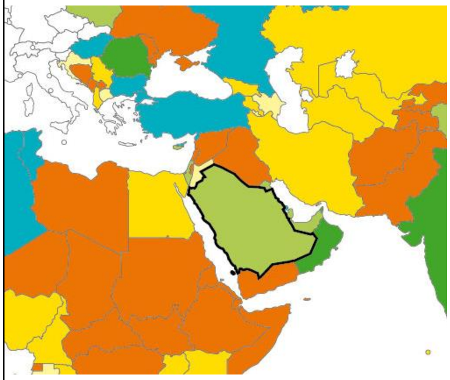
COUNTRY RISK ANALYSIS

Saudi Arabia

DIN SÄKERHET I EXPORTAFFÄRER ekn



COUNTRY RISK CATEGORY

2/7

The country risk categories range from 0 to 7. The lower the number the better the credit rating the country has.

0 1 2 3 4 5 6 7

EKN'S OUTSTANDING GUARANTEES TO THE COUNTRY

SHORT-TERM TRANSACTIONS: SEK 43 MILLION

MEDIUM AND LONG-TERM TRANSACTIONS: SEK 2,737 MILLION

DATE

20/10/2016

Adjustment to lower oil price started

King Salman's accession to the throne in 2015 went according to a carefully devised plan and prompted certain changes in Saudi foreign policy. Decision-making has been handed over to younger-generation princes, which has resulted in more risks being taken as well as direct intervention in regional conflicts. The country's involvement in conflicts poses risks for the royal family, but there are no indications of any threats to its standing.

Saudi Arabia's economy is robust in the short term. Considerable financial resources and oil reserves serve as a buffer against lower oil revenues. In the long term, the economy needs to be diversified and public spending needs to be cut if the economy is to be sustainable. The new economic plan *Vision 2030* will spur economic reforms that open up the kingdom for more trade and investment. Saudi Arabia is a major export market for Swedish companies and is a country to which EKN has high exposure.

THE COUNTRY'S STRENGTHS AND WEAKNESSES

Strengths

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

Weaknesses

- The country is dependent on the oil and gas sector, which generates few jobs.
- Lower international reserves and higher debt in coming years.
- Weak transparency of companies and public institutions.

EKN'S POLICY

Low country risk and unchanged country 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 notch. EKN has a normal risk assessment policy for all buyer categories. For sovereign risk and other public risks, the policy is motivated by the government's strong financial position. A lack of transparency of government authorities and other public bodies as well as limited access to financial information of companies cause problems in 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.
- An improvement in the business environment thanks to stronger institutions and increased transparency.

The policy may be made more restrictive in the event of

- Political unrest in the country and increased regional instability.
- Worse economic performance due to low oil prices for a long period of time.

EKN'S EXPOSURE AND EXPERIENCE

Delays common, but few indemnifications

In the period between 2011 and 2015, EKN issued guarantees for 119 transactions totalling SEK 11.3 billion for Swedish companies exporting to Saudi Arabia. EKN's payment experience is mainly from the construction sector, where payment delays are common. These problems have risen recently due to the increasingly strained public finances. Buyers are waiting for payment from public sector clients and are in turn delaying payment to foreign suppliers. For supplier credits, there have been many cases where local promissory notes or bills of exchange have proven to be effective in the event of payment problems.

COUNTRY ANALYST

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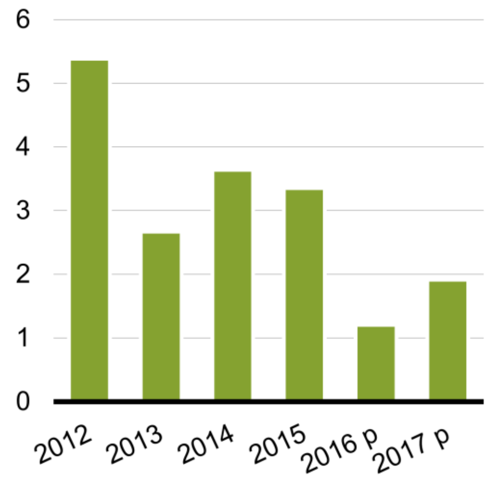
Economic diversification possible in the long term

The accession of the new king in 2015 followed a carefully devised plan and more power has been given to a younger generation of princes. Saudi Arabia continues to jostle for position in the power struggle in the region, especially with Iran, whose increased influence and brighter economic outlook following the easing of the sanctions have the Saudi royal family concerned. Saudi Arabia’s involvement in regional conflicts in the Middle East poses geopolitical risks for the royal family, although there are no indications of any threats to its status at this time. Individual acts of terrorism will continue, but Saudi Arabia’s security apparatus should be able to limit the attacks to a small scale. It is unlikely that they will pose a serious threat to companies and the oil sector. Saudi Arabia will most likely now be forced to exercise greater restraint in Yemen and Syria because of its strained public finances.

Saudi Arabia is the world's largest oil exporter and has large oil and gas reserves. The country has historically tried to keep the oil price high by controlling the supply of oil. This policy was replaced in 2014 with one geared toward attempting to retain market shares. The continuing high Saudi oil production has helped keep oil prices low. Oil revenue, which accounts for the majority of government revenue, has been cut in half. At the current oil price, Saudi Arabia will be forced to cut public spending and diversify its revenue to sustain its economic performance. Growth is forecast to fall to around one per cent this year. The growth rate is estimated to recover to two per cent within a couple years as the fiscal austerity is eased.

GDP GROWTH (% PER YEAR)



Growth is on the decline this year. Data: IMF

Saudi Arabia has now followed in the footsteps of the other countries in the region that have made fiscal reforms. Deputy Crown Prince Mohammad bin Salman recently launched the first of three five-year plans intended to achieve the objectives of *Vision 2030*. The plan aims to reduce the country’s oil dependence, create private sector employment and achieve a balanced budget within five years. The plan is more ambitious than previous development plans, although the targets are too ambitious and the programme is missing details in terms of implementation. Saudi Arabia’s economic diversification is a process that will take decades, but this is a step in the right direction and signals a change. The country will be forced to draw on its financial assets and step up borrowing until these initiatives bear fruit.

The budget deficit will remain high and international reserves will decrease in spite of fiscal austerity. The budget deficit is financed by a combination of reducing government deposits in central bank and increased borrowing, both domestically and internationally. Saudi Arabia has low debt, its net assets exceed its GDP and it has sizeable international reserves, corresponding to nearly three years of imports of goods and services, which is a sufficient buffer in the coming years. The currency is expected to remain pegged to the US dollar at a fixed exchange rate in consideration of its significance for economic stability. The country’s currency, the rial, can be considered by EKN in export transactions financed in local currency.

BUSINESS ENVIRONMENT

Stable banks, weak transparency in legal system

The Saudi banking sector has the capacity to withstand the current difficult situation of low oil price and a harsher economic climate. Banking sector deposits have fallen, but the capital adequacy ratio is high, the share of non-preforming loans is low and the banks are generally well equipped to withstand credit losses. The liquidity support the banking sector receives from the Saudi central bank should also make the situation easier to handle.

The business climate in Saudi Arabia is ranked above average for the Middle East and North Africa, but worse than most other countries on the Arabian Peninsula. The World Bank's Doing Business Index ranks Saudi Arabia 82nd out of 189 countries. One of the aims of *Vision 2030* is to improve this ranking in order to attract more investment. The country’s primary weaknesses are 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.

EKN's payment experience mainly comes from the construction sector, where payment delays are common. Arrears are usually paid in the end and few indemnifications have been paid in these sectors. The reason for the delays appears to be poor payment practices, but there are also cases where the buyer is waiting for payment from clients in the public sector and therefore delays payment.

Access to financial information about Saudi companies is limited. Only two out of six company legal structures are required to audit and publish their financial statements. EKN's experience regarding the quality of information varies. It is often difficult to get hold of financial information and in many cases it has proven difficult to interpret locally audited financial statements.

BUSINESS ENVIRONMENT
Ranking from 0 (worst) to 100 (best)