Research Report on Belarus

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Introduction

Belarus has one of the highest GDP per capita (15 800 USD at PPP[1]) indicators in the Commonwealth of Independent States (CIS) region combined with low inequality and high HDI[2]. In addition, the general level of indebtedness for Belarus has consistently declined over the last years; and the budget has been balanced (current deficit is 0,9% of GDP). However, targeted wage increases, unsupported by productivity, and subsidized lending to ailing sectors are delicate factors which, if not controlled, will fuel inflation, create non-performing loans (NPLs) and affect competitiveness. Furthermore, one of the most critical factors for Belarus is currency risk due to high loan dollarization, low foreign exchange reserves and a devaluating BYR.

Main Economic Indicators of Belarus

Macro indicators	2011	2012	2013
Gross pub. debt, bill BYR	136382	203986	233787
Nominal GDP, bill BYR	297157	530355	636784
Real GDP growth, %	5,5	1,7	0,9
Gross gov. debt/GDP,%	45,9	38,5	36,7
Deficit (surplus)/GDP,%	4,2	1,7	-0,9
Inflation rate,%	108,7	21,8	16,5
Curr. Account balance/GDP,%	-8,4	-2,9	-10,1

Development indicators	2013
Inequality adj. HDI	0,73
GDP per capita (Thou. of USD)	15,8

Sources: RAEX (Europe) calculations based on data from World Bank, IMF, Bloomberg

Low amount of Public debt, though risks of external debt repayment may arise. The structure of the Belarus economy, where more than 60% of the companies are completely or partially owned by the government (see table 1), obliges the authorities to repay more than just the public debt. This elevates the amount of debt outstanding, most of which is external. Therefore, the low amount of foreign exchange reserves and the ongoing devaluation of the local currency, present moderate risks for economic stability. In addition, the current yield for the 7Y USD denominated government bonds sits above 7%, also representing a moderately high cost of refinancing. These risks are expected to be mitigated by ongoing Russian support and the execution of a new Financial Plan by the Belarusian authorities.

Budget has remained balanced in the last years without taking into account directed lending; this clouds the general perspective in regard to the real balance of payments. According to government estimations, the balance of payments presented a narrow deficit in 2013 (0,9% of GDP). Taking into account directed lending, the deficit widens up to 6% of GDP. A potential default on these loans will have a direct impact on fiscal costs. Moreover, these types of credits have contributed to the modest levels of private lending in the past years reducing the efficiency of capital allocation. Adding to this fiscal policy issue, targeted wage

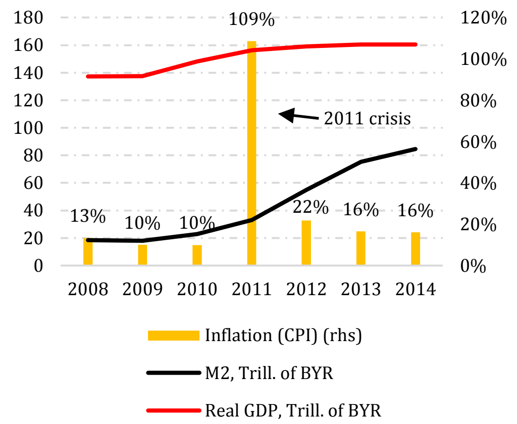
[1] Purchasing Power Parity
[2] Human Development Index

Table 1: Ownership structure of Belarusian enterprises

Type of organization	Share of employment	Ownership
State-Owned Enterprises	19,2%	Government dependent
Budgetary Organizations	19,3%	
Civil Servants	3,6%	
Private with % of State ownership	21,3%	
Private with no State ownership	34.2%	Government independent
Foreign	2,4%	

Source: RAEX (Europe) calculations based on data from IMF

Graph 1: M2, Real GDP and Inflation



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

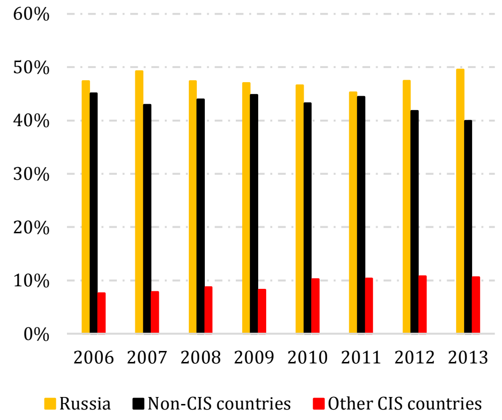
growth is also a problem that has contributed to spur inflation, creates internal imbalances and hinders competition. The new Government Financial Plan aims at solving these two concerns by limiting and controlling the amount of subsidized lending and reduce the emphasis of meeting wage targets.

Monetary policy has been loose, and it will remain that way. Halfway through 2013 the National Bank of the Republic of Belarus (NBRB) tightened monetary policy by raising interest rates and establishing reserve requirements in order to stop the demand for foreign currency deposits. Since then, the NBRB loosened monetary policy again by cutting interest rates and eliminating reserve requirements. At the same time, depreciation of the BYR has not been sufficient enough to balance the current account (it has appreciated in real terms) stalling competitiveness. Nonetheless, an abrupt devaluation of the BYR would harm the general economy due to high levels of loan dollarization and low foreign currency liquidity as will be pointed out later in this report. The above mentioned issue should be closely monitored. Furthermore, money supply (M2) has grown at faster paces than GDP avoiding inflation to ease (see graph 1).

Low levels of competitiveness and unrealized privatization plans impact the economic outlook. During the last couple of years privatization plans have been one of the main objectives for Belarusian authorities. Nevertheless, only a very small part of these plans have been executed (due to adverse market conditions according to the government) and credibility for further and bigger privatizations in the short and medium run has declined. Moreover, the role of the government in the economy is hindering productivity and impeding a better allocation of resources.

The banking sector can be assessed as stable, however, the financial system in general is still strongly influenced by the government and rising debt dollarization represents a risk. Observing the capital adequacy ratio for the banking system along with its ROA, it can be assessed that the banking sector is stable. However, loan dollarization is rapidly increasing and may represent an issue if suddenly an exchange rate turmoil were to exist. NPLs will drastically increase causing a shock due to the lack of foreign currency liquidity of the banking system and the government (in case aid is needed). Regarding the financial system in general, it is still hampered by strong influence from the government, e.g. subsidized lending, state owned banks, among other factors. In addition, the stock market remains undeveloped and non-transparent.

Graph 2: Belarus Trade Turnover (% of Total)



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

High dependence on relations with Russia. Belarus has very close links with Russia. The Russian government provides Belarus with financing, subsidized oil and other energy sources, and it is its main trade partner far from the other CIS countries (see graph 2). This demonstrates the potential risk for the Belarus economy in case of a slowdown in Russian economic activity or damage in their bilateral relation.

Conclusion

Belarus is characterized by a stable general level of indebtedness and a strong GDP per capita. However, the amount of debt in foreign currency combined with the level of foreign reserves and a devaluating BYR raises concerns over Belarus capacity to repay USD denominated debt. Their balance of payments shows a low deficit and an overall balanced budget. Nevertheless, taking into account new directed lending, it can be observed that a higher deficit exists due to inefficient fiscal policy. Current and planned loose monetary policy halts competitiveness and fails to reduce inflationary and exchange rate pressures. Additionally, government policies such as targeted wages and the high amount of subsidized lending show the level of government control in the financial sector. Besides, these measures represent a potential threat for budget balance and effective credit allocation. Finally, rising debt dollarization and tight bilateral relations with Russia, expose the economy to potential currency risks that should be closely monitored.