Kuwait: Fiscal deficit in Q1 FY20/21 was smaller than expected, but set to rise

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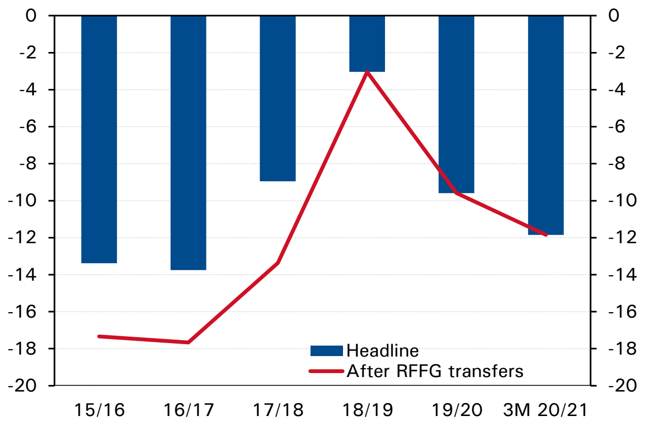
Highlights

- The fiscal deficit in the first quarter of FY2020/21 stood at KD 1.1 billion, much smaller than what the expected budget deficit for the year would imply.
- Low oil prices and pandemic-related restriction measures reduced both oil and non-oil revenues substantially, while total spending fell by 20% y/y driven by low capital spending.
- The financing of the projected large deficit of FY2020/21 could deplete most of the GRF resources.

The budget registered a deficit of KD 1.1 billion for the first quarter of FY2020/21 (April-June), compared with a surplus of KD 1.8 billion in the same period of FY2019/20 (Chart 1), according to the latest data released by the Ministry of Finance. It should be noted, however, that it would be difficult to draw any meaningful conclusions for the budget outcome for the whole fiscal year based on the first quarter results. This is due to timing issues in recording some spending transactions and the fact that spending tends to rise steeply toward the end of the fiscal year. Besides, the first quarter outcome is not commensurate with the government's own projection for a deficit of more than KD 14 billion for the current fiscal year.

Chart 1: Fiscal Balance

(% of GDP)

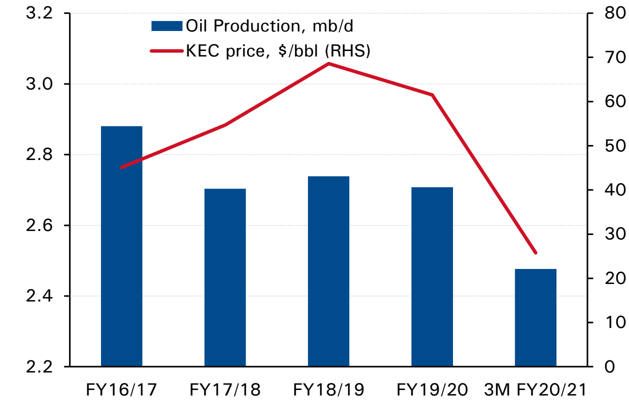


Source: Ministry of Finance, NBK estimates

Revenues fell sharply on lower oil prices and pandemic restrictions

Total revenues in the first quarter of FY2020/21 declined by 72.1% y/y to reach KD 1.4 billion compared to KD 4.9 billion in the first three months of FY2019/20. Oil revenues, which constituted around 96% of total revenues, fell by 71.1% y/y as Kuwait Export Crude (KEC) price plummeted by 62.1% y/y to an average of $25.78 per barrel, while oil production declined to 2.48 mb/d due to OPEC+ production cuts (Chart 2). On the other hand, the pandemic took its toll on non-oil revenues, declining by 84.5% y/y to KD 52.7 million only. Taxes and fees were hit hard, falling by 73%, following the weak performance of Kuwaiti and foreign companies as well as the steep decline in total trade (imports plus exports) during the three months from April to June by 50.1% y/y, according to the Central Statistical Bureau (CSB).

Chart 2: Oil Production and KEC price



Source: OPEC, NBK estimates

Strong decline in spending

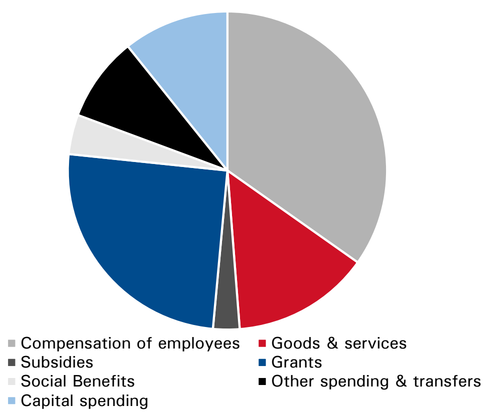
At the same time, total spending fell by 20.4% y/y, reaching KD 2.5 billion, driven by capital spending, which saw a decline of 65.3% y/y to KD 0.1 billion. Meanwhile, current spending plummeted by 15.6% y/y to KD 2.4 billion on account of the decline in compensation of employees, goods & services, grants, and social benefits (by 11.3%, 30.3%, 17.8%, and 44% y/y, respectively). However, the lower-than-expected current spending, especially on wages and subsidies, which are mainly constant, may be related to the time of recording these transactions. Moreover, current spending, which usually rises sharply towards the end of the fiscal year, will eventually catch up with the budgeted amounts.

The pandemic-related restrictions measures adversely affected project awards. In view of the expected large increase in the budget deficit, and the difficulty in containing recurrent spending such as wages and subsidies, capital spending will most likely continue to bear the brunt of fiscal adjustment this year and beyond.

The budget deficit for FY 2020/2021will be larger than what the first quarter results suggest

The revised budget for FY2020/2021, which was approved by parliament in September, was based on a more conservative oil price ($30 versus $55 in the original draft budget) and oil production (2.5 mb/d versus 2.7mb/d) with a projected deficit of KD 14.1 billion. Under these assumptions, oil revenues will decrease to KD 5.6 billion, while non-oil revenues was projected at KD 1.9 billion. On the other hand, total spending allocations (Chart 3) were reduced by about KD1 billion coming mainly from lower capital spending (29.3%) while current spending was kept relatively unchanged.

Chart 3: Relative importance of spending categories in FY20/21 budget
(% of total)



Source: Ministry of Finance

We expect the deficit to be smaller at about KD10.5 billion, or 33% of GDP, (based on $40/bbl for oil price and a 5% spending cut). Under all scenarios, most of the resources left in the General Reserve Fund (GRF) will be used to finance the expected deficit. While long overdue fiscal reforms have become necessary, no fiscal measures will be sufficient to address the public finance position in the short term. Therefore, approving the debt law (likely after the parliamentary elections of December 5) will provide a bridge financing towards addressing the structure of the budget by implementing several revenue and expenditure measures in the context of a comprehensive medium-term fiscal adjustment program. Using the resources in the Future Generations Fund for financing large current spending will not sit well with investors or credit rating agencies.

Table 1: Public finances, KD million unless otherwise stated

	3M FY2018/19	3M FY2019/20	3M FY2020/21	% y/y
Revenues	4,953.1	4,900.7	1,369.0	-72.1
Non-oil	239.4	338.9	52.7	-84.5
Oil	4,713.7	4,561.8	1,316.4	-71.1
Total Expenditures	2,594.4	3,088.4	2,458.4	-20.4
Current Expenditures	2,202.2	2,787.4	2,353.8	-15.6
Compensation of Employees	524.0	427.1	379.0	-11.3
Goods & Services	238.4	824.8	574.8	-30.3
Subsidies	14.4	18.1	143.1	689.1
Grants	1,169.0	1,258.2	1,034.3	-17.8
Social Subsidies	94.3	121.5	68.1	-44.0
Miscellaneous & Transfers	162.1	137.6	154.6	12.4
Capital Expenditures	392.2	301.0	104.5	-65.3
Budget Balance	2,358.7	1,812.2	-1,089.4	...

Source: Ministry of Finance

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