Belarusian Economy in May: Are We in Recession Yet?

Despite the united efforts of the government and the National Bank, the economy is growing very slowly. Belarus remains an economic wonderland.

But if several years ago the growth rates were miraculous, today the miracle is the absence of growth under the expansionary monetary policy and stimulation of investment. Is Belarus in a development recession?

GDP Growth

The GDP report in mid-May disappointed once again: a growth rate of 2.5 per cent in January-April not only fell short of official forecasts, but was also below the previously reported rate of 3.5 per cent from a month ago. For a developing country, which was growing at an average rate of 7 per cent for over a decade, a growth of 2.5 per cent is a recession.

A deeper look at the GDP numbers give even more reasons for concern. If we deduct net taxes from the GDP, we get a gross value added measure that is growing even slower – only a rate of 1.2 per cent. Taxes contribute significantly to GDP growth, and it is difficult to say why precisely (most probably the cause is due to changes in accounting procedures). But the important thing to notice here is that economy is producing only 1.2 per cent more in terms of goods and services, and the rest of the growth is due to the fact that government is collecting more indirect taxes.

Manufacturing, a driver of growth in the past, declined at a rate of 1.7 per cent, despite increases in inventory stocks. Now agriculture and trade drive growth. Agriculture is one of the few industries benefiting from exports. Trade is mostly fuelled by an increase in real wages, which, again, grows faster than labor productivity. Since high growth in wages is not sustainable, the future long-term growth in trade also does not seem probable.

International Trade

The government's hopes of high growth were linked with an increase of exports. Exports, however, did not grow as much as planned, and for some industries it even decreased. Exports of all goods and services declined 17.9 per cent in the first quarter (in contrast with the official forecast of 15 per cent growth). Of course, the major blame goes to oil- refinery products: after the ban on the export of certain refinery goods the exports in this category declined from $4,162.4m in the first quarter of 2012 to $3,304m in the first quarter of 2013.

But export declines are visible over all the main exporting branches of the economy, with the lucky exceptions of dairy products and potash fertilizers. There are two major reasons for declines in non-oil exports. The first one is continuing economic slowdown of the major trading partners of Belarus – Russia and the EU. The second being the real appreciation of the Belarusian ruble. The nominal exchange rate was relatively stable throughout the past year, while inflation was positive. As a result, Belarusian exporters became less competitive on foreign markets, as they face increasing costs and cannot compete with the prices.

Table 1: Official Forecast and Reality: Some of the Economic Indicators

	1st Quarter 2013	**Official Forecast for 2013**
GDP growth rate	2.5%*	8.5%
Labour productivity growth rate	4.5%	9.3%

Exports of goods and services, growth rate	-17.9%	15.2%
Foreign direct investment, $ bln	1.5*	4.5
Real incomes, growth rate	21.4%	6.5%

*Jan-Apr 2013 versus same period last year

The other side of the coin is the increase in imports. Decrease in oil imports explains the overall imports decline, but other types of imports increase. In part this increase is fuelled by the modernization program, which boosted the demand for imported investment goods. But the imports of consumption goods are also increasing. The major reason behind this growth is the increase in real wages (up 22.4 per cent in the first quarter of 2013 versus the same period last year), which surpassed the increase in labour productivity (up 4.5 per cent only).

On the one hand, higher wages stimulated the demand for imported goods, which are often perceived as of a higher quality. On the other hand, higher wages without growth in productivity imply higher costs, and it makes the domestic goods less competitive even in the domestic market. Any attempts to cut consumption imports with administrative measures (like setting administrative sales objectives for retailers) will have a limited effect at best.

Foreign Investments and Foreign Reserves

Macroeconomic stabilisation has born its fruits – foreign direct investment in January-April 2013 nearly tripled compared to the same period last year, growing from $583m to $1,507m. The largest share (88 per cent) of foreign direct investment went to enterprises that are not under direct control of any government agencies.

But the government continues to create precedents that worsen the investment climate in Belarus and its perception by foreign investors. In [the notorious case of Ecomedservice](), government quickly overtook the successful medical business after the death of a patient, without waiting for any judicial decisions. Even if the management of Ecomedservice were indeed responsible for the death (which should be established in court), the imminent and seemingly permanent government takeover may raise concerns by potential investors, both within the country and abroad. What if something happens to your business, will it also be nationalised without court orders?

The inflow of foreign investment is very timely: this year Belarus has to repay a lot of debts, while the foreign trade balance worsens. During April the foreign reserves of the National Bank grew by $106.2m. The arrival of a 440m transfer from the EvrAzES Anti-Crisis Fund contributed to the growth of the reserves in the month when Belarus had to repay $261.8m of an IMF loan.

Would the National Bank be able to sustain its level of reserves without international loans? Improbable. The only possible solution is the privatisation of state enterprises. But today the privatisation to Russian government-run corporations (for example, the possible sale of the government share of VTB bank to its Russian counterpart) is the only viable option. But this kind of privatisation lacks the needed merit-based kind of effective owner it is seeking, as Russian government corporations can hardly be considered effective.

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