

Saudi's Inner Focus

TALES FROM THE EMERGING WORLD | EMERGING MARKETS EQUITY TEAM | December 2024

Eight years ago, Saudi Arabia initiated an ambitious plan to transform its economy and reshape its global identity by 2030. Moving beyond its traditional role as the world's top oil exporter, the Kingdom is positioning itself as a tourist destination as well as an emerging hub for international business and entertainment. Through its Public Investment Fund, Saudi Arabia earlier made strategic international investments in iconic French hotels, Hollywood studios and cutting-edge technology funds. But now, the country's focus is to increase outlays at home.

At the end of October, eight thousand CEOs and business executives converged on Riyadh for the 8th annual Future Investment Initiative (FII) Conference, where a stark reality set in: while international financial leaders were eager to secure additional capital allocations, the Saudi government signaled a pivot toward bolstering the domestic economy by announcing a one-third cut in overseas funding. This shift reflects a growing appreciation that local investments can generate a wide range of benefits.

The headline deals announced had clear connections back to the local market including a \$1 billion agreement with the Hong Kong Monetary authority to support companies based in the Guangdong-Hong Kong-Macao Greater Bay Area looking to expand into the Middle East. Meanwhile, major players like Google, Brookfield and Airbus all inked deals that reinforced the prevailing theme of the conference: capital allocation is strategically tied to driving local growth.

Saudi Arabia now requires foreign companies to base their regional headquarters within the country to be eligible to bid for government contracts. Already, 540 foreign companies have made plans to establish their headquarters in the Kingdom. Yet, foreign direct investment (FDI) has been slow to keep up. The country is aiming for \$100 billion in annual FDI by the turn of the decade, and last year investment flow reached \$25.6 billion, with United Arab Emirates, Luxembourg, France, Netherlands and the UK making up the top five countries investing in the country.

AUTHOR



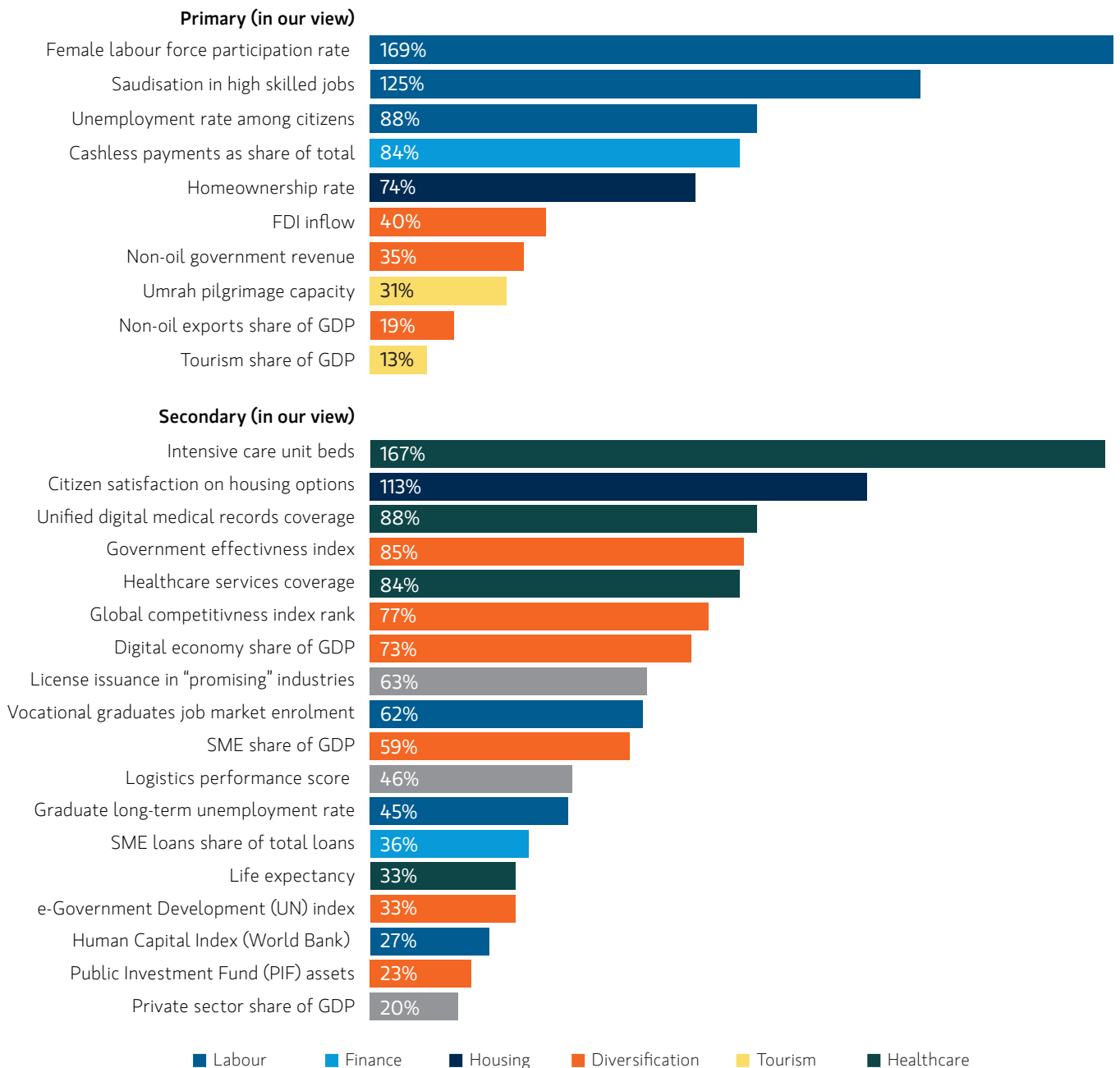
AMY OLDENBURG
*Head of Emerging
Markets Equity*

Since Crown Prince Mohammed bin Salman launched Vision 2030 in 2016, the Kingdom has made remarkable progress to introduce social and economic reforms designed to make the country more attractive to tourists and diversify its economy away from oil (*Display 1*). The country is pursuing different initiatives, from hosting premier global events like Formula 1 Grand Prix races and UFC wrestling, to staging major sporting events like the

2029 Asian Winter Games and the 2034 FIFA World Cup. Additionally, it is positioning itself as a regional video game hub and starting electric vehicle production.

Saudi Arabia is a young country, where 63% of the population is under 30, and its youth are energized by the social and economic transformation. Women, once banned for decades from driving, can now be seen behind the wheel, while unemployment among Saudi women has plummeted

DISPLAY 1
Saudi Vision 2030 Progress Report
 Progress on quantitative metrics by percent



Source: International Monetary Fund Article IV, September 2024. Tellimer Research.

by more than half to just 16% in 2023. Similarly, female participation in the workforce has more than doubled to 35%. Huge strides have also been made toward "Saudization," an initiative to develop local talent in critical industries.

The focus on local growth should bode well for domestic markets. However, data shows Global Emerging Markets Funds remain underweight in Saudi Arabia, at an average weight of 1.8%, while the MSCI EM Index weight to Saudi Arabia is approximately 4%. Investors are keenly focused on execution of Vision 2030 and sustainable results as they consider increasing their allocations to the local Saudi equity market.

The Vision 2030 transformation should ideally attract more investor attention than it already has. The local Saudi equity market has produced eye-catching returns over the last five years, especially in dedicated active domestic equity funds. However, over the last decade, passive investment strategies dominated flows while clients who favored active strategies gravitated toward concentrated portfolios or more diversified global EM strategies with allocations heavily favoring China and India.

Liquidity is another critical factor as managers try to put billions of dollars to work across EM equity markets. The transformation of the Saudi economy is moving in the right direction and its IPO market is among the most vibrant in the world. But, the larger and more liquid stocks

available are primarily in oil and financial sectors, typical for early-stage equity markets.

While compelling investment opportunities may arise in the small- and mid-cap sectors, global investors face critical questions: How many positions can they realistically add to their portfolios? Is it feasible to build substantial stakes that can be easily exited when needed? And then there are valuations. We've seen popular stocks commanding jaw-dropping multiples in the local market - some trading at 100x earnings. Such valuations can make it difficult to rationalize investment decisions when a wealth of alternatives exist across the rest of the EM universe.

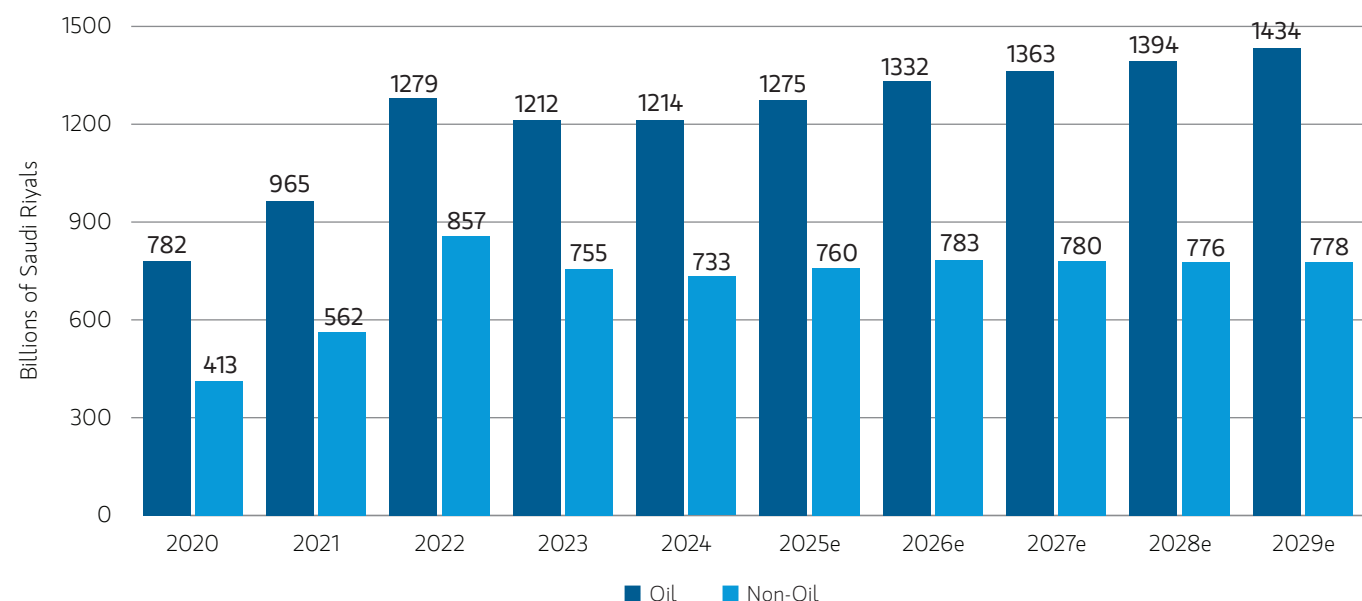
The uncertainty is further compounded by the fact that many global managers have had minimal on-the-ground presence in recent years and missed the fast pace of social reform. Geopolitical conflicts make it difficult for investors to commit significant capital in a region still viewed as risky, despite the Kingdom being largely unaffected in economic terms.

Saudi Arabia's new tourism slogan, "Go Beyond What You Think," invites the world to reimagine the Kingdom as a vibrant and dynamic destination. While the path to achieving the ambitious goals of Vision 2030 presents challenges, it also offers a unique opportunity. For global investors, the landscape is rich with potential, yet navigating Saudi Arabia's growing domestic economy requires a nuanced strategy.

DISPLAY 2

The Steady Rise of Saudi Arabia's Non-Oil Revenues

Oil vs non-oil government revenues (in billions of Saudi Riyals)



Source: IMF, Saudi Ministry of Finance. Forecasts/estimates are based on current market conditions, subject to change, and may not necessarily come to pass.

Risk Considerations

Market values can change daily due to economic and other events (e.g. natural disasters, health crises, terrorism, conflicts and social unrest) that affect markets, countries, companies or governments. It is difficult to predict the timing, duration, and potential adverse effects (e.g. portfolio liquidity) of events. Investments in **foreign markets** entail special risks such as currency, political, economic, market and liquidity risks. The risks of investing in **emerging market countries** are greater than the risks generally associated with investments in foreign developed countries.

IMPORTANT DISCLOSURES

A separately managed account may not be appropriate for all investors. Separate accounts managed according to the particular Strategy may include securities that may not necessarily track the performance of a particular index. Please consider the investment objectives, risks and fees of the Strategy carefully before investing. A minimum asset level is required.

For important information about the investment managers, please refer to Form ADV Part 2.

The views and opinions and/or analysis expressed are those of the author or the investment team as of the date of preparation of this material and are subject to change at any time without notice due to market or economic conditions and may not necessarily come to pass. Furthermore, the views will not be updated or otherwise revised to reflect information that subsequently becomes available or circumstances existing, or changes occurring, after the date of publication. The views expressed do not reflect the opinions of all investment personnel at Morgan Stanley Investment Management (MSIM) and its subsidiaries and affiliates (collectively "the Firm"), and may not be reflected in all the strategies and products that the Firm offers.

Forecasts and/or estimates provided herein are subject to change and may not actually come to pass. Information regarding expected market returns and market outlooks is based on the research, analysis and opinions of the authors or the investment team. These conclusions are speculative in nature, may not come to pass and are not intended to predict the future performance of any specific strategy or product the Firm offers. Future results may differ significantly depending on factors such as changes in securities or financial markets or general economic conditions.

This material has been prepared on the basis of publicly available information, internally developed data and other third-party sources believed to be reliable. However, no assurances are provided regarding the reliability of such information and the Firm has not sought to independently verify information taken from public and third-party sources.

This material is a general communication, which is not impartial and all information provided has been prepared solely for informational and educational purposes and does not constitute an offer or a recommendation to buy or sell any particular security or to adopt any specific investment strategy. The information herein has not been based on a consideration of any individual investor circumstances and is not investment advice, nor should it be construed in any way as tax, accounting, legal or regulatory advice. To that end, investors should seek independent legal and financial advice, including advice as to tax consequences, before making any investment decision.

This material is not a product of Morgan Stanley's Research Department and should not be regarded as a research material or a recommendation.

The Firm has not authorised financial intermediaries to use and to distribute this material, unless such use and distribution is made in accordance with applicable law and regulation. Additionally, financial intermediaries are required to satisfy themselves that the information in this material is appropriate for any person to whom they provide this material in view of that person's circumstances and purpose. The Firm shall not be liable for, and accepts no liability for, the use or misuse of this material by any such financial intermediary.

This material may be translated into other languages. Where such a translation is made this English version remains definitive. If there are any discrepancies between the English version and any version of this material in another language, the English version shall prevail.

The whole or any part of this material may not be directly or indirectly reproduced, copied, modified, used to create a derivative work, performed, displayed, published, posted, licensed, framed, distributed or transmitted or any of its contents disclosed to third parties without the Firm's express written consent. This material may not be linked to unless such hyperlink is for personal and non-commercial use. All information contained herein is proprietary and is protected under copyright and other applicable law.

Eaton Vance is part of Morgan Stanley Investment Management. Morgan Stanley Investment Management is the asset management division of Morgan Stanley.

DISTRIBUTION

This material is only intended for and will only be distributed to persons resident in jurisdictions where such distribution or availability would not be contrary to local laws or regulations.

MSIM, the asset management division of Morgan Stanley (NYSE: MS), and its affiliates have arrangements in place to market each other's products and services. Each MSIM affiliate is regulated as appropriate in the jurisdiction it operates. MSIM's affiliates are: Eaton Vance Management (International) Limited, Eaton Vance Advisers International Ltd, Calvert Research and Management, Eaton Vance Management, Parametric Portfolio Associates LLC and Atlanta Capital Management LLC.

This material has been issued by any one or more of the following entities:

EMEA:

This material is for Professional Clients/Accredited Investors only.

In the EU, MSIM and Eaton Vance materials are issued by MSIM Fund Management (Ireland) Limited ("FMIL"). FMIL is regulated by the Central Bank of Ireland and is incorporated in Ireland as a private company limited by shares with company registration number 616661 and has its registered address at 24-26 City Quay, Dublin 2, DO2 NY19, Ireland.

Outside the EU, MSIM materials are issued by Morgan Stanley Investment Management Limited (MSIM Ltd) is authorised and regulated by the Financial Conduct Authority. Registered in England. Registered No. 1981121. Registered Office: 25 Cabot Square, Canary Wharf, London E14 4QA.

In Switzerland, MSIM materials are issued by Morgan Stanley & Co. International plc, London (Zurich Branch) Authorised and regulated by the Eidgenössische Finanzmarktaufsicht ("FINMA"). Registered Office: Beethovenstrasse 33, 8002 Zurich, Switzerland.

Outside the US and EU, Eaton Vance materials are issued by Eaton Vance Management (International) Limited ("EVM") 125 Old Broad Street, London, EC2N 1AR, UK, which is authorised and regulated in the United Kingdom by the Financial Conduct Authority.

Italy: MSIM FMIL (Milan Branch), (Sede Secondaria di Milano) Palazzo Serbelloni Corso Venezia, 16 20121 Milano, Italy. **The Netherlands:** MSIM FMIL (Amsterdam Branch), Rembrandt Tower, 11th Floor Amstelplein 1 1096HA, Netherlands.

France: MSIM FMIL (Paris Branch), 61 rue de Monceau 75008 Paris, France.

Spain: MSIM FMIL (Madrid Branch), Calle Serrano 55, 28006, Madrid, Spain.

Germany: MSIM FMIL, Frankfurt Branch, Grosse Gallusstrasse 18, 60312 Frankfurt am Main, Germany (Gattung: Zweigniederlassung (FDI) gem. § 53b KWG). **Denmark:** MSIM FMIL (Copenhagen Branch), Gorrissen Federspiel, Axel Towers, Axeltorv2, 1609 Copenhagen V, Denmark.

MIDDLE EAST:

Dubai: MSIM Ltd (Representative Office, Unit Precinct 3-7th Floor-Unit 701 and 702, Level 7, Gate Precinct Building 3, Dubai International Financial Centre, Dubai, 506501, United Arab Emirates. Telephone: +97 (0)14 709 7158).

This document is distributed in the Dubai International Financial Centre by Morgan Stanley Investment Management Limited (Representative Office), an entity regulated by the Dubai Financial Services Authority (DFSA). It is intended for use by professional clients and market counterparties only. This document is not intended for distribution to retail clients, and retail clients should not act upon the information contained in this document.

This document relates to a financial product which is not subject to any form of regulation or approval by the DFSA. The DFSA has no responsibility for reviewing or verifying any documents in connection with this financial product. Accordingly, the DFSA has not approved this document or any other associated documents nor taken any steps to verify the information set out in this document, and has no responsibility for it. The financial product to which this document relates may be illiquid and/or subject to restrictions on its resale or transfer. Prospective purchasers should conduct their own due diligence on the financial product. If you do not understand the contents of this document, you should consult an authorised financial adviser.

U.S.:

NOT FDIC INSURED | OFFER NO BANK GUARANTEE | MAY LOSE VALUE | NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY | NOT A DEPOSIT

LATIN AMERICA (BRAZIL, CHILE COLOMBIA, MEXICO, PERU, AND URUGUAY)

This material is for use with an institutional investor or a qualified investor only. All information contained herein is confidential and is for the exclusive use and review of the intended addressee, and may not be passed on to any third party. This material is provided for informational purposes only and does not constitute a public offering, solicitation or recommendation to buy or sell for any product, service, security and/or strategy. A decision to invest should only be made after reading the strategy documentation and conducting in-depth and independent due diligence.

ASIA PACIFIC

Hong Kong: This material is disseminated by Morgan Stanley Asia Limited for use in Hong Kong and shall only be made available to "professional investors" as defined under the Securities and Futures Ordinance of Hong Kong (Cap 571). The contents of this material have not been reviewed nor approved by any regulatory authority including the Securities and Futures Commission in Hong Kong. Accordingly, save where an exemption is available under the relevant law, this material shall not be issued, circulated, distributed, directed at, or made available to, the public in Hong Kong. **Singapore:** This material is disseminated by Morgan Stanley Investment Management Company and should not be considered to be the subject of an invitation for subscription or purchase, whether directly or indirectly, to the public or any member of the public in Singapore other than (i) to an institutional investor under section 304 of the Securities and Futures Act, Chapter 289 of Singapore ("SFA"); (ii) to a "relevant person" (which includes an accredited investor) pursuant to section 305 of the SFA, and such distribution is in accordance with the conditions specified in section 305 of the SFA; or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA. This publication has not been reviewed by the Monetary Authority of Singapore. **Australia:** This material is provided by Morgan Stanley Investment Management (Australia) Pty Ltd ABN 22122040037, AFSL No. 314182 and its affiliates and does not constitute an offer of interests. Morgan Stanley

Investment Management (Australia) Pty Limited arranges for MSIM affiliates to provide financial services to Australian wholesale clients. Interests will only be offered in circumstances under which no disclosure is required under the Corporations Act 2001 (Cth) (the "Corporations Act"). Any offer of interests will not purport to be an offer of interests in circumstances under which disclosure is required under the Corporations Act and will only be made to persons who qualify as a "wholesale client" (as defined in the Corporations Act). This material will not be lodged with the Australian Securities and Investments Commission.

Japan: For professional investors, this material is circulated or distributed for informational purposes only. For those who are not professional investors, this material is provided in relation to Morgan Stanley Investment Management (Japan) Co., Ltd. ("MSIMJ")'s business with respect to discretionary investment management agreements ("IMA") and investment advisory agreements ("IAA"). This is not for the purpose of a recommendation or solicitation of transactions or offers any particular financial instruments. Under an IMA, with respect to management of assets of a client, the client prescribes basic management policies in advance and commissions MSIMJ to make all investment decisions based on an analysis of the value, etc. of the securities, and MSIMJ accepts such commission. The client shall delegate to MSIMJ the authorities necessary for making investment. MSIMJ exercises the delegated authorities based on investment decisions of MSIMJ, and the client shall not make individual instructions. All investment profits and losses belong to the clients; principal is not guaranteed. Please consider the investment objectives and nature of risks before investing. As an investment advisory fee for an IAA or an IMA, the amount of assets subject to the contract multiplied by a certain rate (the upper limit is 2.20% per annum (including tax)) shall be incurred in proportion to the contract period. For some strategies, a contingency fee may be incurred in addition to the fee mentioned above. Indirect charges also may be incurred, such as brokerage commissions for incorporated securities. Since these charges and expenses are different depending on a contract and other factors, MSIMJ cannot present the rates, upper limits, etc. in advance. All clients should read the Documents Provided Prior to the Conclusion of a Contract carefully before executing an agreement. This material is disseminated in Japan by MSIMJ, Registered No. 410 (Director of Kanto Local Finance Bureau (Financial Instruments Firms)), Membership: the Japan Securities Dealers Association, The Investment Trusts Association, Japan, the Japan Investment Advisers Association and the Type II Financial Instruments Firms Association.