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Saudi Banks Will Benefit from Central Bank's Latest Liquidity Support

From Credit Outlook

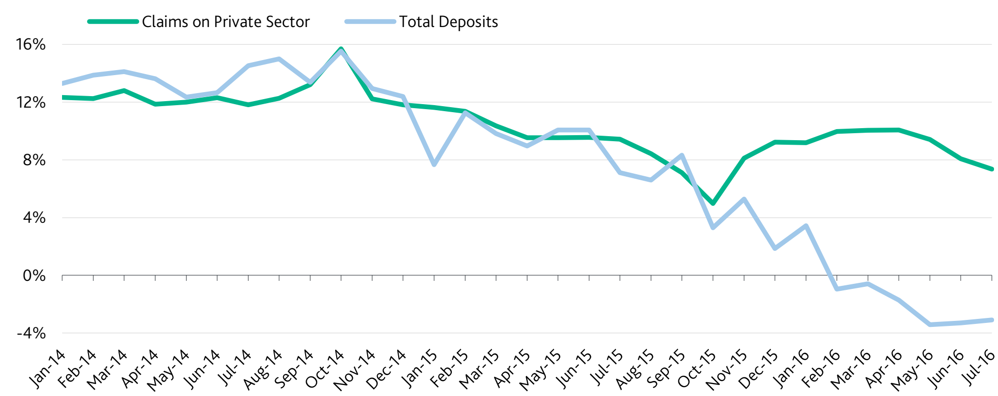
Analyst Contacts:

DIFC	+971.4.401.9536
Olivier Panis *Vice President - Senior Credit Officer* olivier.panis@moodys.com	+971.4.2379.533
Jonathan Parrod *Associate Analyst* jonathan.parrod@moodys.com	+971.4.2379.546

Last Sunday, the Saudi Arabia Monetary Authority (SAMA), the country's central bank, announced that it would provide Saudi banks with about SAR20 billion ($5.3 billion) of time deposits on behalf of government agencies, and introduce seven-day and 28-day repurchase agreements. These moves follow prior deposit injections of approximately SAR12 billion since the start of the year and are credit positive for Saudi Arabia's banks, which continue to face pronounced liquidity pressures as a result of recent deposit outflows, a consequence of depressed oil prices.

Since oil prices plunged in 2014, liquidity trends in the Saudi banking system have reversed.[1] Instead of excess liquidity, reflected by customer deposit growth of 12.1% versus 11.8% growth in credit (defined as claims to the private sector, which include loans, advances and investments) between 2013 and 2014, Saudi banks have experienced the opposite trend in recent years: since 2014, average deposit growth has decreased to 1% versus credit growth of 9.5% (see exhibit). Liquidity has tightened even more since February 2016, when deposit outflows led to a 3.1% year-on-year contraction in total deposits as of 30 July 2016. Government deposits as of July 2016 were down 4.4% from a year earlier because funds were needed to help finance its large fiscal deficit, which we estimate at around 12% for 2016. Private-sector deposits also declined and were down 2.6% year on year as of July, adversely affected by government spending cuts and weakening economic growth. We expect Saudi Arabia's non-oil GDP growth to be 1.6% this year and 2.4% in 2017, versus the 2010-16 average of 6.2%.

Saudi Commercial Banks' Year-on-Year Change in Claims on Private Sector and Total Deposits



Source: Saudi Arabia Monetary Authority

What is Moody's Credit Outlook?

Published every Monday and Thursday morning, Moody's Credit Outlook informs our research clients of the credit implications of current events.

1 See Saudi Banks' Deposit Losses Tighten Liquidity, 4 July 2016.

SAMA's SAR20 billion injection of time deposits adds to an approximately SAR12 billion provision that was extended as short-term deposits and loans to a number of banks earlier this year. These measures should help stabilize banks' regulatory loan-to-deposit ratio for the next six months, which we expect to decrease 100 basis points to around 84% as of September 2016 from 85% in June 2016. Earlier this year, SAMA had increased its maximum loan-to-deposit ratio guidance to 90% from 85%.[2]

In addition, SAMA announced that it would now provide seven-day and 28-day repurchase agreements in addition to one-day repo agreements. When combined with a robust stock of liquid assets to total assets of around 25%, these repurchase facilities will allow banks to access short-term borrowing at a lower and more stable cost than available in the challenged wholesale markets. This will reduce their funding costs, which, as reflected in the three-month Saudi Interbank Offered Rate (SAIBOR) of 2.35% on 27 September, are at their highest since January 2009.

Although the majority of banks continue to rely on funding from non-interest-bearing deposits (around 63% of total funding as of June 2016), recourse to more expensive and confidence-sensitive wholesale market funding has increased in recent months to 7.9% as of June 2016 from 6.1% as of December 2015, commensurate with the contraction in total deposits available in the system. Despite the likelihood of continued pressure on banks' cost of funding into 2017, these SAMA facilities should also support profitability.

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2 As per SAMA's definition, the loan-to-deposit ratio includes long-term borrowing in the denominator.

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Authors
Olivier Panis
Jonathan Parrod

Production Specialist
Shubhra Bhatnagar

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