

Does higher FX purchases mean more rouble dependence on OFZ flows?

FX purchases in May were less than expected, probably due to temporary issues with the Druzhba oil pipeline, but suggest an increase vs. April and imply complete sterilisation of the current account. We think this favours RUB depreciation in the months ahead unless foreign capital continues to flow into Russia's rouble-denominated local state bonds



Source: Terrazzo

The Russian finance ministry announced that it will spend RUB 301 billion (an equivalent of \$4.6 billion at the current FX rate) for FX purchases between 14 May and 6 June, as per the budget rule.

Even though below expectations, the volume of total FX purchases will still be a \$0.5 billion increase in May vs April

The amount includes the RUB 314 billion in extra fuel revenues of the budget expected in May and the RUB 14 billion downward revision in the extra fuel revenues for April. Combined with

the August-December 2018 backlog, when the Bank of Russia put market purchases on hold, the total amount of FX purchased on the market will be \$5.4 billion in May, up from the \$4.9 billion seen in April.

301 bn

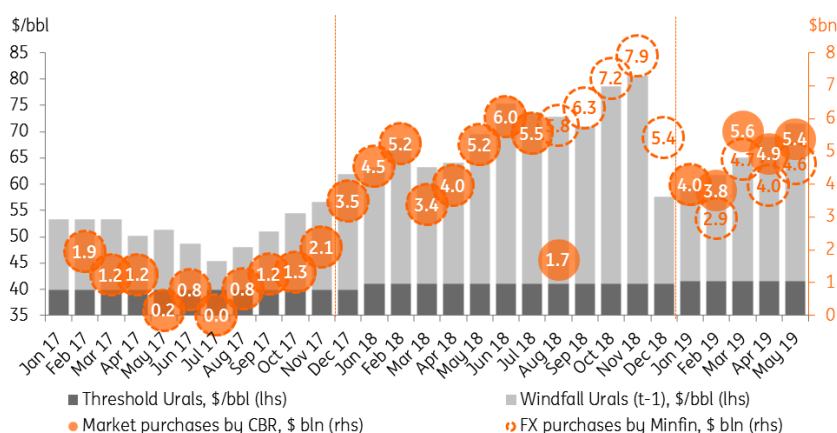
Minfin's FX purchases for May in roubles

Up from RUB 255 billion in April

Lower than expected

In our view, the oil and gas revenues expected by the ministry of finance for May are lower than what the oil prices suggest. In part, this deviation may be partly explained by the temporary outages in the crude oil supply to Europe at the end of April and early-May via the Druzhba pipeline, which accounts for 20% of Russia's oil exports. According to our estimates, those delayed exports have cost the budget up to RUB 25 bn of undercollected revenues. However, given the substitution of the supplies with the sea tankers and the gradual return of the Druzhba, export deliveries and the budget revenues may catch up later.

Monthly FX purchases by Russian Finance Ministry/Central Bank



Source: Bank of Russia, Finance Ministry, ING

Even though below expectations, the volume of total FX purchases will still be a \$0.5 billion increase in May vs. April amid the likely seasonal shrinking of the current account surplus. We continue to expect Russia's current account surplus to decline from \$10-11bn per month in 1Q19 to \$4-6bn per month in 2-3Q19, which suggest a near 100% sterilisation vs. just 40% in 1Q19.

This increases RUB's dependence on the portfolio flows into the Russian local state bonds, which so far have been favourable. According to official data, Russia's rouble-denominated OFZ market saw net capital inflows of c.\$4 billion in 1Q19, and might have seen another \$2-3bn in April, or up to 50% of the supply during the jumbo auctions, helping the rouble to appreciate by 8% in 4M19, significantly outperforming EM peers.

However, further prospects are less clear, as foreign investors have largely restored Russia's

positioning in their portfolio after the 2018 sell-off, while the overall emerging-market risk appetite seems to have saturated amid the more balanced Fed rhetoric and prolonged US-China trade negotiations.

Unless there are positive surprises in the market mood and a change in Russian corporates and households preferences, that so far have been accumulating foreign assets, USD/RUB should trade in the 65-67 range in the coming months.

Author

Dmitry Dolgin

Chief Economist, CIS

dmitry.dolgin@ing.de

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.