BELARUS

Highlights

- **Growth turned negative in 2015 for the first time after 19 consecutive years of positive growth in 1996-2014, and following three years of growth slow-down in 2012-14.** Belarus's growth model, which relies on concentration of resources in the state sector, administrative measures and directed lending, has resulted in three years of below-two per cent growth in 2012-14, and a contraction of 3.7 per cent year-on-year in the first nine months of 2015.
- **The recession in Russia and depreciation of regional currencies in the context of Belarus's economic imbalances exacerbated vulnerabilities and resulted in currency pressures.** Support from the International Monetary Fund (IMF) and from the Eurasian Development Bank could help to replenish international reserves from a very low level and to rebalance the economy, contingent on the authorities' ability to launch an ambitious structural reform agenda.
- **Policies enacted to reduce imbalances.** A new exchange rate-setting mechanism entails higher volatility to balance demand and supply, with preservation of international reserves benefiting from significant priority. Fiscal and monetary policies are tight, amid better understanding that demand-side policies must be helped by structural measures to improve the business climate and attract foreign direct investment (FDI).

Key priorities for 2016

- **Macroeconomic and structural policies should aim to unwind external imbalances.** Directed lending, output targets for enterprises and price controls need to be gradually phased out, monetary policy needs to be reasonably tight amid exchange rate flexibility, fiscal planning needs to be conservative bearing in mind contingent liabilities from the state's participation in the real and financial sectors, restraint should be exercised with respect to wage increases.
- **The private sector needs to play a more dominant role in the economy.** Distortive administrative regulations should be phased out and the playing field in the private sector should be made level and more predictable to attract greenfield private investments. Commercialisation and privatisation of large enterprises needs to be considered in order to enhance competitiveness and resource allocation efficiency.
- **State-owned banks should increase the share of loans offered on a commercial basis.** Directed lending by state-owned banks should be made more transparent and scaled down over time. The Belarus Development Bank, which was established to consolidate and unwind directed lending operations, should adhere to its original mandate.

CONTINUES

Main macroeconomic indicators %

	2011	2012	2013	2014	2015 proj.
GDP growth	5.5	1.7	1.0	1.6	-3.5
Inflation (average)	53.2	59.2	18.3	18.1	15.1
Government balance/GDP	-2.9	0.5	-0.9	0.2	-2.4
Current account balance/GDP	-8.5	-2.9	-10.4	-6.7	-4.9
Net FDI/GDP [neg. sign = inflows]	-6.5	-2.1	-2.7	-2.4	-2.9
External debt/GDP	57.7	54.2	54.2	52.6	n.a.
Gross reserves/GDP	10.2	9.2	9.1	6.6	n.a.
Credit to private sector/GDP	38.6	21.5	21.0	21.8	n.a.

Macroeconomic performance

Recession and economic pressures in 2015 followed three years of anaemic growth. The economy grew by 1.6 per cent in 2014, marking the third consecutive year of a below-two per cent growth. In the first nine months of 2015, Belarus's GDP is estimated to have shrunk by 3.7 per cent year-on-year (y-o-y), driven by significant real contraction in mining (-8.2 per cent y-o-y), manufacturing (-6.8 per cent y-o-y) and construction (-7.6 per cent y-o-y). Foreign currency reserves declined from US$ 3.9 billion in November 2014 to US$ 2.1 billion at the end of September 2015, providing approximately one month of import coverage. The ratio of non-performing loans (NPLs) to total gross loans in the banking sector was reported by the National Bank of Belarus (NBB) at approximately 4.5 per cent in 2014 and at 5.1 per cent at the end of the first quarter of 2015, although monitoring of weaknesses is difficult due to evergreening of government-directed lending. The current account deficit fell from 10.4 per cent in 2013 to an estimated 6.7 per cent of GDP in 2014 and stood at 1.9 per cent of GDP in the first half of 2015. The augmented general government deficit (including directed lending, bank recapitalisation costs and outlays related to public guaranteed debt) was approximately 3.5 per cent of GDP in 2014. In January to July 2015, the budget moved into surplus, with such surplus earmarked towards repayment of foreign exchange liabilities and payment under the government's guarantees to banks. Effective from January 2015, after Belaruskali's solid output and exports in 2014, Belarus reinstated export duty on potash fertilisers to increase budget revenues. Average CPI inflation stood at 18.1 per cent y-o-y in 2014 and at 14.2 per cent y-o-y in January to September 2015. The ratio of general government gross debt to GDP increased from approximately 38 per cent in 2013 to approximately 40 per cent in 2014 and is expected to remain at this level in 2015. On the back of exchange rate movements, loan dollarisation increased from 52.3 to 57.0 per cent and liability dollarisation increased from 63.3 to 67.7 per cent in the period December 2014 to March 2015.

To mitigate external imbalances, the authorities attempted external and internal adjustments tools. Faced with external refinancing risks, a low level of official reserves, looming peak foreign currency public debt redemptions and lack of a longer-term planning horizon for external refinancing options, the authorities sought to engineer a soft landing in 2014 among other things through moderation in wages and tighter credit. In December 2014, the NBB abandoned its crawling peg in the context of depreciation of the Russian rouble. This measure was taken despite initial heavy administrative measures (30 per cent tax applied on foreign exchange purchases, US dollar-indexed local currency deposits, increase of the overnight credit rate from 24 per cent to 50 per cent and of the requirement for mandatory surrender of foreign exchange proceeds of exporters from 30 to 50 per cent in December 2014, and a consumer price increase moratorium). In January to September 2015, the Belarus rouble depreciated against the US dollar by approximately 33 per cent, with knock-on impact on the real and financial sector balance sheets.

Economic prospects depend on quality of internal adjustment and on the regional economic outlook. A GDP contraction of 3.7 per cent in the first nine months of 2015, tight fiscal and monetary policies and reduced demand for exports due to the recession in Russia point to Belarus's negative growth prospects in 2015, with potential downside risks in the absence of international support.

CONTINUES

Major structural reform developments

Comprehensive structural reforms were delayed in the past when the economy was growing. The limitations of the existing growth model are increasingly understood by the authorities, although the will and the ability to implement a far-reaching reform agenda in the context of the economic recession are unclear. The privatisation process has not advanced. Price liberalisation measures lack continuity and may be subject to reversals. Utility tariffs remain well below cost recovery levels. Quasi-fiscal function of the banking sector remains strong and directed lending persists amid discussions on how to downscale it. In the World Bank's *Doing Business 2016* report, Belarus ranks 44th out of 189 economies, with low scores in getting electricity, obtaining credit, paying taxes and resolving insolvency.

The government continued gradual price liberalisation by reversing administrative measures implemented during the crisis in 2011 and in December 2014. In April 2015, the authorities abandoned the sweeping price freeze introduced in December 2014. In addition, the NBB gradually relaxed foreign exchange restrictions imposed in late December 2014. The tax on cash-based foreign exchange purchases was eliminated in January 2015. In February 2015, the NBB lifted the over-the-counter (OTC) currency trading ban, albeit it retaining some limitations. The limitations in the OTC market were mostly removed, with a major exception on sales of foreign exchange subject to a surrender requirement which continues to be sold on the official exchange floor, in May 2015, with a view to switching to the regime of continuous two-way auction in the JSC "Belarusian Currency and Stock Exchange". The mandatory sale of foreign exchange from export receipts was gradually lowered from 50 to 30 per cent of the revenue (to 40 per cent – since 25 February 2015 and to 30 per cent – since 15 April 2015). On 25 February, the NBB cut the reserve requirement rate on foreign currency deposits from 10 to 9 per cent. The reserve requirement rates were unified for all kinds of deposits from 1 July 2015 at 7 per cent, and raised to 8 per cent from 1 September 2015.

The registered unemployment rate remained low amid a significant share of workforce employed in the state sector. By the end of August 2015 the registered unemployment rate in Belarus was 1.0 per cent of the economically active population (up from 0.5 per cent a year earlier), although almost half of the workforce is employed in state-owned enterprises. In April 2015, the President of Belarus signed an ordinance "on preventing freeloading practices" to "engage able-bodied persons in labour and to ensure that they take part in the financing of public spending." The ordinance imposes fines on adults living in Belarus who are unemployed for at least 183 days. Self-employed and full-time students are classified as employed.

Belarus continued consultations with the Eurasian Fund for Stabilization and Development (EFSD) on provision of new credit. The latest round of consultations took place in August 2015 to discuss the government's reforms roadmap which envisages the reduction of directed lending, the reduction of utility subsidies and increased cost recovery of tariffs, price and market liberalisation measures, commercialisation and privatisation of enterprises. The issue is planned to be discussed at the EFSD's council in the fourth quarter of 2015.

In May 2015 the government and the EBRD signed an MoU to privatise Belinvestbank by 2020. The EBRD is considering providing to Belinvestbank (BIB) a micro, small and medium-sized enterprise (MSME) credit line of up to €20 million and a Trade Facilitation Programme (TFP) facility of up to €30 million. This represents part of an effort to prepare BIB for privatisation by attracting strategic private investors. The project will enhance the country's MSMEs' access to longer term credit resources and facilitate international trade involving Belarus's companies.

As a result of the public-private partnership (PPP) capacity building project implemented by UNECE with the support of the EU Delegation and UNDP, the government of Belarus established a national PPP unit and identified a number of pilot PPP projects. The government has requested the EBRD and IFC to support the preparation and financing of the M10 road on a PPP basis.