

**Analytical report:**  
**Economic security of Belarus**  
**(November 2021)**

### **The risks to economic independence**

Western sanctions remain a key factor creating risks and increasing uncertainty in the Belarusian economy. On December 4, the next fifth package of European sanctions was unveiled. At the same time with which the United States, Great Britain and Canada also announced their sanctions measures. Potentially the most painful may be European sanctions against Belavia, GrodnoAzot, Belshina, Belorusneft, as well as US sanctions against the Belarusian Potash Company, which is a trader of Belarusian potash fertilisers. The restrictions on government borrowing adopted by the United States are also significant - for example, US companies and citizens are prohibited from buying new borrowings from the Ministry of Finance of Belarus and the Development Bank for a period of more than 90 days. This measure will complicate the restructuring of the Belarusian state debt, and according to some estimates, it may even affect USD borrowings in the domestic market of Belarus. At the same time, there were no large state-owned banks in the EU sanctions list, measures against which were previously announced in the press. According to the Belarusian authorities, the new sanctions will affect Belarusian exports in the amount of about USD 250-300 million on an annualised basis. At the same time, there are prerequisites for a further increase in sanctions pressure on Belarus - European media report about the start of work on the sixth package of sanctions, which may become larger than the previous ones (it may preliminarily affect up to 300 legal entities and individuals).

In terms of countering sanctions, the Belarusian authorities are counting on the support from Russia. Thus, the Government expects to increase trade with Russia, including due to the reorientation of some of the falling export flows to the Russian market. Russia is also viewed as a key transit route for Belarusian products delivered to end consumers by sea in case of loss of access to the Baltic ports. Official Minsk also estimates the preservation of the current prices of the gas contract as an important resource for compensating losses from sanctions. Thus, according to the signed agreement, Russia will continue to supply gas to Belarus in 2022 at a price of USD 128.5 per thousand cubic metres. At the same time, gas prices in European spot markets reached USD 1200 per thousand cubic metres as of early December. But the efforts of the Belarusian authorities to achieve a joint policy to counter sanctions within the EAEU will not bring meaningful results.

Also, after the publication of the fifth package of European sanctions, the Belarusian authorities decided to introduce retaliatory measures announced back in June, restricting imports from the EU, the USA and a number of other countries. The import ban will apply to a wide range of food products (vegetables, fruits, meat and dairy products, confectionery, etc.), and will be introduced from January 1, 2022, preliminary for six months. According to the Lukashenka government's estimates, these restrictive

measures may affect up to USD 500 million of imports on an annualised basis. The regime hopes to prevent a shortage of goods in the consumer market by reorienting importers to producers from “friendly” countries, as well as by introducing permissive quotas for the import of prohibited goods if needed. At the same time, the announced measures obviously increase inflationary risks, especially in terms of the growth in prices for fruits and vegetables, the dynamics of which in recent months has already been a record one.

As regards integration projects with Russia, it is noteworthy that even a month after the signing of the integration programs, their content was not publicly announced. At the same time, specialised officials of the countries are quite active in bureaucratic work on the implementation of these agreements (interagency working groups are formed, working negotiations are held).

### **The risks to economic growth**

External factors remain key to the future dynamics of the economy. Against the background of stabilisation of external demand, GDP growth in Belarus continued to slow down. So, according to the results of January-October, it dropped to 2.4% compared to 2.7% a month earlier. Industry and the IT sector remain the main drivers. At the same time, if the dynamics in the industry has a downward trend, then the growth of the information and communications sector remains at the level of more than 9%. In the third quarter, the export of HTP companies exceeded USD 760 million, and by the end of the year it is likely to reach USD 3 billion.

The main risk of worsening foreign trade conditions for the country is associated with the effect of Western sanctions. Thus, according to EDB estimates, in the event of a slow adaptation of the economy to sanctions, the drop in Belarus’ GDP in 2022 could be from 1% to 4%. At the same time, according to the basic forecast of the EDB, the economy will still grow by 0.7%. The key factor that determines the sanctions losses will be the willingness of the United States to apply the mechanism of secondary sanctions to counterparties of Belarusian enterprises. At the moment, such a scenario is not predefined. Thus, despite the US sanctions against Belaruskali, which came into effect on December 8, European counterparties continue to cooperate with it. For example, “Lithuanian Railways” officially announced the continuation of the transport of Belarusian potash fertilisers.

Potential problems in the world economy, primarily related to the persisting high level of inflation in developed countries, can also decrease the external demand for Belarusian products. Thus, annual inflation in the United States in October amounted to 6.2% (a record for 30 years), in the EU – 4.1%, in Russia, according to the results of November, the rise in prices accelerated to 8.4%. If such a surge is not short-lived, it could force central banks to tighten policy. For example, the US Federal Reserve has

already begun to cut asset buyback programs, and a cycle of discount rate hikes is expected in 2022. Such a policy traditionally provokes capital outflow from the markets of developing countries and leads to the weakening of their currencies. The Central Bank of the Russian Federation is also pursuing a restraining policy – it is officially announced that it will consider another rate hike to 1 percentage point in December. A significant risk for the Russian economy is the possible intensification of the Russian-Ukrainian confrontation.

The components of domestic demand in the economy have low growth potential. Official statistics indicate that there is an investment depression in the economy – by the end of January-October, investment declined by 7.8%. At the same time, the official plans of the authorities in terms of investments for 2022 are also very modest – according to the government’s expectations, they should increase by only 3.3% after a total failure of 13.3% over the past 2 years. There is stagnation in the consumer market, which can be explained by expensive credit resources and a slowdown in income growth of the population (+ 2.6% in January-September).

Some plans of the authorities also have an ambiguous impact on the economic potential. So, against the background of the adoption of new sanctions and Belarusian “counter-sanctions”, officials’ statements on strengthening the policy of import substitution have intensified: about 170 import substitution projects have already been proposed for a total of almost BYN 13 billion of investments, which is largely seen as an attempt to promote the old idea of launching an investment cycle in a new form. The implementation of such plans in practice will mean more difficult access to resources for the private sector and a decrease in the quality of goods in the domestic market. The reform of taxation of small businesses, which the authorities plan to start from 2022, may also have a negative effect on economic growth. The announced reform as a whole assumes an increase in the tax and regulatory burden on small businesses, providing up to 20% of jobs in the economy, and it should close tax optimization schemes and increase budget collections.

### **The risks of financial instability**

At the end of October, consumer inflation for the second month in a row was fixed at above 10% on an annualised basis. Prolonged maintenance of such price increases is dangerous from the point of view of a possible unwinding of an inflationary spiral. At the same time, the authorities hope for a weakening of inflationary processes, since, according to their assessment, it has largely external causes. So, according to the preliminary forecast of the National Bank, inflation in 2022 should not exceed 6%.

On the whole, the situation on the country’s foreign exchange market is acceptable. Thus, by the end of November, the population retained the role of a net seller of foreign exchange for the fourth month in a row (net sales amounted to more than USD 76

million). Resident legal entities acted as net buyers of foreign currency in the amount of about USD 100 million, which can be explained by an increase in consumer imports at the end of the year. The favourable foreign exchange market allows the authorities to keep the amount of gold and foreign exchange reserves at a level higher than originally planned (USD 8.5 billion versus USD 6 billion). At the same time, the reduction in their size by the end of November amounted to USD 81 million, which is significantly less than payments on the state debt for this period (USD 250 million).

The population's deposits also show a gradual growth – in October BYN deposits grew by 2.2%, and foreign currency deposits – by 0.7%. Although the sustainability of growth in the future still raises questions – the attractiveness of BYN savings is noticeably decreasing against the background of the end of the period of BYN strengthening, high inflation and cut rates by banks. In turn, banks are cutting rates due to the persistence of a significant excess of BYN liquidity in the system. Thus, at the next deposit auction held on December 8, the National Bank attracted BYN 1.1 billion from the market at an average rate of 0.18% per annum, with a total application from banks for placement in the amount of BYN 3.27 billion.

The traditional risk for financial stability is the possibility of the authorities sliding towards soft monetary and budgetary policies. Despite some public discussion between the National Bank and the government on the sources of increasing investment spending, the National Bank continues to declare its adherence to a moderately tough policy. Moreover, the National Bank publicly promotes the idea of a transition to a more progressive inflation targeting policy, which implies expanding the powers of this body. At the same time, the situation with budget execution this year remains ambiguous - according to the results of 10 months, the consolidated budget was executed with a surplus of more than BYN 2.5 billion, but according to the results of the year, the Ministry of Finance still expects a deficit. At the same time, if in public statements the head of the department predicts it at BYN 2.5-2.6 billion, then in official calculations an amount of more than BYN 6 billion appears. revenues will amount to about BYN 3 billion. At the same time, the sources of its financing remain in question in the context of being cut off from foreign markets and the limited capacity of the domestic borrowing market. It is noteworthy that the authorities' attempts to place new BYN bonds in the domestic market in November ended unsuccessfully due to lack of demand.

In solving the problem of servicing the state debt the authorities also count on support from Russia, which, in general, is the main holder of the Belarusian state debt. In particular, the government is negotiating with the EFSF on a new credit program, the size of which could reach USD 3.5 billion (according to other sources, up to 4.5 billion). In the short term, a significant buffer for the authorities is the current size of the gold and foreign exchange reserves, which allows them to count on uninterrupted debt servicing in the next 12-18 months, even in the event of problems with new borrowings.

## **Conclusions**

The main risk to economic growth and financial stability is connected with the Western sanctions in general and the willingness of the US authorities to use the mechanism of secondary sanctions against counterparties of Belarusian sanctioned companies in particular. The speed of adaptation of the economy to sanctions will also be determined by trade, logistics and financial support from Russia.

