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Saudi Economic Review

NCB Monthly Views on Saudi Economic and Financial Developments

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Executive Summary

- The recent pressures on oil prices have been attributed to a background of continued fragile economic recovery on the one hand, and on both relatively global supportive fundamentals along with geopolitical complexity, on the other hand.
- Investors sought safe haven currencies, namely the USD and JPY. The greenback dropped to as low as 1.3121 against the Euro by mid-October but managed regain its losses in November.
- Agricultural, energy and precious metals prices witnessed a decline, while industrial metals was the worst performing sector. Hurricane Sandy closed the month with commodities witnessing their biggest decline in five months.
- The inflation rate is likely to remain below the 4% level towards the end of 2012. However, we expect domestic prices to regain pace by January given the robust growth of the economy and its highly liquid state.
- Tadawul's earnings announcements last month, repeated the quarterly cycle whereby investors withdrew their capital to reassess their portfolios accordingly.
- The maturity of credit maintains its direction towards the medium term category by reaching a share of 17.9%, adding SAR37.7 billion since the beginning of the year
- China and Singapore surpassed the UAE on the leaderboard of the major trading partners, with their share of Saudi exports standing at 15.4% and 8.9%, respectively

View of the Month

'FDI: Displaying Signs of Recovery'

Based on macroeconomic fundamentals, prospects for global FDI inflows will continue to exhibit a modest, but nevertheless steady growth, reaching USD1.8trn and USD1.9trn in 2013 and 2014, respectively.

Macroeconomic Indicators

	2007	2008	2009	2010	2011P	2012F	2013F
Real Sector							
Average KSA Crude Spot Price, Arab Light, USD/BBL	68.3	94.9	59.2	77.6	108.1	105.0	110.0
Average Daily Crude Oil Production, MMBD	8.8	9.2	8.2	8.2	9.3	9.9	10.1
GDP at Current Market Prices, SAR billion	1,442.6	1,786.1	1,412.6	1,679.1	2,163.1	2,272.3	2,437.3
GDP at Current Market Prices, USD billion	385.2	476.9	377.2	447.8	577.6	606.8	650.8
Real GDP Growth Rate	2.0%	4.2%	0.1%	4.6%	6.8%	5.1%	4.2%
Oil Sector GDP Growth Rate	(3.6%)	4.2%	(7.8%)	2.4%	4.3%	6.4%	2.2%
Non-oil Sector GDP Growth Rate	4.7%	4.3%	3.5%	5.5%	7.8%	4.7%	4.9%
Population, million	24.9	25.8	26.7	27.6	28.4	29.2	30.1
Population Growth Rate	3.4%	3.4%	3.4%	3.4%	2.9%	3.0%	3.0%
GDP /Capita, USD	15,444.2	18,495.4	14,147.9	16,244.8	20,355.1	20,760.4	21,619.2
CPI Inflation, Y/Y % Change, Average	4.1%	9.9%	5.1%	5.3%	5.0%	4.8%	4.5%
External Sector							
Merchandise Trade Balance, USD billion	150.6	212.0	105.2	153.7	244.7	276.3	306.8
Oil Exports, USD billion	205.3	281.0	163.1	215.2	317.6	355.1	379.1
Non-oil Exports, USD billion	27.8	32.3	29.1	35.8	46.9	48.4	61.7
Merchandise Imports, USD billion	(81.5)	(100.6)	(86.4)	(96.7)	(119.1)	(127.1)	(134.1)
Net Unilateral Transfers, USD billion	(17.0)	(23.0)	(27.7)	(27.9)	(29.4)	(32.1)	(35.1)
Current Account Balance, USD billion	93.3	132.3	21.0	66.8	158.5	171.1	199.8
Current Account Balance/GDP	24.2%	27.7%	5.6%	14.9%	27.4%	28.2%	30.7%
Net Foreign Assets with SAMA, USD billion	301.3	438.5	405.9	441.0	535.9	642.5	718.3
Fiscal Sector (Central Government)							
Budgeted Expenditure, SAR billion	380.0	410.0	475.0	540.0	580.0	690.0	759.0
Actual Revenues, SAR billion	642.8	1101.0	509.8	741.6	1110.0	1146.8	1220.1
Actual Expenditure, SAR billion	466.2	520.1	596.4	653.9	804.0	771.8	818.2
Expenditure Overrun, %	22.7%	26.8%	25.6%	21.1%	38.6%	11.9%	7.8%
Total Revenues/GDP	44.6%	61.6%	36.1%	44.2%	51.3%	50.5%	50.1%
Total Expenditure/GDP	32.3%	29.1%	42.2%	38.9%	37.2%	34.0%	33.6%
Overall Budget Balance, SAR billion	176.6	580.9	(86.6)	87.7	306.0	375.0	402.0
Budget Balance/GDP	12.2%	32.5%	(6.1%)	5.2%	14.1%	16.5%	16.5%
Break-Even Oil Price	40.5	40.2	60.8	64.1	70.4	62.2	65.0
Financial Sector							
USD/SAR Exchange Rate	3.75	3.75	3.75	3.75	3.75	3.75	3.75
Growth in Broad Money (M3)	19.6%	17.6%	10.7%	5.0%	13.3%	9.7%	7.7%
Growth in Credit to the Private Sector	20.6%	27.9%	-0.6%	4.8%	11.0%	15.9%	15.1%
Average 3M SAR Deposit Rate	4.9%	3.3%	0.9%	0.7%	0.7%	0.8%	1.0%
Average 3M USD Deposit Rate	5.2%	3.0%	0.7%	0.4%	0.3%	0.4%	0.4%
Spread, in Basis Points, SAIBOR-LIBOR	(31.9)	29.7	17.5	38.0	39.5	40.0	60.0

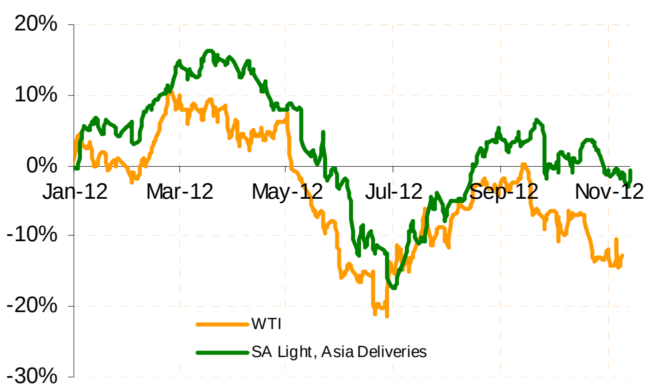
Oil Market

Demand Prospects Decline

Oil market sentiment has weakened over last month, leading to a sequence of price declines only to recover slightly in November, with Brent crude futures falling 16% from this year's peak, trading around USD108 a barrel in early November, amid fears that euro zone failure to resolve its debt turmoil is hindering the global economy. This recent dynamic has been attributed to a background of continued fragile economic recovery on the one hand, and on both relatively global supportive fundamentals along with geopolitical complexity, on the other hand. Any consideration of global economy seems still fairly gloomy, though it points to be coming off the fears of a hard landing in China. Likewise, any consideration of the geopolitical background suggests that a down move in oil prices should not become overextended. The Syrian situation seems like being a never ending internal destruction than to cause spillovers across the region, the outlook for Iraq appears less promising, and the Iranian nuclear issue still seems to be headed on a potentially troubling course. In the short term oil prices are expected to be relatively range-bound, with the prompt Brent contract trading around its year's 9-month average of USD112/bbl.

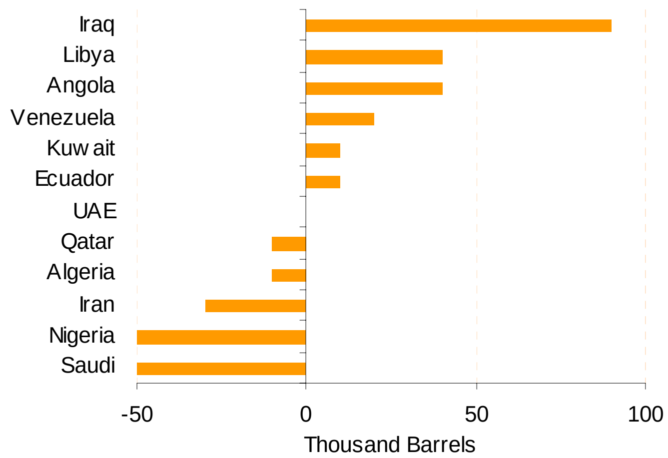
In its latest annual world oil outlook, OPEC expected that demand on its crude will decline through to 2016, attributed to weakening economic outlook and growing reliance on unconventional resources such as US shale oil and shale gas deposits. Global demand for OPEC's oil will shrink to 29.7 mmbd in 2016, about 1.4 million less than this year. While noting that world markets are currently well supplied, OPEC predicts that it may have more than 5 million barrels of daily spare production capacity as early as next year. The US is set to achieve its highest level of energy independence in more than 20 years due to booming oil shale. The combination of weaker oil demand growth and surging non-OPEC supply has prompted OPEC into such radical reassessment of prospects for global demand on OPEC's crude. Meanwhile, it acknowledges uncertainties surrounding the evolution of global oil demand growth, which are largely due to the impact of North America's shale oil and gas major developments. Despite this uncertainty, however, OPEC states are expected to continue to invest heavily in their oil sector, at least in the short term. OPEC Members are undertaking or planning around 116 development projects during the five-year period 2012–16, amounting to investment USD270bn.

Chart 1: Oil Price Developments, YTD



Source: Thompson Reuters

Chart 2: OPEC's Monthly Oil Production Changes



Source: OPEC Survey

On the supply side, OPEC oil production declined in October as Iranian output dropped to the lowest level in 22 years. Output in the 12-member countries slipped 87,000 barrels to an average of 32.092 mmbd in October. Iranian production fell to 2.6mmbd, the lowest level since February 1990. On the other hand, Nigeria's output climbed to an average of 2.09 mmbd in October. Also, Angola increased its production to 1.78 million barrels. Libyan output climbed to 1.49 mmbd barrels a day this month, and plans to increase its crude oil output to 1.7mmbd by 1Q 2013. Iraqi production was unchanged at 3.35mmbd in October, the highest level since May 2000. Saudi Arabia pumped 9.8 mmbd in October, unchanged from September. Meanwhile, due to rising domestic consumption, particularly in the power sector, in the summer months, Saudi Arabia's crude oil exports dropped to 7.08 mmbd in August, the lowest level in a year, from 7.38 mmbd a year ago. In the same month, Saudi Arabia produced 9.75 mmbd.

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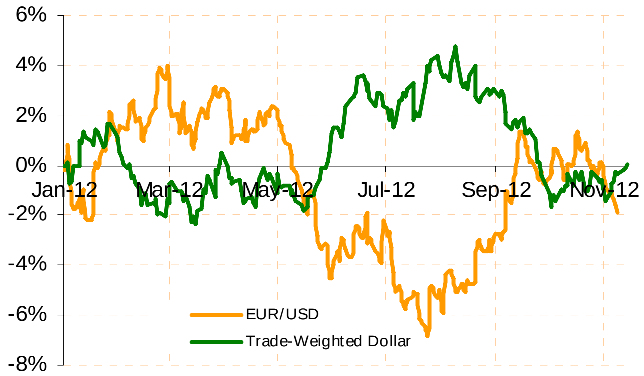
Foreign Exchange

Safe Havens Favored Yet Again

The foreign exchange market is the most liquid and the largest financial market in the world with an approximate turnover of 4 trillion USD per day. Currency prices are currently affected by three powers, the US, Europe, and China. The former has been the highlight during the month of October as the presidential race intensified with the daunting fiscal cliff right around the corner. The Democratic Party secured another four years at the white house as Obama will try to bring the US economy back to its glory years, quite a challenge. The first hurdle is to tackle the "fiscal cliff" ahead of the economy before 2013. During the last debt ceiling agreement, USD1.2 trillion mandated spending cuts and tax increases were agreed upon over the next decade, of which USD607 billion (4% of GDP) would take effect in January if congress fails to amend the US's debt burden. The automatic cuts are expected to drag the US economy into another recession, thus a compromise between the republicans and democrats must be met for the sake of the US and the global economy.

Chart 3: Trade-Weighted Dollar and the Euro

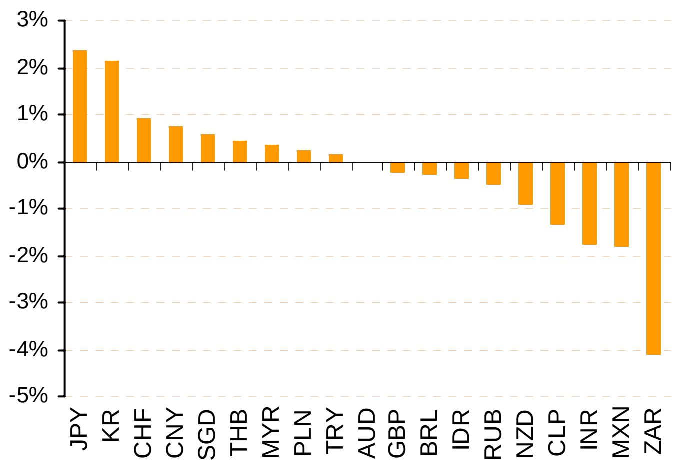


Source: Thompson Reuters

Over in Europe, the debt crisis is prolonged by Greece's inability to trim down their deficit in a timely manner. In their last meeting, finance ministers failed to dissect the debt difficulties of Greece and granted the brittle economy until 2016 to cut their deficit to 2% of GDP. Furthermore, officials struggled to agree upon further financial aid for Greece as a result of the extension, a gap of EUR32.6 billion is need for the Greek economy to stay afloat. Additionally, peripheral economies are still under pressure to also cut down their deficits and maintain fiscal stability. Spain struggles with revenue sources as continuous tax increases trigger more protests.

Meanwhile, the driving force of the global economy, China, had their own political uncertainty as they decided on the next decade's leaders. The Chinese economy has slowed down over the past seven quarters as demand for products declined, hurting their export-led growth. However, growth is expected to regain pace following the politburo reshuffling. As for Japan, quantitative easing seems to be the only solution in sight with debatable effectiveness. The Bank of Japan increased their asset purchase program to JPY66 trillion late last month but remains to be burdened by its currency's safe haven status.

Chart 4: Monthly Foreign Exchange Rate Changes



Source: Thompson Reuters

The aforementioned pushed investors to seek safe haven currencies, namely the USD and JPY. The greenback dropped to as low as 1.3121 against the Euro by mid-October but managed regain its losses, settling at 1.2706 by November 13. As for the Yuan, it hit a 19-year high at 6.2254 against the US dollar. The Japanese Yen settled at 79.41 to the greenback and 100.8158 to the Euro on November 13. The appetite for the USD and JPY is likely to continue for the remainder of 2012.

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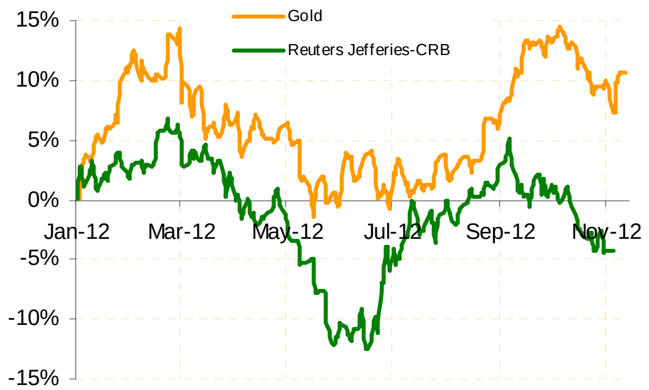
Commodities

Dampened Performance

The month of October saw upward commodity price momentum slowdown. The outlook for GDP growth became a primary concern, especially post China's forecasts being cut by both the IMF and the World Bank. Europe's woes—especially that of Greece's—continued to plague asset classes, and the implications on the results of a US election also played a role. For the month, the agricultural, energy and precious metals prices witnessed a decline, while industrial metals was the worst performing sector. Hurricane Sandy closed the month with commodities witnessing their biggest decline in five months.

Indices across the board also fell in October, with the Thomson Reuters-Jefferies CRB Index losing 4.3%; its worst performance since earlier in May this year. S&P's GSCI also followed suit, as 20 of the 24 commodities tracked by the index dropped. These included a 17% and 6.5% decline in Nymex gasoline and crude oil respectively, as well as a slip in zinc by 11%, and that of nickel by 12%. As for the Dow Jones-UBS commodity tracker, it fell 3.88% for the month, with top downside performing single commodities including industrial metals and coffee. The latter ended the month down 10.86%.

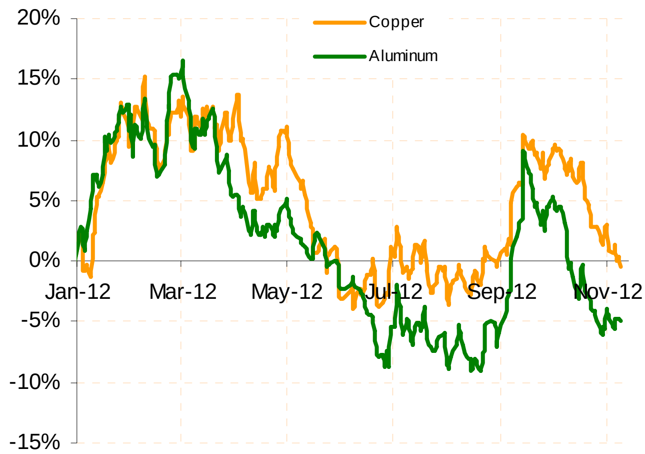
Chart 5: Reuters Jefferies vs. Gold



Source: Thompson Reuters

Nickel prices have been slowing down on the back of China reporting its seventh straight quarter of decelerated growth. Euro area contraction, in terms of services and manufacturing, have also put a dent in the industrial metal. As for zinc, lower global consumption and surplus supply is capping its potential. According to the International Lead and Zinc Study Group (ILZSG)—a UN body—demand for refined zinc is anticipated to fall by 0.3% in 2012, to 12.71 million tonnes. Conversely, supply for mine output is expected to rise by 0.5% to 13.6 million tonnes. Weaker market conditions, however, are set to recover in 2013.

Chart 6: Base Metals



Source: Thompson Reuters

Gold also closed the month's session down, sliding 3.1% for the first time in five months. Spot gold closed at USD1,719.10/ ounce, while comparable metal, US silver, closed at USD32.316/ ounce. Varied uses for silver, such as in electronics, and the medical field are set to provide a bullish base for silver prices come 2013.

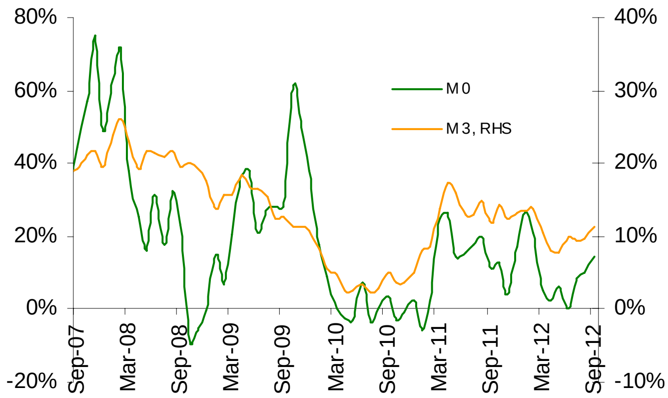
In agricultural softs, larger stocks of coffee, which marked 2.41 million bags on ICE, dampened prices. US coffee closed at USD154.65 Cents/ pound. A high yield year from Brazil put downward pressure on prices, as well as speculation about Vietnam's continued high production levels of Robusta beans. Vietnam is Robusta's top grower. US cocoa closed at USD2,388/ ton, while US sugar fell to USD19.46 Cents/ pound. Going forward, commodity prices are likely to stay within their current ranges as the year comes to an end.

Money & Inflation

Local Prices Expected to Ease Further

The monetary situation for Saudi continues to expand while inflationary pressures subdue, a trend that had been witnessed since March 2012. Saudi's monetary base (M0) recorded an annual gain of 14.3% during September as it reached SAR287.8 billion. The main contributor to growth was, yet again, deposits with Saudi Arabian Monetary Agency (SAMA), which rose by 20% Y/Y, the fastest pace since January this year. Additionally, cash in vault grew at 21.4% during September over the same month last year while dropping 9.8% on a monthly basis. The final item of M0, currency outside banks, gained by 7.8% Y/Y as Hajj preparations were in full gear. The rising pace of M0's growth is expected to continue for October, while decelerating for November and December figures as Islamic rituals end and the record levels from the period between Dec-Apr offset the steady and controlled pace witnessed currently. This will also ease any pressures on local prices which have already been on a downward trend for the past eight months.

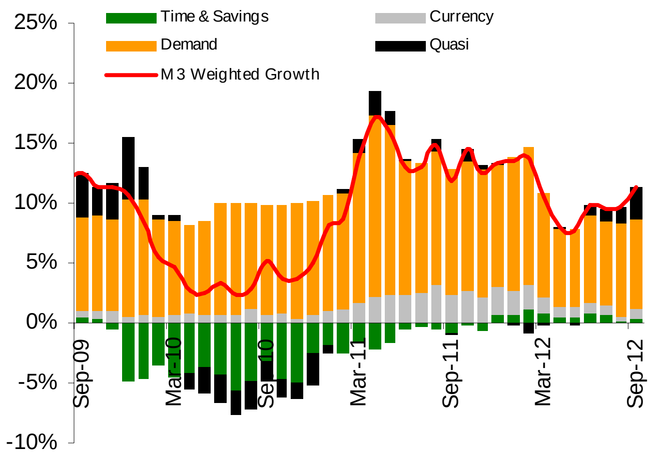
Chart 7: Growth in Monetary Aggregates



Source: SAMA, NCB Estimates

The money supply (M3) undoubtedly has a positive correlation with M0. Consequently, M3 recorded a rise of 11.4% annually by the end of September to reach an all-time high at SAR1.31 trillion. On an annual basis, demand deposits unsurprisingly outpaced time and savings deposits by posting a gain of 14.4% and 1.5%, respectively. However, on a monthly basis, demand deposits dropped by SAR6.8 billion while time and savings deposits added SAR10.4 billion for September. The expansion in the depositary base continues to aid the growth of credit domestically for the private and public sector (see Loans Market section). Furthermore, other quasi-monetary deposits rapidly accelerated at 20.8% Y/Y, the highest growth rate since January 2010 which is in line with growth in Saudi trade activities (see External Trade section). Given the utilization of liquidity witnessed recently, we expect M3 to post an annual gain of 9.75% for 2012, revised down from 10.9% and decelerating further in 2013 to 7.76%.

Chart 8: Money Supply, Contribution



Source: SAMA, NCB Estimates

Consumer prices have dropped, as expected, to 3.6% Y/Y in September from 3.8% Y/Y during the previous month. The drop is largely due to base effects specifically from the "other expenses and services" category which contracted by 0.4% on an annual basis. Food prices have regained their pace to record a gain of 4.0% with further increases expected in the coming months. A subcategory of food, tobacco, rose by 21% for September as local authorities intensify their fight against smoking by imposing price hikes on cigarettes and a recent ban on indoor smoking. In anticipation of the delayed codifying of the mortgage law, rent prices slowed for another month to 8.0% Y/Y from 8.5% Y/Y during the previous month. The inflation rate is likely to remain below the 4% level towards the end of 2012. However, we expect domestic prices to regain pace by January given the robust growth of the economy and its highly liquid state.

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Capital Markets

Tadawul Remains Reluctant

The Saudi stock market, Tadawul, failed to break the negative channel as it slid for a second consecutive month ending October. The earnings announcements last month, repeated the quarterly cycle whereby investors withdrew their capital to reassess their portfolios accordingly. The all-share index dropped 2.6% by mid-October since September but managed to recap most of its losses following the stream of announcements and ending the month on a loss of 0.7% M/M. Since the beginning of 2012, Tadawul has only gained 5.8% by the end of last month, benign as the local economy is more buoyant than ever. The worst performing sector this month was construction, burdened by Al Mojil Group which faces the possibility of liquidation following their inability to repay their debts. The construction sector declined 4.2% during October and, by the end of November 10, has lost 10.8% YTD. Another ailing subcategory in the local equity market was petrochemicals which dropped by 2.8% last month. As the largest listed company, Sabic, pressured the subsector and Tadawul by reporting a drop of 23.0% in earnings as product pricing reduced net income levels.

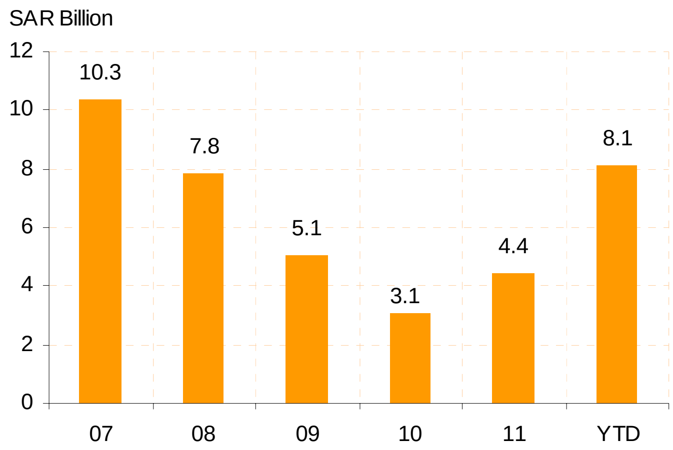
Chart 9: Tadawul All-Share Index

Source: Tadawul

Nonetheless, numerous companies have reported strong growth in profitability and the leading sector last month, energy, posted a 3.3% gain during October. The rise was attributed to Saudi Electricity Company's stellar performance during the third quarter which posted a 32.2% rise over the same period last year. Additionally, the retail sector also stood out as a performer by increasing 2.2% last month, bringing its YTD growth to 15.5% by end of November 10. The leading companies to post the largest income levels within the sector, Hokair, , Jarir, Othaim, and Mouwasat have announced gains in their corporate earnings by 25%, 5%, 13% and 5%, respectively, to boost the sector as a whole.

Investor appetite continues to deteriorate on a monthly basis as the level of activity dropped drastically during October. The average daily traded volumes have dropped to SAR8.1 billion for 2012 YTD as the index fails to hold its ground above the 7000 level. Specifically during October, investors pumped a total of SAR90.0 billion which averages at SAR5.0 billion per trading day, 18.0% lower than September's daily average. Consequently, the price to earnings ratio edged lower to 12.48 by the end of last month which should lure investors into long term investments.

Chart 10: Average Daily Traded Value



Source: Tadawul

As for the primary market, Saudi remains to outperform geographical peers. During November, Dallah, which operates in the health industry, is expected to attract investors by its initial public offering of 14.2 million shares. The price of shares is set to be announced within the coming days. Furthermore, Anaam Company is concluding a rights offering of 8.7 million shares as they continue to rebuild the company which faced many challenges over the years.

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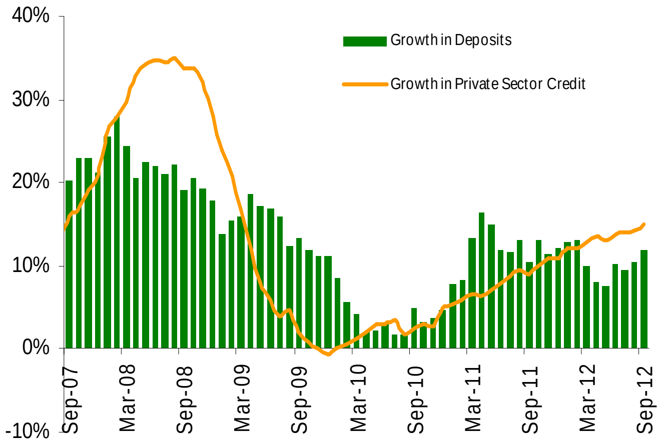
Loans Market

On a Positive Momentum

Growth in banks' deposits continues to provide opportunities to expand the financing capabilities of the banking system. The depositary base of Saudi banks has reached SAR1.18 trillion during September according to the latest SAMA bulletin, a rise of 11.8% over the same month last year. The deposit distribution for businesses and individuals reflects the low interest rate environment as 71.3% reside in demand deposits while time and savings deposits and foreign currency deposits hold 19.2% and 9.6%, respectively for the month of September. Meanwhile the government's composition indicates a cautious and long term investment horizon given the shares of demand, time and savings, and foreign currency deposits at 16.0%, 49.0%, and 35.0%, respectively. The readily available deposits remain to be preferable as the lack of attractive yields continues.

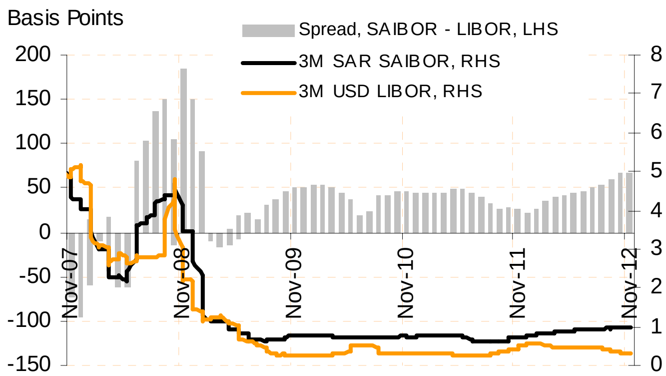
Chart 11: Private Sector Financing



Source: SAMA, NCB Estimates

The combined loans portfolio for local banks reached an all-time high during September at SAR973.2 billion, a 16.2% gain over September 2011. The pace of credit growth in the Saudi economy is gaining momentum and reaching growth levels of early 2009 as banks feel more comfortable to take on risk. The maturity of credit maintains its direction towards the medium term category by reaching a share of 17.9%, adding SAR37.7 billion since the beginning of the year. This confirms local banks' shift to finance SMEs in an attempt to grasp a premature segment as medium term credit recorded a substantial gain of 30.6% during September. Short term funding still holds the largest share at 57.1% with an annual gain 14.7% and long term credit posted a growth of 10.7% Y/Y. The strong growth in lending this year and the, relatively sluggish, pace of deposits has aided the loans to deposits ratio to 82.5% from 77.6% last year.

Chart 12: Liquidity and Risk Detector



Source: Thompson Reuters

The credit portfolio of Saudi banks continues to be largely compromised of the commerce sector which holds 20.7% of banks' total financing, SAR201.7 billion. The commerce sector recorded the slowest growth rate at 1.4% Y/Y as the banking sector pursues diversification. Meanwhile, the second largest financed sector, manufacturing and processing, has regained its momentum by growing at 16.9% Y/Y during 3Q12 following an 11.7% Y/Y growth for 2Q12. Additionally, the vast mega projects in mining and quarrying have been captured by local banks, albeit marginally due to the inability to finance huge long term deals. Credit for mining and quarrying has almost doubled in a span of two years and has recorded a growth 43.7% Y/Y by the end of September. Furthermore, the need of the Saudi economy to expand on utilities, such as water and electricity, has supported local banks on the financing front. The electricity, water, and healthcare sector is financed by banks with an amount of SAR32.2 billion as of September 2012 and the figure is expected to continue its sizable growth. The estimated consumption of electricity is estimated at 240,296 GW for 2012 and expansionary plans are needed to meet the estimated consumption of 289,437 GW by 2015. The building and construction sector financing is also on a positively steep trajectory and is likely to continue once the mortgage law is codified.

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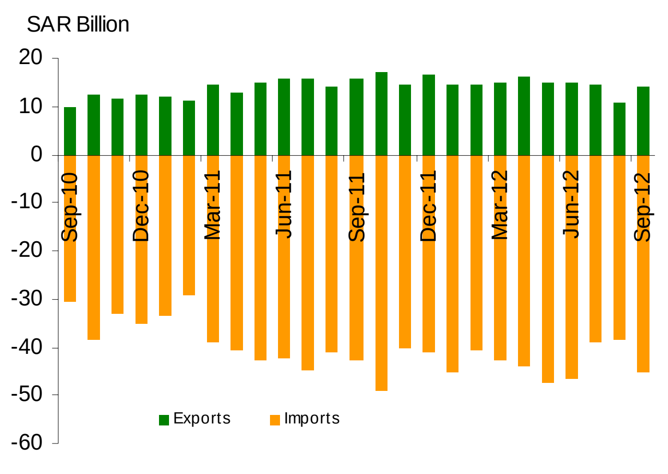
External Trade

Global Prices Pressure Trade Balance

The recently released September 2012 foreign trade figures pertaining to the non-oil sector helped in shedding a light on the trends of exports and imports as well as the major trading partners. In terms of value, non-oil exports decreased by 10.1% Y/Y, driven by a reduced volume of around 13% Y/Y. However, it must be noted that while the suppressed quantity demanded played a pivotal role in pulling exports lower, it did not have the same impact on imports as international prices remained supportive in reducing the net effect on Saudi imports that increased value-wise by 5.2% Y/Y even though the tonnage imported fell by a significant 13.9% Y/Y. On a monthly basis, the downtrend that had been witnessed in both exports and imports since April and May, respectively, had been reversed, an anticipated outcome after the summer and the Eid season.

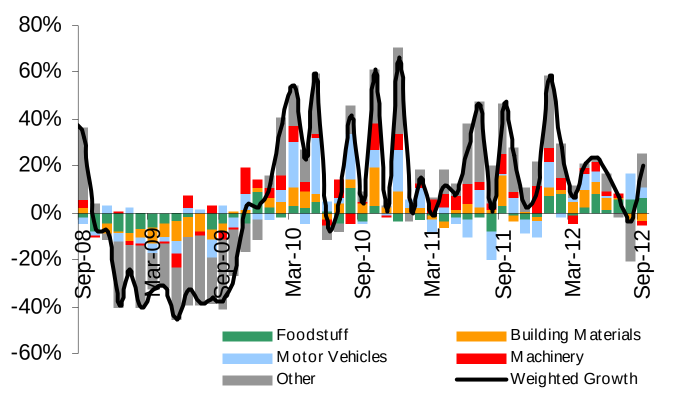
Chart 13: Saudi Non-Oil Trade Balance



Source: CDSI, NCB Estimates

The total value of non-oil exports rebounded from a near two year low of SAR10.8 billion in August to SAR14.3 billion in September. Interestingly, plastic exports led the surge, registering SAR5.6 billion, the highest on record, which propelled its share to 39%, thus, surpassing the petrochemicals share that stood at 34.6%. After nose-diving in August to SAR3.1 billion, the lowest since July 2010, exports related to petrochemicals rose to SAR4.9 billion in September, which was in line with the expectation that the steep fall of around 40%, largely attributed to the decline in exports to Asian countries (excluding Arab and Muslim countries) in general and China in particular, was a blip and not a trend. China and Singapore surpassed the UAE on the leaderboard of the major trading partners, with their share of Saudi exports standing at 15.4% and 8.9%, respectively. On a near term note, We believe that exports to China will remain range-bound, especially that the second-largest economy continues to experience a soft landing scenario after seven quarters of abating GDP growth rates on the back of a slowdown in industrial output and investment spending.

Chart 14: Attribution Analysis of Letters of Credit Opened



Source: SAMA, NCB Estimates

On the import side, the value increased to SAR45 billion, a two month high, with the top three importers being China, US and Germany, as their shares stood at 14.3%, 14.2% and 7.6%. More importantly, the imports of machinery, mechanical appliances, and electrical equipment had posted a historical record of SAR12.7 billion that raised their share to 28.1%, higher than the share of transport equipment that stood at 17.2%. Looking forward, on the financing side, the new Letters of Credit (LCs) for the month of September showed a 20% Y/Y and 25% M/M growth rates, indicating an expected increase in the non-oil exports and imports during the near term. The positive drivers on LCs emanated from foodstuff and motor vehicles that grew annually by 97% and 32%, respectively, while building materials and machinery acted as negative drags. The double-digit growth in Points of Sale, a proxy for retail sales, for the fifth consecutive month signals a strength in domestic demand that will be supportive to an upside movement in Saudi trade. In our opinion, however, August and September figures with their historical lows and highs do represent an anomaly that was a direct consequence of the Eid vacations, and must be taken in that context.

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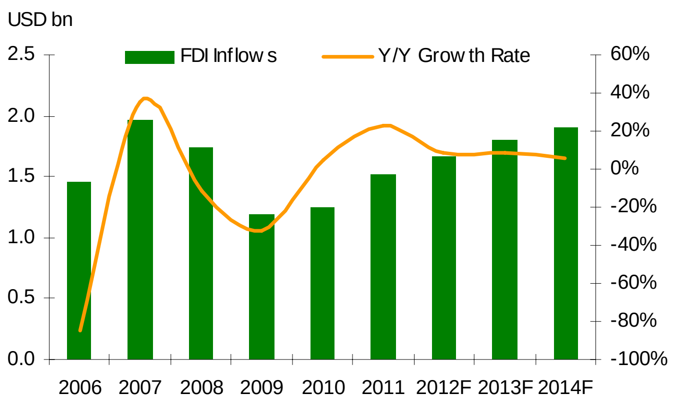
Special Focus:
FDI: Displaying Signs of Recovery

After the global economic downturn in 2008-2009, foreign direct investment (FDI) inflows showed a gradual recovery on the back of higher profits for global transnational corporations (TNCs), as well as a relatively high economic growth in developing countries. Last year, FDI grew by16% Y/Y, surpassing pre-crisis growth levels for the first time. Early 2012 figures, however, marked an inflection point as a retreat in the value of greenfield investments and cross-border mergers and acquisitions (M&A) reversed the positive trend. This is mostly attributed to the resurgence of global economic uncertainty emanating from the European sovereign debt crisis and the observed slowdown of emerging economies. According to UNCTAD, weak M&A levels also suggest a sluggish growth in FDI to be seen throughout the rest of the year. Based on macroeconomic fundamentals, prospects for global FDI inflows will continue to exhibit a modest, but nevertheless steady growth, reaching USD1.8trn and USD1.9trn in 2013 and 2014, respectively. Although investment climate remains misty for the remainder of this year, UNCTAD's World Investment Prospects Survey (WIPS) shows that more than half of the respondents foresee an increase between 2012 and 2014, compared with 2011 levels.

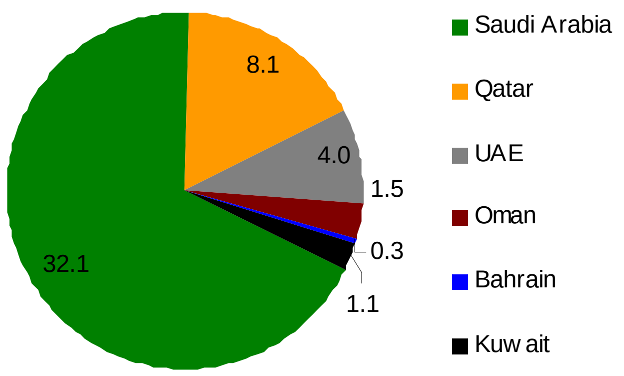
Chart 16: World FDI Inflow



Source: UNCTAD and NCB Estimates

Inflows to developed countries amounted to USD748bn in 2011, about 21% up from 2010. However, the level of inflow remains below the pre-crisis 3-year average by 25%. While the three major developed economies, European Union (EU), North America, and Japan unanimously displayed an upward trajectory, the driving factors for each have varied considerably. As for the EU, growth was attributed to M&As, whereas in North America and Japan, it was driven by TNCs reinvestments. More so for Japanese, TNCs as their purchasing power improved due to an appreciating Yen. Considering that developing and transition economies' FDI inflows account for half of the world's FDI (45% and 6%, respectively), these countries have a pivotal role in determining future global figures as they weigh heavily with a new record high of USD777bn, topping last year's figures by 12% despite economic woes. In contrast to the upbeat figures of developing countries' FDIs, flows to Africa resumed their downward trend, albeit marginal, for the third consecutive year. Least Develop Countries (LDCs) remained in FDI recession with a retreat of 11% down to USD15bn. FDI growth in the year 2012 is therefore expected to spring from developed, developing, and transition economies.

Chart 17: GCC FDI Inflow



Source: UNCTAD and NCB Estimates

The 2011 political upheavals in the Middle East and North Africa (MENA), especially in Syria and Yemen, had convoluted the concurrent economic slowdown and adversely weighed on non-GCC Arab FDI inflows, registering a decline of 26%, down to USD7bn. On the other hand, increased oil revenues in the GCC has stimulated FDI activity after a series of large-scale projects' suspension or cancellation in previous years resulting in FDI inflows to drop by 35%, hitting rock bottom in 2010. However, we expect GCC FDI inflows to moderate around a sustainable level of USD40.7bn. Saudi Arabia, the largest recipient of FDIs in the GCC, had witnessed a 42% fall Y/Y in 2011, realizing USD16.4bn. Almost 90% of FDI inflows to the kingdom were greenfield investments which confirms the direction towards long-term investment. We expect oil and gas to be the leading sector from which FDI growth will occur. As for outflows, they remain range bound around USD3-4bn, reflecting the importance of domestic investment compared to international investment.

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