While preparing for a future protected from the vagaries of the oil markets, Saudi Arabia is likely to struggle with lower oil revenues as it attempts to shore up global markets. It is getting very little help from other OPEC and OPEC+ members, and the more it undergirds prices the more the dynamic US oil sector forges ahead. 2018 was a calmer year for the kingdom's oil sector and fiscal situation. Stronger oil prices and a more stable domestic policy environment put the kingdom's finances on a stronger footing. The country now has ambitious plans to carry out, including Saudi Aramco's initial public offering (IPO), as the global financial and economic landscape becomes more difficult.

Oil sector dynamics: playing defense for years to come

Over the next several years, strong US crude oil and liquids output will coincide with weaker economic conditions and slowing demand for oil worldwide. One exception to the soft global demand picture will be China in 2019 and 2020, mainly because it is adding new mega-refineries tied to petrochemical facilities and, to some extent, increasing strategic and commercial reserves.

Nonetheless, the call on OPEC will decline for two years straight. Despite nearly 1m barrels per day (bpd) of lower Iranian production, a consequence of the US withdrawing its sanction waivers on international companies buying from Iran, higher Iraqi output and some increases in UAE and Kuwait production will cause Saudi Arabia to reign in crude production to under 10m bpd in 2019 and 2020.

Even a restrained Saudi Arabia will not be able to prevent oil prices from falling in 2019 to an average of $63 per barrel for Brent crude, down from $71 per barrel in 2018. A further decline to $55 per barrel in 2020 is likely.

Current account deficit to widen in the next two years

Saudi Arabia needs oil prices to stabilize at around $60 per barrel in order to balance its current account and $10 more dollars a barrel to cover the overall balance of payment flows, including those in its capital account. In 2018 the higher average oil price and 10m-bpd output allowed the kingdom to register a $70bn surplus on its current account and a balance on its capital account. As a result, it was able to staunch the declines in its foreign currency reserves seen since 2014.

This year's expected oil price decline and subdued crude oil output will not provide the means to generate a surplus on the current account. Further drawdowns of foreign assets and more borrowing on the international markets will be needed to cover capital account deficits.

The situation will get worse if the oil price continues to slide in 2020, as we expect. Sizable deficits will reappear in the current account. Saudi Arabia has indicated that it will go ahead with its IPO next year, however, it could be delayed due to a poor oil price environment. If the kingdom does delay the IPO, it will have to use its foreign assets to cover the current account deficit and outflows in its capital account despite higher inflows due to a jump in portfolio investments starting in 2019.

As a result, by the end of 2020 its foreign assets would fall to their lowest level since the peak in 2014.

Non-oil GDP growth will remain subdued while oil GDP will contract

Underlying the balance of payments forecast are weak import numbers reflecting lackluster growth in the economy. 2018 saw a mild recovery in the economy mainly due to higher oil output, stronger manufacturing and service sector output. The decline in oil production in 2019 will more than offset growth in the non-oil economy and cause a small contraction in overall GDP. With oil production expected to be flat in 2020, and mild growth expected in the non-oil sectors, especially manufacturing and services, the overall growth picture next year will show some improvement.

Higher government expenditures, which enjoyed double-digit growth rates in 2017 and 2018, supported non-oil GDP growth last year. In 2019 and 2020 lower oil prices will force some constraints on government spending, but it is likely the authorities will continue increasing both current and capital spending, which is part of the reason that non-oil GDP will grow this year and next.

Budget deficits are expected to equal to 9% of GDP this year (a reversal of the 2018 performance when the deficit shrank to its lowest level since the oil price crash of 2014) and 15% of GDP in 2020 as a result of lower revenues and sustained spending.

Stabilization, let alone growth, will be difficult in the current oil environment

The post-2014 oil price crash, announcement of radical reforms and internal political turmoil and uncertainly took their toll on growth and financial stability. For the greater part of 2018 it looked like the kingdom was beginning of new era of economic stability and growth. The oil markets, however, are not helping, and the need to sustain growth, albeit tepid growth, have complicated the outlook for policy makers. They have very ambitious plans for the economy, which have become more difficult to achieve as financial constraints reappear on the horizon.

Saudi Arabia: Key Economic Indicators

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
GDP growth % change	5.0	10.0	5.4	2.7	3.7	3.7	2.1	-0.7	2.4	-0.5	1.9
Oil GDP growth % change	-0.1	13.3	5.2	-1.5	0.9	4.7	2.8	-3.6	3.7	-5.0	-0.1
Non-oil GDP growth % change	9.0	7.7	5.6	5.7	5.5	3.0	1.6	1.2	1.7	2.3	3.0
Government budget balance % of GDP	4.4	11.6	11.9	5.6	-3.5	15.8	12.9	-9.2	-4.6	-9.6	-15.5
Exports of goods, services and income USD billion	280	396	423	413	382	244	225	259	333	263	251
Petroleum exports USD billion	229	349	374	354	317	167	147	170	245	188	163
Crude oil production million bpd	8.2	9.3	9.8	9.6	9.7	10.2	10.5	10.0	10.3	9.8	9.8
Average export price USD billion	89.5	110.8	112.8	106.8	96.5	48.4	43.6	54.1	71.3	63.4	55.0
Imports of goods, services and income USD billion	185	208	228	242	270	256	206	210	222	223	233
Merchandise imports USD billion	97	120	142	153	158	159	128	123	126	128	133
Current account balance USD billion	67	159	165	135	74	-57	-24	10	71	1	-21
As percentage of GDP	12.6	23.6	22.4	18.1	9.8	-8.7	-3.7	1.5	9.0	0.2	-2.6
Financing of current account											
Capital flows net USD billion	8	-9	-11	-55	-59	-47	-15	-62	-88	-45	55
Debt flows net USD billion	7	-1	10	4	3	-7	6	11	2	13	-14
o/w medium long term, net	2	6	-9	13	-11	4	16	12	1	12	-15
Disbursements	15	20	13	25	10	15	27	22	10	20	0
Amortization	13	13	21	12	20	12	11	9	9	8	15
Change in official assets, net USD billion	35	95	11	70	8	-115	-78	-39	0	-36	18
Total foreign debt USD billion, including ST debt	125	124	134	138	141	134	140	151	152	165	151
o/w medium long term debt	79	85	77	89	79	82	99	111	112	124	109
Foreign assets of central bank USD billion	534	544	656	725	732	616	536	496	497	461	479

Fareed Mohamedi is an international political economist specializing in the geopolitics of energy and energy markets with a special emphasis on the economic development of petrostates and their foreign relations. He has led research teams in several specialized energy consultancies and two national oil companies. He has worked as a macro-economist with economic research institutes in Washington DC, a bond rating agency in New York City and the finance ministry of Bahrain. Fareed is currently Managing Director of SIA-Energy International, the global division of SIA-Energy based in Beijing.

