



## Saudi Monetary Update

### Credit growth continues to rise

- Net credit issued to the private sector increased by SR12.7 billion to record an annual growth of 16.5 percent in May. We expect the credit expansion momentum this year to contribute to an all-time high profit for the banks in 2013.
- Total deposits increased by SR17.7 billion in May taking the annual growth to 16.7 percent. The loan-to-deposit ratio was broadly unchanged at 80 percent in May.
- SAMA's reserve assets continued to grow, adding SR31 billion in May. The additional FX reserves were entirely allocated to investment in foreign securities.
- Bank excess deposits with SAMA remained elevated at SR79.9 billion in May, reflecting the strong liquidity position of the domestic banks.

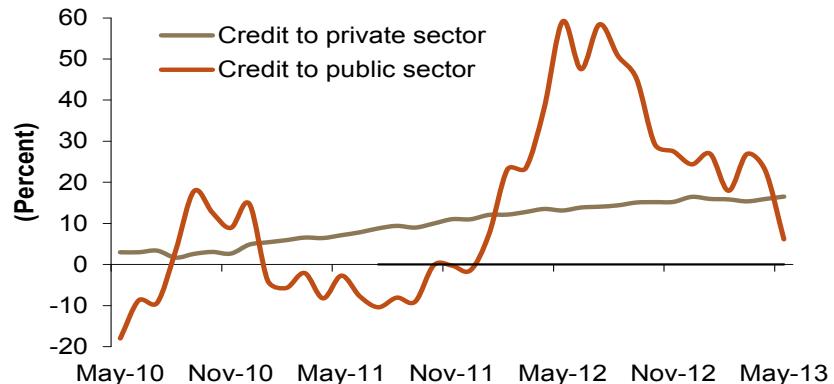
#### Broad money supply surges, but not monetary base

Monetary aggregates continued to show solid growth reflecting strong economic performance. Expansionary fiscal policy and low interest rate environment played an important role in maintaining such a trend. Growth in broad money (M3) accelerated to 16.2 percent year-on-year (1.4 percent month-on-month) in May from 14 percent in April. The narrower M2 measure, which includes demand deposits, time and savings deposits and currency outside banks, also expanded 15.6 percent year-on-year (0.9 percent month-on-month) in May versus 15 percent in April. The growth in both measures were driven by healthy growth in demand, time and saving deposits, which increased 16.2 percent year-on-year (0.7 percent month-on-month) in May compared with 15.8 percent in April. The

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**Figure 1: Bank credits**  
(year-on-year change)





*Broad measures of money supply registered strong growth in May...*

*...while monetary base contracted owing to lower bank reserves.*

*SAMA's foreign assets continued to expand despite lower crude oil prices....*

*... and we expect the trend to continue this year, though at a lower pace than in 2012.*

*Bank aggregate external position improved in May owing to rising gross foreign assets...*

*...while foreign liabilities increased at a slower pace.*

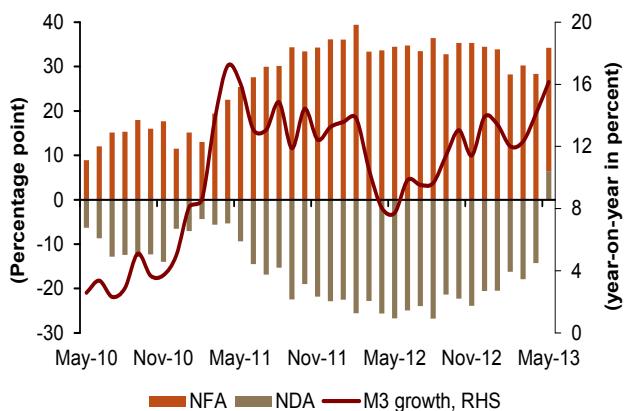
monetary base, however, contracted 2.4 percent month-on-month in May but remained 15.5 percent higher than a year earlier. The monthly contraction in monetary base is mainly due to a 5.5 percent drop in the bank deposits with SAMA. At the same time, currency outside banks recorded a strong monthly growth of 2.4 percent owing to strong domestic demand, putting a floor on the monetary base contraction. Given such monetary dynamic, the money multiplier reversed its downward trend and slightly increased to 4.7 percent.

### Net foreign asset position maintained a positive trend

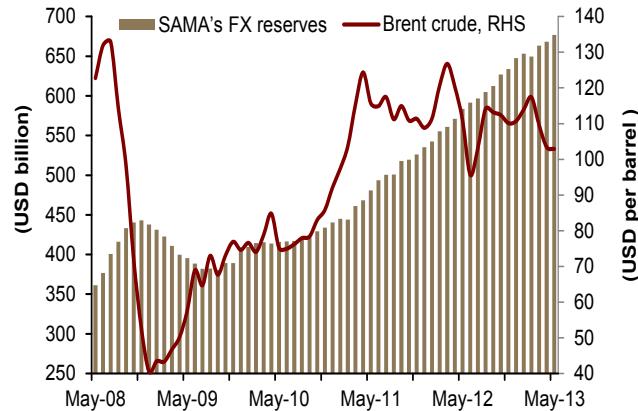
The net foreign assets (NFAs) of the Saudi financial system continued to expand, reaching SR2,677 billion in May compared with SR2,633 billion in the previous month. SAMA added SR31.8 billion to its NFA in May leading to an NFA expansion of 1.3 percent month-on-month as its gross foreign assets rose by SR31 billion compared with SR19.7 billion in the previous month. At the same time, SAMA's foreign liabilities marginally increased from SR4.7 billion at the end April to SR5.7 billion in May. The improvement in gross foreign assets reflects in part a rebound in oil production during April and May, which were scaled slightly up to 9.3 million barrel per day (mbpd) compared with 9.1mbpd year-to-March. Foreign asset position also contributed to an expansion in SAMA's total assets, which grew 1.7 percent month-on-month in May to SR2,602 billion. Within foreign assets, SAMA increased its investment in foreign securities and in foreign currencies convertible to gold by SR55 billion and SR5 billion in May, respectively, while reducing deposits with banks abroad by SR27.3 billion. We maintain our view that the positive momentum in SAMA's foreign assets is likely to slow over the coming few months relative to their strong growth last year as oil prices shift to below \$105 per barrel (pb) and the Kingdom adjusts its production to an average of 9.6mbpd this year.

The NFAs of the commercial banks reversed the previous month contraction to expand by 9.6 percent month-on-month in May. This increase was mainly due to a 7 percent increase in gross foreign assets to SR215 billion despite a 2.6 percent rise in foreign liabilities. At the end of May, bank foreign assets are 2.8 times the foreign liabilities reflecting the strong external position of the local banks. On their domestic position, banks maintained liquid with elevated deposits with the central bank. While contracting by 5.5 percent month-on-month, these deposits recorded SR157.7 billion in May, of

**Figure 2: NFA & NDA contribution to M3 growth**



**Figure 3: FX reserves and oil prices**





*Bank excess deposits with SAMA remained elevated.*

*Bank credit portfolios expanded by 16.5 percent year-on-year in May.*

*We expect the positive credit momentum to remain given the supportive macroeconomic environment...*

*...with medium- and long-term credit taking the lead.*

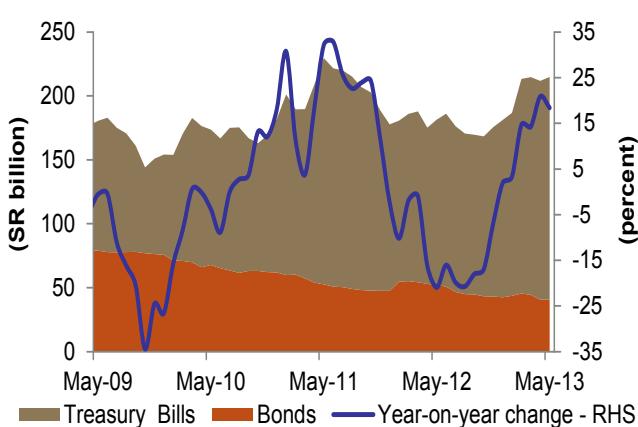
which 51 percent or SR79.9 billion was excess reserves. This reflects the ample liquidity in the Saudi banking system which could translate into higher credit growth in the coming months. With such liquidity conditions and strong growth in broad money supply, the risk is on the upside for domestic inflation.

### Credit to private sector maintains a firm, positive path

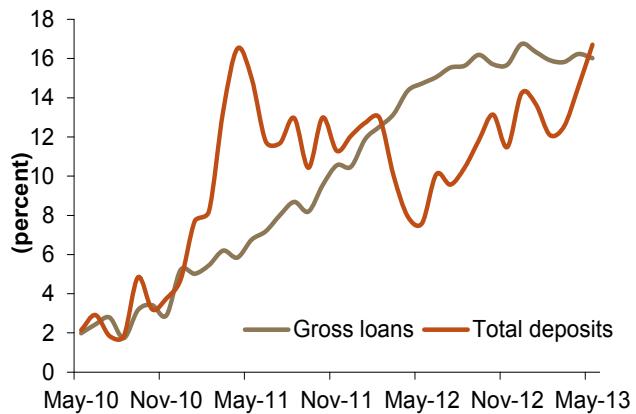
Credit to the private sector (excluding securities lending) expanded 16.5 percent year-on-year (1.3 percent month-on-month) in May compared with 16 percent year-on-year (1.6 percent month-on-month) in April. In nominal terms, banks increases their credit portfolio by SR12.8 billion in May leading to SR61.8 billion of new net credit issued so far this year compared with SR52.6 billion for the same period last year. Loans, advances and overdrafts combined to make the largest contribution (16.4 percentage point) to the year-on-year credit growth in May. In addition, total claims on the private sector, which include investment in private securities, expanded 1.2 percent month-on-month in May pushing the year-on-year growth to 16.5 percent compared with 16 percent the previous month.

We expect growth in credit to the private sector to expand further this year (16 percent year-on-year), although with a smoother trajectory than we saw last year (16.4 percent year-on-year). On this basis, we expect the incremental increase in bank credit issued to the private sector to reach SR154 billion in 2013 compared with SR135.7 billion last year and close to an all-time high record of SR155.3 billion in 2008. Expansionary government fiscal policy and rising disposable income are expected to be the main growth driver, while regional geopolitical risk and external economic environment present a downside risk on general market sentiment, hence credit growth. As we previously highlighted, credit with long-term maturity profiles will maintain a solid expansion on the back of higher government capital spending. Year-to-May, long-term credit expanded by 16.1 percent compared with a contraction of 5.3 percent for the same period last year. As a result, the share of long term credit to total credit improved to 28.6 percent in May compared with 24 percent a year earlier. Medium-term credit should also improve given the government's expansionary consumption spending, gains in Saudi public and private sector employment and the positive outlook for the housing market development. As such, medium term credit expanded by 22.2 percent in May while its share of total bank credit improved from 17.3 percent in May 2012 to 18.2 percent in May

**Figure 4: Bank holding of government securities**



**Figure 5: Bank deposits and loans  
(year-on-year change)**





2013.

*Banks continued to add to their holding of treasury bills...*

*...as government development bonds mature.*

*Bank deposits continued a solid growth ...*

*...which offset the increase in bank lending...*

*...leaving the loan-to-deposit ratio broadly unchanged at 80 percent.*

*3 month Sibor maintained a downward trend since January's peak...*

*...but regional geopolitical risk could increase its volatility.*

*Banks' profits are set to break an all-time record high this year.*

Growth of bank claims on government remained positive in May owing to higher investment in treasury bills, while bank holding of development bonds continues its downward trend. Commercial bank added SR3.1 billion to their treasury bills holding in May leading to a total holding of SR174 billion or 34 percent higher than a year earlier. We expect SAMA to gradually increase treasury bill issuance as government bonds mature and banks remain liquid. In fact, banks prefer to hold treasury bills which generate a higher return than their excess deposits at SAMA. Banks holding of development bonds dropped by 22 percent year-on-year in April, a trend that is likely to remain on the negative side as the government gradually retires its debt.

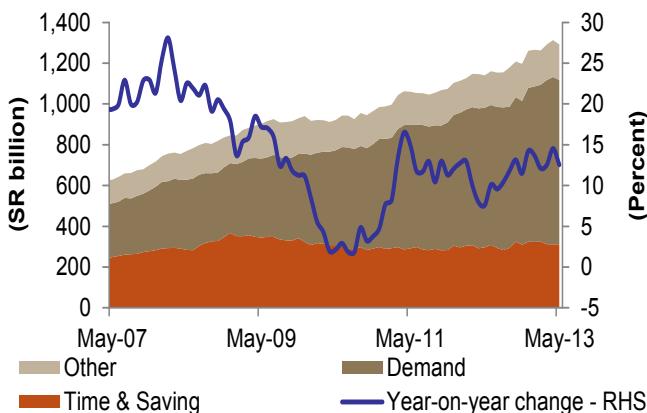
### Funding and liquidity profiles will support record profit

Bank deposits as a main source of bank funding in the Kingdom maintain a solid expansion with a double digit annual growth in the last two years and into this year. In May, deposits increased by 16.7 percent year-on-year (1.3 percent month-on-month) from 14.5 percent year-on-year in April. In nominal terms, bank deposits increased by SR17.7 billion in May with deposits in foreign currencies accounting for most of the increase owing to a seasonal trend during the summer months. As monthly growth in credit to private sector and non-financial government entities (1.2 percent) in May was roughly matched with monthly expansion in deposits (1.3 percent), the system-wide loan-to-deposit ratio was broadly unchanged at 80 percent in May.

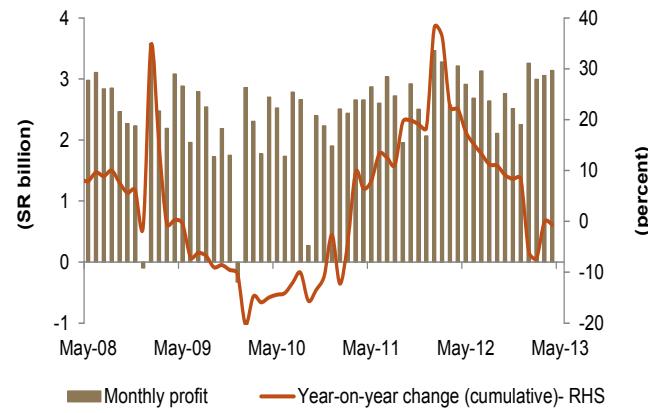
At the same time, three-month Sibor continued on a downward trend after the January peak of 0.9975 percent to record 0.9650 percent on June 23. While the ample liquidity of the banking sector played a role on pushing the rate down, external political and economic environment is likely increase its volatility.

The expansion in credit and low funding costs continue to contribute to a pick-up in bank profits. In May, banks recorded a profit of SR3.2 billion, 11 percent high than their profits in May last year, taking the year-to-May profit to SR15.7 billion. We remain positive on bank profit growth, based on a solid path for credit growth and low funding costs in 2013. In fact, we expect this year's bank profit to surpass the all-time high of SR34.7 billion recorded in 2008.

**Figure 6: Composition of bank deposits**

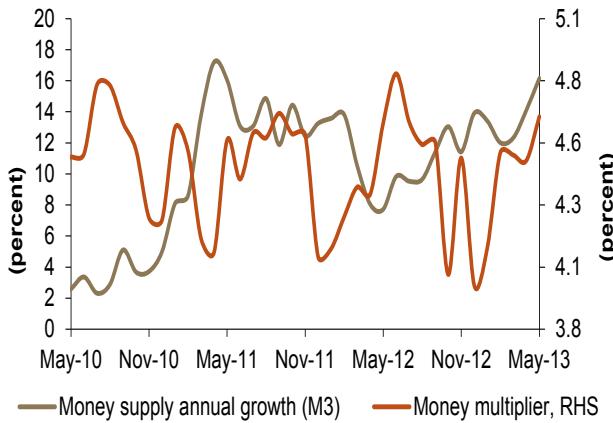


**Figure 7: Bank profits**

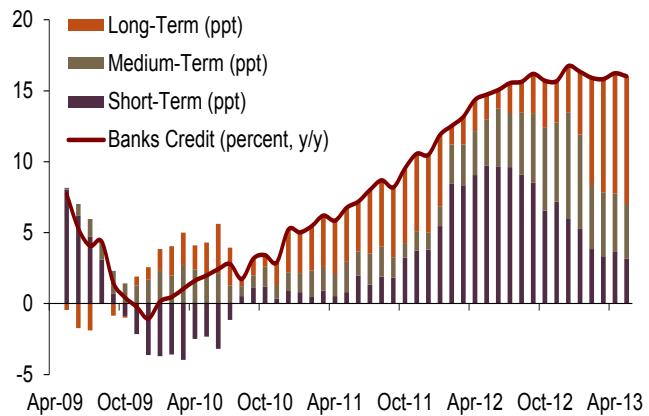




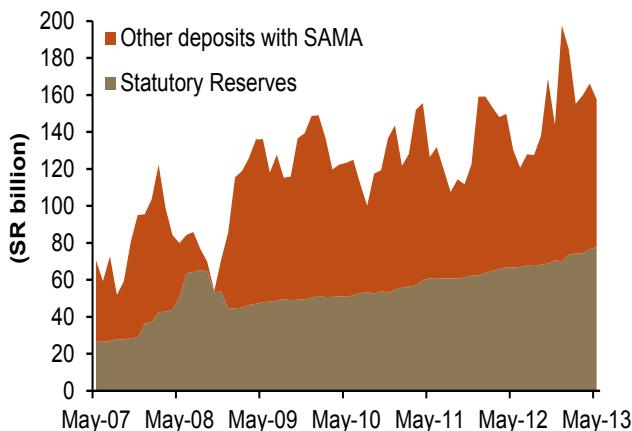
**Figure 8: Both money multiplier and money Supply expand further in May**



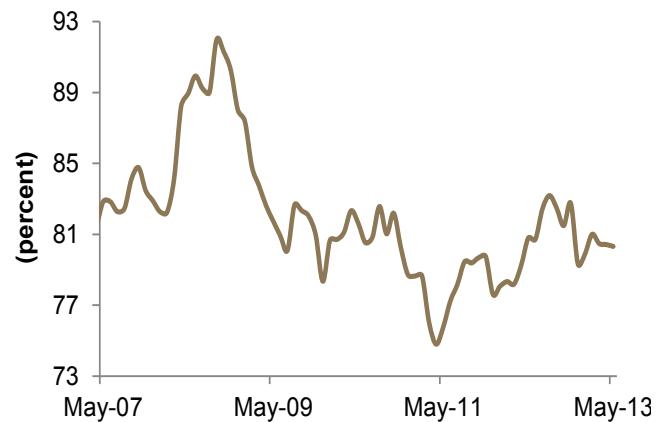
**Figure 9: Long term lending contributed the most to credit growth in May**



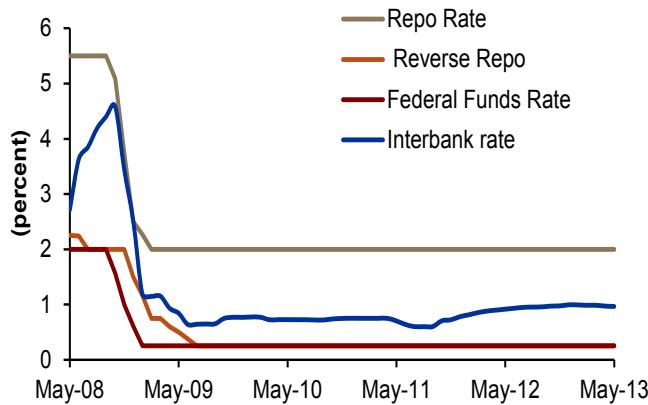
**Figure 10: Bank excess reserves at SAMA remained on the high side**



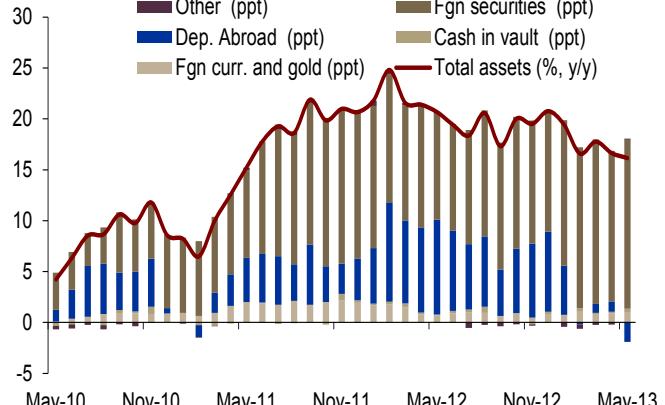
**Figure 11: Loan-to-deposits ratio at 80 percent allows for further growth in lending**



**Figure 12: Policy interest rate is expected to remain on hold**



**Figure 13: Investment in foreign securities contributed the most to SAMA's assets growth**





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