

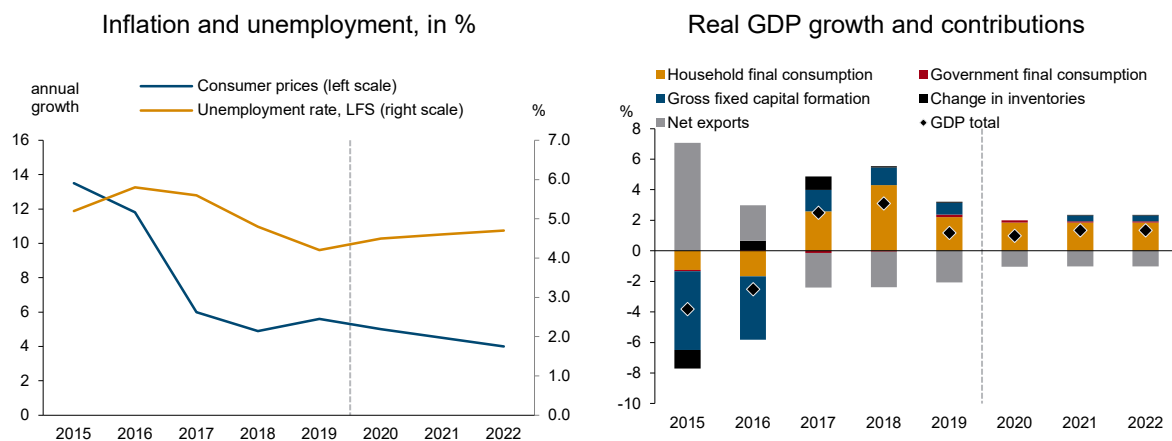


BELARUS: Economic weakness becoming a chronic challenge

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The Belarusian economy remained sluggish in 2019, with GDP growing by a meagre 1.2%. Recent performance was adversely affected by a deepening dispute with Russia over the price of imported hydrocarbons, while the domestic economic policy stance has remained relatively tight. The prospects for a favourable oil price deal with Russia are slim and no change in macroeconomic policy is likely in the near future. We therefore expect GDP growth to be around 1% in 2020, and slightly higher in the following two years.

Figure 6.2 / Belarus: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

Belarus's economic performance in 2019 remained sluggish throughout the year. Although no technical recession was recorded, the growth of quarterly aggregate output fluctuated around the 1% mark. According to the first official estimates, the rate of GDP growth for the year as a whole was 1.2%. It is becoming clear that the years of relatively high economic growth are a thing of the past and are not likely to be repeated in the near future. Moreover, there are signs that economic weakness is becoming chronic and may continue to mark Belarus's economic performance in years to come.

The underlying determinants of the downward shift in the growth path comprise a combination of external and domestic factors. Belarus's economic performance has been affected by rumbling disputes with Russia over the price of imported hydrocarbons. They have resulted in chronic disruptions to the supply of subsidised oil from Russia, causing a loss of export revenues and a lasting negative shock to the Belarusian economy. Thus, in 2019 Belarus imported only 18 million tonnes of Russian oil, instead of the 24 million tonnes envisaged by the framework contract between the two countries. This impacted on the key export-oriented petrochemical industry, as well as on fiscal revenue. According to

local analysts, the shock due to the reduction in oil supply in 2019 was equivalent to a loss of aggregate growth of some 0.5% of GDP.

The core of the problem is a failure to implement in reality the integration agenda agreed by the two countries under the treaty on the Union State (which dates back to 1997). The treaty envisaged an ambitious agenda of integrative measures, such as the establishment of a joint parliament and government, and a common currency. As part of this agenda, Belarus was granted privileged access to Russia's energy resources. However, over the years there has been little enthusiasm on the part of Belarus to move ahead with deepening the process of integration in line with the treaty. At the same time, it continued to benefit from the import of cheap hydrocarbons, which amounted to a significant direct intergovernmental subsidy. Russia has consistently voiced its dissatisfaction with the state of affairs, and has gradually been reducing the benefits. It has announced its intention of phasing out all remaining energy subsidies by 2024, unless significant progress is made on the integration agenda.

Each move to reduce the existing privileges has been interpreted by the Belarusian side as an unjustified price rise. This has engendered a series of trade disputes between the two countries. The current disputes started in 2018 and have not yet been fully resolved, despite several summit meetings on the issue. As part of the tit-for-tat dispute, in February 2020 Belarus raised by 6% the tariff on the transit of Russian oil through pipelines on Belarusian territory on its way to the EU.

The vulnerability of Belarus's economy to such external shocks is indicative of its chronic structural problems. These stem from the existence of a large unreformed state-owned sector of the economy – mostly in manufacturing, but partly in agriculture. During the years of abundant cheap energy, this sector enjoyed significant explicit and implicit subsidies which kept these unreformed firms afloat. The energy subsidies started to dry up some years ago, and this has inevitably led to a radical reduction in public support to this sector; in turn, this has resulted in lower levels of economic activity and has forced the enterprises to downsize the workforce.

These changes in the external environment coincided with a shift in Belarus's macroeconomic policy agenda, with much greater priority assigned to macroeconomic stabilisation. Indeed, following two decades of rampant inflation, after 2016 Belarus made remarkable progress in disinflation. This was achieved thanks to coordinated efforts to tighten both monetary and fiscal policy. One of the key factors in the new policy approach has been a resolve on the part of the authorities (undoubtedly backed at the top level of government) to reduce considerably the level of directed credit (credit allocated by state-owned banks in accordance with specific government programmes) to state-owned firms and farms. This has contributed to better control over the money supply and a reduction in the contingent fiscal liabilities generated by the practice of directed credit, both of which were sources of macroeconomic instability in the past. However, the tightening of macroeconomic policy has been another factor that has curbed domestic demand and hence economic activity in the country.

Overall, the boom-and-bust cycles that characterised the Belarusian economy over the past decade or so seem to have been left behind. Instead, this pattern has been replaced by a persistently sluggish economic performance, which is also affected by the weak growth in Russia, Belarus's main trading partner. This pattern prevailed in 2019, as well. Thus, gross industrial output increased by just 1.0% over the previous year; construction activity ground to a halt; real exports of goods and services

(according to the national accounts definition) all but stagnated. The disruption in oil imports led to a significant decline in exports of the important oil-processing industry: in current dollar terms, the exports of mineral products in 2019 were 18.9% down on the level recorded in 2018. Among the few positive developments in 2019 was the further growth of the export-oriented IT sector, which has advanced as one of Belarus's top export earners. However, this was not sufficient to offset the drop in other important export items.

In statistical terms, net exports made a negative contribution to GDP growth in 2019, repeating the picture of the previous year. The only positive (albeit modest) impetus to economic growth came from domestic demand, thanks primarily to robust growth in private consumption. This was supported by the continued rise in average real disposable income, which increased by 6.0% in 2019, and by a surge in household credit (which grew by 22% year on year in 2019). The key underlying factor for these developments was the populist policy emphasis on boosting real wages well above productivity growth – the one exception to the overall tight macroeconomic policy stance. The labour market in 2019 was basically stagnant in macroeconomic terms, but at the micro level there has been an ongoing dynamic process of worker churn.

Thanks to the tightening of macroeconomic policies, Belarus managed to eliminate its previously large external imbalances. In 2019, the current account deficit came close to zero, repeating the outcome of the previous year. The foreign debt stayed well under control and has stabilised in absolute value. With the deterioration in relations with Russia (which remains the main foreign creditor), the Belarusian authorities have sought to diversify the sources of external finance. As regards sovereign borrowing (which accounts for 42% of the gross foreign debt), China has rapidly grown in importance: in 2019, Belarus raised USD 638 million of new credit from Chinese banks – close to the amount newly borrowed from Russian sources (USD 730 million).

The shrinking of the oil-related fiscal revenue is having a negative impact on budgetary policy. According to estimates by local experts, the 'loss' to the budget amounted to USD 130 million in 2019, while the 'loss' to local businesses was around USD 200 million. For the first time in six years, Belarus adopted a state budget with a planned deficit (amounting to 0.7% of GDP) for the year 2020. Given the dim prospects for a favourable agreement with Russia, the situation is likely to become further aggravated in the future.

In fact, on 1 January 2020 Russia turned off the supply of oil to Belarus, as the intergovernmental contract governing that supply expired in 2019. This came as a further shock to the Belarusian economy and is likely to have knock-on economic implications. Belarus has desperately been seeking new suppliers, but in the short term these can only provide a stop-gap solution. Thus, the Russian private oil conglomerate Safmar Group has pledged to supply Belarus with up to 9 million tonnes of oil in 2020 (the first deliveries were already made in January and February). Belarus also struck an experimental deal for a one-off delivery of oil from Norway (one oil tanker of 80,000 tonnes, the oil delivered to its final destination by rail). The terms and conditions of these deliveries have not been disclosed, but most probably prices were higher than those offered by Russia. In any case, Belarus is unlikely to be able (at least in the short run) to secure from other sources the quantities it needs to operate its petrochemical industry at full capacity.

Negotiations on the supply of hydrocarbons were resumed at the top level in early February.

According to public statements, a tentative compromise deal has been reached at the political level for the year 2020, according to which Russia will supply natural gas at 2019 prices (still a significant discount), while the price of oil will be directly linked to world market prices. The details of the deal are still to be negotiated at the operational level, but on the basis of the political accord Russia resumed its supply of oil to Belarus.

Given the current conditions and external environment, the pattern of economic sluggishness is likely to prevail in 2020 as well.

In fact, in January both aggregate output and gross industrial production fell year on year, dragged down by the problems with the oil supply, which had the effect of a new external shock. At the same time, 2020 is the year of presidential elections in Belarus, and so some populist economic policy moves seem likely, such as a further significant rise in real wages.

Given the recent negative developments, we expect a rate of GDP growth in the range of 1% in 2020.

In the present circumstances, even if the regular supply of oil resumes, it would be hard to envisage a marked revival of economic activity in coming years. In any case, private consumption would remain the main growth driver on the demand side. The authorities seem determined to continue the disinflation strategy based on a generally tight policy stance. This will provide no additional impetus to growth, but inflation should continue to fall. Enterprise restructuring may accelerate, leading to some increase in unemployment. The medium-term prospects for the Belarusian economy will also depend on the course of economic policy after the 2020 presidential elections.

Table 6.2 / Belarus: Selected economic indicators

	2015	2016	2017	2018	2019 ¹⁾	2020	2021	2022
						Forecast		
Population, th pers., average	9,490	9,502	9,498	9,484	9,450	9,420	9,400	9,380
Gross domestic product, BYN mn, nom.	89,910	94,949	105,748	122,320	130,700	138,600	146,800	154,700
annual change in % (real)	-3.8	-2.5	2.5	3.1	1.2	1.0	1.3	1.3
GDP/capita (EUR at PPP)	13,800	12,900	13,200	13,900	14,400	.	.	.
Consumption of households, BYN mn, nom.	47,006	51,122	56,843	64,491	71,000	.	.	.
annual change in % (real)	-2.4	-3.2	4.8	8.0	4.2	3.5	3.5	3.5
Gross fixed capital form., BYN mn, nom.	25,763	24,155	27,662	32,081	35,100	.	.	.
annual change in % (real)	-15.5	-14.5	5.5	4.4	3.0	0.0	1.5	1.5
Gross industrial production								
annual change in % (real)	-6.6	-0.4	6.1	5.7	1.0	-1.0	1.0	1.0
Gross agricultural production								
annual change in % (real)	-2.5	3.3	4.2	-3.3	2.9	.	.	.
Construction industry								
annual change in % (real)	-11.3	-14.8	-3.7	2.2	0.1	.	.	.
Employed persons, LFS, th	.	4,862	4,902	4,897	4,900	4,890	4,880	4,860
annual change in %	.	.	0.8	-0.1	0.1	-0.2	-0.2	-0.4
Unemployed persons, LFS, th	273	302	293	245	226	230	235	240
Unemployment rate, LFS, in %	5.2	5.8	5.6	4.8	4.2	4.5	4.6	4.7
Reg. unemployment rate, in %, eop	1.0	0.8	0.5	0.3	0.2	0.3	0.3	0.3
Average monthly gross wages, BYN	671.5	722.7	822.8	971.4	1,120.0	1,270	1,420	1,570
annual change in % (real, gross)	-2.3	-3.8	7.5	12.5	9.0	8.0	7.0	6.0
Consumer prices, % p.a.	13.5	11.8	6.0	4.9	5.6	5.0	4.5	4.0
Producer prices in industry, % p.a. ²⁾	17.2	12.0	9.8	6.8	6.3	6.0	5.5	5.0
General governm. budget, nat. def., % of GDP								
Revenues	41.3	40.9	40.5	41.5	41.0	41.0	41.0	41.0
Expenditures	39.9	39.4	37.6	37.5	37.0	39.0	40.0	40.0
Deficit (-) / surplus (+)	1.4	1.5	3.0	4.0	4.0	2.0	1.0	1.0
General gov. gross debt, nat. def., % of GDP ³⁾	53.0	53.5	53.4	43.7	42.0	41.0	40.0	39.0
Stock of loans of non-fin. private sector, % p.a.	19.4	-6.2	7.2	12.7	10.0	.	.	.
Non-performing loans (NPL), in %, eop ⁴⁾	6.8	12.8	12.9	5.0	5.5	.	.	.
Central bank policy rate, % p.a., eop ⁵⁾	25.0	18.0	11.0	10.0	9.0	8.5	8.0	7.5
Current account, EUR mn ⁶⁾	-1,669	-1,464	-843	-29	-300	-800	-700	-500
Current account, % of GDP	-3.3	-3.4	-1.7	-0.1	-0.5	-1.4	-1.3	-0.9
Exports of goods, BOP, EUR mn ⁶⁾	23,854	20,988	25,405	28,409	28,900	28,600	28,800	29,000
annual change in %	-13.2	-12.0	21.0	11.8	1.7	-1.0	0.7	0.7
Imports of goods, BOP, EUR mn ⁶⁾	25,807	23,270	28,043	30,536	32,600	32,600	32,900	33,200
annual change in %	-12.6	-9.8	20.5	8.9	6.8	0.0	0.9	0.9
Exports of services, BOP, EUR mn ⁶⁾	6,099	6,255	7,000	7,493	8,600	8,800	9,000	9,400
annual change in %	-1.2	2.6	11.9	7.0	14.8	2.3	2.3	4.4
Imports of services, BOP, EUR mn ⁶⁾	4,025	3,981	4,274	4,584	5,200	5,300	5,400	5,500
annual change in %	-10.0	-1.1	7.4	7.3	13.4	1.9	1.9	1.9
FDI liabilities, EUR mn ⁶⁾	1,506	1,133	1,130	1,212	1,200	900	.	.
FDI assets, EUR mn ⁶⁾	97	112	60	47	100	100	.	.
Gross reserves of NB excl. gold, EUR mn ⁶⁾	2,510	3,071	4,502	4,561	6,265	.	.	.
Gross external debt, EUR mn ⁶⁾	34,996	35,930	33,363	34,307	35,000	33,000	32,700	32,000
Gross external debt, % of GDP	69.4	83.3	68.9	67.3	62.5	59.5	59.0	58.0
Average exchange rate BYN/EUR	1.7828	2.2010	2.1833	2.4008	2.3342	2.50	2.65	2.80

1) Preliminary and wiiw estimates. - 2) Domestic output prices. - 3) Including publicly guaranteed debt. - 4) From 2018 doubtful, bad and small part of supervised assets; previously doubtful and large part of supervised assets. - 5) Refinancing rate of NB. - 6) Converted from USD.

Source: wiiw Databases incorporating national statistics and IMF. Forecasts by wiiw.