

**Analytical report:**  
**Economic security of Belarus**  
**(October-December 2022)**

## The risks to economic growth

The Belarusian economy finished the year in a mixed state. On the one hand, there is an economic crisis associated with a fairly deep recession. In 2022, the fall of GDP was 4.7%, which is the biggest decline since 1995. On the other hand, the current scenario differs from the crisis models that the Belarusian economy has faced before. Previous recessions (2009, 2015-2016) followed an identical scenario: the crisis was triggered by a sharp reduction in external demand. This undermined Belarusian exports, led to a sharp weakening of the national currency, a deterioration in the financial situation in the real sector, and an increase in full and partial unemployment. None of these phenomena is typical for 2022. The reduction in exports does not exceed 6%, and the foreign trade balance reached record levels (USD 4.67 billion in 11 months of 2022). The weakening of the national currency was moderate: 7.95% against the currency basket and 7.39% against the US dollar. As a result, foreign exchange incomes of the population increased: by the end of November, the average salary in USD terms reached a record value of USD 675. According to the Ministry of Economy, GDP in USD terms increased by 7% over 11 months. The financial position of enterprises improved: profits of companies increased (+18%) as well as their profitability, while the share of unprofitable companies decreased (from 13.3% to 12.5%). A vivid indicator of the situation is the real estate market in Minsk, which traditionally attracts the attention of the country's population. If in previous crises the price of real estate, expressed in USD, dropped by tens of percent, and the number of transactions sharply reduced, now the situation on the market is different. Average prices show stability, and the number of transactions in 2022 was the highest ever.

The reason for this strange recession was an unusual combination of multidirectional external factors. While some industries have been seriously affected by sanctions and restrictive measures (potash industry, oil refining, IT industry, woodworking, cargo transportation), for the other part, foreign trade conditions have improved significantly. Belarusian companies in traditional industries (engineering and equipment manufacturing, food industry) were able to take advantage of the situation with the withdrawal of Western companies and occupy the vacated niches in the Russian market. In addition to weakening competition, this result was also driven by the price factor due to the strong Russian ruble.

External factors, and foreign trade in particular, seem to be decisive for the country's economy in 2023 as well. According to the plan of the authorities, Belarus' GDP will grow by 3.8%, while exports will grow by 5.5%. In fact, the focus is on maintaining high demand in the Russian market, as well as the gradual recovery of exports of "sanctioned" industries.

In this context, new sanctions against the Russian oil sector create unconditional risks for the plans of the authorities. So, on December 5, the countries of the European

Union, the G7 and Australia imposed an embargo on the import of Russian oil. In addition, a price ceiling mechanism has begun to operate, extending to other countries that buy Russian oil and use the services of companies from these countries for this. Starting from February 5, similar measures will apply to Russian oil products. The effect of these steps began to appear already in the first month of their action. According to official data, the discount on Russian Urals oil sharply increased in December: the average price in the second half of December - early January fell to USD 47 per barrel, while the Brent price for this period was USD 81.5. Together with the traditional increase in imports at the end of the year, this led to a reduction in Russia's current account surplus: in December it fell to USD 1.7 billion compared to USD 10.3 billion in November and USD 19.7 billion in October. The Russian budget is also suffering serious losses: in December its deficit amounted to a record RUB 3.9 trillion. Problems with the execution of the Russian budget in 2023 may worsen further, as the budget is planned based on the average annual price of Russian oil of USD 70 per barrel. The deterioration of foreign trade and the easing of the budget policy weakened the Russian ruble. At the same time, it is now partially supported by the sale of Chinese yuan by the Russian Ministry of Finance as part of the so-called "budget rule policy". However, if the real oil price differs from the budgeted one for a long time, the Russian government will be forced to revise its parameters and reduce the sale of foreign currency. The embargo on Russian oil products in February could worsen the current situation further: Russia will be forced to reduce refining and increase the supply of crude oil on the world market. This situation simultaneously threatens both a reduction in demand for Belarusian products in physical volume and a drop in foreign exchange earnings due to the weakening of the Russian ruble. As a result, the "strange recession" of the Belarusian economy has a chance to return to the mainstream of the classic crisis scenario.

Without the easing of the sanctions regime, the task of increasing the export of "sanctioned" industries remains objectively difficult. If the growth of potash exports to China can also be achieved through railroad deliveries, then the condition for restoring exports to other key buyers (Brazil, India) is access to port infrastructure. The plans of the Belarusian authorities to accelerate the construction of their own ports in the northwestern part of Russia are still far from being implemented. It is difficult to assess the reality and potential of potash exports through the Caspian ports with further transit through Iran, which is being worked out by Belarusian officials.

Judging by official statements, the problem of redirecting the export of oil products is being solved much better. According to the authorities, in the fourth quarter, Belarusian refineries were supposed to start processing 3.9 million tons of oil, which is close to their optimal load. Information about buyers of oil products is currently not disclosed, however, it can be assumed that the products were sent directly to Russian consumers or in transit through Russian ports. In such a situation, the introduction by

European countries in February of an embargo against Russian oil products will have a negative impact on the work of Belarusian refineries. The production capacity of Russian producers exceeds the capacity of the domestic market, which will increase competition on it and lead to a fall in domestic prices.

At the same time, comparatively high commodity prices remain a favourable factor for the Belarusian economy. If earlier the forecasts about the end of the commodity super-cycle due to the slowdown in the global economy and the risk of recession in the US and Europe dominated the expert community, now the expectations are improving. Markets reacted optimistically to the success of the US Federal Reserve in combating inflation and the abolition of anti-epidemiological measures in China. Forecasts for the European economy are also improving: its adaptability to the loss of access to Russian hydrocarbons turned out to be higher than expected.

The second factor in the growth of the economy planned by the authorities should be the restoration of investment activity. Thus, according to the forecast of the authorities, the growth of investment spending in 2023 will be 22.3%, or USD 2-2.5 billion. This growth should finally interrupt the investment recession that has been going on since 2020. During this period, the annual reduction in investments amounted to about 28% in total (taking into account data for January-November 2022). The implementation of the declared plans in practice depends on the availability of investment projects and the sources of their investment. In previous years, the authorities experienced objective difficulties with this: the announced plans to launch a “new investment cycle” remained on paper. Many factors of previous failures remain relevant: investment optimism and demand for banking resources from the real sector is still weak, while the state budget is running with a deficit even without large-scale investment projects. In such a situation, the greatest potential is seen in attracting Russian loans in the amount of RUB 105 billion (or about USD 1.3-1.5 billion) for import-substituting integration projects. There are still no sufficient grounds to consider the scenario of financing investments from emission sources – in previous years, despite the formal failure of plans, the Lukashenka regime government did not use this measure, which is fraught with the creation of imbalances in the financial market.

In terms of the economic policy of the authorities, we can talk about the continuing trend towards the growth of centralization and state control in the economy. In the spirit of this policy, taxes for small businesses have been raised since January 2023. Officials also announce plans to expand the mechanism for controlling producer prices. The previously introduced restriction on price growth in trade on formal grounds showed a good result. Thus, after the introduction of marginal markups in retail trade for 90% of the consumer assortment, consumer inflation slowed down from 17.4% in September to 12.8% in December. It is also important that such a tough measure aroused broad support in society. Thus, according to the BEROC survey on the mood of households, 63% of

respondents positively assessed this step of the authorities. In general, in the opinion of the government, the centralization of the economy should increase its resilience to external shocks and mitigate the consequences of the economic downturn for the population. At the same time, the reverse side of such measures may be a decrease in the adaptability of the economy and a decrease in its growth potential in the medium term.

The long-term blow to the country's economic potential is also associated with the loss of the IT sector as an economic driver. Due to restrictive measures by foreign companies and the difficulty of doing business in the Western market, the outflow of employees from the sector reached 15 thousand people in 11 months of the 2022. At the same time, the total number of employees of HTP member companies at the beginning of 2022 was about 78 thousand people. As a result, according to the results of the year, the industry's contribution to GDP change turned out to be negative.

### **The risks to financial stability**

Trends in the financial sector are also quite multidirectional. In the deposit market, one can note a restrained growth in BYN deposits of the population, which occurs against the backdrop of falling rates. Thus, in December, fixed-term BYN deposits of the population increased by 2%, and in general for 2022 – by 25%. At the same time, the average rate decreased in the second half of the year: in December, the yield on deposits was at the level of 8-14% compared to 17-20% in the middle of the year. The National Bank has also returned to a more active policy in the financial market: since September, it has re-established the risk-free rate on new bank loans, revising it downward every month. Simultaneously with the growth of BYN deposits, foreign currency deposits of the population continue to decline – in USD terms they decreased by almost 10% over the year. As a result, the share of BYN component in the money supply increased over the year from 42.5% to 50.9%. Different dynamics has been observed for loans since the beginning of the year: with a moderate increase in BYN loans (+11.8% for 11 months of 2022), their foreign currency part is declining (-15.4% over the same period). Formally, this allows us to talk about the de-dollarization of the financial market, but this trend is taking place against the background of its general reduction.

The main trend in the foreign exchange market is a change in the role of the population from a net seller to a buyer. In September-December, the total net purchase of foreign currency by individuals exceeded USD 471.8 million in equivalent. The excess of purchases over sales in recent months is also typical for resident organisations. As a result, a positive market balance for the National Bank is formed only at the expense of non-resident sellers. In general, at the end of the year, the net supply in the foreign exchange market exceeded USD 560 million. This allowed the National Bank, despite the closure of international borrowing markets, to prevent a critical failure of gold and foreign exchange reserves at the end of the year (the decrease was 5.8%, while reserves

have been growing since April). An important role in maintaining the gold reserves was also played by the postponement of the payment of debts to Russia. The risks for gold reserves in 2023 also do not look significant. The government expects to refinance in Russia the costs of servicing the Russian debt, which accounts for about 70% of all payments. A certain intrigue is connected with how the government decides to redeem the issue of Eurobonds in the amount of USD 800 million, the maturity of which expires in February. If the payment is made in BYN to accounts in Belarusian banks, as was done with interest income on bonds, then international agencies will assess this as a default on the main body of the debt.

A sharp decline in the publicity of economic information, including from the side of the National Bank, can be considered a refusal from the previously declared goals of economic policy. Previously, the National Bank set itself the strategic task of moving from a policy of monetary targeting (managing the volume of money supply) to an inflation targeting policy. The latter is based on managing the expectations of agents in the economy, which implies a high level of trust in official information. The National Bank sought to increase the transparency of its activities and make it more predictable for the general public. The rules for holding regular meetings to revise the refinancing rate were determined, following which materials explaining the logic of the National Bank's actions were officially published. For several years, legislative changes have been actively lobbied to increase the independence of the National Bank and give it the right to form and publish its own forecasts for the development of the country's economy. However, at the end of 2022, there was a significant regression in this direction. All the liberal undertakings of the National Bank were curtailed, and the degree of secrecy of economic statistics reached the highest level in sovereign history. Many decisions related to the support of the national economy are also made with the signature stamp "for official use only".

In such a situation, one should expect an increase in the sensitivity of economic agents to any negative information, including that disseminated through unofficial channels. In the event of a crisis situation (for example, with a sharp BYN weakening), the National Bank will be forced to rely on administrative measures, not being able to influence the situation with verbal interventions. Without the growth of trust, it is difficult to fulfil the task of restoring the savings of the population in an organised manner. So, despite the growth of BYN deposits, the total amount of deposits at the end of 2022 is still significantly less than the peak values. For example, compared with the beginning of the pre-crisis 2020, the amount of foreign currency deposits of the population decreased by 42%, and BYN ones – by 25%. The fall compared to 2016 is even more significant – 53% and 31%, respectively.

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

The role of Russia in the current development of the Belarusian economy and ensuring its financial stability is difficult to overestimate, and it continues to grow. Thus, the share of Russia in the export of industrial products for the year increased from 55% to 75%. At the same time, it is characteristic that for the first time in history the balance of trade with Russia was positive for Belarus. In addition to the direct growth of Belarusian exports, this is connected with preferential gas prices for Belarus and a reduction in physical gas imports due to the launch of a nuclear power plant.

In addition to the traditional role of the main trading partner and source of external borrowing, in 2023 Russia can also become an important source of financing investment activities and generating budget revenues. Thus, in the 2023 budget, the government has included gratuitous receipts from foreign states in the amount of BYN 5.43 billion. Part of this amount will be reverse excise tax transfers, which will be allocated by the Russian budget as part of compensation for the oil tax manoeuvre and, according to estimates, will reach BYN 2 billion.

The so-called integration programs of the “union state” started to give the first concrete results. In January 2023, an agreement with Russia on the general principles of taxation for VAT and excises was signed. The document defines the general principles for the collection of these taxes, as well as the creation of a unified system for the administration of indirect taxes. The latter means that Russia will have access to information about the current activities of Belarusian companies. The document also provides for the creation of a new supranational body within the framework of the so-called “union state” – the Supranational tax committee. This body will not receive significant powers, but it has a certain symbolic meaning. An important symbolic gesture could also be the approval of the flag and anthem of the “union state”, which Russian officials are planning to adopt.

### **Conclusions**

The key risks for the Belarusian economy remain related to the external sector. The introduction by Western countries of prohibitive measures against Russian oil and oil products can qualitatively change the situation in the Belarusian economy and spread the crisis to industries not affected by the sanctions. The Belarusian economy is supported by persistently high prices in the commodity markets, the forecasts for which are improving.