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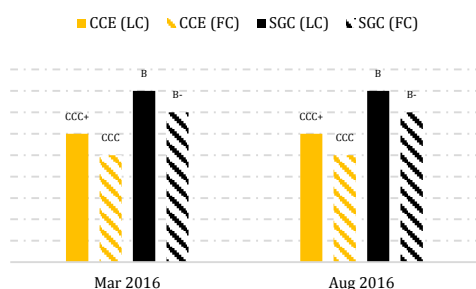
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Ratings

Sovereign Government Credit (LC)	B
Sovereign Government Credit (FC)	B-
Country Credit Environment (LC)	CCC+
Country Credit Environment (FC)	CCC

* These ratings are unsolicited

Ratings dynamics



Main Economic Indicators of Belarus

Macro indicators	2013	2014	2015
Gross gov. debt, BYR bn	251229	314762	420144
Nominal GDP, BYR bn	649111	778456	869702
Real GDP growth, %	1,0	1,6	-3,9
Gross gov. debt/GDP, %	38,7	40,4	48,3
Deficit (surplus)/GDP, %	-0,8	1,1	1,5
Inflation rate, %	16,5	16,2	12,0
Current Account Balance/GDP, %	-	-	-1,9
External debt, USD bn	-	-	22,8
Development indicators	2015		
Inequality adj. HDI	0,74		
GDP per capita, USD th	17,8		
Default indicator	31.03.2016		
10Y Gov Bond Yield, %	7,2		

Source: RAEX (Europe) calculations based on data from the IMF, WB, NBRB, CIA,

Summary

The ratings of Belarus are positively affected by the country's low debt metrics and improving fiscal consolidation. Even though the financial sector keeps showing structural imbalances, the recently implemented reforms could curve these risks in the long run.

External exposure remains one of the country's major risks as imports stood around 70% of GDP in 2015, external debt of the government is relatively high and exchange rate volatility could be triggered following the devaluation of RUB.

Even though the monetary policy is clearly outlined, its implementation could be potentially hindered as some targets are inconsistent with current monetary developments and forecasts of macro indicators.

Financial sector reforms are underway. Authorities have recently instrumented a number of reforms which could lead to a more stable and predictable financial sector. Alongside improvements of banks' risk assessment, the National Bank of the Republic of Belarus (NBRB) is targeting to further develop the stock market and its regulation as well as to strengthen the current regulation in smaller financial industries such as microfinance and leasing.

Furthermore, the recent development of the Institute of Credit Histories is likely to have a positive impact on the already high level of NPLs (6,8% as of 2015) as historical data of debtors would be more available to market participants.

Nonetheless, the structure of the country's banking sector continues to pose a structural risk for the government as the three largest state-owned banks account for 60% of total assets and the government is a minority shareholder in several private banks.

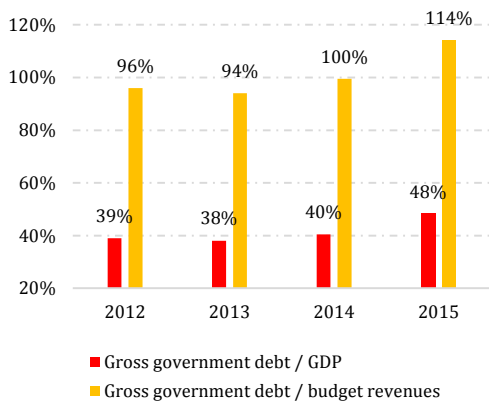
Additionally, the still large amount of loans granted through state-owned banks at subsidized interest rates presents a risk for the fiscal stance of the government as well as for the banks, which offer loans at a market rate. This hurts competition and the effectiveness of the financial markets as rates are not set according to the actual demand for money.

Debt metrics low but increasing. Fueled by further Eurobond issuance and the depreciation of the BYR against the USD, Belarus gross government debt increased by 33% up to BYR 630 tn in 2015. This,

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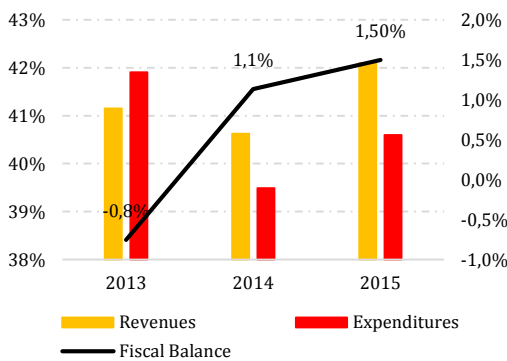
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Graph 1: Government debt metrics, %



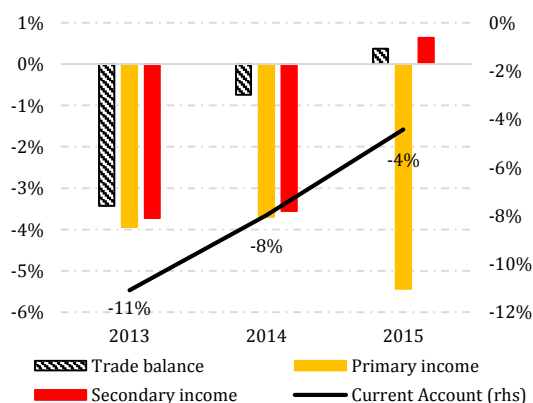
Source: RAEX (Europe) calculations based on data from the IMF and Belarusian Ministry of Finance

Graph 2: Fiscal balance, % GDP



Source: RAEX (Europe) calculations based on data from the IMF and Belarusian Ministry of Finance

Graph 3: Belarus' current account, % GDP



Source: RAEX (Europe) calculations based on data from the NBRB

combined with a meager increase of nominal GDP and fiscal revenues, drove the strongest increase of debt metrics observed during the past four years pushing government debt load up to 48% of GDP and 115% of fiscal revenues in 2015 (see graph 1).

Even though these figures are not worrisome according to the Agency's criteria, the share of FX-denominated government debt (that we estimate at around 70% of total debt) represents a potential risk for the Belarusian government as the country's trade matrix and the recession in Russia are obstacles for raising FX reserves. By end-June 2016, FX reserves at the NBRB stood at USD 4,3 bn and covered as low as 19% of total FX denominated debt and one month of 2015 imports.

However, the creditor and maturity structure of the government debt are two key factors, which contribute to mitigate the country's default risk. The Russian government and banks remain the largest holders of Belarusian debt and FX short-term debt accounted for 20% of the country's gross government debt in April 2016.

Fiscal reforms are consolidating the budget. The authorities of Belarus have implemented a number of changes aimed at consolidating the fiscal balance which range from increase in some tax rates to medium-term budget planning. As a result, the fiscal balance of Belarus has been positive and widening over the past two years, ending 2015 around 1,5% of GDP (see graph 2).

A pension system reform was approved by the president Lukashenko in March 2016. This includes the gradual three-year increase of the retirement age from 55 years for women and 60 years for men and is an important step, which will preserve fiscal sustainability of the pension system in the long run.

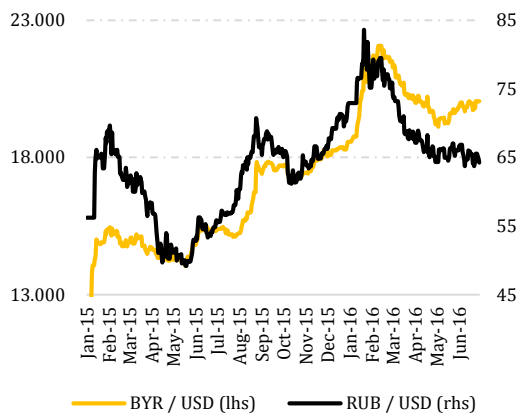
Additionally, government-directed lending and subsidies which have been mainly granted to state-owned enterprises out of public funds have recently lessened and could be showing a shift towards a more competitive industry environment. If these reforms remain in place, the government could be able to build enough resources for social spending as well as higher interest and capital expenditures, while bringing debt down to target levels over the medium term.

Belarus remains affected by external risks. In 2015, the current account of Belarus, while still negative at 4% of GDP, showed a significant improvement from a year ago (see graph 3). The slightly positive trade balance combined with a sharp increase of the secondary income offset the slump of the primary income, which reached -5% of GDP in 2015.

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Graph 4: BYR and RUB exchange rate dynamics



Source: RAEX (Europe) calculations based on data from the NBRB and Central Bank of Russia

However, the weak economic position of Russia damaged the country's trade and is expected to have a negative impact on the whole economy.

Belarus' trading and production activities with Russia (39% of exports and 56% of imports in 2015) are negatively exposed to the contracting economy of the latter (forecast to contract by 2% in 2016 according to the IMF). This resulted into exports to Russia decreasing by 32% in 2015 relative to 2014 and by 6,5% in 1Q 2016 relative to 1Q 2015. Such a decline translated into loss of output in key export industries for Belarus such as agriculture and manufacturing and a consequent contraction of real GDP by 3,9% in 2015.

The introduction of a currency basket value (including EUR, USD and RUB) in 2015 would allow Belarus to stabilize the FX reserves and conduct a more flexible policy towards supporting the currency. Nevertheless, the meager amount of reserves at the NBRB and the country's high dependence on external finance from its partners present one of the main risk factors to the economy.

Monetary policy is contradictory. While the NBRB states clear and well defined monetary guidelines for 2016, the targets and current developments of some monetary instruments seem to contradict each other.

The NBRB is targeting an inflation rate of 12% and the broad money supply to increase by 18% (-/+ 2%) for 2016. Additionally, the exchange rate is set to be based on demand and supply in the FX market with minimal interventions of the NBRB. At the same time, policies are aimed at increasing the FX reserves while lowering dollarization levels in the economy.

As we expect (in line with IMF forecast) real GDP to decline by 2,6% in 2016, both or at least one of the inflation rate and broad money supply targets are unlikely to materialize. Furthermore, with imports at 70% of GDP and BYR still volatile and sensible to RUB fluctuations (see graph 4), there is a high risk of short term exchange rate transmission to prices, ultimately fuelling further dollarization.

Important note for sovereign ratings

This Research Report shall be treated as a supplementary part of the published Press Release included in the following link:

http://raexpert.eu/reports/Press_release_Belarus_05.08.2016.pdf

Both documents shall be treated as essential parts of each other.

For further information on the factors, their weights, methodologies, risks and limitations of these ratings, and other regulatory disclosures, please refer to the Press Release and the website of the Agency.

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