

Kingdom of Saudi Arabia
Saudi Arabian Monetary Agency
Research and Statistics Department



Economic Developments
Second Quarter of 2004

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Latest monetary, banking and financial data of SAMA's Quarterly Statistical Bulletin for the Second Quarter of 2004 indicate the prospect for continued growth of the Saudi economy during the second quarter of 2004. Money supply and bank deposits increased; bank claims on the government and private sectors grew; the upward trend of the Saudi Stock Exchange's performance was enhanced; stability of the Riyal's exchange rate and domestic prices continued to be maintained; crude oil prices in world markets continued to rise. Some economic and banking regulatory and legislative decisions and circulars, aimed at invigorating the banking business and boosting the growth of the domestic economy, were also issued during the quarter.

First: Monetary Developments

Broad money (M3) rose by 2.9 percent (Rls 12.5 billion) to Rls 441.9 billion during the second quarter of 2004 compared to an increase of 4.3 percent (Rls 17.6 billion) during the first quarter of the same year.

The rise in M3 was largely accounted for by bank deposits, with a share of 97.0 percent the total rise in M3, while the share of currency outside banks was 3.0 percent. An analysis of developments in money supplies (M1) and (M2) indicates that M1 rose by 1.6 percent (Rls 3.8 billion) to Rls 242.6 billion compared to a rise of 7.1 percent (Rls 15.8 billion) during the preceding quarter of the same year. Thus, the increase in M1 constituted 30.3 percent of the total increase in M3. M1 represented 54.9 percent of aggregate money supply (M3) at the end of June 2004 compared to about the same percentage at the end of the same month of the preceding year. M2 rose by 2.1 percent (Rls 7.5 billion) to Rls 357.9 billion, or 81.0 percent of aggregate money supply (M3), compared to a growth of 4.2 percent (Rls 14.0 billion) during the preceding quarter of the same year. The rise in M2 over M1 was caused by an increase of 3.3 percent (Rls 3.7 billion) in time and savings deposits. Thus, there was more demand for time and savings deposits than that for demand deposits as a result of higher rates of interest on time and savings deposits.

Second: Monetary Policy

During the second quarter of 2004, SAMA continued to follow an appropriate monetary policy capable of boosting the domestic economic activity and coping with world economic developments with the aim of maintaining a stable exchange rate of the Saudi Riyal and providing adequate liquidity to the banking sector. The Riyal's spot market exchange rate vis-à-vis the US dollar remained steady within a narrow margin (between Rls 3.7495 – 3.7505 per US dollar) around its official parity of Rls 3.75 per US dollar. Continued rise of oil prices and attractiveness of the domestic share market had a favourable impact on the Riyal's exchange rate stability and investors' increased confidence in the domestic economy. SAMA did not make any change in the official interest rates during the second quarter of 2004. Its official Repo rate and reverse Repo rate (ORR and RRR) remained unchanged at 1.5 percent and 1.0 percent respectively. The average value of repurchase agreements (Repo) per day stood at Rls 3,623 million during the second quarter of 2004, while that of reverse repurchase agreements (Reverse Repo) was Rls 852 million. SAMA did not conduct any Fx swap operations with banks during this period. The position of domestic liquidity was adequate to meet finance requirements during the period.

Inter-bank interest rates rose remarkably during the second quarter of 2004. The three-month inter-bank interest rate increased from 1.2 percent at the end of the first quarter to 2.02 percent at the end of the second quarter due to a rise in US dollar deposits interest rates. The differential between the Riyal and the Dollar interest rates on the three-month deposits went up in favour of the Riyal from 11 basis points at the end of March to 40 basis points at the end of June.

As for the public debt, SAMA, on behalf of the Ministry of Finance, offered during the second quarter of 2004 one issue of government development bonds (GDB) on a monthly basis. It also offered three issues of floating rate notes, in addition to treasury bills issued weekly. SAMA has continued to float GDB for domestic banks by auction to ensure effective pricing of these bonds to be in accordance with the market depth and required finance. In general, the volume of issues of GDB declined during the second quarter of 2004 as a result of continued budgetary surplus.

Third: Developments in Commercial Banks' Activity

According to data on the Consolidated Financial Position of Commercial Banks at the end of the second quarter of 2004, commercial banks recorded a lower growth in their performance as compared to the first quarter of the same year. Total assets of commercial banks rose by 2.0 percent (Rls 11.5 billion) at the end of the second quarter of 2004 to Rls 590.7 billion compared to a larger increase of 6.2 percent (Rls 33.9 billion) during the first quarter of the same year.

3.1 Bank deposits

Total bank deposits went up by 3.2 percent (Rls 12.1 billion) to Rls 384.8 billion during the second quarter of 2004 compared to a larger increase of 4.6 percent (Rls 16.4 billion) during the first quarter of 2004. The ratio of total deposits to the total consolidated financial position of commercial banks stood at 65.1 percent at the end of June 2004 compared to 65.2 percent at the end of June 2003.

A classification of deposits by sector enhanced expectations of the growth of the domestic private sector. Deposits of the private sector rose by 3.7 percent (Rls 11.6 billion) during the quarter under study compared to a higher growth of 5.2 percent (Rls 15.6 billion) during the preceding quarter of the same year. Deposits of the public sector also grew by 0.9 percent (Rls 0.5 billion) compared to an increase of 1.3 percent (Rls 0.8 billion) in the first quarter of 2004.

Distribution of bank deposits by type shows that demand deposits increased by 1.9 percent (Rls 3.4 billion) compared to a rise of 8.7 percent (Rls 14.6 billion) during the first quarter of 2004. Time and savings deposits also grew by 3.3 percent (Rls 3.7 billion) compared to a fall of 1.6 percent (Rls 1.8 billion) during the first quarter of the same year. Other quasi-monetary deposits rose by 6.3 percent (Rls 5.0 billion) compared to an increase of 4.8 percent (Rls 3.6 billion) in the first quarter of 2004.

A breakdown of deposits by currency indicates that the higher percentage of increase in deposits was accounted for by foreign currency deposits, which increased by 8.7 percent (Rls 5.7 billion) compared to a lower rise of 2.2 percent

(Rls 1.4 billion) during the preceding quarter of the same year. Domestic currency deposits also went up by 2.1 percent (Rls 6.4 billion) compared to a growth of 5.1 percent (Rls 14.9 billion) during the first quarter of 2004.

3.2 Credit and Investment Activity of Banks

In the area of commercial banks' credit and investment activity in the public and private sectors, total bank claims on both sectors rose during the second quarter of 2004 by 4.7 percent (Rls 20.1 billion) to Rls 447.2 billion compared to an increase of 5.3 percent (Rls 21.6 billion) in the preceding quarter of the same year. Such expanded activity of banks suggests that the Saudi economy continued to grow at good rates during the period. These claims constituted 116.2 percent of total deposits at the end of June 2004 compared to 113.3 percent at the end of June 2003.

Developments by sectors indicate that total bank claims on the private sector went up by 10.7 percent (Rls 25.8 billion) compared to a growth of 5.6 percent (Rls 12.8 billion) during the preceding quarter of the same year, constituting 69.4 percent of total deposits at the end of 2004 compared to 61.3 percent at the end of June 2003. In contrast, total bank claims on the public sector (loans to public institutions and investments in government securities) went down by 3.3 percent (Rls 6.1 billion) compared to a growth of 5.0 percent (Rls 8.8 billion) during the first quarter of the same year. Total bank claims on the government sector represented 46.6 percent of total deposits at the end of June 2004 compared to 51.9 percent at the end of June 2003.

A review of bank credit according to maturity shows that short-term credit (less than one year) rose by 10.1 percent (Rls 15.5 billion) compared to a rise of 5.0 percent (Rls 7.3 billion) during the first quarter of the same year. Medium-term credit (one to three years) went up by 12.0 percent (Rls 4.7 billion) compared to a rise of 3.7 percent (Rls 1.4 billion) in the first quarter of the same year. Long-term credit (for more than three years) increased by 9.1 percent (Rls 6.1 billion) compared to an increase of 5.9 percent (Rls 3.7 billion) in the preceding quarter of the same year.

A breakdown of bank credit by economic activity during the second quarter of 2004 indicates that financing for “other” purposes (the bulk of these were loans to individuals) rose by Rls 11.1 billion to Rls 102.7 billion compared to a rise of Rls 9.4 billion during the first quarter of the same year. Bank credit for “finance” purposes increased by Rls 4.0 billion to Rls 21.1 billion against a decline of Rls 5.3 billion in the first quarter of the same year. Credit for "manufacturing and processing" rose by Rls 2.8 billion to Rls 29.0 billion against a decline of Rls 1.7 billion in the first quarter of the same year. Credit for "Services" purposes went up by Rls 1.9 billion to Rls 11.5 billion compared to a rise of Rls 0.8 billion during the first quarter of the same year. Credit for “commerce” grew by Rls 1.6 billion to Rls 52.4 billion against a decline of Rls 1.1 billion. Credit for "building and construction" increased by Rls 1.5 billion to Rls 23.1 billion against a fall of Rls 0.3 billion. Credit for "government and semi-government sectors" went up by Rls 1.3 billion to Rls 27.0 billion against a fall of Rls 0.1 billion. Credit for "agriculture and fishing" also grew by Rls 0.7 billion to Rls 3.4 billion in the first quarter of 2004.

3.3 Commercial Banks’ Foreign Assets and Liabilities

Total foreign assets of commercial banks fell during the second quarter of 2004 by 3.0 percent (Rls 2.8 billion) to Rls 89.3 billion against a rise of 13.6 percent (Rls 11.0 billion) during the first quarter of 2004. Their total foreign liabilities also declined by 6.9 percent (Rls 3.1 billion) to Rls 41.6 billion against a growth of 11.7 percent (Rls 4.7 billion) in the first quarter of 2004. Thus, their net foreign assets increased by 0.6 percent (Rls 0.3 billion) to Rls 47.7 billion compared to a higher growth of 15.5 percent (Rls 6.4 billion) during the first quarter of 2004.

3.4 Reserves, Capital, Profits and Branches of Commercial Banks

Banks raised their liquidity position during the second quarter of 2004, with total cash in vault and deposits with SAMA increasing by 4.5 percent (Rls 1.0 billion) to Rls 22.3 billion against a decline of 20.0 percent (Rls 5.3 billion) during the first quarter of 2004. The ratio of total reserves to total bank deposits at the end of June 2004 stood at 5.8 percent compared to 6.1 percent at the end of June of 2003. The bulk of the rise was accounted for by deposits with SAMA, increasing by Rls 0.3 billion. Cash in vault also rose by Rls 0.7 billion.

Banks increased their capital and reserves by Rls 0.6 billion, or 1.1 percent, to Rls 53.7 billion compared to a rise of Rls 6.1 billion, or 13.0 percent during the preceding quarter of the same year. Capital adequacy of commercial banks according to Basel Standard stood at 17.6 percent at the end of June 2004. Banks also realized profits of Rls 4.3 billion during the second quarter of 2004 compared to Rls 3.7 billion during the preceding quarter of the same year, denoting a rise of 16.2 percent.

The number of commercial banks' branches operating in the Kingdom stood at 1,209 at the end of the second quarter of 2004 compared to 1,210 at the end of the first quarter of the same year. The Central Province accounted for the decrease of one branch.

3.5 Banking Technology

SAMA, in co-operation with commercial banks, has continued to develop banking technology in the Kingdom. As for the Saudi Riyal Inter-bank Express (SARIE), an integrated plan was made during the second quarter involving coordination among all concerned authorities in case a new bank would participate in SARIE and unification of the technical procedures for participation of new banks in SARIE. The plan and unified procedures were applied for the participation of the International Emirates Bank in SARIE. SARIE technical team also designed a system that allows exclusion of banks from SARIE gradually and automatically. This was applied previously on Saudi Cairo Bank and Saudi United Bank. As regards linking SARIE with the new systems, SARIE was linked to "Sadad" system in the tests environment to electronically transmit clearing from "Sadad" to "SARIE" via a link. Necessary tests for linking SARIE with "Tadawul" system were also implemented. As for future developments, a study on upgrading "SARIE's Firewall" and linking it with SAMA's e-trust Centre to issue digital unified certificates was completed. Replacement of all SARIE's hardware with new advanced hardware was also approved. This project has already started and will be completed after about 7 months. The integrated plan to activate the use of "Direct Debit" in the Kingdom was finalized. By using direct debit via SARIE, frequent and periodic payments (of bills for different utility services such as electricity, water and

communications as well as regular monthly installments such as installments of car and insurance companies) can automatically be settled with no need for a customer to personally visit the bank. SARIE allows any bank to debit a customer's account and transfer funds to the beneficiary's account with any bank in the Kingdom at a ceiling amount determined by the customer for regular payment debit. A comprehensive pamphlet, which contains rules and regulations related to the direct debit scheme in addition to educational and marketing information, was issued. Banks shall officially follow the rules and regulations contained in this pamphlet as of 1 September 2004.

As for statistics of banking technology, the number of automatic teller machines (ATMs) increased by 223 to a total of 3,899 during the second quarter of 2004 compared to a rise of 208 in the same period of the preceding year. The number of ATM cards rose by 106.8 thousand to a total of 6.1 million compared to a fall of 11.4 thousand during the second quarter of the preceding year. Cash withdrawals through ATMs increased by Rls 5.8 billion to Rls 50.3 billion against a fall of Rls 8.3 billion during the same period of the preceding year. Cash withdrawals through banks' network went up by Rls 3.7 billion, and withdrawals through SPAN also rose by Rls 2.0 billion. Total number of transactions increased as well by 15.9 million to 103.6 million compared to a rise of 2.5 million in the second quarter of 2003.

The number of Points of Sale (POS) terminals increased during the second quarter of 2004 by 3,461 to a total of 32.5 thousand compared to a rise of 2,246 during the same quarter of the preceding year. The value of sales transactions made through POS terminals grew by Rls 325.2 million to Rls 5.8 billion.

The value of transactions executed through SARIE was up by Rls 392.1 billion to Rls 2,113.5 billion during the second quarter of 2004 compared to a rise of Rls 83.2 billion in the same quarter of 2003. The number of transactions also increased by 32.5 thousand to 318.7 thousand compared to a rise of 1.1 thousand during the same period of the preceding year.

With regard to clearing house operations, the number of clearing houses at all SAMA's branches in the Kingdom stood at 10, of which 3 are in Riyadh, Jeddah

and Dammam. Automated Clearing houses were developed in 2001 by introducing modern machines, which use light scanning technique for archiving copies of cheques instead of the microfilm technique used previously. The number of cheques (incoming and outgoing) cleared through clearing houses stood at 2.0 million during the second quarter of 2004, and their value totaled Rls 129.7 billion. The number of commercial and personal cheques stood at 1.7 million, with a total value of Rls 90.1 billion. The number of (certified) banks' cheques was 298.8 thousand, with a total value of Rls 39.6 billion.

Fourth: Share Market Developments

The domestic share market has been growing constantly since the beginning of 2000, recording its peak growth in 2003. The general share price index went up from 2,081 points during the second quarter of 2000 to 3,613 points during the second quarter of 2003 and further to 4,437 points at the end of the last quarter of 2003. Such large increases in the share market were due to a number of factors, including continued increase of overall economic activity due to improved oil revenue which represent outstanding alternatives for investing in shares, a rise in companies' profits, increased confidence in the domestic market, a decline in interest rates on deposits and expanding number of investors.

During the second quarter of 2004, the general share price index rose by 58.1 percent over its level in the same quarter of the preceding year to reach 5,713. The number of shares traded also increased by 104.8 percent to 3,412 million, and their value rose by 217.0 percent to Rls 540.2 billion. The number of transactions grew by 313.5 percent to 3.7 million. Market capitalization went up by 61.2 percent to Rls 769 billion.

Fifth: Price Indices

Domestic prices recorded a small decline during the period 1999-2002. The general price index, issued by Central Department of Statistics, went down from 100.0 in 1999 to 98.0 points in 2002. The decline was accounted for by a fall in price indices of "fabrics, apparel and shoes", "house furnishings", "transport and

communications” and “all food”. However, it rose in 2003 by 0.6 percent to 98.6 points.

During the second quarter of 2004, the general price index went up by 0.4 percent over its level during the same quarter of the preceding year. As a result, price indices of all food group increased by 3.2 percent, followed by other expenditures group by 0.6 percent and medical care group by 0.2 percent. In contrast, price indices of "fabrics, apparel and shoes" declined by 2.7 percent, followed by "house furnishings" by 1.8 percent, "transport and communications" by 0.2 percent and "education and entertainment" by 0.8 percent. Housing remained nearly unchanged.

Sixth: Supervisory and Control Developments during the Second Quarter of 2004

6-1 Legislative and Regulatory Developments.

- (a) Royal Order No. a/114 was issued on 13/5/1425 approving the constitution of the Board of Commissioners of the Securities and Exchange Commission. The Board consists of 5 members and its Chairman reports directly to the Prime Minister.
- (b) At its meeting held on 19/4/1425 (7/6/2004), the Council of Ministers issued its Resolution approving taking necessary regulatory measures for completing the merger of 8 money changer firms operating in the Kingdom under one banking corporation and licensing establishment a joint-stock company for this purpose. The company shall have a capital of RIs 3000 million divided into 60 million nominal shares, the value of each share was set at RIs 50, provided that half of these shares shall be floated within 30 days as of the date of publishing the Royal Decree approving the establishment of such company. Money changers' business shall be ceased; their commercial registers shall be cancelled; their firms shall be closed down; such firms shall be non-existent as of the date of announcing the Minister of Commerce and Industry's decision on the establishment of the new company. These money

changers shall be prohibited from conducting any banking activity in the Kingdom, including money changing business.

- (c) SAMA issued its circular No. 166/B.C.S. on 30/6/2004 regarding the plans for adopting the new Capital Adequacy Rules (Basle2).

6-2 Domestic Developments Regarding Opening Branches by Foreign Banks in the Kingdom.

- (a) The Council of Ministers, at its meeting held on Monday 12/3/1425, approved licensing the Deutsche Bank, B.N Bariba and JP Morgan Chase to open branches for conducting banking and investment business in the Kingdom.
- (b) The Council of Ministers issued its Resolution on 3/5/1425 (21/6/2004) approving "Bank of Muscat" to open a branch in Riyadh.

Seventh: Regulatory Developments in the Saudi Economy during the Second Quarter of 2004.

The Saudi economy witnessed some domestic regulatory developments during the second quarter of 2004. The most important of these are the following:

- 7-1 The Council of Ministers issued on 12/4/1425 (31/5/2004) its Resolution approving the expansion of employment fields and job opportunities for women.
- 7-2 The Council of Ministers issued on 12/4/1425 (31/5/2004) its Resolution approving the Anti-Disguise Law.
- 7-3 The Council of Ministers issued on 14/3/1425 (31/5/2004) its Resolution approving modification of the name of the General Secretariat of the Labour Force Council to "The Labour Agency for Planning and Development" at the Ministry of Labour.