

Research

Saudi Arabia Reclassification

FTSE
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Saudi Arabia Reclassification

Executive summary: Saudi equities take to the global stage

FTSE Russell announced the classification of Saudi Arabia as a Secondary Emerging market within the FTSE Global Equity Index Series (GEIS) on March 28, 2018, as part of the Country Classification Interim Update. The Kingdom's entry into the international equity markets marks a major milestone in its quest to grow and diversify its economy.

- **A large, high-income economy.** Saudi Arabia is one of the largest economies in the developing-markets universe, and among the world's wealthiest countries.
- **A push for economic diversity.** The Saudi government is embarked on an ambitious pro-growth initiative called Vision 2030 to diversify its economy away from oil dependency. Recent market-opening reforms are a cornerstone of these plans.
- **Plans for Aramco IPO move forward.** The Aramco IPO is seen jump-starting the government's wider-ranging privatization program and supporting longer-term efforts to broaden its commodity-centric equity market.
- **Removing barriers to foreign investment.** Saudi market authorities, in collaboration with FTSE, have moved rapidly and significantly to ease foreign investor access to its capital markets within the country classification process, continuing to improve corporate transparency and governance.
- **A rigorous inclusion evaluation process.** Saudi Arabia has met or exceeded the nine-point, rules-based FTSE criteria and independent external advisory process for inclusion as a Secondary Emerging market in an international equity-market benchmark.
- **Proactive investor engagement.** The FTSE Country Classification process is unique among index providers and designed to be transparent and research-driven. External advisory committees ensure that the criteria used to determine country classification meet the needs of global investors and are judged objectively.
- **Prominent emerging-market status.** Using the FTSE Saudi Arabia Inclusion Index Series, the country makes up 2.7% of the FTSE Emerging Index, ranking it among the 10 largest emerging stock markets. The planned initial public offering of national oil giant Saudi Aramco could almost double that weight to an estimated 4.6%* and significantly raise the EM index's Middle East exposure.

*Based on the official Saudi target valuation of US\$2 trillion for Aramco, a 5% float and an investable market capitalization of US\$100 billion.

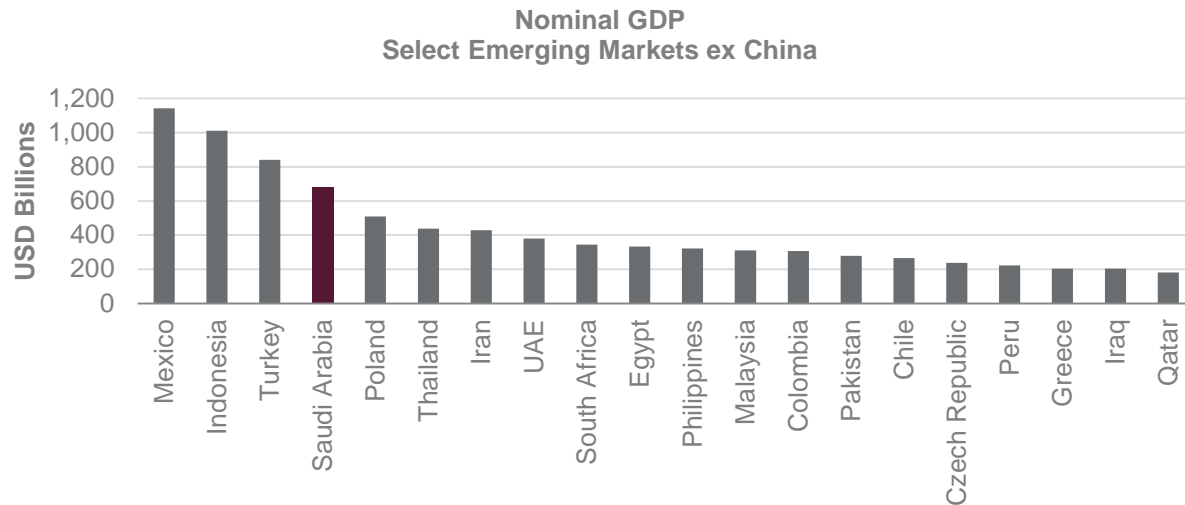
Source: FTSE Russell. Data as of February 28, 2018.

Saudi Arabia: A large economy with a vision

Saudi Arabia is a large, wealthy nation in the early stages of a bold initiative to grow and diversify its economy away from its dependency on its oil industry, which accounts for 43% of GDP and 75% of exports.¹

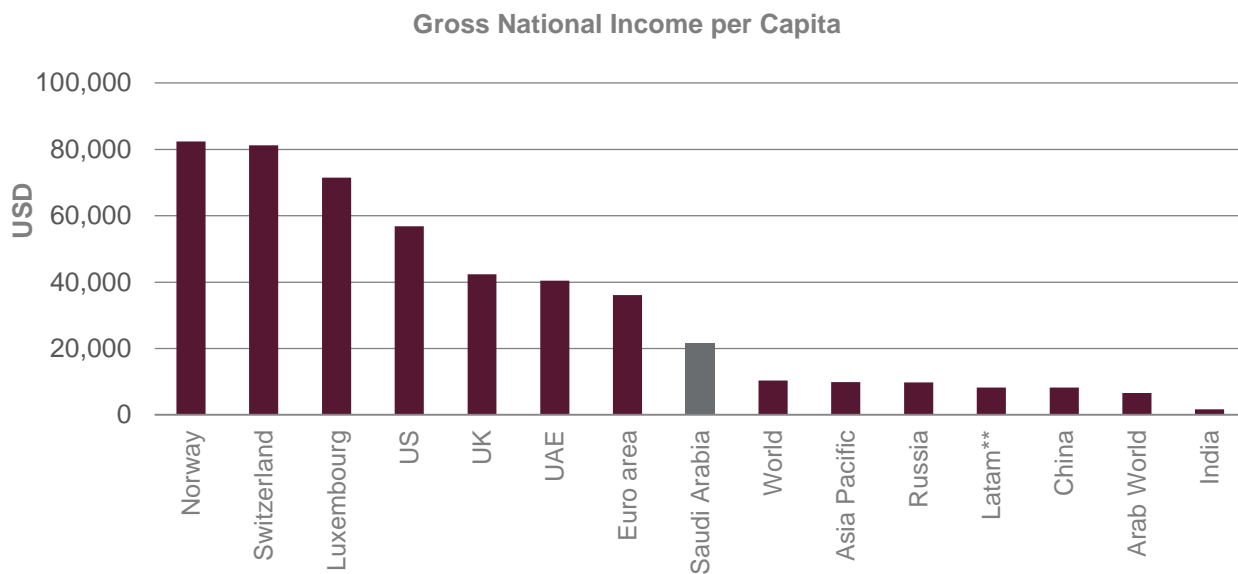
At nearly US\$684 billion in nominal GDP, it ranks as the largest economy in the Gulf region and the fourth-largest economy in the emerging-market (EM) universe, excluding China (at US\$11.2 trillion). With a gross national income per capita of around US\$22,000, the Kingdom is also classified as a high-income economy by the World Bank, placing it above most of its emerging-market peers.

Chart 1. Saudi Arabia is one of the largest economies in the emerging-market universe



Source: World Bank. Data as of December 31, 2017, except for Egypt and Pakistan, which are as of December 2016.

Chart 2. Saudi Arabia also ranks as a high-income nation



**Latin America and Caribbean nations
Source: World Bank. Data as of December 12, 2016.

¹ US Department of Commerce International Trade; July 2017, export.gov <https://article?id=Saudi-Arabia-Market-Overview>

Vision 2030: The blueprint for change

Despite the Kingdom's considerable wealth, the downturn in oil prices since 2014 has strained the economy. As oil revenues fell, the Saudi government tightened monetary conditions and cut public spending. Amid declining inflation, GDP dropped by 0.5% in 2017, versus growth of 1.7% the prior year.

Responding to broad structural shifts in the global oil markets, Saudi Arabia has embarked on an ambitious economic transformation plan called Vision 2030, introduced in mid-2016.

Spearheaded by Crown Prince Mohammed bin Salman bin Abdul-Aziz Al Saud, Vision 2030 sets strategic goals that revolve around four main categories: economic diversification, business environment improvement, capital-market liberalization and social reforms.² Its chief goals include:

- Increasing the private sector's GDP contribution from the current 40% to 65%
- Raising non-oil export contribution to GDP from 16% to 50% by growing the mining, tourism and entertainment, logistics and housing-construction sectors
- Boosting the GDP contribution of small and medium-sized enterprises
- Lowering unemployment from 11.6% to 7%, while increasing the participation of women in the workforce
- Developing its infrastructure by expanding high-speed broadband coverage and building a competitive renewable energy sector
- Bringing 50% of its military equipment spending in house
- Adding half a million new private sector jobs by 2020
- Increasing foreign direct investment in line with more developed economies.

Chart 3. Vision 2030 aims to diversify the economy from oil dependency



Source: FTSE Russell. Data through December 31, 2017.

² Saudi Arabia Ministry of Finance <https://mof.gov.sa/en/Pages/default.aspx>

Aramco IPO to open Saudi oil industry to investors

A main pillar of Saudi Arabia's economic restructuring is its plan to publicly list a minimum 5% of national oil giant Saudi Aramco, expected to take place in early 2019. The initial public offering (IPO) is seen kick-starting the country's broader privatization program and supporting its longer-term efforts to significantly diversify its domestic capital markets.

Proceeds of the IPO—forecast in a consensus range of US\$50 to US\$100 billion on the Saudi's official target valuation of US\$1-US\$2 trillion—will be mainly redirected to the economy through the Public Investment Fund (PIF), Saudi Arabia's sovereign wealth fund, which will have the mandate to spur domestic investment and encourage development of non-oil industries.

The Aramco IPO will count as one of the largest emerging-market foreign investment fund flotations in history, joining the likes of Chinese Internet companies Tencent (2004) and Alibaba (2014); and South Korea technology giant Samsung affiliates Samsung SDS and Cheil Industries (2014).

Plans for the IPO continue to progress. The company's tax rate was changed in 2017 to 50% from 85%, which will allow for a higher valuation of the company, and broad subsidy reform is linked with the preparation for the company's listing. The lower tax rate implies that Aramco profits will be transferred to the government via dividend payments to the Public Investment Fund, the country's sovereign wealth fund, as well as through taxes.

Saudi Arabia's capital markets

The Saudi government has prioritized the opening of its capital markets to foreign investment as a critical part of its long-term efforts to grow and diversify its economy.

The country initially opened its stock market to direct foreign investment on June 15, 2015, overturning policies that had historically limited direct investment in the shares of Tadawul-listed companies to Saudi and resident foreign investors and other Gulf Cooperation Council (GCC) investors. (The latter group gained access in December 2007 as part of the move to create a GCC common market.) Until 2015, non-GCC foreign investors could only gain exposure to Saudi-listed stocks indirectly through derivatives and investment funds. This new capital-markets policy set eligibility and registration rules for qualified foreign investors (QFIs), overseen by the country's stock market regulator, the Capital Market Authority (CMA).

With a market capitalization of nearly US\$452 billion and 176 listed companies as of February-end 2018, the Saudi Stock Exchange, Tadawul, is the largest equity exchange in the Middle East.

The Tadawul is also among the region's most liquid stock exchanges. According to the most recently available trading data compiled by the World Federation of Exchanges, it accounted for 38% of the region's total equity trading value (in US dollar terms) and 14% of shares traded in 2016—second only to Borsa Istanbul in trading activity. Average daily trading volume for the FTSE Saudi Arabia All Cap Index averaged US\$600 million over the past year.

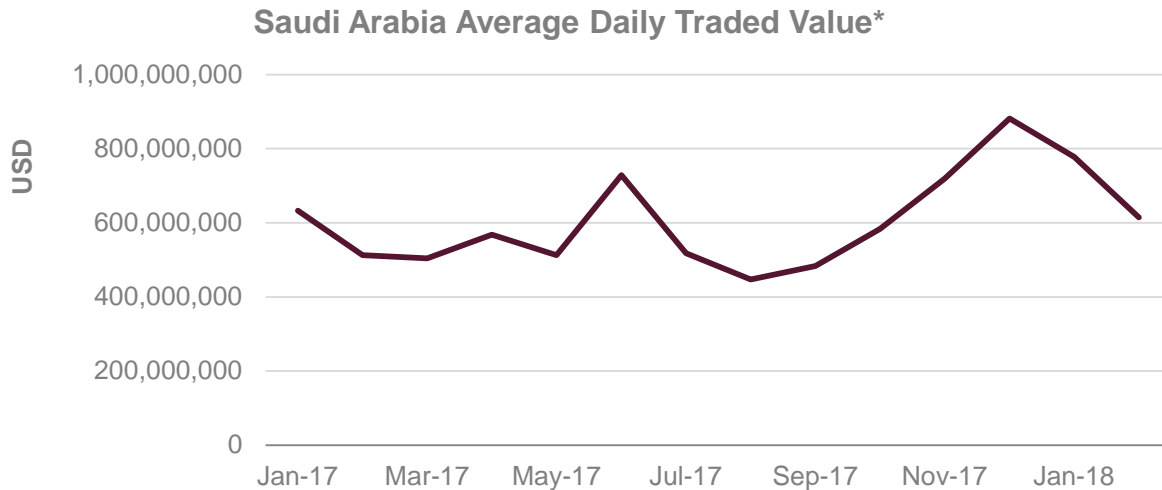
Chart 4. Tadawul is an active Middle East exchange

Middle East Exchanges: Value and Volume of Equity Trading (2016)*

| Exchange | Annual Value of Traded Shares (USD millions) | Number of Trades |
|--------------------------------------|--|------------------|
| Borsa Istanbul | 327,118 | 106,491 |
| Saudi Arabia Stock Exchange | 306,315 | 27,254 |
| Tel-Aviv Stock Exchange | 51,970 | 12,440 |
| Dubai Financial Market | 36,160 | 1,301 |
| Iran Fara Bourse Securities Exchange | 20,368 | 24,059 |
| Qatar Stock Exchange | 18,964 | 998 |
| Tehran Stock Exchange | 18,604 | 16,651 |
| The Egyptian Exchange | 17,015 | 5,959 |
| Abu Dhabi Securities Exchange | 13,336 | 389 |
| Amman Stock Exchange | 2,581 | 786 |
| Beirut Stock Exchange | 905 | 11 |
| Palestine Exchange | 446 | 34 |
| Bahrain Bourse | 332 | NA |
| Total | 816,575 | 196,575 |

*Trades effected through exchanges' electronic order books.
Source: World Federation of Exchanges. Data as of January 2017.

Chart 5. Saudi daily trading value averaged above US\$600 million in the past year



*Based on constituents of the FTSE Saudi Arabia All Cap Index
Source: FTSE Russell. Data through February 28, 2018.

Emerging market index inclusion process

While an important first step, it takes more than the opening of a market to attract foreign capital. Investors must be assured that important criteria for market efficiency and quality (such as asset security, ease of access and trading) are met. Ensuring that those investor conditions are achieved lies at the foundation of the FTSE Russell country classification evaluation process.

Saudi Arabia's classification comes after FTSE Russell's rigorous evaluation process and constructive engagement with Saudi regulators and stock market officials. To attain the Secondary Emerging classification, a market must satisfy nine of the 21 key market quality and regulatory criteria, referred to as the FTSE Quality of Markets Matrix.

FTSE Quality of Markets Criteria Matrix: Saudi Arabia

| Criteria | Secondary Emerging | Sept 2017 | Sept 2016 |
|---|--------------------|------------|------------|
| World Bank GNI Per Capita Rating | | High | High |
| Credit Worthiness | | Investment | Investment |
| Market and Regulatory Environment | | | |
| Formal stock market regulatory authorities actively monitor market (e.g., SEC, FSA, SFC) | ✓ | Pass | Pass |
| No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income | ✓ | Pass | Not Met |
| Custody and Settlement | | | |
| Settlement—Rare incidence of failed trades | ✓ | Restricted | N/A |
| Custody-Sufficient competition to ensure high quality custodian services | ✓ | Pass | Not Met |
| Clearing & Settlement—T + 2 / T + 3 | ✓ | T+2 | T+0 |
| Dealing Landscape | | | |
| Brokerage—Sufficient competition to ensure high quality broker services | ✓ | Pass | Not Met |
| Liquidity—Sufficient broad-market liquidity to support sizable global investment | ✓ | Pass | Pass |
| Transaction costs—Implicit and explicit costs to be reasonable and competitive | ✓ | Pass | Pass |
| Transparency—Market depth information / visibility and timely trade reporting process | ✓ | Pass | Pass |

N/A -Saudi Arabia operated a pre-funded settlement cycle and hence did not experience failed trades.

For a more detailed set of FTSE Russell's Country Classification criteria, see the Appendix on page 18.

The FTSE Russell Country Classification Process

FTSE Russell classifies stock markets as either Developed, Advanced Emerging, Secondary Emerging or Frontier following a rigorous, systematic and research-based process. Markets are assessed against a set of 21 criteria referred to as the FTSE Russell Quality of Markets Matrix, which is used to evaluate the suitability of inclusion based on each market's scale, regulatory environment, liquidity, stability and ease of non-domestic investor access.

The FTSE Russell process was developed in conjunction with and is supported by an independent Country Classification Advisory Committee, which consists of senior market practitioners with a wide range of technical expertise in trading, portfolio management and custody services. With support from its independent advisors, FTSE Russell also actively engages with local authorities on technical issues or concerns that may require improvement in order to meet international standards.

FTSE maintains a "Watch List" for markets potentially approaching reclassification and, as a policy of engagement, to help them understand the steps needed to meet international standards. On this basis, the Country Classification Advisory Committee makes recommendations to FTSE Russell's Governance Board, which renders the final decision on classifications. The Annual Country Classification announcement is published each September and an Interim Update is published in March. http://www.ftserussell.com/sites/default/files/indexing-the-world_0.pdf

Consistent with the Principles for Financial Benchmarks published in 2013 by International Organization of Securities Commissions, which promotes regulatory standards for world's securities and futures markets, the operation of the country classification process is overseen by FTSE Russell's strong internal governance structure, and is supported by independent advisory committees consisting of senior market practitioners with extensive global market knowledge and experience.

FTSE Russell classifies countries according to objective criteria and engages with stock exchanges, regulators and central banks in those countries where markets are being considered for potential promotion or demotion. The transparency of the process provides portfolio managers and asset allocators with a clear view of expected future index evolution.

To give investors time to plan for potential classification changes, FTSE Russell operates a Watch List of those countries with scores on the Quality of Markets matrix that have been judged to have met (or are becoming close to meeting) the technical criteria required for reclassification. Saudi Arabia was added to the FTSE Watch List for possible reclassification to Secondary Emerging market status in September 2015. Since then, FTSE Russell's annual and interim updates have noted the Kingdom's steady progress toward meeting international equity-market norms (see ftserussell.com/sites/default/files/ftse_saudi_arabia_inclusion_indexes.pdf).

Clearing final criteria hurdles

In its early stages, Saudi Arabia's new registration process presented a high bar for participation, hindering foreign capital inflows. But Saudi policymakers moved quickly to make the market more foreign-investor friendly and aligned with the views and practices of the international investment community.

As part of the annual country classification review in September 2017, FTSE Russell announced that, given the number and speed of Saudi Arabia's recent enhancements, investors required more time to fully assess the operational efficacy of market changes. This was especially true for those to the QFI registration process and the Independent Custody Model (ICM), which would not be effective until January 2018.

Since September 2017, supported unanimously by the FTSE Country Classification Advisory Committee, FTSE Russell has engaged extensively on behalf of international investors with local stakeholders in Saudi Arabia, including with the local arms of global brokers, custodians and banking entities. Particular focus was given to the requirements of passive investors. The Saudi authorities listened and responded promptly to concerns expressed by the market practitioners who comprise the FTSE Russell advisory committees (asset managers, asset owners, custodians, and those involved in trading and broking global markets).

A streamlined QFI process

QFI registration was made a part of the account-opening process conducted via an Assessing Authorized Person (AAP)—which, under the Qualified Foreign Financial Institution Investment in Listed Securities rules, must have a dealing or custody license—replacing the previous separate approval process conducted by the CMA. Among the key improvements:

- Applicants now register all funds and subsidiaries they manage in one application rather than applying individually.
- Client on-boarding happens at the global broker-level, with no requirement for a direct relationship between the end beneficiary and the local broker.

These changes have significantly streamlined the process, with registration now taking between five to seven working days versus the one month from receiving the completed documents it had been typically taking previously.

New rules for failed trade settlement

Under the revised Independent Custody Model, effective January 21, 2018, custodians are permitted to reject buy trades not funded by their clients and transfer the settlement obligation to the local broker. (Funding lines are supported by a letter of guarantee, issued by the clearing agent).

The rationale behind this shift is to spread the risk as more brokers entered the market. HSBC Saudi Arabia is the largest custodian in the country (and in the Gulf region as a whole). Previously, HSBC Saudi Arabia operated on a daily credit limit of US\$16 million per national identification number (NIN), raising the risk that, if the situation occurred, the firm would not be in a position to settle a large amount of failed buy trades not pre-funded by its clients. The lack of a central counterparty clearinghouse in Saudi Arabia (though one is planned for 2019) combined with the size of the Saudi market added to this risk. Feedback from local brokers and advisory investors since the January 2018 ICM enhancement has indicated that the new process meets the trading requirements associated with a market entering a global equity benchmark.

Saudi Arabia: Key Events

| Historical milestones | | Market reform milestones | |
|-----------------------|---|--------------------------|---|
| 1932 | The Kingdom of Saudi Arabia is founded | 2016 | <ul style="list-style-type: none"> Relaxes QFI eligibility rules: foreign institutional investors required to have at least US\$1 billion in assets under management (AUM), down from US\$5 billion previously Relaxes QFIs ownership rules: individual funds may own up to 10% of the shares of a single listed issuer; up from 5%. Also removed the maximum ownership allowed by QFIs from 20% per issue Introduces Real Estate Investment Trust (REIT) regulations |
| 1938 | Oil is discovered and production begins under the US-controlled Arabian American Oil Company | | |
| 1960 | Saudi Arabia is a founding member of OPEC | | |
| 1972 | Saudi Arabia gains control of 20% of Aramco | 2017 | <ul style="list-style-type: none"> Allows QFIs to participate in IPOs, vs only secondary deals previously Launches <u>Nomu</u>, a parallel equity market with less stringent listing requirements for smaller companies Adopts new CMA Corporate Governance rules Migrates from T+0 settlement cycle to T+2 with a Delivery versus Payment (DvP) model Eliminates cash-prefunding requirement for placing orders Authorizes securities lending and short selling |
| 1980 | Saudi Arabia assumes full control of Aramco | | |
| 1993 | Consultative Council is created, composed of a chairman and 60 members chosen by the king | | |
| 2003 | The king grants Consultative Council powers to propose legislation without his permission | 2018 | <ul style="list-style-type: none"> Reduces AUM requirements to US\$500 million from US\$1 billion and removes the need for QFIs' subsidiaries and managed strategies to submit separate applications Enhances Independent Custody Model to shift obligation for settling failed trades from the custodian to local brokers TO COME: Introducing a clearinghouse for derivatives trading and cross-list stocks with other Gulf and international exchanges; moving from a volume-weighted average price process to an auction method for determining closing prices |
| 2005 | Saudi Arabia joins the World Trade Organization | | |
| 2015 | Saudi Stock Exchange (<u>Tadawul</u>) opens to direct foreign investment, with restrictions | | |
| 2016 | Government unveils Vision 2030 | | |

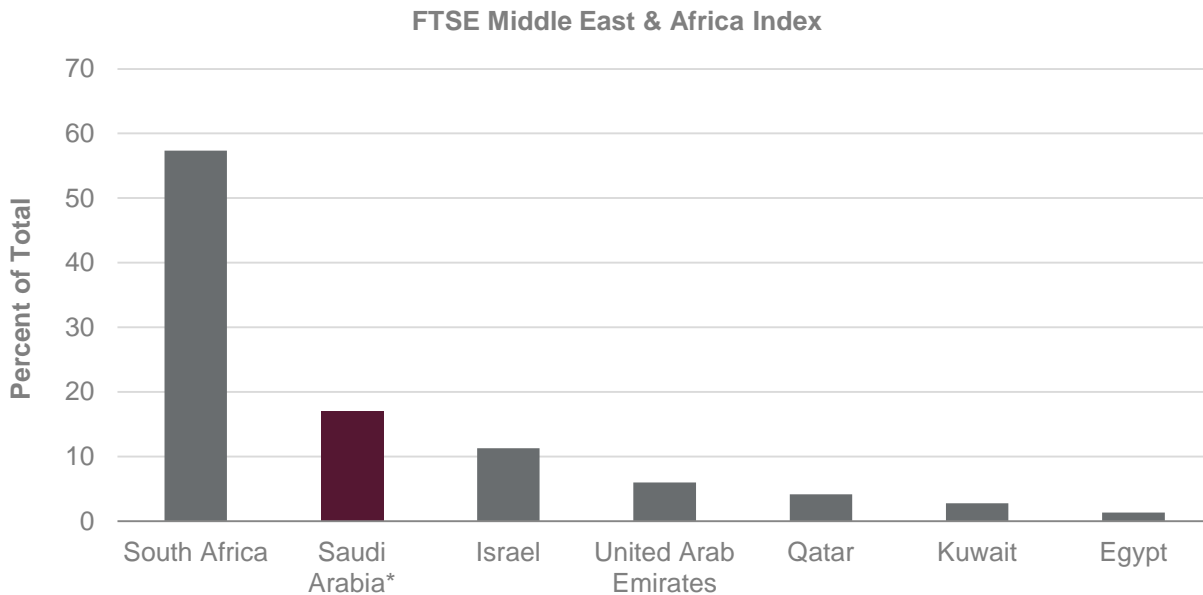
Source: FTSE Russell, Saudi Ministry of Finance

Prominent emerging market status

Saudi Arabia's inclusion in the FTSE benchmark is the largest such event in the developing equity markets since 2001, and an important development for both passive and active investors.

The country comprises 17% of the FTSE Middle East & Africa Index, second only to South Africa in market size among the index's constituents.

Chart 6. Saudi Arabia is the largest equity market in the Middle East

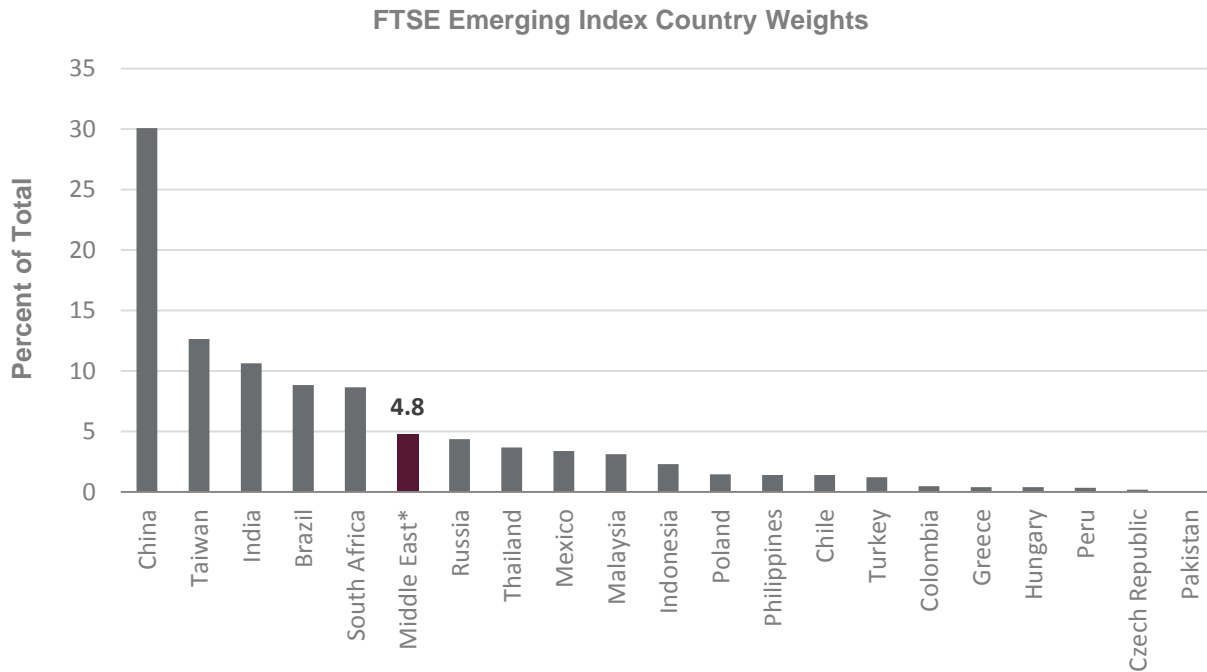


*Saudi Arabia represented by the FTSE Saudi Arabia Inclusion Index.
Source: FTSE Russell. Data as of February 28, 2018.

At 2.7% of the FTSE Emerging Index, the Kingdom ranks as the 10th-largest stock market in the index. With an estimated US\$200 billion of passive assets tracking the FTSE Emerging Index, the inclusion of Saudi Arabia, upon completion, could attract approximately US\$5.4 billion in passive inflows. The country joins smaller neighbor Kuwait, which was reclassified as a Secondary Emerging market in the FTSE GEIS benchmarks in September 2017 and will be implemented in two 50% tranches in September and December this year. Kuwait's reclassification is expected to draw as much as US\$800 million of passive inflows.

The entry of these two Gulf markets significantly strengthens the Middle East's presence within global equity benchmarks. Along with current constituents United Arab Emirates, Qatar and Egypt, the two newcomers increase the Middle East's exposure to 4.8% of the FTSE Emerging Index and to 6.8% of the FTSE Emerging Index excluding China.

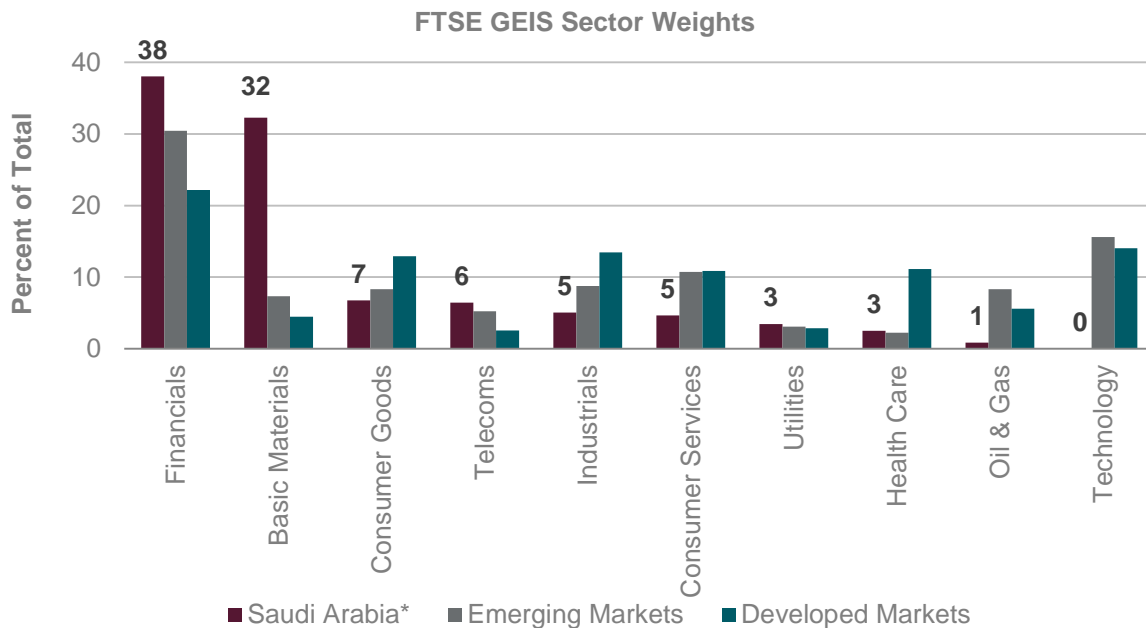
Chart 7. Saudi's entry bolsters the Middle East's presence in emerging stocks



*Includes current constituents UAE, Qatar and Egypt; Saudi Arabia represented by the FTSE Saudi Arabia Inclusion index
 Source: FTSE Russell. Data as of February 28, 2018.

The Saudi equity market is heavily concentrated in Financials and Basic Materials stocks. The two sectors account for more than 70% of the FTSE Saudi Arabia Inclusion Index, well above their weights in the emerging-market and developed-market indexes. Notably, for a country virtually synonymous with the oil markets, there are few ways to directly invest in the sector. Oil & Gas stocks make up less than 1% of the inclusion index, significantly underweight versus international peers.

Chart 8. Saudi equity market is concentrated in Financials and Basic Materials



*FTSE Saudi Arabia Inclusion Index.
 Source: FTSE Russell. Data as of February 28, 2018

Banks comprise half of the top 10 public Saudi Arabian companies by market capitalization, accounting for nearly 30% of the FTSE Saudi Arabia Inclusion Index. Al Rajhi Bank is the world's largest Islamic bank based on total assets.³ Top-listed Saudi Basic Industries is the world's fourth-largest chemical producer by sales.⁴

Chart 9. Banks make up half of the 10 largest stocks by market capitalization

| FTSE Saudi Arabia All Cap Index: Top 10 Companies by Market Capitalization | | | | |
|--|--------------------|------------|-------------------------|----------------------------------|
| Company | ICB Sector | % of Index | Market Cap USD billions | Avg. Daily Traded Value USD Mil. |
| Saudi Basic Industries | Chemicals | 15.7 | 21.0 | 101.4 |
| Al Rajhi Banking & Investment | Banks | 11.6 | 15.5 | 59.4 |
| National Commercial Bank | Banks | 8.4 | 11.3 | 6.5 |
| Saudi Telecom Co | Telecommunications | 5.2 | 6.9 | 4.4 |
| Samba Financial Group | Banks | 4.8 | 6.5 | 5.3 |
| Saudi Arabian Mining Co-Ma'aden | Mining | 4.2 | 5.6 | 7.4 |
| Almarai Co Ltd | Food Producers | 4.0 | 5.4 | 5.1 |
| Riyad Bank | Banks | 3.9 | 5.2 | 1.6 |
| Saudi Electricity | Electricity | 3.2 | 4.3 | 5.6 |

Source: Tadawul and FTSE Russell. Data as of February 28, 2018.

Financial services companies also dominate the 10 largest stocks by foreign ownership. This is an outgrowth of the Kingdom's entry into the World Trade Organization in 2005, when it relaxed many restrictions on foreign insurers and banks as part of efforts to accelerate the country's integration into the global trading system.

³ Islamic Finance.com and Islamic Financial Services Board data

⁴ Chemical & Engineering News, (July 25, 2016), "Global Top 50 Chemical Companies"

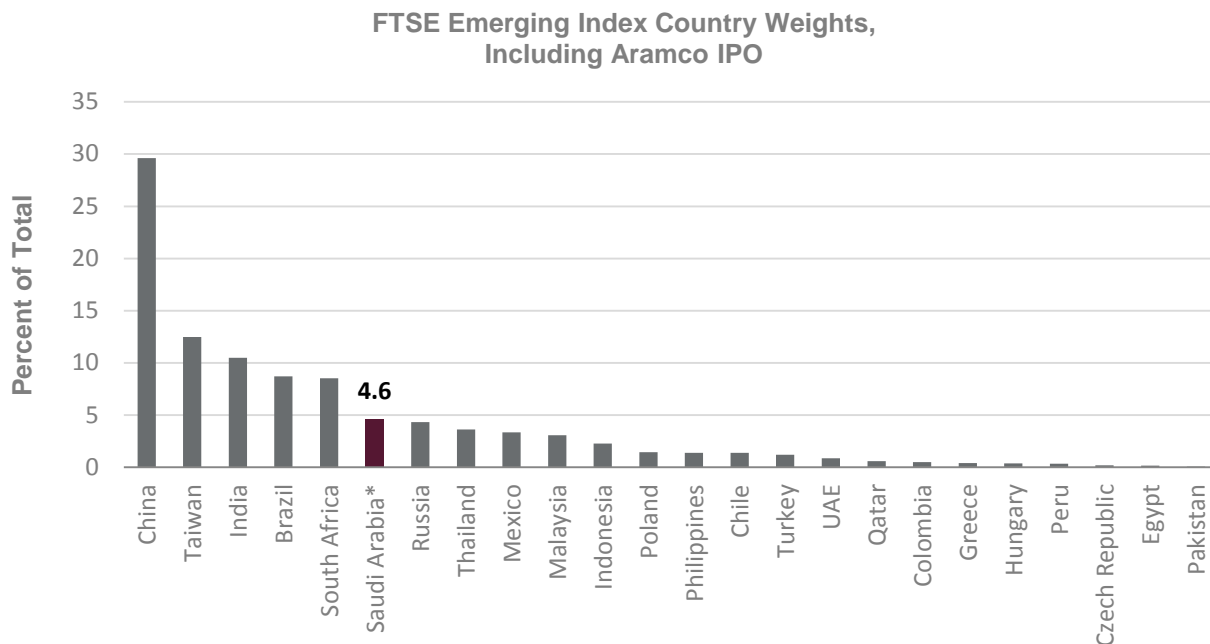
Chart 10. Insurers and banks dominate the largest foreign-owned Saudi stocks

| FTSE Saudi Arabia All Cap Index: Top 10 Companies by Foreign Ownership | | | |
|--|------------|---------------------|-----------------|
| Company | ICB Sector | % Foreign Ownership | Maximum Limit % |
| BUPA Arabia | Insurance | 41.8 | 49 |
| MetLife AIG ANB | Insurance | 40.8 | 49 |
| Saudi Arabia British Bank | Banks | 40.8 | 49 |
| Alawwal | Banks | 40.6 | 49 |
| Arab National Bank | Banks | 40.6 | 49 |
| Rabigh Refining & Petrochemical | Oil & Gas | 38.1 | 49 |
| Allianz Saudi Fransi Cooperative | Insurance | 33.1 | 49 |
| Chubb | Insurance | 32.6 | 49 |
| Arabia Insurance Cooperative Co. | Insurance | 32.1 | 49 |
| Alinma Tokio Marine | Insurance | 29.4 | 49 |

Source: Tadawul and FTSE Russell. Data as of February 28, 2018.

The Saudi Aramco IPO would significantly elevate the Kingdom’s emerging-market presence. Each US\$10 billion of capital raised increases Saudi Arabia’s weight in the FTSE Emerging Index by an estimated 24 basis points. Thus, assuming a 5% float and an IPO market capitalization of US\$100 billion, Saudi Arabia’s weight could rise to 4.6% of the FTSE Emerging Index and to 6.6% of the index excluding China—about matching Russia and surpassing Thailand and Mexico.

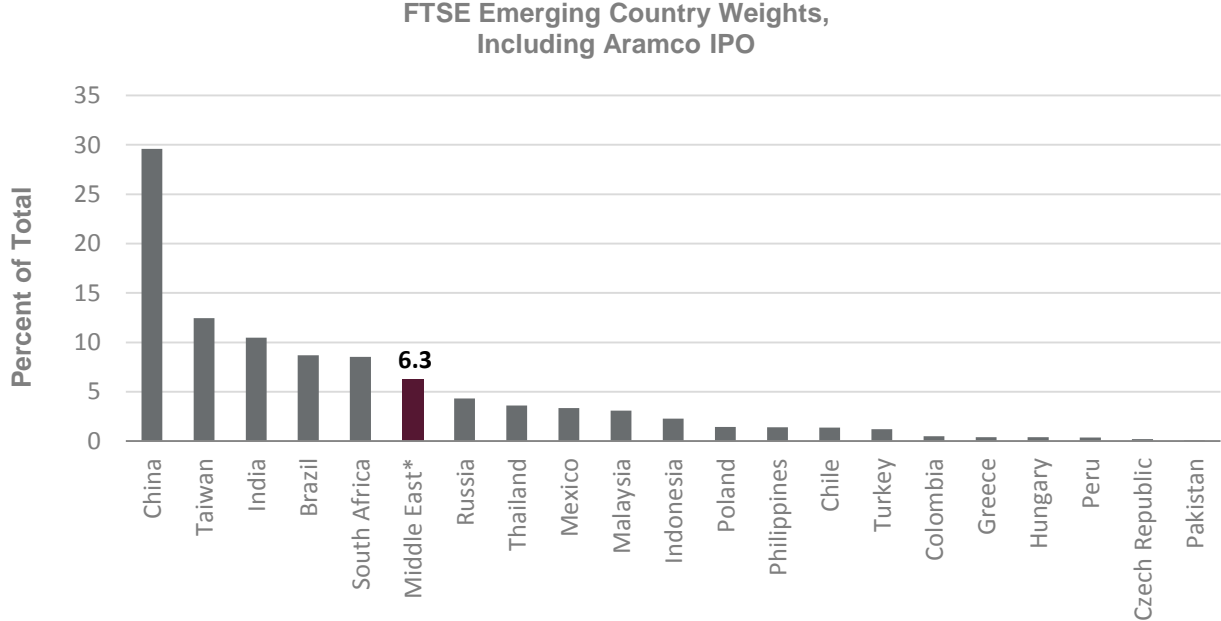
Chart 11. Aramco IPO would elevate Saudi Arabia’s emerging-market position



*FTSE Saudi Arabia Inclusion index, assuming Aramco IPO market capitalization of US\$100 billion.
Source: FTSE Russell. Data as of February 28, 2018.

The Aramco flotation would also significantly boost the FTSE Emerging Index's Middle East exposure. Including Kuwait and assuming an IPO market capitalization of US\$100 billion, the listing will raise the Middle East weight by an estimated 150 basis points to 6.3%.

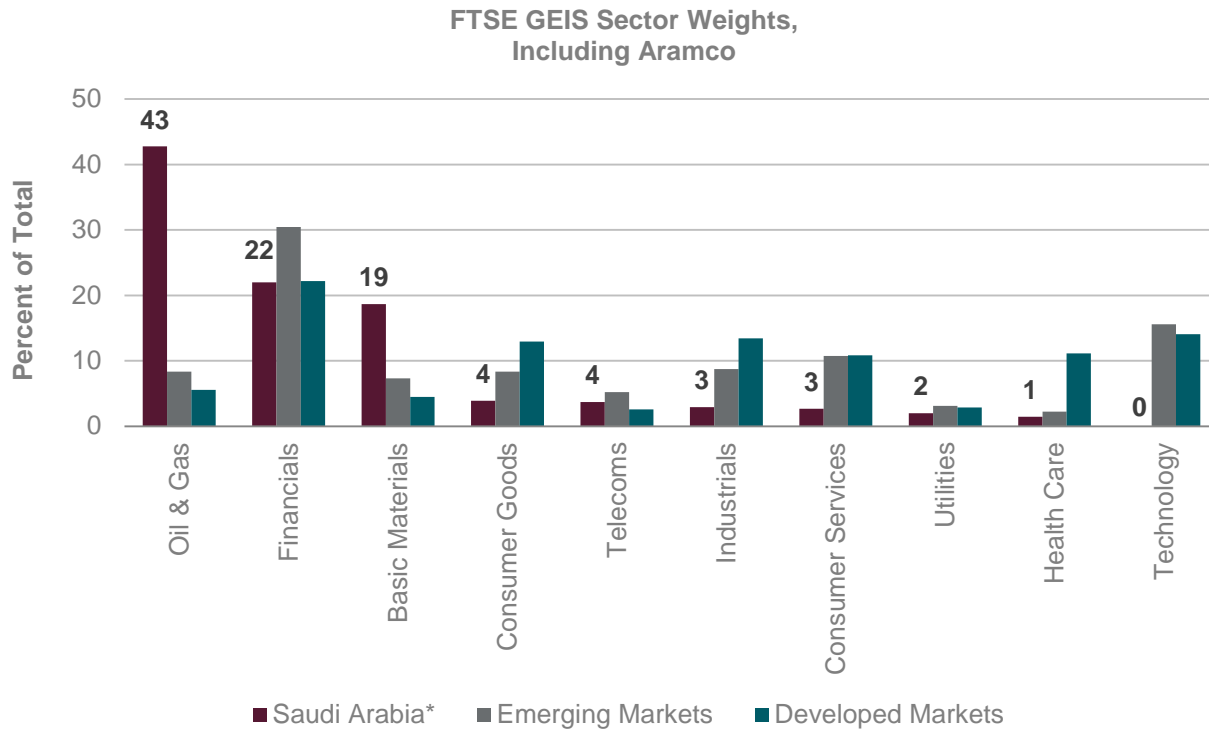
Chart 12. Aramco IPO would also lift the Middle East's presence in emerging markets



*Includes current constituents UAE, Qatar and Egypt; Saudi Arabia represented by the FTSE Saudi Arabia Inclusion Index, assuming Aramco IPO market capitalization of US\$100 billion.
 Source: FTSE Russell. Data as of February 28, 2018.

Similarly, the Aramco addition would dramatically alter the Saudi market's sector composition. A US\$100 billion IPO capital raise could lift the Oil & Gas weight to roughly 43% of the FTSE Saudi Arabia Inclusion Index—a significant overweight relative to that of emerging and developed-market peers. It would also dilute the Saudi market's concentration in Financials and Basic Materials to around 22% and 19%, respectively.

Chart 13. Aramco IPO would dramatically alter the Saudi market's sector profile



*FTSE Saudi Arabia Inclusion Index, assuming an Aramco IPO market capitalization at US\$100 billion.
Source: FTSE Russell. Data as of February 28, 2018.

Index inclusion implementation

With such large inclusions to an index, implementation needs to be undertaken carefully to ensure that mechanisms are operating as expected, to minimize price pressure on new constituents and to spread outflows from those markets being sold down.

Saudi Arabia inclusion

The table below outlines the implementation plan for Saudi Arabia's entry into the FTSE Global Equity Index Series, based on a Saudi weight of 2.7% in the FTSE Emerging Index. The implementation will commence in conjunction with the March 2019 semi-annual review and be completed by December 2019. The initial 25% tranche will be split over March and April 2019 to ensure a smooth phasing-in of Saudi Arabia. The remaining 75% will be implemented in conjunction with the quarterly reviews in June, September and December 2019.

| Review Schedule | Tranche One March | Tranche Two April | Tranche Three June | Tranche Four September | Tranche Five December |
|----------------------------------|-------------------------------|-------------------------------|------------------------------|--------------------------------------|-------------------------------------|
| Effective Date | Open Monday March 18, 2019 | Open Monday April 22, 2019 | Open Monday June 24, 2019 | Open Monday September 23, 2019 | Open Monday December 23, 2019 |
| Saudi Arabia Inclusion Factor | 10% | 15% | 25% | 25% | 25% |
| Total | 10% | 25% | 50% | 75% | 100% |

Source: FTSE Russell.

Aramco inclusion

Depending on the timing of the Saudi Aramco IPO, FTSE Russell proposes to implement Saudi Aramco's inclusion into the FTSE GEIS as follows:

- If the IPO of Aramco takes place prior to the commencement of Saudi Arabia's transition into GEIS, Aramco would be included as part of the Saudi Arabia implementation.
- If the IPO of Aramco takes place during the transition, the proportion of Saudi Aramco to be included at IPO would be equal to the percentage of Saudi Arabia that had been transitioned as of the IPO date. The remainder would be added in conjunction with the remaining transition of Saudi Arabia.
- If the IPO of Aramco takes place after the transition is completed, Aramco would be treated as a standard IPO.

Further clarification will be provided once a listing date and details regarding the size of the offering are announced.

Conclusion

Saudi Arabia's promotion to Secondary Emerging market status in FTSE GEIS recognizes rapid and commendable development of the country's equity markets, following a rigorous index-inclusion process that has spurred major market reforms that improved foreign investor access and confirmed the security of assets. The Kingdom's entry expands and diversifies the opportunity set for both passive and active investors, and gives access to a large, dynamic economy within the emerging-market universe.

Appendix

| FTSE QUALITY OF MARKETS CRITERIA | | | | |
|---|-----------|-------------------|--------------------|----------|
| Criteria | Developed | Advanced Emerging | Secondary Emerging | Frontier |
| World Bank GNI Per Capita Rating | | | | |
| Credit Worthiness | | | | |
| Market and Regulatory Environment | | | | |
| Formal stock market regulatory authorities actively monitor market (e.g., SEC, FSA, SFC) | ✓ | ✓ | ✓ | ✓ |
| Fair and non-prejudicial treatment of minority shareholders | ✓ | ✓ | | |
| No or selective incidence of foreign ownership restrictions | ✓ | ✓ | | |
| No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income | ✓ | ✓ | ✓ | ✓ |
| Free and well-developed equity market | ✓ | ✓ | | |
| Free and well-developed foreign exchange market | ✓ | ✓ | | |
| No or simple registration process for foreign investors | ✓ | ✓ | | |
| Custody and Settlement | | | | |
| Settlement - Rare incidence of failed trades | ✓ | ✓ | ✓ | ✓ |
| Custody-Sufficient competition to ensure high quality custodian services | ✓ | ✓ | ✓ | |
| Clearing & Settlement - T + 2 / T + 3 | ✓ | ✓ | ✓ | ✓ |
| Settlement - Free delivery available | ✓ | | | |
| Custody - Omnibus and segregated account facilities available to international investors | ✓ | ✓ | | |
| Dealing Landscape | | | | |
| Brokerage - Sufficient competition to ensure high quality broker services | ✓ | ✓ | ✓ | |
| Liquidity - Sufficient broad market liquidity to support sizeable global investment | ✓ | ✓ | ✓ | |
| Transaction costs - implicit and explicit costs to be reasonable and competitive | ✓ | ✓ | ✓ | |
| Stock Lending is permitted | ✓ | | | |
| Short sales permitted | ✓ | | | |
| Off-exchange transactions permitted | ✓ | | | |
| Efficient trading mechanism | ✓ | | | |
| Transparency - market depth information / visibility and timely trade reporting process | ✓ | ✓ | ✓ | ✓ |
| Derivatives | | | | |
| Developed Derivatives Market | ✓ | | | |

Source: FTSE Russell. Data as of February 28, 2018.

FTSE SAUDI ARABIA ALL CAP INDEX

| Company Constituents | Market Cap (USD) | Index Weight (%) | Avg. Daily Trading Value (USD) | DTV as % of Market Cap | Days to Trade \$1Bil. Basket |
|---|------------------|------------------|--------------------------------|------------------------|------------------------------|
| Saudi Basic Industries Corp | 20,958,323,334 | 15.7 | 101,360,425 | 0.48 | 1.6 |
| Al Rajhi Banking & Investment | 15,516,078,714 | 11.6 | 59,371,253 | 0.38 | 2.0 |
| National Commercial Bank* | 11,254,577,293 | 8.4 | 6,548,079 | 0.06 | 12.9 |
| Saudi Telecom | 6,882,862,704 | 5.2 | 4,398,358 | 0.06 | 11.7 |
| Samba Financial Group | 6,451,803,856 | 4.8 | 5,268,575 | 0.08 | 9.2 |
| Saudi Arabian Mining Co-Ma'aden | 5,564,783,079 | 4.2 | 7,374,981 | 0.13 | 5.7 |
| Almarai Co. Ltd. | 5,363,890,889 | 4.0 | 5,088,073 | 0.09 | 7.9 |
| Riyad Bank | 5,154,387,649 | 3.9 | 1,550,920 | 0.03 | 24.9 |
| Saudi Electricity | 4,261,917,856 | 3.2 | 5,551,435 | 0.13 | 5.8 |
| Alinma Bank | 3,888,328,934 | 2.9 | 103,726,239 | 2.67 | 0.3 |
| Yanbu National Petrochemicals | 3,852,891,769 | 2.9 | 3,439,569 | 0.09 | 8.4 |
| Saudi Arabian Fertilizer | 3,309,735,224 | 2.5 | 1,429,387 | 0.04 | 17.4 |
| SAVOLA | 2,569,551,559 | 1.9 | 2,572,676 | 0.10 | 7.5 |
| Saudi Kayan Petrochemical | 2,502,719,782 | 1.9 | 35,415,111 | 1.42 | 0.5 |
| Jarir Marketing | 1,999,040,077 | 1.5 | 2,436,362 | 0.12 | 6.2 |
| National Industrialization | 1,576,657,672 | 1.2 | 3,342,818 | 0.21 | 3.5 |
| Etihad Etisalat | 1,455,758,473 | 1.1 | 13,578,490 | 0.93 | 0.8 |
| Rabigh Refining & Petrochemical | 1,396,816,255 | 1.0 | 26,696,664 | 1.91 | 0.4 |
| Emaar Economic City | 1,392,664,587 | 1.0 | 2,751,395 | 0.20 | 3.8 |
| Dar Al Arkan Real Estate Development | 1,378,632,109 | 1.0 | 82,791,222 | 6.01 | 0.1 |
| Bank Albilad | 1,260,267,179 | 0.9 | 2,296,014 | 0.18 | 4.1 |
| Saudi Industrial Investment Group | 1,207,655,388 | 0.9 | 2,560,989 | 0.21 | 3.5 |
| Mouwasat Medical Services | 1,130,341,573 | 0.8 | 962,532 | 0.09 | 8.8 |
| Advanced Petrochemical | 1,125,172,830 | 0.8 | 2,595,745 | 0.23 | 3.3 |
| Tawuniya | 1,076,117,244 | 0.8 | 5,771,861 | 0.54 | 1.4 |
| Saudi Cement | 1,011,914,087 | 0.8 | 1,062,461 | 0.10 | 7.1 |
| Sahara Petrochemical | 952,846,098 | 0.7 | 5,094,337 | 0.53 | 1.4 |
| Abdullah Al Othaim Markets | 890,748,740 | 0.7 | 2,509,159 | 0.28 | 2.7 |
| Saudi International Petrochemical | 890,117,234 | 0.7 | 4,543,311 | 0.51 | 1.5 |
| Bank Al-Jazira | 860,815,401 | 0.6 | 6,209,506 | 0.72 | 1.0 |
| BUPA Arabia | 817,086,633 | 0.6 | 4,660,295 | 0.57 | 1.3 |
| Saudi Airlines Catering | 786,638,509 | 0.6 | 3,695,924 | 0.47 | 1.6 |
| Al Tayyar Travel Group | 779,852,384 | 0.6 | 8,304,075 | 1.06 | 0.7 |
| Middle East Healthcare** | 659,432,253 | 0.5 | 1,681,026 | 0.25 | 2.9 |
| Saudia Research and Marketing | 648,600,912 | 0.5 | 10,414,711 | 1.61 | 0.5 |
| Yanbu Cement | 646,160,307 | 0.5 | 2,337,642 | 0.36 | 2.1 |
| Saudi Ground Services | 614,229,582 | 0.5 | 3,079,534 | 0.50 | 1.5 |
| Dallah Healthcare Holding | 551,094,579 | 0.4 | 773,329 | 0.14 | 5.3 |
| Qassim Cement | 536,213,103 | 0.4 | 429,938 | 0.08 | 9.4 |
| Mobile Telecommunications Co. Saudi Arabia (Zain) | 535,360,702 | 0.4 | 2,538,692 | 0.47 | 1.6 |

| | | | | | |
|---|-------------|-----|-----------|------|-----|
| Fawaz Abdulaziz Alhokair | 508,433,725 | 0.4 | 2,999,943 | 0.59 | 1.3 |
| Saudi Dairy & Foodstuff | 505,525,225 | 0.4 | 1,553,006 | 0.31 | 2.4 |
| National Petrochemical | 460,763,139 | 0.3 | 789,862 | 0.17 | 4.4 |
| Saudi Pharmaceutical Industries | 457,522,371 | 0.3 | 596,261 | 0.13 | 5.8 |
| Arabian Cement | 449,980,002 | 0.3 | 1,571,216 | 0.35 | 2.1 |
| Yamamah Saudi Cement | 431,528,078 | 0.3 | 1,022,451 | 0.24 | 3.2 |
| National Agriculture Development | 353,687,940 | 0.3 | 1,243,717 | 0.35 | 2.1 |
| Arriyadh Development | 345,280,821 | 0.3 | 733,775 | 0.21 | 3.5 |
| National Medical Care | 317,608,271 | 0.2 | 4,433,795 | 1.40 | 0.5 |
| National Gas & Industrialization | 295,054,396 | 0.2 | 234,761 | 0.08 | 9.4 |
| Al Hammadi Company for Development and Investment* | 292,936,565 | 0.2 | 4,963,092 | 1.69 | 0.4 |
| Eastern Cement | 288,551,636 | 0.2 | 295,827 | 0.10 | 7.3 |
| City Cement | 268,955,294 | 0.2 | 1,875,644 | 0.70 | 1.1 |
| Saudi Chemical | 268,537,717 | 0.2 | 963,095 | 0.36 | 2.1 |
| Herfy Food Services | 257,181,601 | 0.2 | 1,842,975 | 0.72 | 1.0 |
| Saptco | 256,739,461 | 0.2 | 780,499 | 0.30 | 2.5 |
| Real Estate/Saudi Arabia | 248,120,950 | 0.2 | 235,286 | 0.09 | 7.9 |
| Northern Region Cement | 246,705,064 | 0.2 | 2,338,801 | 0.95 | 0.8 |
| United International Transportation Co. Ltd. | 245,636,296 | 0.2 | 2,528,787 | 1.03 | 0.7 |
| United Electronics | 244,937,845 | 0.2 | 3,679,171 | 1.50 | 0.5 |
| Najran Cement | 207,900,168 | 0.2 | 2,136,441 | 1.03 | 0.7 |
| Zamil Industrial Investment | 201,236,701 | 0.2 | 338,934 | 0.17 | 4.5 |
| Dur Hospitality* | 193,125,883 | 0.1 | 901,283 | 0.47 | 1.6 |
| Al Jouf Cement | 189,827,800 | 0.1 | 3,951,610 | 2.08 | 0.4 |
| Aseer | 184,455,725 | 0.1 | 996,702 | 0.54 | 1.4 |
| Tabuk Cement | 173,093,353 | 0.1 | 4,925,974 | 2.85 | 0.3 |
| Aldrees Petroleum | 166,390,689 | 0.1 | 1,165,770 | 0.70 | 1.1 |
| Saudi Ceramic | 163,646,908 | 0.1 | 658,411 | 0.40 | 1.9 |
| Methanol Chemicals | 157,728,966 | 0.1 | 5,308,670 | 3.37 | 0.2 |
| Abdulmohsen Al Hokair Group for Tourism and Development | 148,680,239 | 0.1 | 2,396,807 | 1.61 | 0.5 |
| Red Sea Housing Services | 144,871,610 | 0.1 | 341,533 | 0.24 | 3.2 |
| Astra Industrial Group | 142,633,923 | 0.1 | 310,855 | 0.22 | 3.4 |
| Bawan Co Ltd | 133,661,307 | 0.1 | 823,991 | 0.62 | 1.2 |
| Saudi Marketing Company | 127,458,603 | 0.1 | 1,080,310 | 0.85 | 0.9 |
| Hail Cement | 118,446,914 | 0.1 | 1,870,611 | 1.58 | 0.5 |
| Saudi Arabian Amiantit | 116,048,196 | 0.1 | 2,620,566 | 2.26 | 0.3 |
| Mediterranean & Gulf Insurance & Reinsurance | 109,648,828 | 0.1 | 3,190,976 | 2.91 | 0.3 |
| Al Abdullatif Industrial | 93,843,826 | 0.1 | 161,210 | 0.17 | 4.4 |
| Al-Hassan G.I. Shaker | 84,535,877 | 0.1 | 501,902 | 0.59 | 1.3 |

*State joint-stock company

**Closed joint-stock company

Source: FTSE Russell. Data as of February 28, 2018.

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