

July 2020

MARMORE FIRST TAKE

Tripling of VAT in Saudi Arabia

The move could pressure
consumer demand

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HIGHLIGHTS

- Saudi Arabia had announced several austerity and revenue generation measures on 10th May 2020 to shore up its finances in a low oil price environment. The tripling of Value Added Tax (VAT) rate from 5% to 15% was one of them. The tax levy came into effect on 1st July 2020. However, the government would bear VAT on education, private healthcare and first house bought by the citizen, provided its cost does not exceed SR850,000.
- The steep increase in VAT seems to have impacted consumer behaviour before and after its implementation.
- While there have been reports of people intending to be more cautious of spending after VAT hike, there seems to have been sharp uptick in retail sales as people sought to buy appliances, cars, gold etc. in the run up to its implementation. This buying spree had been boosted by the complete lifting of curfew from 21st June.
- The impact of increase in VAT has been apparent in real estate sales that have reportedly dropped by 85%, from SR10.9bn in the last week of June to SR1.7bn a week later when the tax came into effect. Businesses have also reported slowdown after the tax hike.
- Consumer price inflation in June 2020 had increased by 0.5% year-on-year and had remained around 1% in recent months. Analysts expect it to surge by up to 6% year-on-year in July owing to increase in VAT. When the 5% VAT initially came into effect on 1st January 2018, CPI for the month had increased by 3% year-on-year.
- Retail sales has already been affected due to lockdown and curfews to contain spread of COVID-19. Though curfews have been completely lifted, salary cuts, job losses and uncertainty over duration of COVID-19 are still in the air. In addition to hike in VAT, the cost of living allowance for government employees has also been suspended as part of austerity measures. These would dampen consumer spending and in turn affect businesses.
- IMF has opined that it might not be advisable to hike consumption taxes during current times. Though the hike in VAT might not be a popular move given the timing and the steep increase, it could help in generation of stable non-oil revenue for the government in the long run. According to actual data as of 2018, VAT collections have been SAR 46.7 billion (1.6% of GDP) and non-oil revenue was at 10% of GDP. Considering the increased VAT rate for second half of 2020, the revenue from VAT for 2020 would increase to 3.2% of GDP (SAR 77.3billion) and non-oil revenue would be at 12% of GDP.

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