Russia: Strong budget surplus means less borrowing

The full year budget surplus is on track to come in at RUB2.5 trillion, or 2.5% of GDP, overshooting the new government's target by RUB0.5 trillion and supporting its decision to cut this year's borrowing by that amount. The net placement of RUB1.7 trillion in OFZ for 2019 could be revised, but not dramatically, as long as the budget rule remains intact

Source: istock

The Finance Ministry reported a strong RUB2.5 trillion (3.5% of GDP) federal budget surplus for the first nine months of 2018, overshooting both the RUB2.2 trillion consensus and our RUB2.3 trillion forecast. The outperformance was caused, not so much by the high oil price, but rather thanks to 15% YoY growth in non-oil revenue (vs. the annual plan of 10% YoY), which is a result of more efficient collection procedures, as well as tightly controlled 2% YoY expenditure growth, at the lower range of the annual 2-5% growth guidance.

The current trend suggests that the full-year surplus may remain at RUB2.5 trillion, exceeding the RUB2.0 trillion implied by the most recent revision in the macro assumptions incorporated into the official budget draft. As this is caused by an improvement in the non-oil balance, it also justifies the recent Finance Ministry's decision to cut the 2018 net local debt placement programme by RUB480 billion (including RUB380 billion open market placements) to RUB560 billion. With RUB360 billion net placement year-to-date, another RUB200 bn need to be placed in 4Q18

2.5 trillion

9M18 budget surplus (RUB)

(3.5% GDP)

Better than expected

We also see scope for a reduction in the massive RUB1.7 trillion net local debt placement programme scheduled for 2019 if the actual rouble exchange rate next year turns out to be weaker than the RUB63.9/USD drafted into the budget. According to our estimates, each RUB1/USD depreciation boosts the annual budget revenue by RUB80 billion and allows a reduction in debt issuance by that amount.

As a reminder, with the budget rule in place, any revenues received in 2019 as a result of the Urals price exceeding the $41.6/bbl threshold are supposed to be accumulated as government FX reserves and can't be used to finance current expenditures. The official budget draft for 2019 assumes a headline budget surplus of RUB1.9 trillion under a $63.4/bbl Urals price. However, cleaned from extra oil revenues the budget would be in RUB1.4 trillion deficit - requiring a net local debt placement of RUB1.7 trillion amid a scheduled reduction of other liabilities by RUB0.3 trillion.

As long as the budget rule is in place, the debt programme could be reduced as a result of rouble depreciation, higher than expected non-oil revenues or lower than expected expenditures. There are also calls to ease the budget rule - i.e. to increase the cut-off oil price by $5/bbl, which according to our estimates would add extra RUB650-700 billion of oil revenues available for spending and therefore would allow lowering the borrowing programme by that amount. Given the worsening in market conditions, we wouldn't rule out such a measure. However, changes to or a suspension of the budget rule would not be advisable from the standpoint of consistency in the budget policy framework.

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