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Executive Summary

The year 2017 was eventful for Saudi Arabia. The Kingdom announced various measures which laid the bedrock for the nation fulfilling its "Vision 2030" plan. During the year, KSA introduced numerous key reform measures, including 5% value-added tax (VAT), excise duty on tobacco and carbonated/energy drinks and an increase in electricity tariffs and fuel prices. The year also witnessed a number of capital market reforms, such as the launch of the NOMU Parallel market and introduction of the T+2 settlement cycle.

Whilst 2017 was the year when the way forward was laid out, 2018 is likely to be the year when measures are undertaken to fulfil the ambitious vision. The 2018 budget focuses on higher capital spending in non-oil sectors such as transport, construction and utilities. The government also announced measures to boost growth in the private sector, including SAR 72 bn stimulus, with focus on housing, exports and manufacturing.

In 2017, the government announced a slew of economic and social reforms to help unlock the young country's full potential. Reform process is expected to pick up full steam and accelerate in 2018. The following is a list of reforms to be initiated or implemented in 2018:

- **Fiscal**: Subsidy rationalisation will continue in 2018. The government already increased the prices of certain fuels as of 31 December 2017. The coming year is likely to witness more calibrated price increases, in line with the government's fiscal roadmap. The government is also expected to announce further allowances and salary increases if the reforms start pinching the common Saudi. In our view, the government will steadily, but cautiously, move ahead with the necessary and stated fiscal reforms during the year; however, it will be flexible enough to leave room for manoeuvre as far as their pace is concerned.

- **Financial market:** The year is expected to witness the inclusion of Saudi Arabia in the emerging market indices MSCI and FTSE Russell, and the listing of Aramco, the world's largest IPO. Additionally, from 1 January 2018, foreign investors can now participate in IPOs for smaller companies within the Kingdom through NOMU, helping the country attract foreign investments into the SME segment. The year 2018 would also be when Saudi financial markets fully integrate with the global financial ecosystem.

- **Social**: Saudi women will be permitted to drive and enjoy sports and other forms of outdoor entertainment starting this year. Moreover, the Kingdom is expected to begin issuing tourist visas to foreign travellers and allow cinemas to be opened this year. These progressive reforms will bring women further into the economic mainstream and give boost to tourism and entertainment sectors.

Overall, in 2018, we expect KSA to undertake concrete and significant steps towards becoming a more wholesome economy, with various engines of growth other than the current one: oil. The year would also witness the Saudi industry and society becoming more integrated with the world and starting to reap the benefits of this development. While we do expect some minor speedbumps along the way, the direction and momentum of global integration is irreversible.

This positive economic outlook is likely to be reflected in the equity market as well, which would further be boosted by foreign inflow due to the Kingdom's inclusion in MSCI and FTSE Russell emerging market indices. The on-going shift in the Saudi economy, in our view, will benefit the Financials, Telecom, Chemicals, Food and Cement sectors the most.

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2017 Macro-Economic Review

Last year was a transformational one for Saudi Arabia with the introduction of key economic and social reforms. The government made considerable progress in implementing key reforms announced under Vision 2030 and the National Transformation Program (NTP) 2020. In 2017, the Kingdom declared a 5% value-added tax (VAT) on most goods and services, introduced excise duty on tobacco and carbonated/energy drinks and increased electricity tariffs and domestic oil prices. Other big announcements included the launch of mega infrastructure projects such as NEOM and the Red Sea tourism project, a corruption crackdown and the removal of restrictions preventing women from driving in 2018.

The year also saw several capital market reforms such as the launch of the Nomu parallel market, reclassification of sectors and introduction of the T+2 settlement cycle. To boost foreign investment, the Capital Market Authority (CMA) allowed direct foreign investment in the Nomu parallel market, effective from 1 January 2018 and signed a memorandum of understanding with the Saudi Arabian General Investment Authority (SAGIA) to set up a framework to allow non-resident foreign investors to own a stake of 10% or more in publicly traded companies. The Kingdom has also signed a deal with US based Nasdaq to upgrade the country's financial market infrastructure which is expected to be completed by 2020.

Oil prices at highest levels in two years at around US$64 per barrel

The positive impact of the reforms is illustrated by the fact that, Fund manager Blackrock Inc. and private equity firm Blackstone Group are planning to open offices in the Kingdom. Public Investment Fund has committed to invest US$20 bn to a US$40 bn in infrastructure investment fund with Blackstone Inc. to invest in various sectors including medical care and education.

Additionally, Saudi Arabia is also focusing on developing the domestic automotive industry and is encouraging global vehicles manufacturers to start local operations in the country. As a result of the concerted efforts, Bentley motors has entered into a joint venture with SAMACO in November 2017 to deliver sales and after sales service in the Kingdom.

In June 2017, global index compiler MSCI added Tadawul to a watch list for potential inclusion in the MSCI Emerging Markets Index. The addition to the MSCI watch list was a major milestone and reflects the Kingdom's significant progress in capital market reforms. The REIT market also experienced significant traction in 2017, as six REIT funds were listed, while another nine funds were approved.

Oil prices made a modest recovery following the OPEC's agreement to cut oil production. However, this was not enough to sustain economic growth. To make it more impactful, OPEC and allied non-members extended the agreement until the end of 2018, which is likely to support oil prices and growth prospects in 2018.

The Kingdom is making a conscious and visible effort to wean itself away from addiction to oil revenue and the same is reflected in the 2018 budget presented by the government.

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Overview of Budget 2018

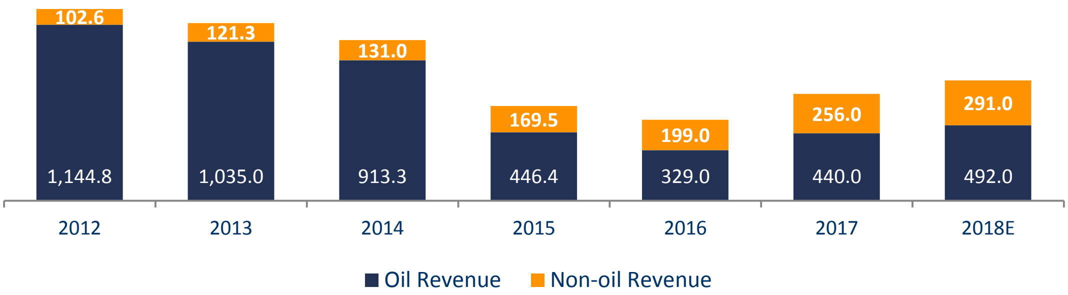
Budget boosts health, infrastructure and transport sectors

Government spending focuses on productive sectors

The Saudi government came up with an expansionary budget policy for 2018. Government expenditure is projected to increase to SAR 978 bn from SAR 890 bn budgeted last year. Additionally, the National Development Fund and the Public Investment Fund would be expending SAR 83 bn and SAR 50 bn, respectively, in 'off-budget spending'. Focus on structural reforms and increased spending signifies a shift in the government's stance towards an expansionary policy during the next few years.

Revenue is expected to grow 12.6% y-o-y to SAR 783 bn in 2018, led by new taxes and energy price reforms. Oil revenue is estimated to grow to SAR 492 bn, while non-oil revenue is forecasted to accelerate to SAR 291 bn. Capital spending is budgeted to grow 14% y-o-y in 2018 to SAR 205 bn compared with SAR 180 bn in 2017. The higher capital spending would favor non-oil sectors such as transport, construction and utilities. A large part of this capital spending would go to support Vision 2030 initiatives and boost growth in the private sector. The government recently announced energy prices reforms and selective taxes on tobacco and soft drinks. These initiatives should drive GDP growth to 2.7% in 2018 vis-à-vis the -0.74% rate seen in 2017.

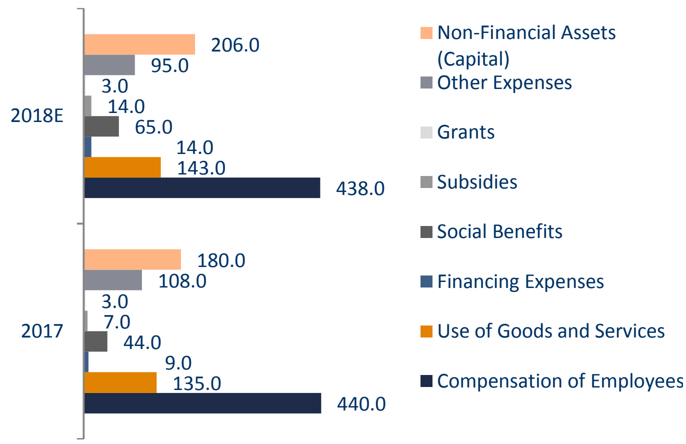
Revenue Break-up (SAR bn)



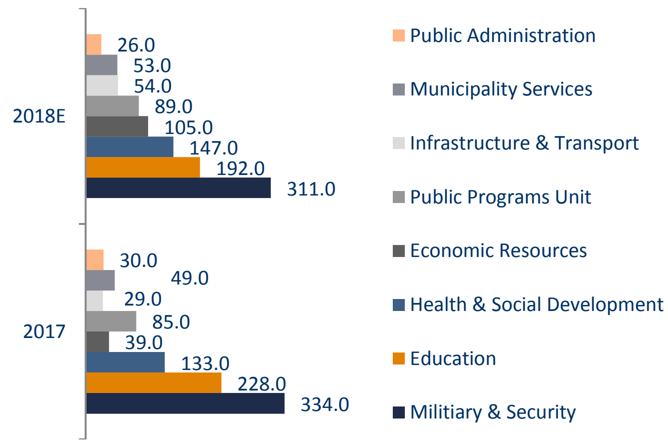
Source: Ministry of Finance, E-Estimate

The highest share of budget spending in 2018 would go to the defence and security sector for the first time. Around a third of the budget spending has been allocated to the defense and security sector (SAR 311 bn). Other sectors allocated significant budget shares in 2018 include health, education and economic resources. The government also announced a SAR 72 bn stimulus for the private sector, which focuses on housing, exports and manufacturing. The major portion of this package (48%) would be allocated to the real estate sector, SAR 21 bn to residential housing loans and SAR 14 bn to developing technologies.

Estimated expenditure 2018 versus 2017 (SAR bn)



Budget allocation, segment-wise (SAR bn)



Source: Ministry of Finance, E-Estimate

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Oil Outlook 2018

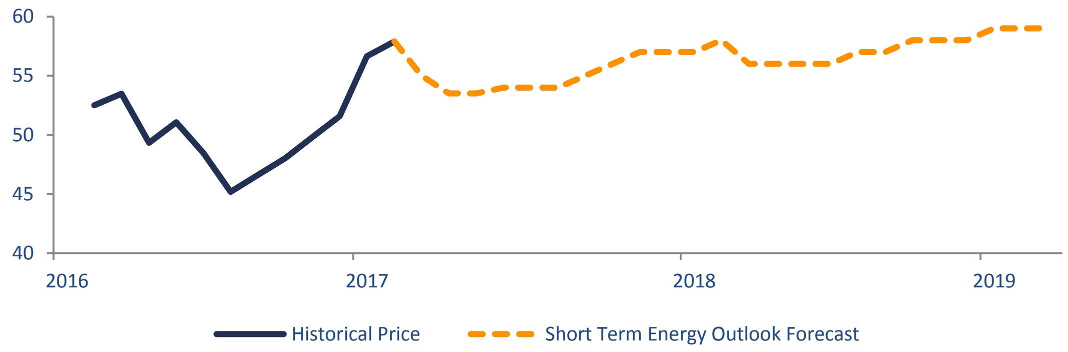
Oil prices firm up on strong demand amid constrained supply

Increasing oil prices are expected to boost economic growth levels in Saudi Arabia in 2018. As per the International Monetary Fund (IMF), the Kingdom needs oil prices at US$70 per barrel in 2018 to break even. The break-even oil price in 2017 was US$73.10 in Saudi Arabia vis-à-vis US$96.60 for 2016. According to IMF, the medium-term oil price assumption was based on the futures market. WTI Crude oil prices are expected to remain around US$60 per barrel. Various global investment banks too have raised their projections for oil prices in 2018. Goldman Sachs has projected that Brent crude will aim at an average of US$62 per barrel in 2018. JP Morgan forecast oil prices at US$60 per barrel in 2018 owing to OPEC's willingness to balance markets.

As WTI Crude oil prices rose to their highest level in two years (around US$64 per barrel), enabling the Kingdom to deliver a budget that targets growth and investment, whilst maintaining fiscal restraint and lowering fiscal deficit. The increase in oil prices was due to the settlement between OPEC and non-OPEC oil producers to maintain production cuts of 1.8 mn barrels per day throughout 2018, along with a review in the middle of the year.

Short Term Energy Outlook Crude oil price (US$ per barrel)

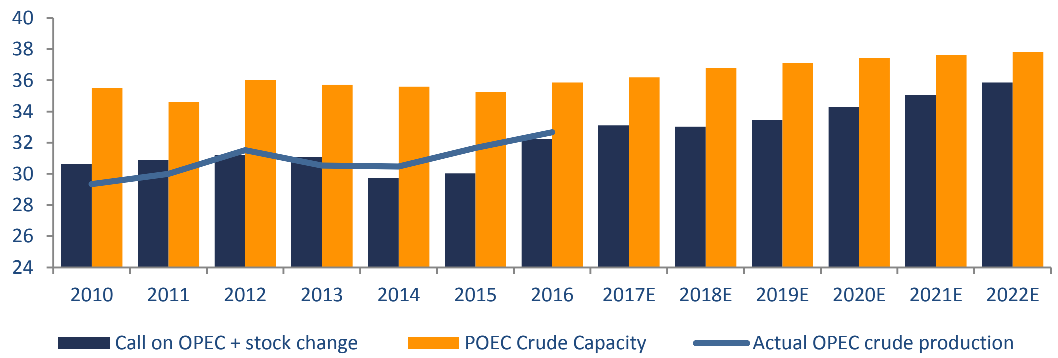
Oil prices to stabilise around US$60 per barrel



Source: Short-Term Energy Outlook, January 2018, and CME Group

On the flip side, the International Energy Agency said that US shale producers are more active now that oil prices have reached US$60. US drilling and well completion rates have picked up as prices have recovered. If US shale production revives in a big significant way, it could reduce oil prices next year.

Global oil market balance (mb/day)



Source: International Energy Agency, Oil 2017

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Fiscal Prudence to Be the Way Forward

VAT implementation, first step towards fiscal consolidation

Saudi Arabia will no longer be a tax-free country. After the collapse of oil prices three years ago, the government of Saudi Arabia has sought to enhance revenues by implementation of 5% value-added tax (VAT) on most goods and services. VAT is a part of long-term tax reforms to reduce the Kingdom's dependence on oil revenues.

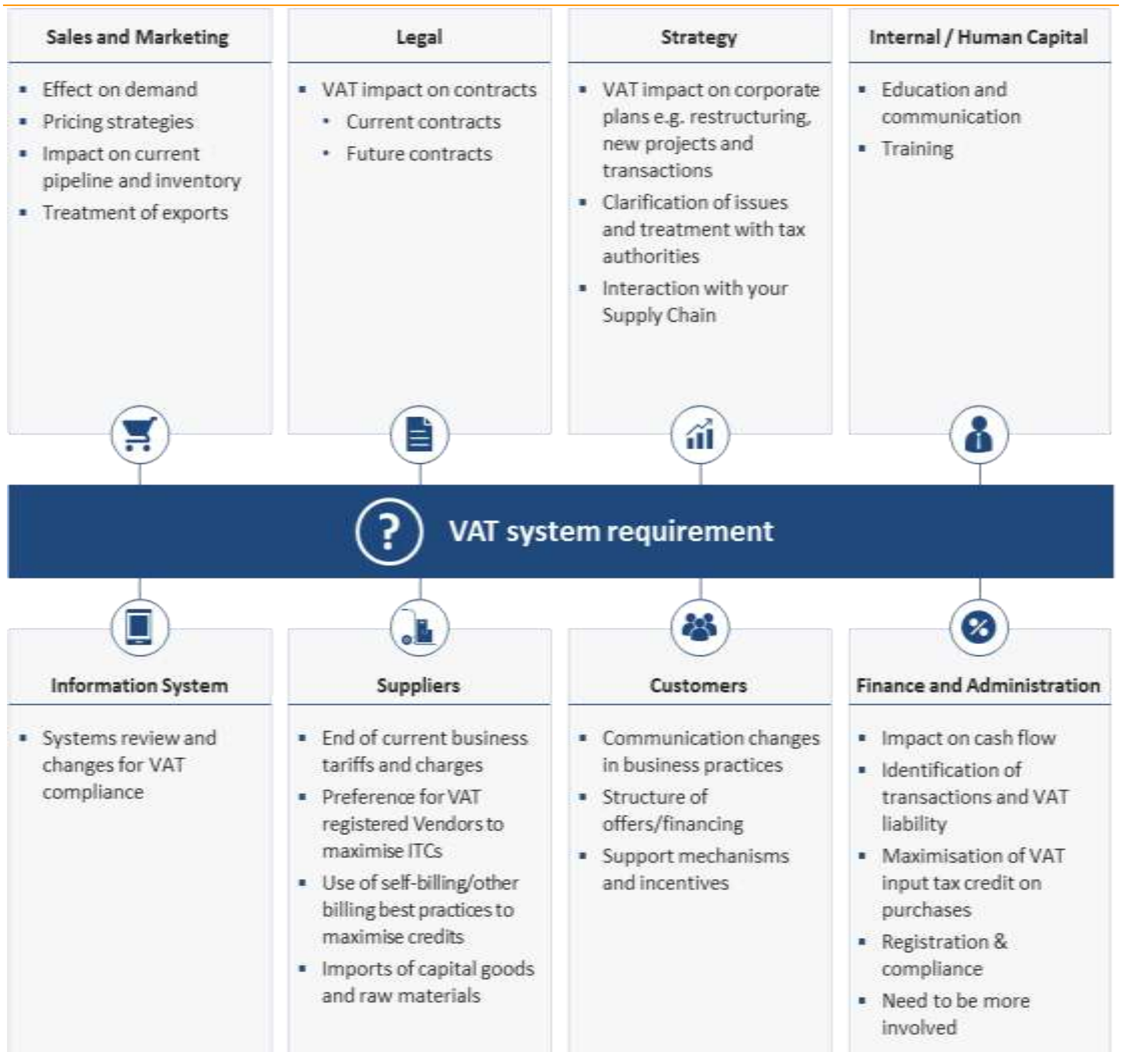
The threshold limit for required VAT registration for businesses has been fixed at annual revenue of over SAR 375,000. Businesses with annual revenue between SAR 187,500 and SAR 375,000 can voluntarily register with the tax authority to avail the benefits under the VAT regime. There will be a few exemptions from VAT such as rent, real estate sales, few medications, airline tickets and school tuition.

The introduction of VAT will lead to hike in prices across commodities, industries and services. However, the impact will be mostly felt on the following industries:

- Consumer and industrial products
- Technology, media and telecommunications
- Financial services
- Real estate

VAT and impact areas in implementation cycle

VAT expected to boost government revenue but will have negative impact on small businesses



Source: Deloitte & Touché (M.E.), The Introduction of VAT in Saudi Arabia – February 2017

Most businesses are expected to pass on VAT to consumers, resulting in a price increase for most goods and services. This will decrease the spending power of consumers and induce them to be more judicious in their spending. Companies will have to take several innovative measures to lessen the impact on their businesses.

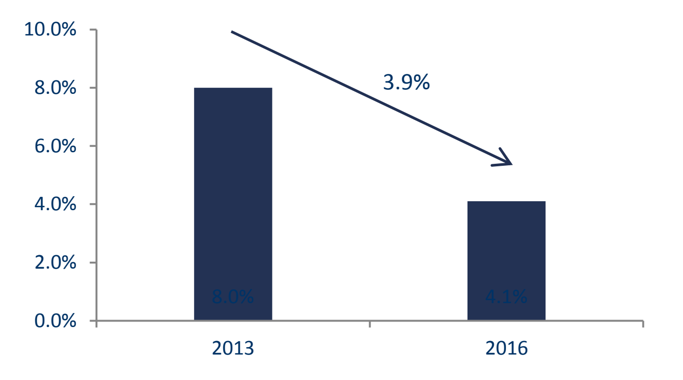
The impact of the VAT levy will be more pronounced on the sale of luxury goods and accessories, the demand for which is expected to drop sharply. Also, we anticipate that small and medium-sized companies will be the hardest hit as they will find it more difficult to adapt and will have to incur additional expenses to ensure regulatory compliance.

On the flip side, the measure will be positive for the country's fiscal health and the economy, as it will help citizens rationalise their consumption habits and decrease the domestic consumption of oil products, indirectly, helping Saudi Arabia increase its oil reserves and exports.

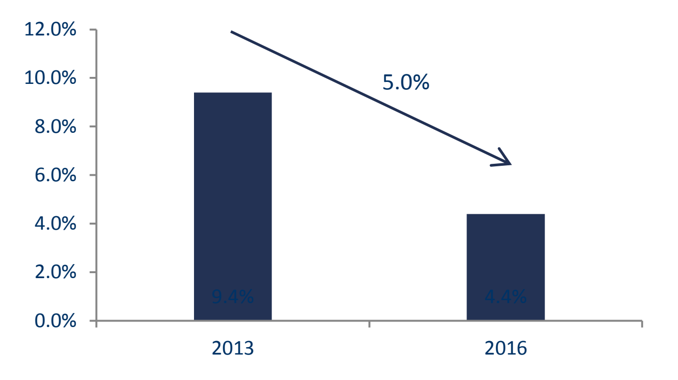
Government committed to subsidy rationalization

In 2015, reeling under low oil prices, which put a strain on the Kingdom's fiscal health (budget gap soared to more than 15% of economic output in 2015), Saudi Arabia decided to rein in fuel and power subsidies, which its citizens had enjoyed since the black gold boom.

Petroleum subsidy (% of GDP)



Energy price subsidy (% of GDP)



Source: Country authorities, IEA, and IMF staff estimates

The Kingdom raised fuel prices in December 2015 and announced plans for further increases as part of a plan to transform the economy and balance the budget by 2020. Also, authorities announced plans to gradually ease out fuel and power subsidies by 2020.

Subsidies on fuel and electricity to be eased out by 2025

Saudi Arabia - recent energy price measures

	Gasoline	Diesel	Electricity	Gas
December 2015	Price of higher-grade gasoline increased by about 50%, to US$0.24 per litre, while regular gasoline increased from US$0.12 to US$0.2 per litre	Diesel prices increased from US$0.07 per litre to US$0.12 per litre for the transportation sector and US$0.09 per litre for the industrial sector.	The authorities announced a reduction in electricity and water subsidies. Electricity tariffs for households increased by 35% on average.	Price of Methane and ethane gas raised from US$0.75 per litre to US$1.25 per litre and to US$1.75 per litre, respectively
July 2010			Increased the average price of electricity sold to non-individual users by over 20%.	

However, the sluggish economy put a spanner on the Kingdom's initial plans and forced authorities to recalibrate their approach. As per the new approach, Saudi Arabia is extending its timeline to cut energy subsidies to 2025, as the government seeks to offset the impact of austerity measures on the stagnating economy.

Whilst the speed of reform has decelerated, it is still firmly moving in the stated direction. As per the new measures, domestic gasoline prices are to reach parity with international levels till 2025 – compared to the previous target of 2020. Also, local diesel prices too will gradually and steadily be increased to 90% of international prices till 2025.

Other prices will be changed as follows:

- Local prices of natural gas and ethane will be raised to 75% of international prices between 2020 and 2021, with the imposition of a price cap in 2021. Prices of liquefied natural gas, including propane and butane, will be raised to 90% of international levels in 2020; the earlier plan was for international parity that year.
- Kerosene and liquefied petroleum gas for households will be 100% linked in 2019. Previously, the target was 2020.
- Jet fuel will be lifted to international levels in 2018, earlier than the previous plan for a gradual rise from 2019 to 2020.
- Other oil liquids used for power generation, such as heavy fuel oil 180-cst and HFO 380-cst, Arab light crude and Arab heavy crude, will be 90% linked by 2025. The old programme set 2020 as the year to achieve 100% parity
- Residential and commercial electricity prices, previously scheduled to reach 100% of international levels this year, will now be raised gradually between 2018 and 2025.
- Industrial electricity prices will now be raised gradually between 2019 and 2025 compared with the earlier plan to reach international levels this year.
- Water prices will also be adjusted upwards.

As part of reforms, on December 31, 2017, Saudi Arabia increased fuel prices. Octane 91 fuel was increased from 75 halalas per litre to SAR 1.37 per litre and 95 octanes from 90 halalas per litre to SAR 2.04 per litre. Diesel for industries and utilities will cost SAR 0.378. The price of diesel for transport remains unchanged at SAR 0.47. Kerosene price also remains unaffected at SAR 0.64. The prices include Value Added Tax (VAT)

Going forward, it is expected that the undertaken measures will be subject to economic developments and would be tweaked as per situational needs, with the government looking to finely balance austerity measures with economic growth.

Government takes proactive measures to protect ordinary Saudis from price inflation

Citizen Account Program to offset the impact of VAT and subsidy cuts on ordinary Saudis

Starting 21 December 2017, to cushion ordinary low- and middle-income Saudi families from the impact of various economic reforms, the Ministry of Labour and Social Development announced Citizen Account Program for more than 13 million beneficiaries. The support is offered through direct cash transfers to beneficiaries. The support compensates for the increase in prices as a result of the correction in electricity and gasoline prices, and the application of VAT on food and beverage commodities. Every three months these allowances will be reviewed to ensure that the amount of the benefit meets the requirements of the households

Further, King Salman issued an order to increase the salaries and allowances of Saudi Arabia's public sector employees and military people from 1 January. Soldiers on duty in Yemen will receive a bonus of SAR 5,000 Saudi, while state employees will get SAR 1,000 a month as the cost of living allowance for one year, as per the royal decree carried by the Saudi Press Agency.

King Salman also ordered an allowance of SAR 500 for pensioners and another payment of SAR 500 for social security beneficiaries. The state raised student allowance by 10% for a year and will bear the cost of VAT for citizens using private health and education services, as per the SPA report. Moreover, the government will pay VAT – not exceeding SAR 850,000 – for the purchase of a first home by Saudi citizens.

For 2018, we believe the Kingdom is committed to fiscal prudence and subsidy rationalisation. However, the pace and intensity of the measure would vary depending on the social and economic climate, as the government seeks to orchestrate a smooth societal and fiscal transition.

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Impact of Reforms On the Economy

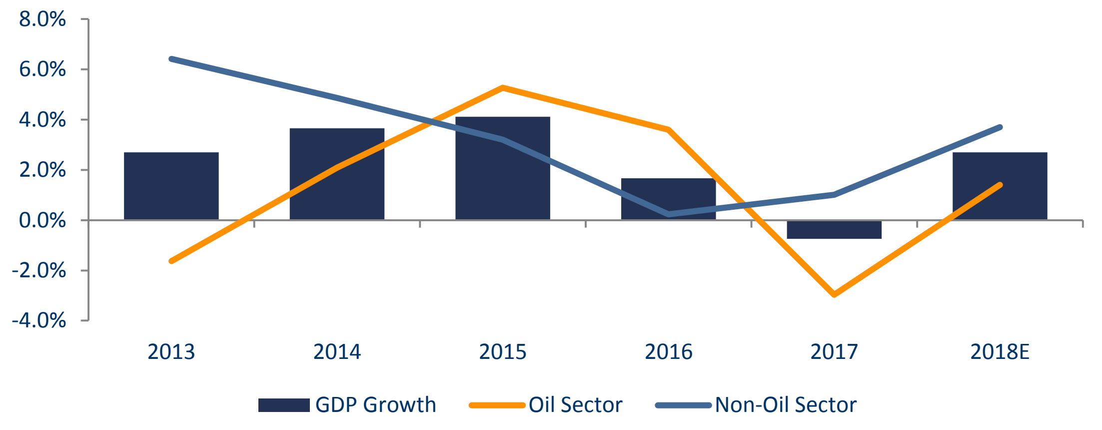
Economy to emerge stronger after reforms

Non-oil sectors spur economy

Saudi Arabia's GDP growth contracted to 0.74% in 2017 from 1.67% in 2016. The slowdown was driven by a 2.97% decline in the oil sector. Non-oil GDP growth accelerated to 1.01% in 2017 from 0.23% in 2016, but failed to compensate for the sluggish oil prices.

In 2018, the government expects real GDP to grow at a 2.7% rate, bolstered by a strong 3.7% non-oil GDP growth rate. Non-oil government revenue is expected to improve substantially following an expansionary fiscal policy, the introduction of VAT and the expat levy. Oil GDP is expected to increase slowly by 1.4% as the government reduces output in line with the OPEC agreement.

Saudi Arabia Real GDP Growth (2013-2018E)



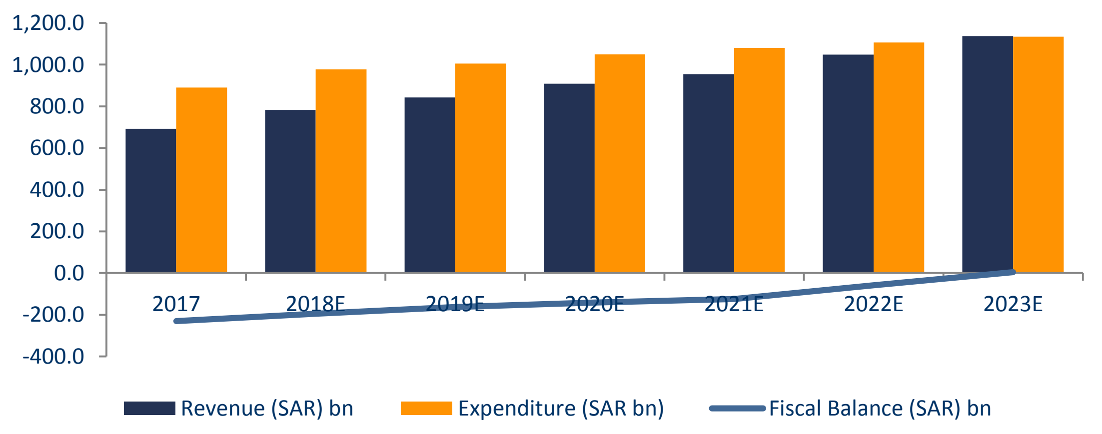
Source: Ministry of Finance, E-Estimate

Fiscal deficit to narrow

Fiscal deficit to narrow; inflation on the rise

Saudi Arabia's fiscal deficit is projected to narrow considerably to SAR 195 bn in 2018, compared with SAR 230 bn in 2017. This is mainly due to an increase in non-oil revenue (SAR 291 bn in 2018, up 13.7% y-o-y) and restraints on non-productive spending. Also, of help would be the positive momentum in oil prices and energy price reforms that could boost oil revenue (SAR 492 bn in 2018, up 11.8% y-o-y).

Revenue expenditure and fiscal deficit estimates until 2023 (SAR bn)



Source: Ministry of Finance, E-Estimate

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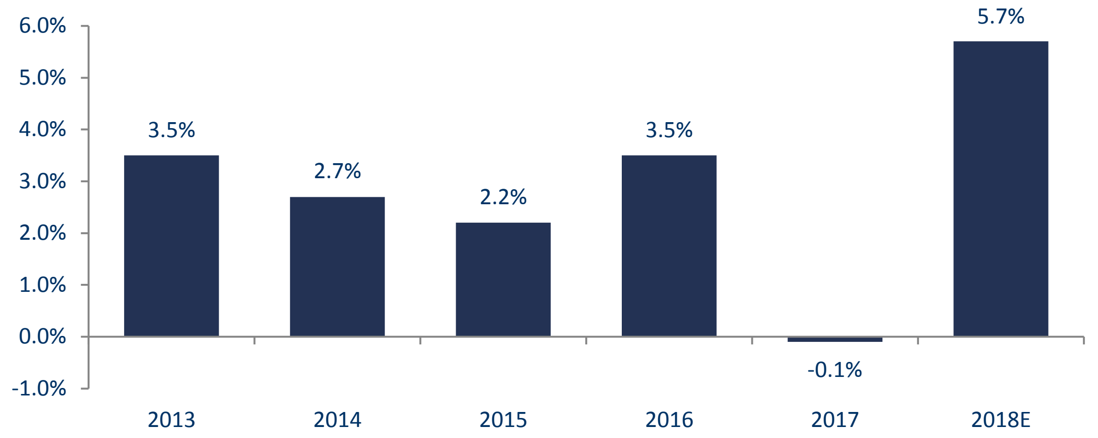
The deficit would be financed by drawing down from the stock of government deposits/forex reserves and domestic and international borrowing. The government is likely to continue with an expansionary budget stance and has extended its target of achieving a budget surplus from the year 2020 to 2023.

Reform measures spike inflation

Saudi Arabia Inflation (2013-2018E)



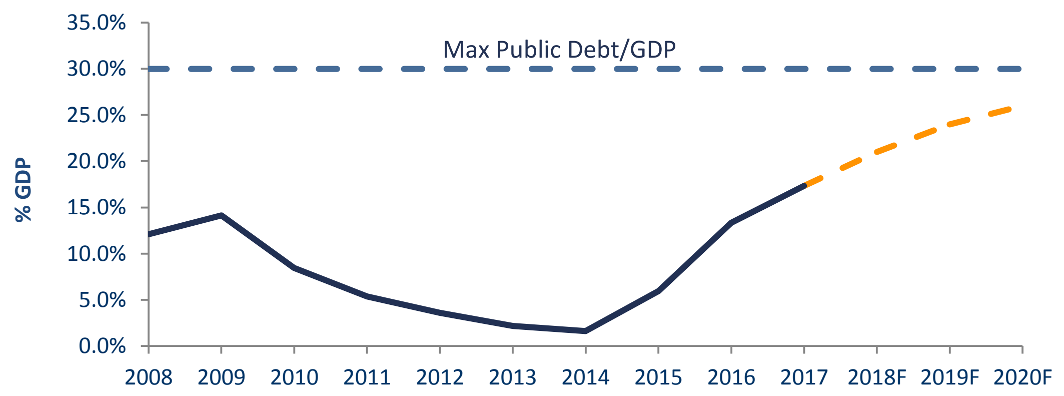
Source: SAMA

The flip side of the economic reforms is expected in price rises. Inflation is set to rise to 5.7% in 2018 from a negative rate of 0.15% last year, mainly due to the implementation of VAT and energy price reforms.

Government Debt

During 2017, the government has raised about SAR 134 bn from international and domestic bonds/Sukuk issuance. These issuance attracted huge demand and were over oversubscribed by about 3-4 times, reflecting investors' confidence in the domestic economy. At the end of 2017, total public debt stood at SAR 438 bn. The government plans to borrow about SAR 117 bn this year, which would increase the public debt to SAR 555 bn by the end of 2018. Ministry of Finance projected that the public debt will increase to SAR 673 bn in 2019 and SAR 749 bn in 2020. The government of Saudi is committed to keeping debt/GDP below 30% over the fiscal balance period.

Saudi Arabia: Public Debt (% GDP)



Source: Haver Analytics, Saudi Ministry of Finance, Emirates NBD Research

Overall 2018 will be the year when economic and monetary reforms will be pressed ahead and the economy is firmly put on the path of fiscal prudence with non-oil sectors the primary growth drivers.

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Financial Market Reforms to Boost Equity Markets

Inclusion in MSCI and FTSE Russell emerging market indices to attract foreign capital inflows

Developing robust capital markets is a key part of the Kingdom's Vision 2030 plan to transform its economy and decrease reliance on oil. It has taken massive strides towards achieving that goal in the past two years. Until mid-2015, foreigners investing in Saudi Arabia's capital market could only do so through swaps, which were restrictive, complicated and expensive. Thereafter, to attract foreign investors and capital, the country's capital markets regulator and stock exchange carried out a series of investor-friendly rule changes. The measures included reforms to enable qualified financial institutions to directly invest in capital markets and simplification of rules to encourage more international institutional investor participation. The capital markets regulator also changed the settlement cycle to T+2, established a delivery-versus-payment model and adopted the Global Industry Classification Standard (GICS).

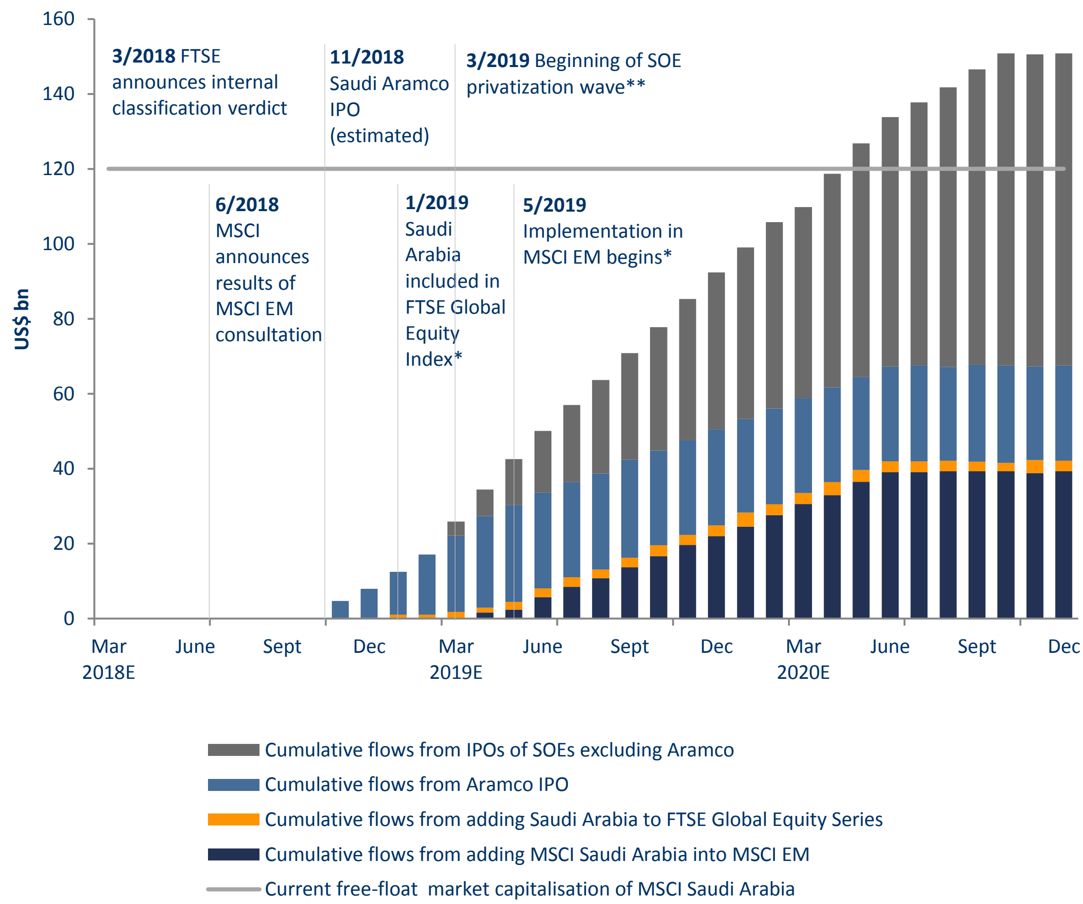
The reforms, along with the strengthening and reinforcement of the corporate governance framework, enabled international index compilers such as MSCI and FTSE to consider the MENA region's largest capital market for inclusion into their emerging market index

In June 2017, MSCI included the Saudi Stock Exchange (Tadawul) in the organisation's watch list and listed it for a potential upgrade in 2018. There seems to be a broad consensus that a decision on the MSCI inclusion will be taken in mid-2018 and addition will follow in mid-2019.

Shortly thereafter, at the end of September 2017, during the International Market Review, FTSE Russell released a statement that said Saudi Arabia will soon meet the criteria to be promoted from unclassified status to a secondary emerging market. FTSE said it would assess upgrading the Saudi market in March 2018.

2018 to be a high octane, action packed year for Saudi Arabian equity market

Equity Market inflows to reach US$144.5 bn by December 2020



Source: State Street Global Advisors, Transforming Saudi Arabia's Capital Markets – October 2017

More than US$1.5 bn in assets are benchmarked by money managers to the MSCI Emerging Markets index family If Saudi Arabia's stocks are reclassified by MSCI, the Kingdom's equity market could receive inflows of about $38 bn from passive funds that track that benchmark alone, according to State Street Global Advisors. Inclusion in FTSE Russell could lead to another US$4.4 bn in flows to the country's equities market, assuming it would represent 2.7% of the index, as per Mohamad Al Hajj, an equities strategist at the research arm of EFG-Hermes Holding in Dubai.

Possible inclusion in MSCI and FTSE could lead to inflows of several billions of dollars into Tadawul, not only through passive funds but also from active funds that track these indices. The size of inflows will depend on the absolute value of funds tracking MSCI and FTSE at the time of addition and Tadawul market capitalisation. Saudi Aramco's potential IPO could increase the weightage of Saudi Arabia in these indices as the company's market capitalisation could be more than a trillion dollars.

Saudi Aramco IPO

The Saudi government announced that the Kingdom had changed Saudi Aramco's status to a joint stock company as of 1 January 2018. The announcement was made as the Kingdom prepares to sell a stake of less than 5% of state-owned Aramco. It is expected to be the world's largest ever IPO. Saudi Aramco could be listed on the London, New York and Hong Kong stock exchanges. However, Tadawul is pushing to be the "exclusive" venue for the initial public offering of Aramco.

Opening of NOMU for SME firms

Saudi Arabia recently launched a parallel market, Nomu, for small and medium enterprises with fewer listing requirements so that it serves as an alternative market for companies to go public. From 1 January 2018, foreign investors were allowed to participate in the IPO of smaller companies in the Kingdom. This decision by the government will help the country turn its stock market into a gateway for a rise in investment from foreign investors. SMEs will be able to expand and develop their businesses, thus contributing to economic growth and sustainability.

Adopting International Financial Reporting Standards (IFRS)

Saudi Arabia has adopted IFRS accounting standard in two phases. In the first phase, all listed companies, banks and insurance companies were required to be IFRS compliant by 1 January 2017 and in the second phase all unlisted companies has to transition to IFRS for SME framework from 1 January 2018. Adoption of IFRS accounting standard will enhance quality reporting, transparency and comparability and is expected to increase foreign investment in the Saudi markets.

Entry for qualified investors

On January 10, 2018, Saudi Arabia's Capital Market Authority announced that it will reduce the minimum assets under management requirement for qualified foreign institutions (QFIs) and let foreign investors to own up to 49% of listed securities. The new amendments include elimination of CMA's review and approval of QFIs qualification, Assets under management or custody requirement for QFIs will be lower from US$ 1 bn to US$ 500 mn.

In another important measure to make market more efficient, liquid and secure, Saudi Stock Exchange (Tadawul) announced that it will be updating Independent custody model (ICM), which will develop QFIs access to the market and will improve the flexibility in trading limits for ICM clients. Tadawul will also come up with a new optional model to allow asset managers to aggregate orders of managed assets – discretionary portfolios and investment funds.

We expect the year to mark the fructification of the reforms undertaken in Saudi Financial sector and herald its entry into the global financial high table.

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Progressive Social Reforms to Unlock Latent Tourism and Private Sector Potential

As part of Vision 2030, Saudi Arabia is moving forward by opening up its society and liberalising its strict laws. This year will see a progressive move towards a more liberal and open society. Major changes are expected.

More entertainment avenues as cinemas set for return

After a 35-year ban, the government indicated that it will begin granting commercial movie theatre licences in 2018. By March 2018, it expects opening the doors of the first cinema hall. As per AMC CEO Adam Aron, the movie market in the Kingdom of 30 mn people could be worth US$1 bn. The lucrative opportunity is being eyed by various international and regional chains.

Women will be allowed to drive …

Following a royal decree in September 2017, it was announced that the long-standing ban on women driving will be lifted in June 2018. The move is expected to spur growth, as it will empower women and enable them to make a bigger contribution to the Saudi economy. This will also enable the country to achieve its 2030 target of having 30% women active in the workforce, up from 22% currently. Vision 2030 aims to lift that to 30%. Moreover, getting more women into the workforce is also the key to achieving the government's goal of generating 65% of the GDP from the private sector.

Women empowerment and tourism friendly measures to boost economy

...and watch sporting events and concerts

Customarily, Saudi men and women are separated in public places. However, that restriction is slowly but steadily being relaxed. In October 2017, the General Sports Authority, the country's governing body for sports, announced that three of the country's biggest stadiums will begin "accommodating families" in early 2018. Men and women were able to sit together in music concerts and events. The three earmarked stadiums in Riyadh, Jeddah and Dammam will be ready to accommodate families from early 2018. The authority added that restaurants, cafes and video screens would be set up inside the venues.

Welcome mat to be laid out for foreign tourists

Starting 2018, tourists will be able to visit Saudi Arabia for the first time. The Saudi Tourism and National Heritage Commission announced that the Kingdom would issue its first tourist visas in 2018. Previously, visas were restricted to people travelling to the country for work or to visit its holy sites. The initiative is in line with the Kingdom's ambitious plans to grow its tourism industry. To boost tourism, the Kingdom has already announced several projects, including building a series of resorts on about 100 miles of the Red Sea's sandy coastline. The open door to foreign tourists will go a long way in helping the Kingdom achieve its target of 30 mn visitors a year by 2030, up from 18 mn in 2016.

NEOM economic zone project, an economic hub in making

In October 2017, Saudi Arabia unveiled NEOM, a megacity project bordering Jordan and Egypt. The new city will be spread over 26,500 sq. km, along with a 468 km waterfront. It will have its own tax and labour laws and an autonomous judicial system. The project will be backed by an investment of more than US$500 bn from Public Investment Fund and international investors. It is expected to contribute about US$100 bn by 2030 to the Kingdom's GDP and serve as an economic hub for the energy, transport, biotech, food, technological and digital sciences, advanced manufacturing and media production sectors.

We expect the course set for the liberalisation of society in Vision 2030 to continue being implemented in 2018 with more progressive measures (taken or announced).

January 29, 2018

Top Sectoral and Stock Ideas for 2018

In light of our expectations on how the economy will pan out in the coming year, and the contours of the government's stated economic vision, we expect Financials, Telecom, Chemicals, Food and Cement to be the top-performing sectors in the year. The following is a detailed thesis on why we opine the sectors are sound investment bets:

Banks

- We expect the economy to pick up in 2018, which should help stabilise the financial sector and lower the current NPA levels. The year would witness the stabilisation of financial performances in Saudi banks after two years of significant pressure.
- On-going strategic initiatives to implement Saudi Vision 2030 are expected to drive growth in private sector lending.
- Improved loan growth and lower cost of lending are also forecast to raise NIMs, boosting the bottom line and enabling banks to pay higher dividends.
- Our top picks in the sector are Al Rajhi Bank, Bank Albilad and Alinma Bank.

Chemicals

- Vision 2030 has emphasised the focus on petrochemicals as one of the major future economic drivers.
- Global demand on chemical products is expected to double by 2030, with Saudi chemical companies likely to be major gainers due to their low cost of production.
- The government is expected to further incentivise the sector and give it a leg up.
- Our top picks in the sector are SABIC, YANSAB, SAFCO, TASNEE, SIIG, Saudi Kayan and Advanced Petrochemical.

Telecom

- The sector has been beaten down by the market on account of negative news reports.
- While it is witnessing challenging times, we believe the sector has reached its trough and is ripe for a bounce back.
- The sector is available at very cheap valuation.
- The telecom sector is considered one of the pillars of Vision 2030, with telecom infrastructure, broadband, creativity in advanced technologies, and investment in the digital economy being the key focus areas. The government's push will help mitigate some of the recent negative developments in the sector.
- Our top picks in the sector are Saudi Telecom and Zain KSA.

Insurance

- The mandatory health insurance announced by the Council of Cooperative Health (CCHI) for all Saudi employees remains a key growth driver for the Saudi health insurance sector.
- The industry is ripe for consolidation, which is expected to benefit larger players such as Bupa.
- Our top pick in the sector is Bupa Arabia, due to the following:
    - The company continues to be the dominant insurance player in Saudi Arabia and has witnessed consistent expansion in market share over the past few years.

Food

- An expected increase in consumer spending owing to a rise in salaries and allowance is anticipated to boost the sector.
- Our top pick in the sector is Almarai, due to the following:
    - Almarai is the Middle East's largest dairy producer and among the most trusted brands in the region.
    - If the current geo-political tensions between Saudi Arabia and Qatar ease in the coming year it will allow Almarai in making a comeback in an important market.

Cement

- Bad news in the sector has already been factored in, due to which companies are trading at attractive valuations. We believe the worst is over for the sector, and it is due for a rebound.
- The housing ministry is set to undertake various initiatives to grow the sector, and it is likely to witness improvement in construction activity, led by recovery in oil prices and the economy in general.
- If the current geo-political concerns in the Gulf states ease in the coming year, it will provide a fillip to the sector.
- The sector is a good dividend play.
- Our top pick in the sector is Southern Province Cement.

Summary Valuation Table

S.No	Company	Sector	TASI Code	CMP (SAR)	MCAP (SAR bn)	EV (SAR bn)	2018E PE	2018E PB	2018E EV Sales	2018E EV EBITDA	2018E ROE (%)	2018E DY (%)
1	Saudi Telecom	Telecom	7010	69.30	138.2	126.7	13.8	2.1	2.4	6.7	15.9	6.0
2	Zain KSA	Telecom	7030	7.18	4.2	14.3	27.6	0.7	1.8	5.3	3.8	-
3	Bupa Arabia	Insurance	8210	88.40	7.1	6.9	11.7	2.5	0.8	-	22.2	3.5
4	Al Rajhi	Banks	1120	69.30	112.4	-	11.6	1.9	-	-	16.8	5.2
5	Bank AlBilad	Banks	1140	22.14	13.6	-	12.8	-	-	-	11.8	3.1
6	Alinma Bank	Banks	1150	20.16	30.1	-	13.9	1.4	-	-	10.3	3.8
7	SABIC	Chemicals	2010	104.60	312.2	357.2	14.5	1.8	2.3	7.5	12.3	4.5
8	YANSAB	Chemicals	2290	62.30	35.1	33.9	14.9	2.5	4.5	9.8	12.7	6.0
9	SAFCO	Chemicals	2020	69.60	29.0	28.8	21.2	3.9	8.6	16.2	17.1	4.3
10	Saudi Kayan	Chemicals	2350	11.08	16.6	39.1	16.3	1.1	3.6	8.9	6.6	-
11	TASNEE	Chemicals	2060	17.26	11.5	29.3	19.0	-	2.7	-	-	-
12	ADVANCED	Chemicals	2330	42.55	8.3	8.9	11.8	2.6	3.7	10.3	21.1	6.9
13	SIIG	Chemicals	2250	21.00	9.4	22.5	9.2	0.8	3.1	8.2	10.0	4.9
14	Southern Cement	Cement	3050	49.95	7.0	7.5	15.6	2.1	6.2	12.8	14.7	5.7
15	Almarai	Food	2280	52.60	52.5	64.3	22.8	3.3	4.2	14.8	15.8	1.7

Source: Bloomberg, FALCOM Research

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