



POLICY PAPER

No. 7 (109), April 2015 © PISM

Editors: Marcin Zaborowski (Editor-in-Chief) ● Wojciech Lorenz (Managing Editor)
Jarosław Ćwiek-Karpowicz ● Aleksandra Gawlikowska-Fyk ● Artur Gradziuk ● Dariusz Kałan
Piotr Kościński ● Sebastian Płociennik ● Patrycja Sasnal ● Marcin Terlikowski

Never Ending Crisis —Prospects for the Belarusian Economy

Anna Maria Dyner, Kacper Wańczyk¹

During 2014, the Belarusian economy experienced serious problems, which were deepened by the crisis in Russia. Further deterioration of the economic situation in Russia and Belarus' other trade partners such as Ukraine mean that 2015 could be much worse. That is why the Belarusian authorities need external financial support, although this need is still not forcing them to conduct structural reforms. Moreover, as presidential elections are planned for November, the president, Aliaksandr Lukashenka will traditionally try to postpone reforms and impose pro-social policies.

The Russian Factor

The condition of the Belarusian economy is closely tied to the situation in Russia. Half of Belarusian exports go to Russia,² which is also the country's main creditor. There are estimates that Russian subsidies in previous years reached about 15% of Belarusian GDP. Hence, the crisis in Russia (the IMF predicts that, in 2015, its GDP will shrink by 1.5%³), triggered by international sanctions and the decreasing price of oil products, is the major negative factor influencing the Belarusian economy.

In 2014, the Belarusian economy grew by 1.6%, although official estimates were 3.3%. This year, the authorities changed the 2015 economic growth forecast to 0.2% to 0.7%, from the previous 2%, which may be the first sign of stagnation before a full blown recession. Another sign of the economic challenges may be the rising level of gross external debt. According to National Bank of the Republic of Belarus, this had reached more than \$40 billion (about 52.8% of Belarusian GDP) by 1 January 2015.⁴ Although, in comparison to majority of European states, this data does not look bad, the process of deterioration has

¹ Kacper Wańczyk is head of Division of Ukraine and Moldova, Eastern Department, Ministry of Foreign Affairs. This publication expresses only the opinions of the author himself and cannot be considered the official position of the Ministry of Foreign Affairs of the Republic of Poland.

² State Customs Committee of the Republic of Belarus, "Itogi vneshey trgovli Respubliki Belarus za yanvar–dekabr 2014 goda," www.gtk.gov.by/en.

³ International Monetary Fund, "World Economic Outlook," p. 3, www.imf.org/external/pubs/ft/weo/2015/update/01/pdf/0115.pdf.

⁴ National Bank of the Republic of Belarus, "Valovoy vnesniy dolg Respubliki Belarus," www.nbrb.by/statistics/externaldebt.

continued for several years (by 1 January 2009, gross external debt had reached only \$15 billion⁵) and there are limited options that Belarus could exploit in order to reverse this tendency.

EU sanctions on Russia and, even more so, the Russian embargo on EU food products, seriously limited trade relations between the two partners in 2014. Fearing that enterprises from the EU would try to re-export goods via Belarus to the Russian market, the Kremlin decided to start controlling Belarusian food imports and banned the majority of types of food and agricultural produce such as meat, fruit and dairy products (which contradicted the agreement of Customs Union). That step was very painful for Belarus, especially as food and agriculture production represent almost 30% Belarusian exports to Russia.⁶ From January to September 2014, in comparison to the same period of 2013, Belarusian exports of pork decreased by 58.1%, milk and cream by 21.7%, sausages and similar meat products by 33.1%, tyres by 34.6%, fruits by 24.9%, machines and mechanisms for harvesting and threshing crops by 28.6%, tractors by 27.4%, and trucks by 22.8%.⁷ And all these areas of production are pivotal for the main Belarusian enterprises. Summing up, comparing to 2013, Belarusian exports to Russia in 2014 shrank by 8.8%, while imports decreased only by 2.7%. Moreover, the negative trade balance increased from \$6 billion in 2013 to nearly \$7 billion in 2014.⁸

Belarusian exporters were also hit by the devaluation of Russian ruble, which reduced the profitability of exports. Taking into account that the crisis in Russia will deepen this year, Belarusian exporters will face serious problems, and without support from the government in searching new markets, many of them will be threatened with bankruptcy.

Serious consequences for the Belarusian budget may also result in a “tax manoeuvre” in the natural resources sector, implemented by the Russian authorities. From the beginning of 2015, the Russian government decreased export taxes and excise on crude oil and oil products, at the same time increasing the natural resources tax. For Russia, the consequences will be reduced dependence on oil exports, and an increase in extraction. For Belarus, however, it will mean a serious rise in oil prices, which will hit the profitability of local refineries. For compensation of such losses, the Belarusian authorities asked Russia to abandon the existing rule, according to which Belarus has to pay export taxes to Russia on oil products that were made using Russian crude oil and sold outside the Customs Union. The Russian authorities agreed, but only for 2015, so it will mean that, in the second part of this year, the Belarusian government will have to start a new round of negotiations.

Moreover, Belarusian refineries, due to decreasing prices for oil and gasoline, will also lose some revenues. In the autumn of 2014, their profits were about \$30 per tonne (according to first deputy prime minister, Uladzimir Syamashka). In 2015, the profitability of the oil refining sector may fall to as low as \$10 per tonne.⁹ Considering that Belarus sold 13.8 million tonnes of oil products in 2014,¹⁰ it is likely that Belarusian refineries will earn \$276 million less in 2015. Such losses may result not only in suspending the modernisation of Belarus’ both refineries, but also in reducing the possibility of subsidising unprofitable branches of the economy such as agriculture (kolkhozes).

⁵ For more see: National Bank of the Republic of Belarus, “Valovoy vneshniy dolg Respubliki Belarus v razreze sektorov ekonomiki i finansovykh instrumentov v sootvetstvi s Rukovodstvom po statistike vneshnego dolga (MVF, 2003 g.),” www.nbrb.by/statistics/externaldebt.

⁶ Ministry of Economic Development of the Russian Federation, “Vneshnyaya torgovlya Rossiyskoy Federatsii s Respublikoy Belarus v yanvare–sentyabre 2014 goda,” www.ved.gov.ru/exportcountries/by/by_ru_relations/by_ru_trade.

⁷ *Ibidem*.

⁸ National Statistical Committee of the Republic of Belarus, “Osnovnyye pokazateli vneshney torgovli,” http://belstat.gov.by/ofitsialnaya-statistika/otrasli-statistiki/torgovlya/vneshnyaya-torgovlya_2/osnovnyye-pokazateli-za-period-s-___po-___gody_10/osnovnyye-pokazateli-vneshnei-torgovli.

⁹ For more see: T. Manenok, “NPZ ne prosyat gospodderzhki,” *Belorusy i rynek*, www.belmarket.by/ru/316/65/25450/HP3-не-просят-господдержки/htm.

¹⁰ National Statistical Committee of the Republic of Belarus, “Eksport vazhneyshikh vidov produktsii,” http://belstat.gov.by/ofitsialnaya-statistika/otrasli-statistiki/torgovlya/vneshnyaya-torgovlya_2/osnovnyye-pokazateli-za-period-s-___po-___gody_10/eksport-vazhneyshih-vidov-produktsii.

The situation in the Russian economy also has a serious influence on the labour market in Belarus.¹¹ So far, as the economic situation in Belarus has worsened, a number of Belarusians decided to look for jobs in Russia, especially as they do not have to apply for any kind of work permission. Today, due to the worsening situation in Russia, the rate of work migrants from Belarus is very likely to decrease, which may be reflected in a higher unemployment rate in Belarus. The crisis in Russia not only reduces the number of posts available to Belarusians, but, due to the weakening of Russian ruble, salaries in Russia have ceased to be attractive in comparison to those in Belarus.

Unlike in previous years, Russia will not be able to support the Belarusian economy. The Belarusian authorities were counting on a \$2 bln loan from Russia, but in March they received only \$110 mln. What is more, Belarus is still waiting for the last tranche of a loan from the Anti-crisis Fund of the Eurasian Economic Community (\$400 mln), but there the main creditor is also Russia, so it is very doubtful that Minsk will receive it.

Additional Negative Factors

The Belarusian economy will also be heavily influenced by the situation in Ukraine, which is its second largest trading partner, with a trade volume of 7% (2014). In 2013, 68% of all Belarusian exports to Ukraine were oil products, and 8% were machines. The main import products were metallurgical products (23%) and electricity (9%). In 2014, compared to 2013, Belarusian exports to Ukraine shrank by about 17%, while imports from Ukraine dropped by 2%.¹²

Further negative elements were observed on the home front. One was the cyclical recession that started at the very beginning of 2014. This was accompanied by the increasing growth of prices, mainly stimulated by the increase of food product prices.

The financial situations of companies continued to worsen in from January to November 2014, when more than 1,000 companies recorded losses (compared to 875 in 2013, and 468 in 2012). The share of such losses in the total net income for the economy in the same period was 25.8% (23.2% in 2013, and 4.8% in 2012). This was partly due to falling external demand for Belarusian products (as a result of the above-mentioned external factors—see data below concerning exports to Russia), and also to the effect of the growth of costs (mainly in the sphere of labour, where, according to data for January to September 2014, they grew by 18%, and in the capital, Minsk, by as much as 21.8%), which was the result of government policies designed to stimulate the economy.¹³

Small growth was assured by two factors. On one hand, it was stimulated by the growth of household disposable income, as during 2014 households still had at their disposal a considerable amount of resources. According to an initial assessment by the Research Centre of the Institute of Privatisation and Management, households' disposable income was to grow by 2.9% for 2014. This element, however, weakened at the end of the year with the fall in the value of the Belarusian ruble. On the other hand, growth was influenced by the partial improvement of exports, significantly in the export of potash fertilisers (mainly to China), but partly also of oil products. Some analysts also point out the partial tightening of the budget policy as a positive element that had an influence on GDP growth.

¹¹ Russia is the main destination for Belarusian labour migration.

¹² For more see: Ministry of Foreign Affairs of the Republic of Belarus, "Vneshnyaya torgovlya Belarusi," <http://mfa.gov.by/export>; National Statistical Committee of the Republic of Belarus, "Import tovarov v Respubliku Belarus po stranam SNG," http://belstat.gov.by/ofitsialnaya-statistika/otrasli-statistiki/torgovlya/vneshnyaya-torgovlya_2/osnovnye-pokazateli-za-period-s-__-po-____gody_10/import-tovarov-v-respubliku-belarus-po-stranam-sng; National Statistical Committee of the Republic of Belarus, "Eksport tovarov Respubliki Belarus po stranam SNG," http://belstat.gov.by/ofitsialnaya-statistika/otrasli-statistiki/torgovlya/vneshnyaya-torgovlya_2/osnovnye-pokazateli-za-period-s-__-po-____gody_10/eksport-tovarov-respubliki-belarus-po-stranam-sng.

¹³ As some Belarusian economists usually point out, a traditional answer of the Belarusian government to cyclical recession is stimulation. Unfortunately, as the specialists underline, this leads to deepening the cycle itself and, some day, it may reach a point when it will be impossible to control it.

Throughout the year, with continuous loss of currency reserves¹⁴ (with a short-term reverse in the middle of the year) pressure on devaluation grew. Finally, in December 2014, the National Bank of Belarus introduced a package of measures aimed at stabilising the financial market. Some bank interest rates were raised by 50%, and an obligation to sell 50% of export revenues on the foreign exchange market was introduced. A 30% temporary tax (for citizens and legal persons) on the purchase of foreign currency was also introduced (in January 2015 it was lowered, first to 20%, than to 10%, and eventually cancelled). Despite these measures, Belarusian ruble lost 49% of its value against USD over the year.

Growing Unemployment

One of the more visible signs of negative tendencies in the Belarusian economy is the decision of the authorities to freeze salaries, regardless of the fact that it is an election year. The average salary in February 2015 decreased to the equivalent of \$419¹⁵ (in December 2014, it was \$465¹⁶). Moreover, the inflation rate exceeded 16% in 2014,¹⁷ which also had a negative influence on the level of Belarusians' incomes. Moreover, for the first time during a 15 year period, the rate of unemployment could exceed 6%,¹⁸ and, due to the deteriorating economic situation, the number of part-time workers rose rapidly. If this situation continues, it may cause extreme pauperisation of society.

Another negative social effect of stagnation in the economy was the situation on the labour market. Government stimulation of the economy led to an increase in production costs, mainly labour costs. Companies, influenced by the recession, decided to cut the heaviest burden, which led to growing unemployment.¹⁹

Despite all these problems, according to a survey by the Independent Institute of Socio-Economic and Political Studies (December 2014) Belarusians saw 2014 as relatively stable, especially compared with their assessments from 2011, a year of serious destabilisation on the financial market.²⁰ Their assessments of their own private situations were even more optimistic, with 48% of them describing 2014 as "successful" (33% in 2011), and 32% saying it was "unsuccessful" (45% in 2011).²¹ Analysts underline that this was the result of the situation in Ukraine; comparing themselves to Ukrainians, Belarusians decided that things were still not as bad as they could be.²² It should also be noted that it is not the first stagnation and/or economic crisis that Belarusians have experienced in the previous five years.

¹⁴ For 1 April 2015 it was only \$4.56 billion, which is the worst result since April 2007, and is able to cover only the equivalent of one month of imports. For more see: National Bank of the Republic of Belarus, "International Reserve Assets of the Republic of Belarus," www.nbrb.by/eng/statistics/reserveAssets/assets.asp.

¹⁵ National Statistical Committee of the Republic of Belarus, "O nachislennoy sredney zarabotnoy plate rabotnikov Respubliki Belarus v fevrale 2015 g.," http://belstat.gov.by/ofitsialnaya-statistika/otrasli-statistiki/naselenie/trud/operativnaya-informatsiya_8/o-nachislennoi-srednei-zarabotnoi-plate-rabotnikov-respubliki-belarus-v-yanvare-2015-g.

¹⁶ National Statistical Committee of the Republic of Belarus, "O nachislennoy sredney zarabotnoy plate rabotnikov Respubliki Belarus v dekabre 2014 g.," http://belstat.gov.by/ofitsialnaya-statistika/otrasli-statistiki/naselenie/trud/operativnaya-informatsiya_8/o-nachislennoi-srednei-zarabotnoi-plate-rabotnikov-respubliki-belarus-v-dekabre-2014-g.

¹⁷ National Statistical Committee of the Republic of Belarus, "Indeksy tsen i tarifov," http://belstat.gov.by/ofitsialnaya-statistika/otrasli-statistiki/tseny/godovye-dannye_3/indeksy-tsen-po-otdelnym-sektoram-ekonomiki.

¹⁸ According of official statistics, the unemployment rate for 31 January was 0.7%, while on 31 December 2014 it was 0.5%. For more see: Ministry of Labour and Social Protection Republic of Belarus, "Sostoyaniye rynka truda," www.mintrud.gov.by/ru/sostojanie.

¹⁹ Officially, unemployment in Belarus is very low—in last five years at the level of 1%. However, the real rate of unemployment is probably higher. Usually, in state-owned companies, when stagnation comes, employees are given unpaid leave en masse, or work only part-time (on paper they remain employed).

²⁰ The question asked was "How was the year that passed in comparison to the previous one." In December 2011, 74.7% of responders answered "harder," while in December 2014, 45.6% marked this answer.

²¹ "On whose heads were all the 'cones' falling," IISEPS Research, 6 January 2015, www.iiseps.org/analitica/813/lang/en.

²² *Ibidem*.

Stagnating External Trade

The overall situation in external trade may be seen as stagnating, as trade turnover fell by 13% for 2014. However, it should be underlined that this was mainly due to the fall in imports, which shrank by 15%. Exports decreased by 11%, but, as mentioned above, the main positive driving factor behind the support of GDP growth from the external side was the rapid growth in exports of potash fertilisers. According to data for January to December 2014, exports of this product grew by 69.5%.²³ This was observed despite the fact that, in 2013, the Belarusian potash producer Belaruskaliy, and Uralkaliy, Russia's single exporter of this fertiliser, broke the long-lasting alliance that had helped both companies to build a strong position on global markets.²⁴

Belaruskaliy's good results were an effect of external factors and the company's price policy. The supply deficit on the global potash market deepened in 2014. Demand from China and India, the main importers, reached record levels (in China demand rose to its highest point since 2008, and growth of demand in India was close to 50%). In addition, Belaruskaliy lowered export prices (by around 13%, according to Belstat data for January to December).²⁵ This allowed the company to increase its exports to China, enter the U.S. market for the first time in years, and gain contracts in Brazil.

Belaruskaliy's good situation is important not only with regards to the macroeconomic situation. It is worth remembering that the company is one of major supporters of Belarusian financial stability. For example, the company took loans from Russian and Azeri banks used by the Belarusian government for completion of currency reserves. Also, Lukashenka repeatedly uses Belaruskaliy's assets to stabilise the national budget, usually charging the company a special tax or duty when a given year is difficult. It was no different in 2015, when, from 1 January, a duty on potash export was reintroduced and a 75% tax on income levied.

The IMF—The Last Chance Creditor

Experts taking part in the last IMF mission to Belarus, which worked there in March 2015, summed up the situation of the Belarusian economy perfectly. According to them: "Belarus' economic model continues to make it highly vulnerable to economic shocks, as was illustrated once more by the recent market turmoil, triggered by a deteriorating external environment. The recurrent pressures are rooted in the continual inability of Belarus' over-determined central-planning model to deliver sustainable growth. Frequent bouts of expansionary macroeconomic policies have fuelled inflation and external imbalances, and left the country highly dependent on ad hoc external financing."²⁶

Nevertheless, interest in a new stand-by loan from the International Monetary Fund is regularly expressed by representatives of the Belarusian government, all the more so as Belarus sees such a loan as a small counterweight to Russia's financial support.

A loan from the IMF is needed extremely urgently for macroeconomic stabilisation, especially as Belarusian foreign currency reserves have decreased to dangerously low level. Moreover, the shrinking of these reserves has been constant over a period of 10 months. Even worse, Belarus has to pay back about \$4 billion dollars to all creditors during this year.²⁷ That is why Belarus urgently needs not only foreign

²³ "Belarus: Makroekonomicheskiy prognoz," Institut Privatizatsii i Mienadzhmenta, 2 December 2014, National Statistical Committee of the Republic of Belarus, "Statisticheskiy biulleten – Statisticheskoe obozrenie Belarusi, 2014," www.belstat.gov.by/bgd/public_bulletin/index_597.

²⁴ This may be partly due to the fact that, in August 2009, shortly after the announcement of Uralkaliy's wish to withdraw from joint trade with the Belarusian Potash Company, the general director of Uralkaliy and the president of the board of BPC, W. Baumgartner, was arrested in Minsk. He had gone to Belarus on the invitation of the Belarusian prime minister, to discuss further functioning of the BPC. Currently, Baumgartner is back in Russia, cleared of all charges (he was accused of acting against the interests of the shareholders of BPC).

²⁵ National Statistical Committee of the Republic of Belarus, "Statisticheskiy biulleten – Socialno-ekonomicheskoye polozhenie Respubliki Belarus w yanvare–dekabre 2014 g.," www.belstat.gov.by/bgd/public_bulletin/index_591.

²⁶ International Monetary Fund, "Statement by the IMF Mission to the Republic of Belarus," www.imf.org/external/np/sec/pr/2015/pr15117.htm.

²⁷ At the beginning of April, Belarus fully paid back the IMF loan.

investments, but also foreign credit support, and the main source of this is the International Monetary Fund. But is very doubtful that the IMF will reach a decision quickly on whether to give the loan to Belarus.

The main condition for starting talks about new stand-by programme is that the Belarusian authorities have to “demonstrate their preparedness to make decisive changes (fully flexible exchange rate, appropriately tight macroeconomic policies, and bold, frontloaded structural reform) to their policies.”²⁸ Neither does the IMF want to be part of the political game in Belarus, so no decision about a new stand-by programme should be expected before the presidential election scheduled for November, even more so because the period after the election is the only one in which the Belarusian authorities may decide on serious structural reforms. Moreover, the IMF will be more cautious because, during the previous stand-by programme in 2009, the Belarusian authorities did not realise any reform they had promised. That is why the IMF is very likely to tighten criteria for granting a loan. So, even if Belarus tries to manage repayments on its external debts, taking into account the shrinking level of currency reserves, as well as other economic problems, it seems almost obvious that the Belarusian authorities may face a problem with solvency.

How to Avoid a Full Blown Crisis

Because of the lack of structural reforms, prospects for the Belarusian economy are grim. The last IMF mission stated (in fact re-stated, for it is a constant recommendation) that “deep structural reform remains critical to promote sustainable future growth and break with the cycle of recurrent crises.”²⁹ The IMF mission suggested that the Belarusian authorities have to adopt and implement a comprehensive reform agenda, which should include “decisive price liberalisation (...), the swift phase out of mandatory targets for enterprises, credible plans for privatisation in the corporate and banking sectors, and a strengthening of safety nets to protect the vulnerable.”³⁰ So if the Belarusian authorities want to avoid future turmoil, they have to conduct: deregulation of trade markets, privatisation, reforms of the financial sector, limitation of state support for the economy, and develop the sector of small and medium enterprises. But the main problem is that, even if the authorities in Minsk realise such necessities, they have never show any real will to conduct them so far.

Internal economic problems are exacerbated by the downturn in the markets of Belarus’ main partners, especially Russia and Ukraine. The crisis in both states had started before the conflict in Ukraine, was deepened by the deterioration in Russian–Ukrainian relations and Western sanctions imposed on Russia, and, according to international prognosis, is not likely to change for the better in the coming months, which is bad news for Belarusian exporters. Such a situation will also negatively affect the labour market in Belarus, and a rising rate of unemployment may become a growing problem for the Belarusian authorities.

Economic crisis in Russia and Belarus will also have a negative effect on the prospects of the Eurasian Economic Union. Even if the presidents of Russia, Belarus and Kazakhstan decided that they wanted to create a monetary union, in the current economic realities it sounds rather like a political fiction. Moreover, it seems that, in an extreme case, the deteriorating economic situation in the region may also have a negative effect on the whole project of reintegration of post-Soviet space.

Nevertheless, the economic crisis will not change the people’s attitude towards the authorities, including Lukashenka, especially as, once more, a “negative adaptation” to the situation in Belarus can be observed. Moreover, Belarusians are really afraid of such consequences of social revolution as they see in Ukraine (political instability, economic crisis, war, loss of part of the state’s territory). That is why people are more likely to support incumbent president in the upcoming elections.

²⁸ International Monetary Fund, “Statement by the IMF Mission to the Republic of Belarus,” www.imf.org/external/np/sec/pr/2015/pr15117.htm.

²⁹ *Ibidem*.

³⁰ *Ibidem*.

In the current geopolitical situation, primarily connected with the situation in Ukraine, the European Union should start work on a new conception concerning policy towards Belarus (as part of a new Eastern Neighbourhood Policy). The starting point for such work should be the maintaining of current forms of cooperation. That is why the EU countries should consider providing financial aid for Belarusian authorities, such as by supporting Belarusian efforts to obtain the IMF's stand-by programme (but only under strict economic conditions) or increasing the level of funds for projects being realised in Belarus by the European Bank for Reconstruction and Development, especially those connected with supporting small and medium enterprises, as well as regional development projects.

Poland should also continue its readiness to support Belarus in its efforts to join the World Trade Organisation, and continue technical dialogue with Belarus, especially in trans-border, logistics and tourism cooperation.

However, the main condition for increasing the level of cooperation (the unsuspended possibility for the European Investment Bank to cooperate with Belarus) should be releasing political prisoners and improving the situation in the sphere of human rights in Belarus.