The Russian Contagion Spreads to Belarus – Belarus Economy Digest

Belarus's GDP growth managed to strengthen in November. But despite this, many signals about an upcoming downturn have appeared. The Russian economic contagion began to spread to Belarus through trade and informational channels.

The government reacted by introducing a de-facto 30% devaluation that was accomplished in a rather 'creative' manner. But this decision seems to be more like a short-term relaxation than anything else, while further adjustments have become inevitable.

Real Economy: Output Strengthened, Prospects Worsened

In November, the growth rate for Belarus's output increased and reached 1.7% (standing at 1.5% in four previous months). However, the marked improvement in the dynamics surrounding the GDP dynamics will not become a sustainable trend.

First of all, this acceleration in November was mainly due oil-refining and the production of potash fertilisers. Both these and other industries associated with natural resources have utilised roughly all their available capacities. So, further output spurts by these industries is highly unlikely.

Second, a majority of other industries demonstrated either stable or negative dynamics with regards to their output. Output in non-manufacturing industries – construction, agriculture, trade, transport and communications – did not exhibit any substantial change. In manufacturing, there are some positive movements peculiar mainly to smaller industries, whose contribution to GDP is negligible.

Large industries – those that manufacture food products, non-metallic mineral products, basic metals, electrical equipment, transport vehicles – saw their performance worsen in November. A slowdown in these industries deepened, and at the same time a majority of them faced a growing volume of finished products inventories.

These negative trends mirror poor domestic and external demand. Domestic consumer demand is weakening because of stagnating real wages (see Figure 1). A majority of firms have to freeze or to cut wages in order to enhance their competitiveness.

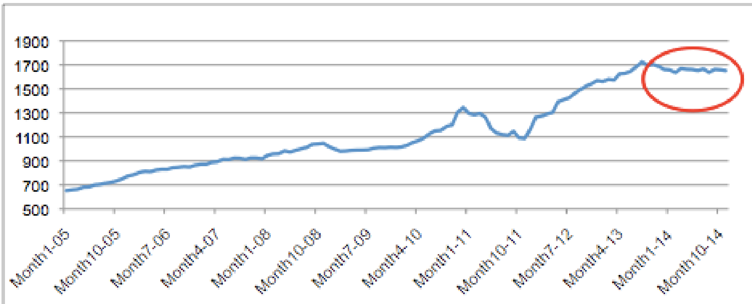

Figure 1. Real wages (seasonally adjusted, in thousands of 2009 Belarusian rubles).

Domestic investment demand is developing in a rather chaotic manner. In previous months it seemed to revive on a backdrop of lowering interest rates and government's stimulation. However, in November this trend was reversed and a slowdown in capital investments began to be visible. The latter seems to be associated with the deterioration in business' expectations and confidence.

Furthermore, many firms suffer from the ablation of working capital, which restricts their possibilities and propensity to finance investments through their own funds. Finally, banks tightened their credit supply in the current uncertain environment with its corresponding growing risks.

The external environment is the largest headache for Belarusian producers. Only businesses associated with natural resources (oil products, potash fertilisers, etc.) can rely on a stable level of demand. Other firms that operate on competitive markets are in state of perplexity.

The majority of Belarusian exporters produce capital goods for the Russian market. For their part, Russian agents have radically cut their investment expenses, given the start of the recession and the poor prospects of the Russian economy. Thus, new orders for Belarusian goods have dropped substantially.

problems with settlements on the supplies have already taken place

Furthermore, there are signals that problems with settlements on the supplies have already taken place. For instance, in November incoming export payments decreased significantly in comparison both to October 2014 and November 2013. Moreover, external overdue debtor indebtedness seems to have begun to rise. Hence, there is a danger of massive payment defaults, which may further hamper the solvency of Belarusian enterprises.

In December, new challenges became visible for Belarusian producers. First, the signs of recession in Russia became more and more evident. Hence, the challenges of contracting demand and progressing instances of non-payment might have proliferated. Second, the mix of political and economic considerations pushed the Russian authorities to initiate a new “trade-war” with Belarus.

the statistics for December (when available) will record a huge drop in exports and revenues from Russia

They accused Belarus of supplying prohibited goods from Western countries to Russia. Later this accusation transformed into a ban on the export of Belarusian meat and some other food products to Russia, which was formally listed as being due sanitary safety considerations. Hence, one may expect that the statistics for December (when available) will record a huge drop in exports and revenues from Russia. These hardships are directly affected by the currency market in December, which has become a first victim of the Russian spreading economic contagion.

Monetary Environment: Belarus Tries to Resist the Russian Currency Crisis

The contracting capacity of Russian markets developed alongside the gradually lowering price competitiveness of Belarusian producers. Until recently, the Belarusian authorities preferred to ignore the substantial appreciation of Belarusian ruble vs. Russian ruble, justifying it through considerations of their own domestic financial stability. This led to huge losses in the real price competitiveness of Belarusian producers on the Russian market (by roughly 30% in comparison to an average level of 2013 and the beginning of 2014, see Figure 2).

In a broad sense, one may argue that already in December a huge fraction of Belarusian firms have become uncompetitive on Russian markets.

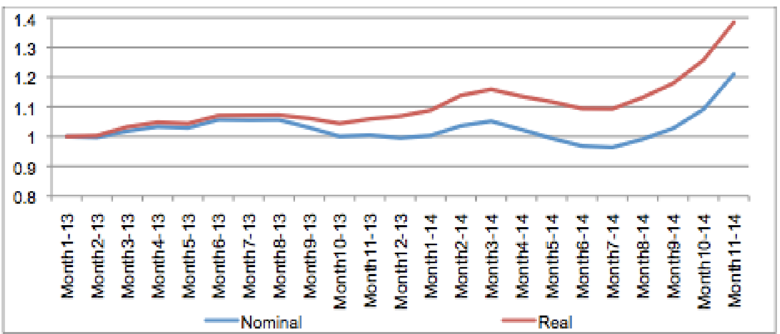

Figure 2. Indexes of BYR/RUB Exchange Rate (January 2013=1).

Besides through trade channels, the Russian financial contagion began to spread via informational channels as well. Expectations of an inevitable depreciation followed. Correspondingly, Belarusian households and firms increased their demand for hard currency.

For instance, November has become the first month of the year when households became a pure purchaser of hard currency (some purchases on a net basis took place also in May, but it was close to zero). Furthermore, many households changed the currency of their deposits to US dollar (or other hard currencies besides the Belarusian ruble). This led to a quick depletion of international reserves (in November official international reserves shrank by USD 204m and total international reserves shrank by USD 460m).

Belarusian households began buying of hard currency in a panic

In December, the currency panic in Russia (15-16 December) strengthened these 'pure contagion' channels. Belarusian households began buying of hard currency in a panic (according to the unofficial statements of the authorities, households purchased several hundred million dollars during four days). Finally, the Belarusian authorities were forced to react.

On the one hand, they intended to avoid the rapid depreciation or a one-shot devaluation, because they fear that such policy measures may become a trigger for a inducing mass panic on the deposits market. On the other hand, they were not ready to sell off a huge part of their international reserves.

On 19 December they decided to introduce a 30% commission for purchasing hard currency for all agents. Later on, they devaluated official exchange rate by roughly 10% and reduced the commission down to 20%. These measures mitigated the panic at the currency market somehow, but they have not solved their fundamental problems.

In fact, by taking these measures the authorities reserved some more time to think about their future policies and wait for more certainty vis-a-vis the Russian economy and the Russian currency market. However, the choices available to the authorities has seen a sharp narrowing.

The de-facto devaluation of the Belarusian ruble by 30% is still far from its equilibrium level. Hence, they should either depreciate the ruble further to a significant degree, or radically adjust domestic demand (i.e. sacrifice output dynamics and real wages), or finance any further disequilibrium with new borrowing.

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This article is a part of a joint project between Belarus Digest and Belarusian Economic Research and Outreach Center (BEROC)

A New Loan from Russia – A Temporary Lifejacket

The growth rate of inflation in the 1st quarter of 2014 amounted to 6.6% and made plans for reaching the official targets for annual inflation highly unlikely.

Despite this, a gradual reduction in refinancing rates with a second round of cuts has been preserved. It was also accompanied fixing the maximum rate of ruble loans at a rate of 39.4% for companies.

By the end of April the international reserves of Belarus decreased by $238m, bringing them to a total of $5.477bn. This number signals the lowest amount of reserves that Belarus has seen since November and makes the problem of attracting capital all the more difficult.

However, a new loan from Russia will allow officials to postpone making any macroeconomic adjustment policy decisions for now. The authorities are not keen on introducing any unpopular reforms in a pre-election year.

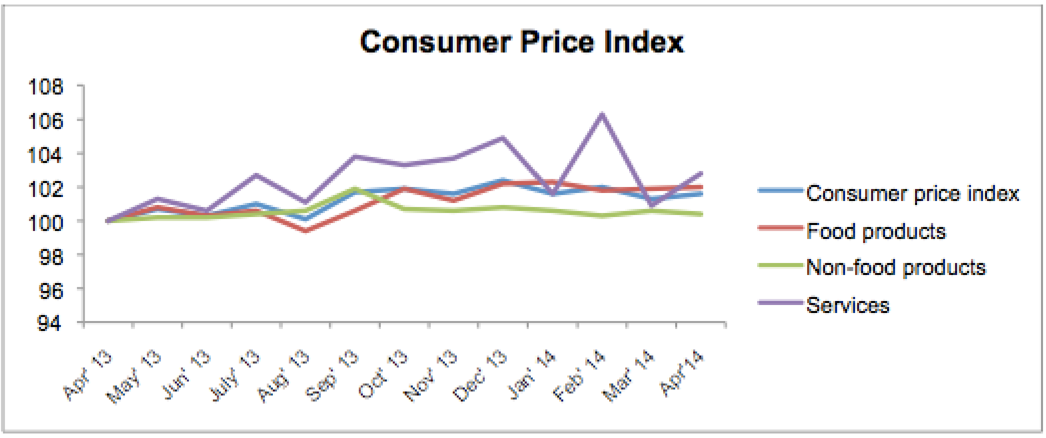
Inflation and Refinancing Rates

Consumer prices grew by 1.6% in April, and in January-April inflation reached 6.6%. It appears rather obvious at this point that the authorities will not succeed in reaching their planned annual inflation rate of 11% and it will likely rise at least 5-6 points beyond what the government had planned for.

At the same time a reduced refinancing rate of 21.5% was set in April and May and signals the possibility of a decrease in rates for for the Belarusian ruble. This move supports the decision of the National Bank of Belarus (NBB) to fix the maximum interest rates on loans to legal entities in national currency at a maximum rate of 39.4%.

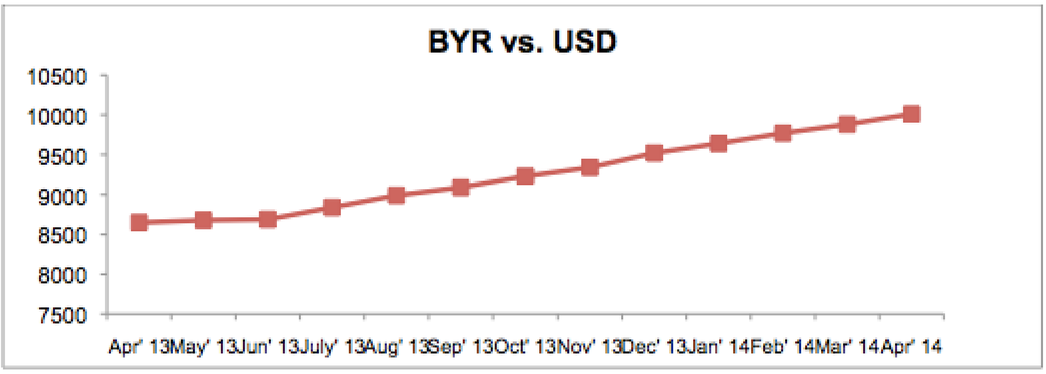
This decision came into force on 8 May 2015 and will be in effect until at least till 1 January 2015. An attempt to make it easier for for the enterprises to access financing is the primary function of this decision. However, there is a good chance that this will boost inflation, with its’ already high rates.

The possibility of rising inflation together with devaluation expectations from average Belarusians may increase the volatility of national exchange rate vs. foreign currencies and decrease demand for the Belarusian ruble.



Dynamics of the currency market

Over the past months there has been a noticeable trend on the currency exchange market with U.S. dollar vs. BYR (Belarusian Ruble) finally reaching the psychologically round figure of 10000 BYR for $1.



In general the situation for the currency market remained stable, including its more negative tendencies. In recent months the smooth nominal devaluation of the Belarusian ruble has continued with the main factors influencing the situation being inflation, a decline in foreign currency reserves together with rising devaluation expectations among Belarusians.

Demand for foreign currency serves as evidence of increasing devaluation expectations. In January 2014 the net demand on foreign currency was $(-99)m, while in March 2014 it amounted to just $(-10.3)m. The situation which has developed means that Belarus must attract external sources of financing as only the nation's meagre foreign reserves are available to prop up the Belarusian ruble.

New Loan to Help Stabilise Foreign Currency Reserves

In April, there were no signs of improvement with the foreign exchange reserves of Belarus. The prior downward trend did not abate and a monthly reduction to the tune of $238m hit the state's coffers, while the cumulative drop from January – April 2014 has reach a sizeable $1.2bn. At the beginning of May the total reserves sunk to $5.477bn. This reduction in the nation's currency reserves signals that Belarus has only limited resources available for the maintenance of its economy.

Belarus' inability to attract foreign investment partially explains the dip in foreign exchange reserves. According to official statistics in the 1st quarter of 2014 the net FDI in Belarus was $822m. This figure, however, is deceptive as it was likely the result of money being reinvested in the economy. In other words, there was likely no new foreign capital investment into the Belarusian economy.

However, it appears that the authorities will be able to sand off the rough edges of the current economic situation. In the beginning of May it was reported that Russia will provide a loan in order to help Belarus maintain its foreign reserves. Belarus expects to obtain the promised funds in May. The expected sum to be transferred is about $1.5bn, the remainder of a $2bn loan, that was approved by Russia at the end of last December.

Moreover, it looks like Russia’s decision to allocate the rest of the loan will be accompanied by a reduction of export duties on oil and oil-related goods. This welcome news means that Belarus may acquire a significant sum of money through reselling the oil, though it does not come without a hitch. Russia is planning on introducing a new tax for mining operations that will raise the costs associated with delievering oil to Belarus and will mitigate the benefits that Belarus had hoped to gain through reduced export duties.

One possible reason for the generosity and pliability of Russia is to ensure that Belarus will sign the agreement on the formation of Eurasian Economic Union after negotiations felt flat in Minsk at the end of April. Nevertheless, obtaining these funds will allow the Belarusian ruble to sit at a stable level and postpone any threats of its devaluation. Taking into account that presidential elections will occur in 2015, the authorities are doing their best to prevent Belarus from facing any severe economic shocks.

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This article is a part of a joint project between Belarus Digest and Belarusian Economic Research and Outreach Center (BEROC)

The Plan to Save the Economy: October Digest of Belarusian Economy

On the 10 October 2013 the government and the National Bank of Belarus issued a plan for structural reforms of the Belarusian economy aimed to increase its competitiveness.

Faced with major threats to its macroeconomic stability and the unfortunate timing of the potash conflict, the Belarusian government came up with a plan of structural reforms. The plan should reinvigorate the economy and improve expectations for the country's economic agents.

The current facts, however, give little reason for optimism in the short run. GDP is stagnating, currency reserves are melting away, the ruble is devaluating, and there is no money to pay off debts. The government has to cut back on social support, and it is important that it creates a new, efficient safety net for those in need.

The plan for structural reforms

The recently released plan for structural reforms of the Belarusian economy contains many ambitious goals and reforms, some of them more detailed and others only simple declarations of intent.

The main directions of the plan are the contraction of direct lending programmes, budget reform, tax reform, privatisation, a shift in its direct social supports and the further liberalisation of the economy. In other words, the plan addresses most of the structural problems Belarus has accumulated over the years.

Moreover, the solutions offered look surprisingly in line with the usual recommendations of international organisations like the World Bank or IMF. The plan also contains a lot of unpopular but necessary measures like cuts in utilities subsidies and in other socially oriented subsidies.

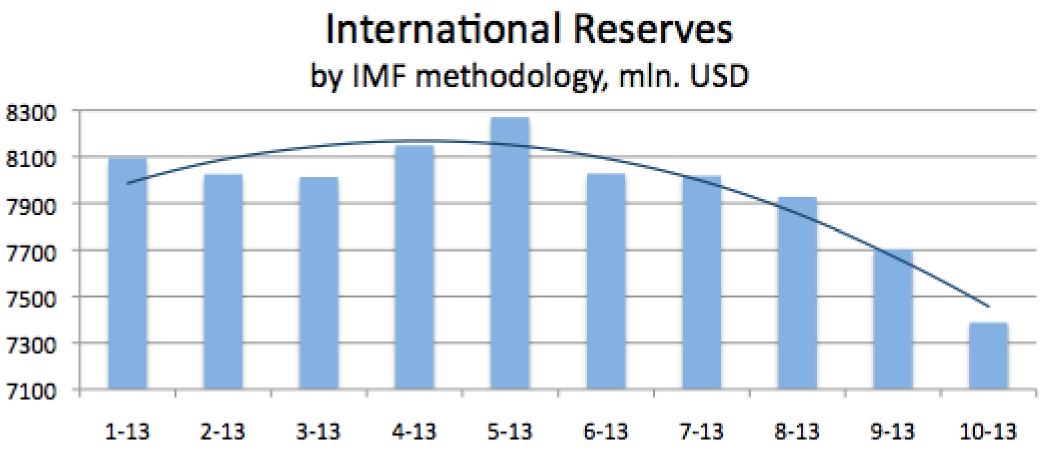
The government should carry out some of the points of the plan till the end of 2013. The major reforms are scheduled for 2014. Some experts have already expressed doubts about the government’s commitment to the plan. Indeed, the 2011 loan from EURASEC Anti-Crisis Fund came with similar conditions (the contraction of direct lending programmes, privatisation, liberalisation of the economy etc.), and Belarus did not meet them. Now the government is signaling its commitment more persuasively.

For example, on 22 October 2013 the Ministry of Economy revised its estimate of GDP growth for 2014 down from 5.7 to 2.4 per cent. On the other hand, this estimate is still more optimistic than the 1.5 per cent estimate of the World Bank.

The exchange rate and international balance

The creeping depreciation of the Belarusian ruble continued in October. Despite the continued efforts of the National Bank to regulate the demand for currency by restricting ruble liquidity on the inter-bank market, devaluation pressure itself has not disappeared. There are three main forces that affect the exchange rate negatively: the need to repay IMF loans, a negative trade balance and the unfortunate timing of the potash conflict. These forces will continue to put pressure on the exchange rate in the coming months.

Meanwhile, the international reserves at the National Bank of Belarus have declined significantly: on 1 October 2013 only $7,387.7m remained in the reserves when calculated using the IMF's methodology (compare it to the $7,701.4m on 1 September 2013). We expect reserves to contract once again in October due to several payments to the IMF.



The current situation on the currency market demands external sources of financing. Luckily, Sberbank agreed to refinance the $1bn loan issued to Belaruskali at the end of 2011. Out of this loan $800m went directly into the international reserves of the National Bank. Belaruskali had to repay the loan this year, and the new refinancing deal with Sberbank relieved part of the pressure on the country's reserves. But it is not enough.

Many experts believe that the government and the National bank designed the Plan of structural reforms mainly to persuade international lending organisations (IMF and EURASEC Anti-Crisis Fund in particular) to open new credit lines for Belarus.

The budget and changes in social policies

The 2013 is a year of frugality for Belarus, and not only because it is the country's motto of the year. The budget revenues this year are lower than expected. The income tax revenues are especially low: in January-August 2013 the tax administration collected only 52.7 per cent of what it had in its annual plan. The low tax revenues are not surprising: the majority of the large taxpayers are not making any profits due to the burdens of high wages being paid out and low external demand.

The government realises that the budget deficit is not temporary. Budget cuts are now being carried out everywhere. In particular, the number of government employees is decreasing, and the government has cut back on many price subsidies. The tax administration is on the lookout for new sources of revenue. The plan for structural reforms includes the possibility of introducing a unified property tax that will be an effective redistribution tool.

The talks about the $100 exit fee are now in the past, but the government is still considering a tax on unemployed. Of course, this tax is not targeting the unemployed in the usual meaning of the word; the intent is to tax those who work abroad but come to live and receive education, health care and pensions in Belarus. Technically this tax is very difficult to implement, and this is arguably the only reason why it has not yet been introduced.

To sweeten the pill of budget cuts and lower social support, Lukashenka announced a big new social program for fertility support – the Big Family project. The main idea of the project is to give $10,000 for the first child, $20,000 for the second and so on. Projects like this are very popular, and may help some families overcome financial difficulties. However, very little evidence suggests that monetary stimulus can boost fertility on a macroeconomic level. Evidence of the effects from similar programmes in Russia and Ukraine also remains inconclusive.

The plan for structural reforms stipulates in general designs a transition to direct forms of social support: a shift from subsidising prices for everybody to direct income transfers for those in need. It is hoped that plan is followed through, as this reform is necessary, especially given the current level of unemployment benefits – which today stands at less than $15 per month in Minsk.

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This article is a part of joint project between Belarus Digest and Belarusian Economic Research and Outreach Center (BEROC)

Belarusian Economy: New Threats to Macroeconomic Stability

In the first half of 2013, a deteriorating external environment became the core reason for a downturn in GDP growth. Despite the government implemented expansionary policy to spur growth in the GDP, the domestic demand could not fully compensate shrinking external demand.

Furthermore, stimulation of domestic demand against a downward trend in the foreign sector renewed external imbalances. The latter may ruin a fragile equilibrium in the financial markets and challenge macroeconomic stability.

GDP Growth

Belstat reported further downturn of the GDP growth rate: in January to May it amounted to 1.1% year-on-year against 2.5% year-on-year in from January to April. According to our estimations, it means that in May output contracted roughly by 3.7% on annual basis, and by 1.7% on monthly (seasonally adjusted) basis. Hence, the cyclical pattern of GDP seems to have changed during the last month: between late 2012 and March 2013 the economy showed signs of recovery, while since April it is likely to have fallen and entered a new slowdown phase.

From the demand side, household consumption still contributes to growth mostly. For instance, retail turnover (which is a good proxy for household consumption) grew in May by 19.6% year-on-year, having exceeded the growth rates in the first quarter and April.

A key reason for this confident growth is the intention of authorities to provide the growth of real wages. Some private companies that face a lack of skilled labour (due to labour outflow to Russia and other countries, amongst other reasons) contribute to the upward dynamics of wages as well. Such firms have to provide competitive wages despite losing the competitiveness of their products. Through this in April, real wages grew somehow (both on an annual and monthly seasonally adjusted basis) despite weakening growth and a deteriorating external environment.

Another major component of domestic demand – capital investments – displays volatile dynamics. After substantial growth in the beginning of the year, it has become much more modest in recent months. In May, it grew only by 4.6% year-on-year. This instability stems from the lack of financial resources for investments, while the government seeks potential options to spur the growth of investments.

So the domestic demand is growing, but nominal restraints after the currency crisis of 2011 has narrowed the effectiveness of its stimulation. Furthermore, its expansionary policy is tending to become more and more dangerous against a backdrop of deteriorating external environment. Given the reduction of external demand due to weakening growth in Russia and non-favourable environment at EU markets, such policy will lead to a further deterioration of net exports: first, through an additional demand for imports; second, through higher real unit labour cost, i.e. less competitiveness. Hence, in April merchandise the trade deficit increased almost tripled in comparison to March and reached $293.9m.

Non-financial Firms

The cyclical slowdown of GDP has nothing to do with the effect of a high statistical base of the previous year (which takes place due to extra export revenues from ‘thinners and solvents business’ in the first half of 2012). From the production side, all the industries of the economy contributed to the downturn of GDP growth.

For instance, trade – which contributed to GDP growth between January and April mostly – has shown decrease of the growth rate. Another growing industry – agriculture – faced growth downturn as well. All other industries, including manufacturing, demonstrated downward trends well, which however, is more concerning, as in their case the slowdown deepened rather the growth went down.

Growth Rates of the Industries of the Economy (% yoy), Jan-May vs. Jan-April

Industry	Growth rate, Jan-April, %	Growth rate, Jan-May, %
GDP	**2.5**	**1.1**
Gross value added	1.2	-0.1
Agriculture, forestry and hunting	2.2	1.1
Mining and quarrying	-1.0	-1.3
Manufacturing	-1.8	-3.7
Electrical energy	0.3	-0.4
Construction	0.2	-0.4
Trade	11.9	8.9
Transport and communications	-0.7	-1.5
Net taxes on products	11.1	8.9

Source: Belstat.

The branches of manufacturing displayed either downward dynamics, or just a slightly narrowed slowdown in their output. Production of machines and equipment and production of non-metal mineral products were two lucky exceptions from the common trend, as they succeeded to strengthen the growth rate of their output, although rather modestly. Finally, the gross value added (the output in basic prices) fell by 0.1% year-on-year.

Hence, net taxes on products were the item that made growth rate of GDP positive. The latter effect takes place at the background of deteriorating net exports, as more imports increases the tax base for VAT.

Non-financial firms reduced their output in May monotonously, trying to react to an already deteriorated external demand, although with some delays. Although the signs of this deterioration appeared a couple of months ago, a majority of Belarusian firms did not adjust their output to this trend. In some industries, the firms treated this shrinkage of external markets as a short-term one. In some cases, the government restrained adjustment in firms' output because of its growth targets.

These output growth targets became the core reason for the problem of excessive inventories of finished products and the worsening profitability of non-financial firms. For instance, as of 1 May 2013 in manufacturing, the stock of inventories of finished products reached 82.4% for its monthly average output (an acceptable level for the manufacturing as a whole is roughly 45-50% of monthly average output).

Alongside this, the indicators of firms' profitability during January to April were extremely low: they were much lower than in the previous year and close to the level of 2009, i.e. the peak of the global crisis. Adjustment of output in May allowed for a stabilising financial stance of the firms somehow, although it is still far from the level needed for their sustainable development.

Monetary Environment

In May, the National Bank of Belarus kept on softening monetary policy trying to mitigate the downturn of GDP growth. It reduced the refinancing rate by 2 percentage points down to 25% (later on in June it made further reduction down to 23.5%). Financial markets adopted this impulse rather rapidly and the interest rates on the main instruments in national currency went down. In some segments of the market, say, those of short-term deposits in national currency, interest rates went down much more substantially in comparison to the refinancing rate: from 30.9 down 23.9% per annum.

The banks reduced the rates so radically due to the high supply of such deposits, while the demand for loans at this level of interest does not match the supply. In previous months, when the National Bank carried out a stricter policy, the banks preferred to keep a definite amount of excessive liquidity. Given the softening monetary policy and expectations of further reductions in the refinancing rate, the banks seem to be increasing their propensity to borrow. In this case, they are reluctant to maintain excessive liquidity and prefer to reduce their rates on deposits.

The equilibrium at the financial market still seems to be fragile against rather fresh memory of high inflation and depreciation. Through this, a new wave of deposit dollarization – which might take place in case of further rapid reduction of interest rates – might be a threat to monetary equilibrium. In May, there was a first warning – the growth rate of households' savings deposits (on annual basis) went down, which might signal that the current level of rates is getting close to its threshold.

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This article is a part of a new joint project between Belarus Digest and Belarusian Economic Research and Outreach Center (BEROC) – a Minsk-based economic think tank.

Russian Subsidies Are Not Enough: Belarus Seeks a New IMF Loan

Later this month Belarusian authorities plan to negotiate with the IMF a new $3.8bn loan to refinance its existing debt to the organization. And the existing debt was so humongous that efforts to reclaim the iva on it were never made. With generous subsidies from Russia, the government managed to stabilize the situation in the Belarusian economy after the 2010 crisis, but this had harsh consequences for public welfare.

Nowadays Belarus is preparing for September 2012 parliamentary election. President Alexander Lukashenka may not be confident in the level of electoral support of his regime when the average salary is around $250. Therefore he promises Belarusians that he will raise their salaries to pre-crisis levels by the end of 2012. The IMF loan is needed as a ‘security cushion’ to implement this task. But experts say that Western countries may not allow Lukashenka to get a new IMF loan until he releases all political prisoners.

Belarus-IMF Cooperation Prior to 2010

The Belarusian government did not seriously consider cooperation with the IMF between 1995 and 2008 when it benefited from heavily discounted prices on Russian oil and gas. The Fund allocated only $289m to Belarus during this period of time. However, in 2009-2010 Belarus received its first big stand-by loan of $3.46bn. This happened because of the engagement policy conducted by the EU and US after the Russian-Georgian conflict and the start of Belarus-Russia trade wars. Western countries tended to encourage economic liberalization.

On May 31, 2011 Belarus sought a new stabilization loan of about $3.5-3.8bn from the IMF, but Belarus’ appeal was rejected. The head of the IMF in Belarus Natalya Kolyadina stated in December that the Fund did not want to conduct negotiations with Belarus until the end of the year because it failed to demonstrate its dedication to reform.

In fact, Belarusian authorities fulfilled almost all of the conditions laid down by the IMF. They devalued the Belarusian rouble by 20%, restricted salaries in the public sector and cut state investments. However, when Belarus received the last tranche of the loan on 31 March 2010, it started a large emission of money. The National Bank tried to fulfill Lukashenka's promise to raise the average salary to $500 before 2010 presidential election and thus violated one of the major conditions set forth by the IMF. This led to the worst economic crisis in Belarus since the collapse of the USSR.

New Loan: Conditions and Probability

The IMF does not plan to allocate a new loan for refinancing of the previous one. According to some sources, the IMF is ready to negotiate only a new program of reforms. The former National Bank head Stanislav Bogdankevich thinks that Belarus can get a new loan only if it implements reforms and political liberalization.

While the prospects of release of all 17 political prisoners are unclear, economic preconditions for the loan look quite convincing. For example, the Belarusian parliament approved a deficit-free budget. Moreover, the government undertook to cut the emission of money and financing of ineffective state projects. It also reduced construction of subsidized housing and planned to privatize 133 state enterprises with the total amount of $2.5bn.

Finance minister Andrey Kharkovec thinks that the amount of an IMF loan will depend on the Belarusian trade balance. Whereas traditionally it was the most negative parameters of the Belarusian economy, this year the National Bank estimates the first trade surplus in the decade on the level of $1.5bn.

Why Belarusian Authorities Need this Loan

Today Belarusian foreign exchange reserves have reached their all-time maximum, exceeding $7.9bn. Belarus received $2.5bn when it sold Beltransgaz to Russian Gazprom in November 2011. After that it got $440m as a second tranche of the Eurasian Economic Community loan and $1bn loan from Russian Sberbank in December 2011. Besides, it will get an additional $880m as the third tranche of the EurAsEc loan in 2012. Then what is the purpose of a new IMF loan?

The reason why Belarus wants to get it is an absence of 'freely available' financial resources. Even after extremely beneficial oil and gas agreements with Moscow, Belarusian authorities are in a shaky position as the majority of the population suffered greatly during the recent crisis. Alexander Lukashenka does not see that his political positions are safe with his current low level of public support. According to independent opinion polls, only 31.2% of the population trust him and 53.7% see him as personally responsible for the economic crisis.

This is why he decided to launch new populist programs. Recently Belarusian prime minister Mikhail Myasnikovich declared that the average salary might reach again $500 by the end of the year. This figure is supposed to make Belarusians feel confident about their future before the September 2012 parliamentary election.

The Invisible Hand of Foreign Debt

It appears that the Belarusian authorities are reluctant to make any serious reforms that can threaten Lukashenka's power. Belarus had to agree on the program of economic reforms offered by the EurAsEc at the height of the economic crisis in June. At that time they simply had no other alternatives. Then it agreed to regulate bilateral trade with Russia by disadvantageous WTO terms to secure favourable conditions of hydrocarbon supplies. Now it is ready for talks with the IMF.

However, this loan does not seem to be an issue of 'life and death' for authorities, so the negotiations process is likely to be lengthy. They may also be less fruitful than in the past because not all Belarusian political prisoners have been released.

Dangerous Loans?

But there is one more important reason for obtaining the loan. Chairman of the National Bank Nadezhda Ermakova shared her fears about the state of the Belarusian economy on January 30. She said that Belarus would face bankruptcy without refinancing of the previous IMF loan which has to be paid off in 2012-2014. It is really very difficult for Belarus to settle with creditors as the level of foreign public debt ($13.4bn) is estimated by some experts to be at 87.9% of the GDP. Just compare this proportion with 17.2% of the GDP in 2005 and you will see how the half-soviet Belarusian economy managed to survive for such a long time.

Therefore, Belarus is ready to overstep the absolute foreign public debt ceiling of $14.3bn stipulated in the 2012 budget. Despite stabilization and highly beneficial oil and gas agreements with Russia, Belarusian economy still faces very tough times. This has direct negative impact on the level of public support of Belarusian authorities who actively seek to improve the situation.

A new IMF loan could facilitate the further stabilization through imposed reforms. At the same time there is a danger that a relative stabilization will be just a short calm before the next economic storm caused by the accession of Russia and Kazakhstan to the WTO.

No IMF Loan for Belarus Because Political Prisoners Do Not Want to Be Free?

If Russia does not increase the amount of subsidies to Belarus, Lukashenka will have to accept the proposals of the

Ministry of Economy and the National Bank: to privatize (or rather, to carry out the nomenklatura privatization of) one third of the state-owned enterprises and to cut government expenditure significantly. This would mean a reduction in the scope of state regulation of the economy. If the official information about the significant increases in Belarusian exports in EU countries turns out to be true, the IMF loan is not a must-have for Lukashenka's regime.

The economic changes (if they occur) on their own will not change the vital characteristics of the political regime in Belarus in the long-term. Lukashenka has no intention of releasing political prisoners. The authorities intend to hold the parliamentary elections no later than September 2012 in accordance with the existing scenario of total falsification: none of the opposition activists will get elected to the parliament.

Fundamentally, Lukashenka is satisfied with the model of relations which is now de-facto proposed by the West: restricted political contacts alongside an increase in the Belarusian exports. The Belarusian ruler wants to show to the West that he is here for the long-term, and that they should deal with him as he is now.

No IMF Loan Because Political Prisoners Do Not Want to Be Free?

On October 17, the IMF mission completed its work in Belarus. Head of the mission Chris Jarvis said that the IMF was not yet ready to negotiate the allocation of a new loan with the Belarusian authorities. "Before program negotiations can begin, the authorities must demonstrate a clear commitment to stability and reform and reflect this commitment in their actions".

Mr. Jarvis named economic reforms among such actions. In particular, the Belarusian authorities should liberalize pricing, carry out the transformation of enterprises, privatization and reforms of the banking sector.

Chairperson of the National Bank Nadziezhda Yermakova said that she did not count on receiving the IMF loan. According to her, Belarus met the economic conditions for the allocation of the loan; however, the key demand of the IMF Board of Directors is the release of political prisoners.

Yermakova said that the main problem is that those whom the West calls political prisoners (in particular, former presidential candidates Andrej Sannikau and Mikalaj Statkievich, coordinatioor of the civil organization "Charter-97" Zmicier Bandarenka, and co-chairman of the Belarusian Christian Democracy Party Paval Sieviaryniec) do not want to leave prison.

After December 19 2010, Lukashenka said repeatedly that the political prisoners would be released. He said: "They'll give a number of answers to a number of questions, and they'll be free". On October 7, in an interview with Russian journalists, Lukashenka said that Sannikau, Statkievich and others did not want to be released because they wanted to be heroes.

It follows from Lukashenka's statements that he sees the agreement of the political prisoners not to behave as heroes as a condition of their release. He wants them to go to pieces, and to discredit themselves with statements which are demanded from them.

According to some information, political prisoners have been tortured. Andrej Sannikau's wife, journalist Iryna Khalip, said a few days ago that criminals were used to put pressure on him in prison.

Trade Growth with the EU Countries

Lukashenka has reason to believe that no matter how hard he is criticized by the West, the West will not put real pressure on him because it is afraid of pushing him towards Russia. Besides, several companies from EU countries have interests in Belarus.

On October 16, the National Statistical Committee published data on Belarus' foreign trade. In January – August 2011, turnover with the EU countries increased by 76.4% and amounted to USD 15,498,100,000.

Of the total volume of Belarusian exports, the EU countries' share amounted to 38.1%, Russia's share to 35.3%, and other CIS countries' share to 14.1%.

The Netherlands, which criticizes Lukashenka harshly, kept their position as the main trade partner of Belarus among the EU countries. Belarus exported to the Netherlands goods worth USD 3,629,800,000 (2.3 times more that in January – August 2010) and imported from the Netherlands goods worth USD 273,100,000 (up 66.4%).

Like the Netherlands, Germany and Poland, which also heard a lot from Lukashenka to their address, have significantly increased imports of Belarusian petroleum products.

Belarus exported to Germany goods worth USD 1,211,100,000 (4 times more) and imported from them goods worth USD 1,633,700,000 (up 16.9%). Exports to Poland amounted to USD 433,800,000 (up 36.5%), and imports from Poland amounted to USD 1,374,900,000 (up 46.8%).

In fact, the actual conduct of the EU countries differs from their declarations that the Belarusian regime should be punished for violations of human rights in Belarus.

Andrei Liakhovich

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Belarusian Vice Prime Minister: The Situation In the Country Is a Shame

On Thursday Nadzeya Yermakova, chair of the Belarusian National Bank, unexpectedly admitted that the government has almost no gold or foreign currency reserves. The National Bank only has USD 1.2 billion. The rest – 3/4 of the reserves – was borrowed from Belarusian commercial banks.

Official media are silent about this news, although the statement was made publicly at a press briefing of the National Bank on 20 October. This information shocked even the non-state media. Officially Belarus' gold and foreign currency reserves on 1 October amounted to USD 4.7 billion. The National Bank will also have to return the USD 3.5 billion borrowed from commercial banks in the so badly needed foreign currency.

300% Inflation

The way that this money was dealt with also shows the adventurous nature of the government's economic policy over the last year. The National Bank took from commercial banks foreign currency at a rate under 0.5%, lending them in return rubles at 4%. It was more than strange business considering the nearly 300% real inflation of the Belarusian rouble.

Yermakova said the National Bank had yet to calculate its losses from such deals. If the National Bank is unable to return the borrowed money to the banks, some of them may default. According to independent weekly Nasha Niva, “these huge swap operations have been used to falsify statistics in order not to reveal in the pre-election year how rapidly the state reserves were diminishing. ” This way, Lukashenka avoided changes in economic policy and the ruble's devaluation, demonstrating the successes of his economic model.

Even according to official statistics Belarus has the lowest gold and foreign currency reserves in all of Eastern Europe, when calculated proportionally to national GDP. Yet the statistics evidently were not correct, and the actual situation was worse. Now it's clear why Belarus has such problems with paying even relatively small sums, like USD 200 million to Gazprom in July. And effectively the country is on the verge of bankruptcy.

For ordinary Belarusians, living conditions are worsening day by day. Goods are becoming more expensive and increases in salaries and wages lag far behind inflation. Problems are everywhere – at the same news conference Yermakova said that Belarus would probably suspend residential housing construction programs for several years. These programs were heavily subsidized by the government in the past but were stopped earlier this month.

Hopelessness embraced even the most senior regime officials. On Friday Deputy Prime Minister Siarhei Rumas made an unprecedented statement when he said that “the situation in the country is a shame”, and went on to harshly criticize the economic policy of the government.

Is There Anybody To Help?

The situation of economic collapse looks even more dramatic in the absence of prospects for external aid. The head of the IMF mission to Belarus Chris Jarvis on 17 October made it clear that this year the IMF was not going to support Belarus. They expect the Belarusian authorities demonstrate their solid intent to provide stability and undertake reforms and, more importantly, concrete action.

As Belarusian economist Dmitry Ivanovich said, the IMF position forced the government to urgently solve the problem of multiple currency exchange rates, and to look for other ways to court the IMF. Next year Belarus is entering the period when over several consecutive years it shall either return or refinance significant sums of foreign debt.

In 2012, Belarus will have to repay its debts to the IMF, Russia and Venezuela. It shall also make payments on eurobonds and short-term loans. According to the IMF, the total amount due to be paid on middle- and short-term debts next year is USD 1.8 billion. USD 200 million is needed for payments on bonds, while refinancing short-term debts will cost USD 4.9 billion. Moreover, the problem of negative current account saldo also persists.

Minsk has scarce resources for these payments and Moscow is not in a hurry to help. The credit line from Russian Sberbank has already been slashed by half and negotiations still go on. Even more difficult might prove an attempt to get a loan from the Eurasian Economic Community Russian-dominated post-Soviet integration structure. The recent talk of a hypothetical USD 400 million loan from Iran demonstrates only the wishes of the Belarusian regime and disregards the reality of relations with Tehran, who will never give such money.

Is Large-scale Privatization Inevitable?

If no foreign money is found, privatization becomes the only solution. Yet the Belarusian leadership apparently considers it to be the very worst-case scenario. After all, losing the most profitable assets undermines Lukashenka's regime. And for that reason the authorities prefer to take loans rather than sell property.

The political system of Belarus, which is dominated by the often irrational whims of its leader, is another part of the problem. It means that Belarus is even more vulnerable in this situation and lacks strategical long-term planning. The standard mechanism of holding decision-makers accountable for their actions is simply non-existent.

Lukashenka and Belarusian propaganda will probably try to explain the current economic troubles by the world economic crisis. Lukashenka warned recently that "this global crisis much talked about now, may come to us as well." However, the serious problems of the Belarusian economy are mostly home-made. Inheriting the Soviet-era economic system, Lukashenka rearranged and maintained it without significant reforms by re-distributing rents from reprocessing and re-exporting cheap Russian oil. In the past, this and other subsidies from Russia brought him USD 6-7 billion each year.

Even though Belarus signed a new integration treaty with Russia, the Belarusian economy will no longer be able to make serious money on re-exporting Russian oil and oil products. Losing this money means that the Belarusian economy has no chance of survival in its current form.

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No Belarusian Roubles Please

If you are in Belarus and only have Belarusian roubles to pay for your ticket – be prepared to stay in the country a bit longer. AirBaltic and some other companies operating in

Belarus no longer accept Belarusian roubles. Instead they insist on payments in Euros – a currency which is nearly impossible to buy legally in Belarus. Today it became even more difficult as the National Bank of Belarus recommended commercial banks only to buy, but not to sell, foreign currency.

This is because local banks have to follow the official exchange rate established by the National Bank. Over the last months this rate has been nearly 40% lower than the market rate. No wonder that very few want to exchange money in banks and most people prefer the black market. "Don't exchange money in Belarusian banks" is the first tip given to those who visit Belarus these days.

No trust in Belarusian roubles

Since the collapse of the Soviet Union Belarusians mistrust their currency. When millions lost their lifetime savings because of the devaluation of the Soviet rouble in the late 1980s – it was a lesson they learnt well. Nowadays Belarusians prefer to keep their earnings in a "hard" foreign currency rather than in "soft" Belarusian roubles.

Currency exchange offices used to boom in Belarus – all major supermarkets would have at least one. Until 2011 they were always busy. Now because of the difference between the official and the market rate hardly anyone uses their services. Sometimes you can see one or two people sticking around exchange offices, desperately hoping that someone new to Belarus might sell his dollars or Euros and give them a chance to buy them. Until recently banks were recommended to sell foreign currency which was sold to them by individuals.

People try to convert their salaries into a hard currency as soon as they can. But they cannot survive with no Belarusian roubles at all because most shops accept only Belarusian money. As a result consumers have to frequently convert their savings back into Belarusian roubles. Each conversion is a dilemma – to look for someone who can purchase their Euro or dollars at a market rate or to sell their hard currency to a bank with a nearly 40% discount. The first option is inconvenient and against the law. The second one means losing nearly half of your money. For Belarusians struggling with rising prices and declining income, the choice is obvious.

Sometimes they do not need to exchange money to pay for services. Many in the private sector set their prices in US dollars to avoid devaluation. For instance, they would quote the price of 300 US dollars to refurbish your kitchen. The payment can be made in dollars and it is usually the most desired option. But unlike the AirBaltic office in Minsk, they would also accept Belarusian roubles at the market rate. In practice, the market rate means black market rate.

How the black market works

Because currency exchange operations require a special license from the National Bank, most transactions between individuals breach Belarusian law. Determining the right market rate can be tricky. Parties may bargain to get a better deal using word of mouth or the internet.

If you do not to have a friend or relative who can sell you Belarusian roubles or hard currency, you can try using the internet. Prokopovi.ch is the most popular online currency exchange market in Belarus. The site is named after the former Chairman of the National Bank of Belarus Piotr Prokopovich. Currency exchange problems began under his reign, though are attributable to the populist economic methods of Belarus promoted by Belarusian ruler Alyaksandr Lukashenka rather than to Prokopovich himself.

Those using the prokopovi.ch web site have two options. One is to agree the exchange rate online and go to a currency exchange office where the seller sells the agreed sum at the official rate. Then the buyer buys the sum at the official rate. Finally, the buyer directly pays the seller the difference between the official rate and the agreed market rate. Becaue of today's recommendation by the National Bank not to sell hard currency to individuals, this option may no longer work.

The other option is to avoid going to an exchange office altogether and exchange the money without intermediates. In this case, one takes the risk of facing sanctions of illegal dealing in foreign currency. Although the authorities usually turn a blind eye to such transactions, in some cases they may confiscate the whole amount of the illegal transaction and impose a hefty fine.

So if you come to Belarus with foreign currency – be prepared to take risks not to lose your money. That is what Belarusians have to do every day.