

Analytical report:
Economic security of Belarus
(October 2021)

Minsk

The risks to economic growth

Against the background of the end of the recovery growth in foreign markets, GDP growth in Belarus continued to slow down in September and amounted to 2.7%. Industry remains the driver of the economy, accounting for up to two-thirds of the total GDP growth. According to statistics for January-September, growth in this sector slowed down to 7.9% compared to 8.6% a month earlier. The slowdown in industry will continue in the remaining months, and by the end of the year its growth, according to the government's estimates, will be 5.3%. Agriculture remains depressed - according to the results of 9 months, it declined by 6.6%. At the same time, despite the difficulties with personnel, the information and communications sector retains high growth rates - its growth in September reached 9.6%. As a result, the annual economic growth will be higher than the original plans of the authorities, and according to the estimates of most international organizations (IMF, EDB, rating agencies) it will be 2-2.5%.

At the same time, forecasts of international organizations for 2022 are much more pessimistic and mostly fluctuate in the range from a fall of less than 1% to an increase of less than 1%. This assessment is explained by the deterioration of the situation in the external sector, which is associated both with the end of the period of rapid growth of the world and Russian economies, and with the strengthening of the sanctions effect. At the same time, domestic demand will not be able to assume the role of a driver of the economy and the current stagnation trends will continue in it. So, according to the National Bank, in the third quarter of this year, the impact of domestic demand on economic growth was negative, due to a significant drop in investment, a slowdown in income growth and weak consumer lending.

In such a situation, the authorities stepped up in the implementation of the previously announced plans to increase investment in the economy. So, according to the statements of officials, several large projects for the modernization of large state-owned enterprises should become the drivers of investment growth. In particular, it is announced about the expansion of bus production at the Minsk Automobile Plant (MAZ), a deep modernization of the Minsk Tractor Works (MTZ), the construction of a new workshop at Grodno Azot, the organization of the production of raw materials for cardboard at Mogilevkhimvolokno. At the same time, the key constraint for the implementation of these plans is obviously the difficulty of finding finance. A possible solution in this situation could be the return of the authorities to the practice of tied Chinese loans, which has been curtailed since 2018 amid the failures of such projects and significant financial gaps for the budget associated with their implementation. This can be evidenced by the intensification of contacts between the government and representatives of Chinese business. Thus, in October, negotiations were held with the Chinese company City Construction as a possible contractor for the construction of a new nitrogen plant. The government is counting on Chinese investors when implementing a new project at the "Polymir" plant.

The authorities do not give up on the announced method of increasing the efficiency of the public sector through its consolidation and the creation of state corporations. So, already in November, it is expected to adopt a decree on the creation of a corporation for agricultural machinery, which will unite MTZ, Gomselmash and a number of other manufacturers.

The authorities are also close to the return of active import substitution practices. Thus, the Ministry of Antimonopoly Regulation and Trade has published a draft decree, according to which retail companies will be provided with indicators of the minimum share of domestically produced goods in the turnover (at least 85%). They will be fined for non-compliance with it.

In general, we can say that the steps taken by the authorities to stimulate economic growth are increasingly beginning to resemble the measures actively used in the early 2010s, relying on public investment by increasing the state debt and administrative restriction mechanisms.

The risks of financial instability

The acute problems typical for the financial market in the second half of 2020 - the first half of 2021, under the influence of a favourable external environment, have been largely levelled out at the moment. Thus, the situation of permanent net sale of foreign currency by the population returned to the foreign exchange market (in October it amounted to almost USD 80 million). The National Bank explains this situation by a slowdown in the growth of household income and an increase in the attractiveness of BYN deposits (rates on them increased simultaneously with BYN strengthening). Companies also generated a significant net supply - the net sale of foreign exchange by organizations in October amounted to more than USD 400 million. Thanks to this, the foreign exchange market, against the background of the absence of large external borrowings, again became the main source of support for the country's gold and foreign exchange reserves - at the end of the month, their size exceeded USD 8.5 billion.

There is also an improvement in the deposit market: the growth of BYN deposits has become stable, although the pace of this process remains low (+ 6.6% since the beginning of the year). At the end of September, foreign currency deposits of the population also slightly increased. As a result, the situation with bank liquidity has radically changed - if earlier during the year the National Bank strictly limited the provision of liquidity to banks (the number of fulfilled applications at monthly auctions was sometimes 5-10% due to fears that BYN resources would be used in the foreign exchange market), now there is an excess of BYN in the system. So, according to the results of the auction on November 3, banks placed 7-day deposits in the National Bank in the amount of BYN 1 billion at an average rate of 1.42% per annum. Even accelerated inflation has not yet had a noticeable effect on the financial market - despite inflation growth to the level of 10.2% in September, the maximum rates on BYN deposits of the population even slightly decreased.

Due to the external conjuncture, budget execution is developing very favourably. At the end of January-September, the budget of the public administration sector was executed with a surplus of more than BYN 200 million (0.16% of GDP) with its planned annual deficit at BYN 5.86 billion. expenses. This was facilitated by both the growth of budget revenues and the government's policy of restraining budget expenditures.

An important factor influencing the money market may be the expansion of the government's support to the public sector with the help of new financial instruments. Thus, in October, the regime adopted a decree significantly expanding the powers of the Asset Management Agency. The authorities expanded the agency's sectoral powers

(previously, this institution worked only with agricultural organizations), and also gave it the right to issue government-guaranteed bonds. These bonds can be used by the agency to buy out bad debts from banks and, accordingly, financial recovery of troubled organizations. It is not expected that this financial transaction will be accompanied by a structural transformation of such enterprises aimed at addressing the root causes of chronic problems.

Since the bonds issued are guaranteed by the government, such a policy mitigates the problem of bad debt by accumulating fiscal and public debt risks. At the same time, even the current level of guarantees accumulated by the state poses a significant threat to the state debt. Thus, according to the EDB study, if a risk scenario is implemented in 2022 (such a scenario assumes a sharp deterioration in the performance of state-owned enterprises), the size of the expanded public debt of Belarus could grow from the current level of 48% of GDP to 61% of GDP. At the same time, the likelihood of a risk scenario increases with the sanctions pressure and a simultaneous weakening of demand in foreign markets.

The authorities acknowledge the difficulties in servicing the public debt in the medium term and the limited sources of its refinancing. Due to the closure of foreign borrowing markets and the freezing of relations with international financial organizations, the government is forced to rely heavily on borrowing from Russia and its affiliated structures. For example, officials say they are holding talks with the EFSF on the launch of a new program (previously, the possible size of such a program was estimated at about USD 3 billion). At the moment, work is underway to agree on a matrix of measures funded under the new program. At the same time, the announced goals of the program are traditional - increasing the efficiency of the public sector, optimizing the social security system, developing competition and dedollarization of the economy. It is noteworthy that the current steps taken by the Lukashenka authorities in many respects contradict these priorities of the Fund.

The risks to economic independence

On November 4, at last, sectoral programs for deepening integration were signed within the framework of the so-called “union state” of Russia and Belarus. The approval process of them took almost three years. Although even after the official signing the full content of the programs was never made public, it is obvious from their summaries that, compared to the original version, the documents turned out to be largely devaluated. Blocks associated with the creation of common supranational bodies, as well as steps such as the creation of a common budget and tax system, and unified sectoral regulators have disappeared from the documents. In general, the current version of the signed programs does not imply an economic integration comparable to integration within the EU. In addition, the implementation of the programs will be extended in time and will require a lot of legislative work in each of the countries (according to Russian Prime Minister Mikhail Mishustin, more than 400 legislative acts and agreements must be adopted). The signed programs also do not remove painful issues for Belarus, such as the formation of equal gas prices and compensation for losses from Russian tax manoeuvre.

At the same time, the signing of integration programs can be viewed as an important symbolic gesture in the context of sanctions pressure on official Minsk. The

EU promises to adopt a fifth package of sanctions already in November. According to media reports, it will contain, among other things, measures directed against Belavia and a number of banks. In addition, in December the American sanctions against Belaruskali will begin to operate, which threatens the Belarusian fertilizer producer with the closure of transit corridors through Lithuanian and Latvian ports. In such a situation, it is Russian companies and transport routes that will play a key role in minimizing sanctions damage. In this regard, the statistics of the work of the oil refining sector in Belarus, and in particular of the Naftan plant, is indicative. Despite the US sanctions against Naftan and the formal refusal of large Russian oil companies to supply raw materials, this manufacturer does not experience critical problems. According to the authorities' forecast, the volume of oil refining at Belarusian refineries by the end of the year will be about 16.8 million tons, which is 3% more than in 2020. Some analysts consider this level of performance to be optimal from an economic point of view (taking into account the priority of producing light high-margin products). At the same time, the sanctions obviously reduce the margins of the company's production (for example, the losses of Belarusian refineries are estimated at USD 80 million), and create additional requirements for credit resources.

Conclusions

The most significant risk to the economy is the further weakening of external demand, coupled with the increasing impact of European and US sanctions. This combination of factors simultaneously creates threats to economic growth, stability of the financial system, increases budgetary risks and risks of growth in public debt. Russia continues to play an important role in levelling these factors, especially in terms of providing financial support and helping to minimize sanctions damage.

