Analytical note:

Monitoring of the situation in the field of economic security of Belarus

(November 2015)

Minsk

The risk of financial instability

Summarizing the results of the month, we may state the deterioration of the situation on the financial market. The net demand for currency among the population and the legal entities has been fixed for the second consecutive month, while in November it increased significantly (up to USD 254.3 mln. as compared to USD 70.7 mln. a month earlier). In the banking system at the beginning of December, there was a sustained deficit of ruble liquidity, which is caused by both the reduction of ruble deposits and a sharp increase in lending to the economy (debts of the organizations on ruble loans in October increased by 4.2%). This is due both to seasonal factors (deterioration of the traditional results of foreign trade in the last months of the year) and the tough measures of the National Bank, aimed at cheapening the cost of credit. Thus, in November, a sensational decision was adopted by the authorities aimed at promoting long-term ruble deposits. Instead of granting an unconditional right to the depositor to withdraw the deposit within a 5-day period the authorities have introduced the classification of deposits as revocable (with the possibility of early withdrawal) and irrevocable, which are impossible to be removed without the consent of the bank. This measure is intended to prevent the now-familiar “wave” in the deposit market, when in the period of weakening of the national currency and growth of devaluation expectations a significant (up to 10-15% of the total) flow of ruble deposits into foreign currency and cash is observed. Also starting from 01.04.2016 the authorities introduced taxation of the interest income on short-term deposits: ruble deposits with a term of up to one year and foreign currency up to two years. According to the authorities, this measure will stimulate long-term deposits (currently 80% of ruble deposits and 60% of foreign currency deposits are placed for up to a year), which will make the resource base of banks more predictable and reduce the cost of investment and housing loans. In addition to legislative changes, the banks were also reported informal recommendations to retain the deposit rates at 20-25% per annum for revocable deposits and at 25-30% for irrevocable deposits. Such harsh measures of monetary authorities involve a risk reduction of ruble deposits and increased demand for the currency market. According to the National Bank, such risks were taken into account at decision-making, and currently the dynamics is more optimistic than expected. So, in November the outflow of ruble deposits amounted to BYR 1 trn. (about 2.1% of deposits) instead of the expected 10% of the resource base of banks. In such conditions, the National Bank is forced to carry out operations to support the bank liquidity, which further increases the pressure on the currency market.

Perhaps the only unambiguously positive news may be considered a small (less than 1%), but still a growth of foreign reserves for second month in a row (in October by USD 38 mln. to the level of USD 4,666,700,000.). However, the traditional deterioration in the foreign exchange market by the year end and the absence in the nearest future of large foreign income may reverse this trend.

The risk for economic independence

It is clear that in the developing Russian-Turkish conflict Belarus will not join the economic sanctions of the ally. As a result, we may expect the public claims to the Belarus over the resale of the sanctioned Turkish goods, as well as tightening up of sanitary control for Belarusian products, up to a ban on supply of products of particular manufacturers. The irony is that the conflict between Moscow and Ankara broke out just a week after the Turkish-Belarusian Investment Forum in Istanbul, where acting Prime

Minister Andrey Kobyakov expressed the hope for “explosive” development of economic relations between Belarus and Turkey.

At the same time, despite a slight cooling of the Belarusian-Russian relations because of the lack of unequivocal support by the Belarusian authorities of the Russian foreign policy, one should not expect their deterioration to the level of trade wars. Furthermore, many bilateral issues at the moment are solved much easier than it was 2-3 years ago. Thus, in working order the both countries agreed on the amount of Russian oil to be delivered in 2016, which had often been used by the Russian government as a factor of pressure; the authorities plan to receive USD 1.1 bln. of Russian oil fees to the Belarusian budget; the negotiations, initiated by Belarus on an additional discount on the price of oil in the amount of USD 5 per tone, are in progress; the issue of “integration projects”, which involves participation of the Russian capital in privatization of the most attractive Belarusian enterprises, are actually removed from the agenda. Apparently, there are quite good chances to receive funding under the program of the Eurasia Foundation for Stabilization and Development, which matrix of measures has already been agreed and the decision on a loan allocation may be taken in the first week of December this year.

The risk of economic recession

The situation in the real sector of the economy continues to deteriorate. The fall in GDP in January-October has accelerated to 3.9% compared to 3.7% a month earlier. However, the reduction in the industry amounted to 7.1%, in agriculture and wholesale trade to 3.9%, and the retail and housing showed a slight increase (0.7%). After several months of reduction the stocks in the industry increased again, which level reached 71.7% of the average production. The officials hope that according to the results of the year a fall in GDP will not exceed 3.5-3.6%. However, taking into account the reduction by 20% of the plans for the construction program, the fall by 5.4% in real incomes and the deterioration of the terms of foreign trade, even this forecast looks optimistic.

There are no prerequisites to expect drastic changes in GDP growth. We may hardly take seriously and consider a possible driver of economic growth all the mega-projects of the authorities (in particular, construction of the Belarusian-Chinese industrial park and the complex “Minsk-World”). Although the state-run media appear with statements that construction of the complex “Minsk-Mir” in the long run will lead to the GDP growth of 6-7% per year, it will at its best repeat the fate of the Belarusian-Chinese technology park. Thus, as far as the implementation of the Chinese project has started, the expectations of it continue to decrease. If investment in the park was initially determined at USD 30 bln. for 15 years, now the optimistic estimates fell to USD 2-4,6 billion investment for the period until 2020 . Moreover, the total effect on the country's GDP in five years in the best case will be in the range of 0.9-2%. Given the size of the tax benefits provided and the risks of competition from the park residents for domestic producers, even such an increase is unlikely to be satisfactory.

To date, the government has not yet formulated the strategic plans to overcome the crisis, and did not approve the budget and the predicted documents in 2016. Moreover, at the beginning of December and it has not formed a new Government, despite the fact that the previous government left the office still on October 16th. Obviously, the main reason for such a long pause in making the planned decisions became the negotiations with the IMF, which representatives visited Minsk last November. Although during the negotiations the Belarusian authorities highly appraised the chances of reaching an agreement with the fund, they did not manage to agree on launching a joint program, the amount of lending in the framework of which should amount to USD 3 bln. However, the remote negotiations with the Fund are expected to continue in the coming weeks, and the final decisions about the program or rejection will be taken in the first quarter of 2016.

In general, the authorities, including the President himself, have publicly agreed with the proposed measures, the IMF economic reform, marking the differences only in the period of their implementation. Thus, according to some sources, the reform of housing and communal services with introduction of a full refund of the entire cost of the services will be extended by the authorities for up to 5 years instead of the 6-18 months proposed by the Fund. For the first time the willingness to raise the retirement age is also voiced, but only after the “council with the people”, the form of which is already being developed. The willingness is expressed to cut directive funding of the public sector and to tighten control over its efficiency. Thus, since 01.01.2016 the only source of funding for government programs will be the Development Bank, which will provide resources on a competitive basis. Achieving the goals of the funded governmental programs should also become a criterion for evaluating the work of directors of the state-owned enterprises. At the same time the complete rejection of the directive financing is not in question. In some cases it appears to be quite reasonable, for example, the decision by state banks to purchase bonds of the Belarusian Metallurgical Plant for the amount of USD 250 mln. due to the complexity of the latter with servicing the investment loans because of falling commodity markets. But often, the motive appears to be the desire to maintain the large Soviet enterprises at all costs, regardless of their prospects at the changing markets (e.g. in case of allocation of regular state aid in the amount of USD 5 mln. to the Light Industry Enterprise “Kamvol”).

In fact, the reform of managing the state property is still in the initial stage of development. The pilot sites, on which it is planned to test modern methods of corporate management, should become some wood processing enterprises to be transferred to the Bank for development of operational management after the failure of the state program of industry modernization. Apparently, only in case of success of this project we may expect to reform the decision-making mechanism for managing state property and redistribution of powers from the ministries and local authorities for the benefit of businesses.

Conclusion

The authorities' actions in the financial market and the real sector of economy continue to be quite different. If the authorities are already not afraid to carry out the conversion and take stringent measures to achieve the goal at the foreign currency deposit market (in this case – the reduction of inflation), the policy concerning the public sector of the economy remains conservative. The situation of uncertainty persists regarding both strategic and operational plans for the economic policy of the authorities to overcome the deepening recession. According to the inaugural speech of Alexander Lukashenko, there is no consensus and political will to carry out comprehensive economic reforms.

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