



Currently stable, but trouble on the horizon

In spite of the falling oil price, the accession of the new king and the military intervention in Yemen, the political and economic situation in Saudi Arabia is stable. Enormous financial resources and oil reserves serve as a satisfactory buffer against lower oil revenues. The accession of the new king in January 2015 followed a carefully devised plan and is not expected to lead to any change in political direction. Saudi Arabia is expected to continue positioning itself in the ongoing power struggle in the region and continue its expansionary economic policies. The new king naming his nephew the crown prince puts a generational shift sooner in the order of succession. This raises the risk of an internal power struggle, but also the hopes of political modernisation. At the current oil prices, Saudi Arabia will be forced to decrease public spending and diversify its revenues within a couple of years. A decrease in subsidies and government stimulus packages to counteract discontent increases the risk of social unrest in the country. The Saudi economy is strong in the short term, but the country will need to diversify its economy and cut public spending within a couple of years in order to make its economic growth long lived. Over the past decade, Saudi Arabia has made certain economic reforms which gradually open the kingdom up to trade and investments and the country is a large export market for Swedish companies.

THE COUNTRY'S STRENGTHS AND WEAKNESSES

Strengths

- The world's largest oil exporter with enormous oil and gas reserves.
- Very good buffer in the form of large international reserves, strong export revenues and low debt.
- Well capitalised and liquid banking sector.

Weaknesses

- The country is totally dependent on the oil and gas sector, which generates few jobs.
- The issue of succession could lead to both political and economic instability.
- A complex business environment and weak transparency of companies and public institutions which complicates the risk assessment.

Unchanged policy

EKN categorises Saudi Arabia in country risk category 2 – an assessment made in collaboration with the OECD. Saudi Arabia has been placed in this country risk category since 2005 when the country was upgraded one level. EKN has a standard risk assessment policy for all buyer categories. For sovereign risk and other public risks, the policy is justified by the government's strong financial position. The banking sector is solid and has good financial ratios. Lack of transparency in terms of authorities and ministries as well as in many companies limits access to financial information, which can create problems for credit assessments.

WHAT MIGHT CAUSE A CHANGE IN THE COUNTRY POLICY?

The policy may be made less restrictive in the event of

- Increased diversification of the economy.
- Improved business environment via stronger institutional capacity and increased transparency.

The policy may be made more restrictive in the event of

- Political unrest in the country and increased regional instability.
- Substantially worse economic trend due to a low oil price for a long period of time.

EKN'S EXPOSURE AND EXPERIENCE

Delays common, but few indemnifications

In the period between 2010 and 2014, EKN issued guarantees for 124 transactions totalling SEK 11.3 billion for Swedish companies exporting to Saudi Arabia. EKN's payment experience mainly comes from the building and construction sector, where payment delays are common. The reason for the delays appears to be poor payment practices, but there are also cases where the buyer, in turn, is waiting for payment from clients in the public sector and delays payment as a result.

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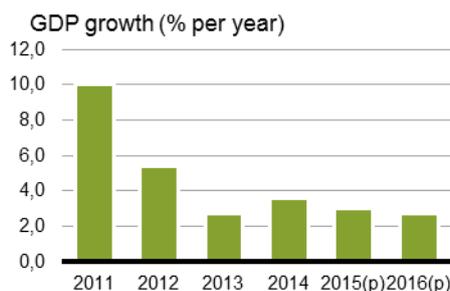
Younger generation increasingly in the spotlight

The prospects of the Saudi royal family remaining in power are premised on the financial capacity provided by oil and on them being able to maintain a unified stance regarding the succession issue. Politics is a combination of carrot and stick, where the enormous wealth paves the way for generous government spending to curb demands for reform while opposition is suppressed. There is little transparency with respect to the division of powers and decision-making processes. Salman, born in 1935, ascended to the throne in January 2015 following the death of his brother Abdullah. The succession issue is constantly on the agenda, because the kings have thus far been selected from among the older sons of the country's founders. Once power is transferred to the next generation, there could be major tensions and the legitimacy of the royal family could be called into question. The time for the transfer of power to the third generation is approaching, given that King Salman appointed his nephew the crown prince and his son the deputy crown prince in 2015. The new king has clearly demonstrated that he is capable of contesting decisions made by his predecessor, but there is very little indication of any change in political direction during the current king's reign.

Saudi Arabia's actions in the conflict in Yemen are a sign of a power struggle in the region. Iran is accused of supporting the rebels in Yemen and Saudi Arabia has responded with airstrikes in Yemeni territory. Riyadh is concerned over the increasing influence of Iran in Iraq and the brighter prospects of Iran reaching an agreement on the nuclear power issues with the US and EU. The most significant political risks a couple years down the road are the succession issue along with external factors, such as the oil price and the political developments in Iran, Iraq, Syria and Yemen, which are destabilising factors for the royal family.

Lower oil prices led to new strategy

Saudi Arabia is the world's largest oil exporter and has enormous oil and gas reserves. Revenue from the oil sector is vital for the country's growth and accounts for 90% of government revenue. The sharp oil price decline in the latter half of 2014 has been an eye-opener for Saudi Arabia and led the country to switch strategies. The country has traditionally influenced the oil price by opening and closing its oil taps, a policy which was replaced in autumn 2014 by attempts to retain market shares. A lower oil price eliminates investments in more expensive forms of production such as North American shale oil, but is also a drain on the country's own economy. Lower revenues from oil exports and continuing high spending are forecast to send a budget that was balanced in 2014 careening into a deficit estimated at 15% in 2015. To balance the budget in 2016, the oil price needs to go up to closer to USD 100 per barrel, which is an unrealistic scenario. However, Saudi Arabia has low debt, its net assets exceed its GDP and it has sizeable international reserves, approximately three years of imports of goods and services, which serves as a secure



buffer in the coming years. Growth in the private sector is driven by government stimulus packages and publicly funded projects. GDP growth is estimated to come in at around 3% per year in 2015 and 2016. The main purpose of the country's expansionary spending policies has been to create jobs and support growth in the non-oil-related sector of the economy. As a result of the increasing young population, GDP growth should exceed an estimated 4% to prevent unemployment from increasing.

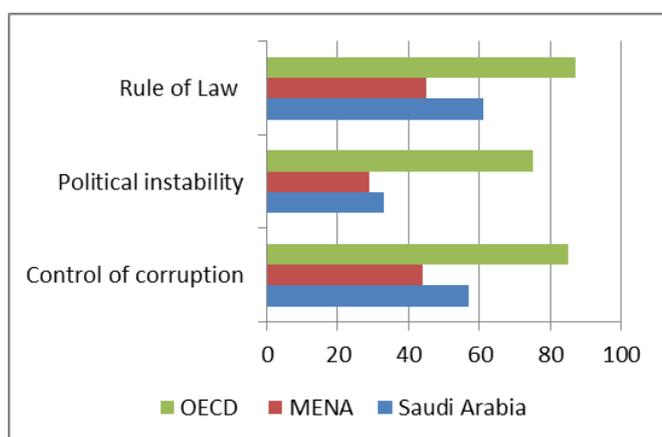
The country's current account balance will go from a high surplus to a deficit in 2015 due to the lower oil price. However, it is expected to get back to a small surplus already in 2016. The Saudi economy is strong in the short term with its enormous financial resources, but the country will need to diversify its economy and cut public spending within a couple of years in order to make its economic growth long lived.

BUSINESS ENVIRONMENT

Weak transparency of legal system

Saudi Arabia's business climate was generally ranked high by the World Bank. However, there are weaknesses, such as the enforcement of judicial decisions and the management of insolvencies, mainly due to legal proceedings taking a very long time and the outcome being uncertain.

Widespread bureaucracy, corruption and a lack of transparency in the legal system serve as risks for foreign parties. The World Bank's Doing Business Index ranks Saudi Arabia 49th out of 189 countries in its most recent rankings. EKN has conducted a review of the legal structures for businesses and accounting regulations in Saudi Arabia. The summary shows that only two of the



six legal structures are required to have audited financial statements and publish them by submitting them to the ministry of commerce. This can limit the availability of financial information. EKN's experiences regarding the quality of information also vary. It is often difficult to get hold of financial information and in many cases it has proven difficult to interpret locally audited financial statements.

The currency, the riyal, is pegged to the US Dollar. The exchange rate against the US dollar has been the same since 1986. The fixed exchange rate has been important for market confidence and consequently for foreign investment in the country. There are not any restrictions on payments or transfers of import or export transactions. The currency can be assessed by EKN in transactions financed in local currency. The banking sector is well-capitalised, has sizeable liquid assets and low levels of bad loans. EKN estimates that the banking system has the capacity to overcome the current situation of relatively low oil prices.

EKN's payment experience mainly comes from the building and construction sector, where delays are common. Often two to three months but even up to two years. However, there have not been any indemnifications in these sectors. The reason for the delays appears to be poor payment practices, but cases also occur where the buyer, in turn, is waiting for payment from clients in the public sector and therefore delays payment. There have been problems in relation to processing bills of exchange in certain cases.