Monthly monetary indicators
April bank lending look sanguine, SAMA draws on foreign deposits

- April private sector credit growth highest since August
- Central bank drawing down foreign bank deposits to finance spending
- Continued decline in deposits due to foreign currency - not customer - deposits
- Broad money supply growth of 2.1% slowest since 1999, turnaround expected

Private sector credit growth looks to be taking a modest yet healthy track toward recovery according to the latest central bank data, supporting our forecasts for credit growth of 8% in 2010. The Saudi Arabian Monetary Agency’s (SAMA) monthly bulletin released on Sunday, shows claims on the private sector by Saudi banks expanded by an annual 3.6% in April to SR750.63 billion, the highest rate of growth since August. A project finance pipeline of greater than $44 billion this year in power, water, airport infrastructure, energy and petrochemical sectors is likely to support improvements of credit growth for the remainder of the year. Banks, however, remain susceptible to risk aversion.

In April, month-on-month private sector credit growth accelerated to 0.65% from 0.49% in March, while claims on the public sector eased 2.9% after expanding more than 15% in February and March. The April monthly rise included a 0.4% increase in private sector loans, advances and overdrafts, in addition to a 3% rise in private security investments (both local and international). While credit growth is likely to fluctuate in the summer months, we expect similar rates of growth in the second half of 2010 to support our annual growth forecast.

![Private sector credit growth slowly picks up](chart.png)

Source: SAMA
Subdued bank lending has prompted companies to draw on their cash positions to finance working capital needs. Private sector firms began a process of de-leveraging in 2009 and we expect they will begin to move away from these policies later this year. Bank deposits fell in April for a fourth month, according to SAMA data, declining to SR911.87 billion, off 3% from year-end 2009 levels. There has not, however, been any noticeable drop in customer deposits. Rather the low-interest-rate environment is compelling businesses and individuals to shift funds from interest-bearing time and savings deposits into non-interest bearing demand deposits, from which capital can be deployed more quickly.

While demand deposits rose 5.8% between December and April, time and savings deposits eased 4.9%. Banks, being awash with liquidity, are not adopting an aggressive attitude toward building deposits. As of April, the loan-to-deposit ratio for banks was 82%, up from 81% in March.

The main driver of lower overall deposits, then, was falling foreign currency for both businesses and government entities, which dropped 22.6% in the first four months of the year, including a 5% decline in April due mainly to currency fluctuations and businesses reducing their foreign currency holdings. Letters of credit deposits, moreover, witnessed a 19% month-on-month decline in April, due to lower volumes; fewer new LCs were opened to finance imports of motor vehicles, machinery and food, for instance.

Still, foreign trade flows continue to improve due to greater domestic demand in Asia as well as a pick up in domestic demand in the kingdom. New LCs signed to finance private sector imports rose 22.9% in April from the year earlier. LCs posted sharp year-on-year drops, often exceeding 30%, for much of 2009 due to a slowdown in domestic activity. But they have consistently risen since November of last year, including a peak 54% jump in March, which we believe bodes well for overall foreign trade expectations for 2010.

**Guarded recovery**

The government continues to take the role as primary financier for strategic Saudi projects as private sector firms linger on the sidelines. In April, central bank foreign assets declined month on month for the first time since September, as the SAMA drew down deposits in banks abroad by 7.5%, or SR23.9 billion, over the month. High oil prices, which averaged above $80 a barrel in March and April, have enabled SAMA to quickly replenish its net foreign asset holdings to SR1.55 trillion, the highest level since February 2009, although still off a peak of SR1.66 trillion in November of 2008.
SAMA had built up its deposits with banks abroad throughout the latter part of last year as oil prices recovered, its primary goal to keep funds in liquid form to support stimulatory state spending. While public spending will continue to remain high, we still expect Saudi Arabia to post a small fiscal surplus in 2010, with risks to the downside should oil prices hold within the $55-$65 dollar range for a prolonged period.

That the recovery is guarded is evident in money supply data. In April, annual growth of broad money (M3) grew 2.6% to SR1 trillion, the slowest rate of growth since 1999. For comparison purposes, money supply growth peaked above 21% in mid 2008, and throughout 2009 remained above 10%. We regard this persistent decline in money supply growth as a byproduct of the sluggish lending atmosphere and expect that in the coming months, as loan growth resumes, we could see a marginal improvement in money supply numbers. Money supply is more of a function of lower borrowing trends that have accumulated, and there is a lag effect.

In the meantime, money supply will not be a factor spurring inflation, which rose in April to 4.9%, the fastest pace since last June, stemming from a 5.1% rise in food and beverage costs and a 9.6% acceleration in the rent and utilities prices. Rental index inflation has fallen consistently in the last four months and is now at its lowest level since August 2007. Food prices, by contrast, have picked up pace, registering their fastest year-on-year growth in more than a year in April. Monetary policy actions are not presently the solution to addressing price pressures in the domestic economy, with inflation stemming more from supply bottlenecks.
Disclosure appendix

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