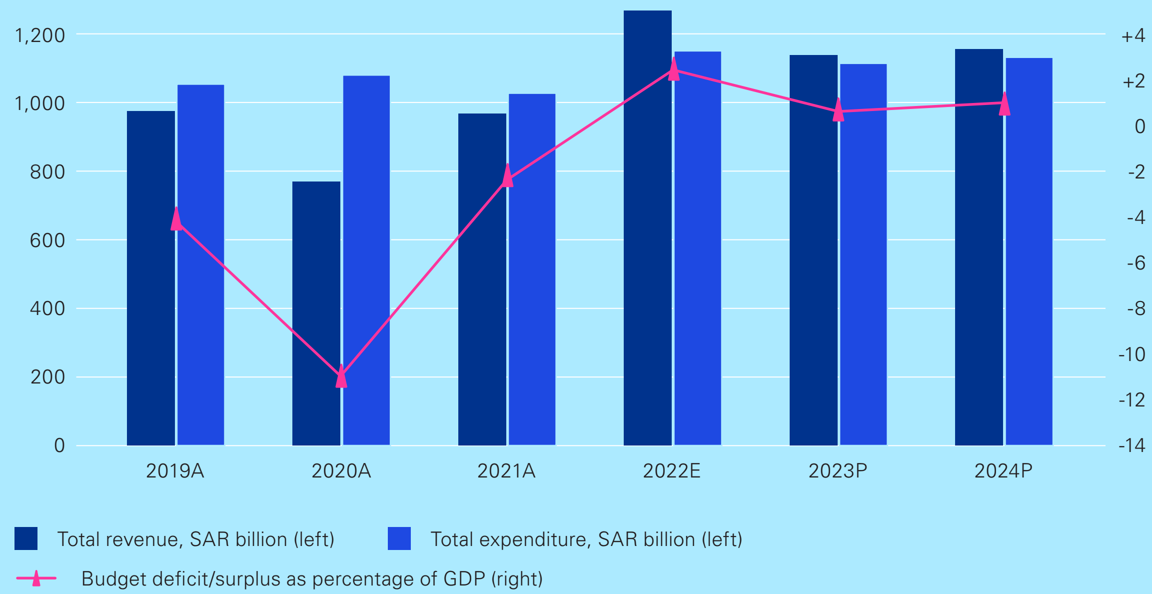
Total spending will fall from an estimated SAR1,132 billion in 2022 to SAR1,114 billion in 2023. The main drivers of this declining trend will be a reduction in spending on Goods and Services, and broader spending efficiency savings, which will help to control operating expenditures even as compensation of employees is set to rise.

The government will remain commmitted to spending on projects that support its Vision 2030 goals and vision realization programs. CAPEX is projected to increase further, to SAR157 billion in 2023, up 4.0% YoY relative to the estimated outcome for 2022. Financing has been allocated in areas such as Giga projects, regional development and economic diversification in terms of creating new product markets (or enhancing existing ones). On balance, the government will seek to maintain a balance between fiscal sustainability and meeting its economic and social objectives.

Budget deficit and public debt

The 2022 budget position estimate indicates a significant improvement in both nominal terms and as a percentage of GDP, a trend that is being driven by a sharp rise in both revenues and nominal GDP growth (the latter being the denominator). The budget position improved from a deficit of SAR73 billion in 2021 (2.3% of GDP) to an estimated surplus of SAR102 billion in 2022 (2.6% of GDP) – the 2022 budget statement had envisaged a surplus of SAR90 billion, or 2.5% of GDP (see figure 6).

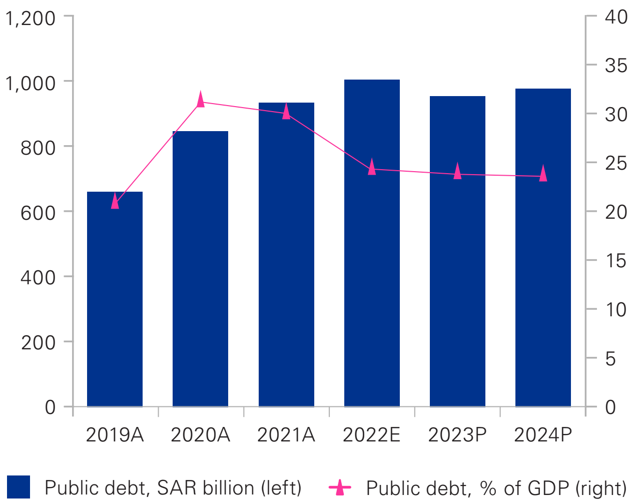
Figure 6: **Fiscal position**



Source: MoF, Budget Statement 2023

A robust revenue position, efforts to contain expenditure and a rise in nominal GDP will together maintain a budget surplus (of SAR16 billion, or 0.4% of GDP) in 2023. Downside risks to this scenario remain amid potential external shocks. However, we note that the government remains commited to fiscal sustainability, particularly through Vision 2030's Fiscal Sustainability Program, which includes, for example, the acceptance of conservative assumptions in relation to future oil prices. This conservative budget approach is expected to support the accuracy of budget forecasts relative to final outcomes.

Figure 7: **Public debt**



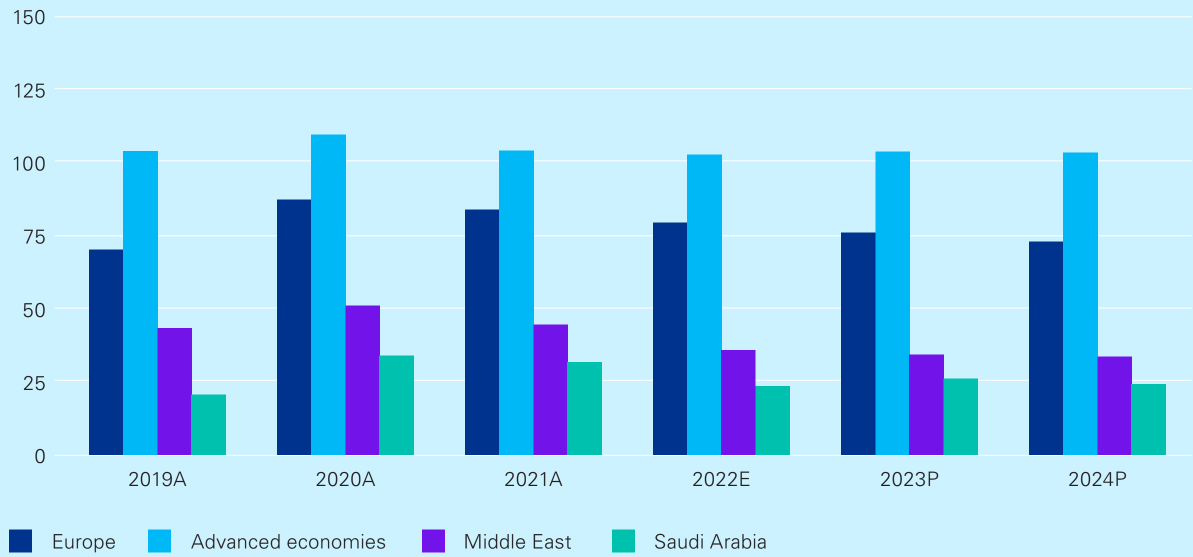
Source: MoF, Budget Statement 2023

A combination of a transition from a budget deficit to a budget surplus and nominal GDP expansion supported a sharp reduction in the public debt stock to GDP ratio from 30% in 2021 to an estimated 24.9% in 2022 (see figure 7). This estimate is similar to the 25.9% public debt to GDP ratio envisaged in the original budget statement for 2022. Nevertheless, we note that in nominal terms the public debt stock remained stable, at SAR985 billion in 2022 compared with SAR938 billion in 2021. This reflects the fact that, despite an improvement in the revenue position, the government increased expenditure by more than envisaged in the original budget statement for 2022, and as revenues were in part diverted to fiscal reserves.

In 2023, another budget surplus along with continued healthy nominal GDP growth will support a further drop in the public debt to GDP ratio, to 24.6%. The public debt stock in nominal terms will remain stable in 2023 – it is expected to remain at around SAR951 billion – largely owing to the government's plan to divert part of its income surpluses to fiscal reserves and supporting a range of public development funds.

Saudi Arabia's public debt-to-GDP ratio has historically remained significantly lower than that of its peers. The ongoing improvement in Saudi Arabia's public debt metrics indicates that the divergence in performance relative to its peers is set to widen (see figure 8).

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



Source: IMF

Expenditure by sector

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

Education

Education spending increased from SAR192 billion in 2021 to an estimated SAR195 billion in 2022, representing a 1.8% YoY increase. We note that the 2022 estimate is SAR10 billion higher than was originally set out in the 2022 budget statement. Investment in online education infrastructure continued in 2022, even as the authorities continued to build physical infrastructure that includes modern school buildings. Education spending is set to remain largely stable, at SAR189 billion in 2023. The government will continue in its efforts to align Education spending to Vision 2030 goals. The focus will as a result continue to move towards expanding research capabilities and on improving the quality of the education system more generally.

Healthcare and social development

Spending on the Healthcare and social development component is estimated at SAR198 billion in 2022, up a modest 0.6% YoY but substantially higher than the planned spending of SAR138 billion announced in the 2022 budget statement. A number of initiatives resulted in an overshoot of actual versus planned spending. Spending on establishing media- and Internet-based facilities continued, for example. Healthcare spending included an opening of specialized clinics and virtual clinics, in addition to maintaining momentum in Saudi Arabia's Covid-19 vaccination program. The 2023 budget for Healthcare and social development, at SAR189 billion, is set to remain relatively stable. A wide-ranging number of initiatives are planned for 2023 that will continue recent trends, such as Localization Programs, expanding access to healthcare and related services, as well as further investment in health-related physical infrastructure.

Infrastructure and transportation

Spending on Infrastructure and transportation fell by an estimated 8.8% in 2022, to SAR47 billion. Despite the contraction, a number of projects either progressed or were completed during the year, including support for house-builders and transport infrastructure-related projects. The completion of several large-scale infrastructure projects such as roads and networks, as well as a continued expansion in the use of private sector and development funds, will result in spending on this component contracting by 26.9% in 2023, to SAR34 billion. Nevertheless, the government will continue to support developments that enhance the quantity and quality of Saudi Arabia's transportation, housing and communications sectors, alongside other projects designed to support the government's Vision 2030 agenda.

Defense

Actual Defense spending is expected to have increased from SAR202 billion in 2021 to SAR245 billion in 2022, and is forecasted to rise further, to SAR259 billion, in 2023. This is consistent with the long-term intent to moderate spending in a way that enables investments in new capabilities for the military and security organizations, supports sustainment of existing platforms, integration across defense and security, bringing digital and technology led reform to the fore, investing in defense science and technology whilst delivering efficiency in spending. The YoY increase also supports growth opportunities for Defense and security local industrial and technology sector which continues to expand. This will particularly be positively impacted by acquisition and support strategies and policies which will be able to channel the increased spending in a way that creates sustainable local, regional and global supply chains.

Risks and challenges

Global imbalance in oil markets transmits oil price volatility and undermines public sector balance sheets

The high international oil prices witnessed since the Covid-19 pandemic started to ease – first as global economic growth started to recover (driving increased global demand for oil) and then as geopolitical events have created global energy supply constraints (a supply-side shock) – have provided a significant fillip to Saudi Arabia's public sector balance sheet, affording the authorities with fiscal space in the event of economic shocks. However, high international energy and food prices have transmitted high inflationary conditions in the country's advanced economy trading partners, prompting major central banks to raise interest rates that could result in a global economic contraction. Any sharp changes in economic trends raises the risk of supply-demand imbalances in the oil market, with policy interest rate-induced recessions likely to cause a drop in demand for oil (and thus prices for this commodity), a scenario that could see Saudi Arabia's 2023 fiscal year public budgetary assumptions shift from conservative to optimistic.

High global inflation raises unplanned public sector expenditure through its impact on goods and services costs

Current projections for public revenue and spending in 2023 could be derailed in the event of global inflationary pressures remaining elevated (and the related impact of monetary policy responses in advanced economies on global demand). Saudi Arabia's non-oil domestic economy relies on a combination of oil-related financial inflows and the economic health of trading partners – these factors transmit into the domestic economy through a variety of channels, for example, consumer and investor confidence. Weak non-oil economic growth in the event of economic shocks abroad would in turn undermine non-oil revenues in Saudi Arabia. High global prices for a range of (non-oil) commodities also raises the risk of inputs into government consumption and investment proving more costly than is currently envisaged in the 2023 fiscal year budget statement. Such a scenario would directly lead to either higher than projected spending, or a cut in government provision of good and services.

Economic indicators

Key indicators

	2018A	2019A	2020A	2021A	2022E	2023P
Economic output						
Nominal GDP (SAR billion)	3,062	3,014	2,638	3,126	3,957	3,869
Nominal GDP (% change YoY)	18.6	-1.6	-12.5	18.5	26.6	-2.2
Real GDP (% change YoY)	2.5	0.3	-4.1	3.2	8.5	3.1
Budget						
SAR billion						
Total revenue	906	927	782	965	1,234	1,130
Oil revenue	611	594	413	562	842	-
Non-oil revenue	294	332	369	403	392	-
Expenditure	1,079	1,059	1,076	1,039	1,132	1,114
Surplus / (Deficit)	-173	-132	-294	-73	102	16
Gross public debt	560	678	854	938	985	951
% of GDP						
Total revenue	29.6	30.8	29.6	30.9	31.2	29.2
Oil revenue	20.0	19.7	15.7	18.0	21.3	-
Non-oil revenue	9.6	11.0	14.0	12.9	9.9	-
Expenditure	35.2	35.1	40.8	33.2	28.6	28.8
Surplus / (Deficit)	-5.6	-4.4	-11.1	-2.4	2.6	0.4
Gross public debt	19.0	22.8	32.5	30.0	24.9	24.6
Trade and external sector						
Export (SAR billion)	1,104	981	652	1,036	-	-
of which oil exports	869	752	448	693	-	-
Current account balance (SAR billion)	271	143	-74	121	-	-
Current account balance (% of GDP)	9.2	4.8	-2.8	3.9	-	-

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

Source: IMF, MoF, Budget Statement 2023

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

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