

Analytical note:
Monitoring of the situation in
the field of economic security
of Belarus
(January 2016)

The risk of financial instability

The opinion expressed upon the economic and financial results of December regarding the potential weakening of the Belarusian ruble was completely realized. Under the conditions of the falling oil prices and the Russian ruble rates, the authorities had to implement a more flexible exchange rate formation mechanism, which resulted in weakening of the national currency against US dollar within the January period by more than 12%, and by almost 10.4% against the currency basket. Such dynamics of the national currency was determined by a series of negative factors, which appeared by the end of year in the currency market. Thus the demand for currency in December exceeded the supply for almost USD 300 mln.). The balance of foreign trade in goods has sufficiently decreased in comparison to the previous months (the negative balance for November-December exceeded USD 1.25 bln.). The peak of payments on the external national debt servicing in December and January (more than USD 1 bln. in each of the months) put serious pressure on the international currency reserves of the National Bank. Thus in December 2015 – January 2016 the latter reduced for almost USD 560 mln. (or more than by 12%) and closely approached the benchmark of USD 4 bln. The reduction of the gold and currency reserves (hereinafter referred to as the gold and currency reserves) might have been much more significant, should the National Bank have not found in December-January the resources in the internal market through issuing obligations for the total amount of around USD 1.7 bln. The obligations were traditionally purchased by the banks, which reached excessive currency conditions during the year. It became possible as a result of simultaneous reduction of the currency crediting (reserves of the foreign currency loans reduced for USD 1.8 bln during the year.) and increase of the foreign currency deposits (for USD 220 mln.). Besides, in January the two largest state-owned banks (Belarusbank and Belagroprombank) attracted around USD 115 mln. foreign currency loans, which with a high rate of probability were also forwarded for purchase of the obligations of the National Bank. The current amount of the gold and currency reserves does not allow material spending for the currency interventions, therefore the decision of the authorities to increase the national currency volatility was predetermined.

In turn, the continued devaluation and falling oil prices pose a number of problems to the authorities requiring rapid decisions. Thus, the decline in oil revenues, the deterioration of the economic dynamics in Russia and the increased costs of servicing the state debt make it impossible to execute the budget adopted in December for the year of 2016. And if the Russian Government in a similar situation discusses the state budget sequestration by at least 10%, the plans of the Belarusian authorities were not publicly disclosed. At the same time according to some sources of information, a tax at the rate of 10% may be introduced for the Internet and cellular communications, to increase the budget revenues. The plans to raise the retirement age are also so far only at the stage of public opinion preparation.

Weakening of the ruble in January well below the forecasted values (up to BYR 21,000-21,500 per dollar, compared with the forecasted BYR 18,650 for the year 2016 in average) casts doubt on the authorities' plans on inflation at the rate of 12%. In fact, the Government has shifted targets to 17-18% per annum. Acceleration of inflation from the value reached in 2015 (12% according to official statistics) will negatively affect the cost of credit resources and attractiveness of the current interest rates on ruble deposits. The latter are still under administrative pressure of the National Bank. Thus, in January, upon

the urgent recommendation of the regulator the banks were forced to lower the interest rates on ruble savings cards for up to 3% per annum and on foreign currency savings cards – up to 0.2%. As a result the reduction of ruble deposits continued for 7 consecutive months and their currency equivalent (approximately USD 1.2 bln.) reached the lowest level since 2011.

The reduction of foreign exchange nominal of the GDP increases the relative level of foreign debt. For example, over 2015 the foreign debt decreased from USD 12.53 bln. to USD 12.4 bln., but in relation to GDP it increased from 16.6% to 22.7%. This ratio is closer to the safety threshold set by the authorities at the level of 25% of the GDP, and the probability exceeding it is high enough in the near future. As a result, the situation with the debt servicing is gradually approaching the critical point. Till now the external debt was possible to refinance by intense increase of the domestic currency debt. However, firstly, the domestic market resources are limited enough, and judging by the volume of loans in 2015, which amounted to approximately USD 2.14 bln., are close to exhaustion. Secondly, the practice of refinancing the public debt actually due to the foreign currency deposits of the population leads to leaching of currency from the country, decrease in potential investment resources and higher prices for the foreign currency loans in the domestic market.

The risk for economic independence

In this situation, the importance of success in the negotiations with potential lenders (IMF and EFSR) substantially increases, which in theory should make the Belarusian authorities more flexible and willing to compromise. However, despite this, today the beginning of the joint programs with both the IMF and EFSR is a big question. Some solutions of economic block of the Government adopted in January (the abolition of restrictions in retail pricing, the rising cost of housing and communal services (HCS) for the population, the development of HCS payment subsidy mechanism for the low-income citizens, which will start working on the 1st of May) could be the first signs of the future agreement with the IMF. However, Alexander Lukashenko expressed his opinion on inadmissibility of fundamental reforms, linked with some of his decisions on cooperation with the international lenders, which raises serious doubts. In case of EFSR, alongside with the need to harmonize the program of reforms (even if not as tough as in case of the IMF), another problem appears regarding the adequacy of the resources available to the creditor. Thus, according to the Russian Deputy Finance Minister Sergey Storchak, the Government has decided to suspend lending to foreign countries because of problems with fulfillment of the Russian budget. In this regard, it is believed that even in case of a positive decision on the loan by EFSR, the one will still have to wait for the actual money, because the Russian contribution exceeds 88% of the Fund's resources. The emergency request for the IMF assistance from Tajikistan, which was also a member of the Eurasian Economic Community and was entitled to receive the EFSR loans, but had to look for other sources of credit, is indicative enough in this regard.

On the other hand, the problem of external debt service in 2016 and can be solved by political means, since the basic payment account for the Russian government, ESFR and other affiliated structures of the Russian Government. In this context, an interesting telephone conversation between Putin and Lukashenko was held at the initiative of the latter, which touched upon the “synchronization of actions in the current circumstances”, and shortly thereafter an informal meeting in Sochi took place. It can be assumed that the

leadership of Belarus once again will try to avoid the reforms through capitalization of the Russian concessions in foreign policy, military and possibly in economic field.

The risk of economic recession

The year of 2015 was marked by the first in 20 years officially recorded economic recession. At the end of 12 months, the decline in GDP was 3.9%, which coincides exactly with the similar Russian index. At the same time the decline was recorded in all integrated sectors, except the retail trade. To improve the economic dynamics it is intended to implement the collective decision of the Government and the National Bank to stimulate the economic growth without accumulation of macroeconomic imbalances. The document contains 93 clauses, containing plans of action for the authorities, and is quite eclectic and contradictory by its concept. The resolution includes the measures substantially different either in scope (such as the negotiations on WTO accession are combined with holding tastings to promote domestic products and bringing the share of e-commerce to 2%) or in focus. Alongside with the sufficiently market-based measures (reduction of preferential support of the public sector, the increased use of bankruptcy mechanism, better targeting of social support) in the decision, a lot of policy indicators and restrictive measures (reaching the share of domestic goods in retail trade at 70-75%, reducing the cost of construction by not less than 10%, etc.). In essence, the decision is a compilation of the pre-existing plans of various ministries and departments, and nothing fundamentally new is contained in it.

It fully reflects the concept of preserving the current economic model with only some adjustments and the decision of the authorities to adjust Directive No.3. In terms of cheap oil and gas the emphasis of this directive moved from energy saving to diversification of the foreign trade, i.e. actually the reduction of dependence on the Russian market. Thus, the previously stated principle was documented regarding distribution of exports by 2020 in the proportion of “one third - one third - one third”, when it will equally refer to the EAEC (mostly Russia), the EU and other countries, including the “long-arc” countries. An important means of achieving this goal, according to the authorities, is organization of cooperation with the relevant transnational corporations, to attract them to investment and integration of production chains. It seems that the main way to solve this problem would be privatization, but the privatization list made by the authorities for 2016 contains only 60 companies and is virtually identical to the similar list for 2015.

Conclusion

The deteriorated economic situation poses a tangle of serious problems to the authorities, the most difficult of which are: the lack of resources to service the external national debt, problems with the budget execution and the risk of further GDP decline. The earlier announced agreements to obtain the IMF loan have not been reached yet, and judging by the public statements of A. Lukashenko, the chances are small. In such situation, the option for obtaining Russian funding under some concessions, including the non-economic sphere, becomes increasingly likely.

