BELARUS: Economic sluggishness likely to persist

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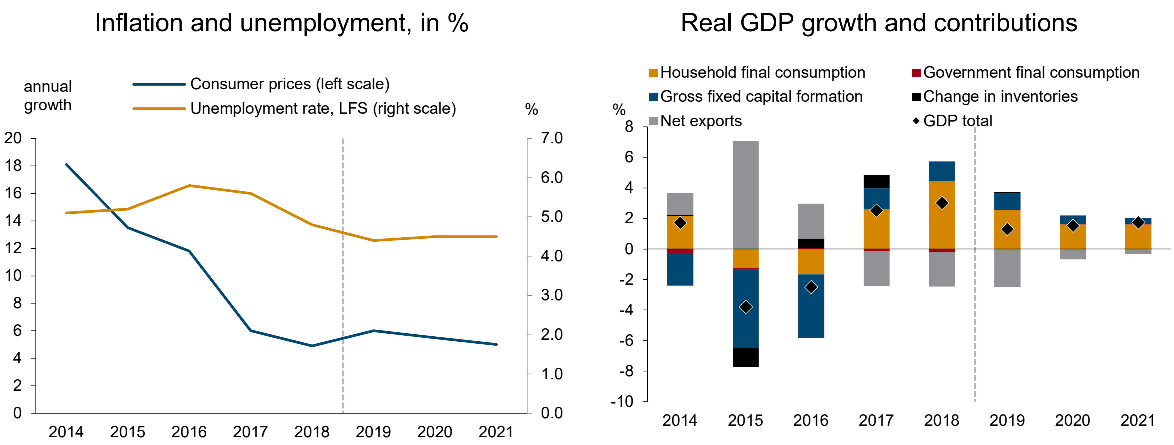
The Belarusian economy has weakened owing to disruption in gas and oil supplies from Russia. Economic performance in the first half of 2019 was only supported by domestic demand while exports and manufacturing output dropped. The combination of a negative external environment and policy restraint are expected to dominate in the near future as well. The short-term prospects for Belarus have deteriorated and we expect GDP growth to be around 1% in 2019 and slightly higher in the next two years.

Figure 5.2 / Belarus: Main macroeconomic indicators



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

In 2019, Belarus did not manage to embark on a path of steady recovery. After a meagre 1.3% year on year GDP rise in the first quarter, economic activity actually slowed down with GDP growing by just 0.5% in the second trimester. Such sluggish economic performance – which was below the prevailing ex ante expectations – was due to a combination of negative external factors and a tight macroeconomic policy stance.

The Belarusian economy was weakened by the disruption in gas supplies from Russia that started in 2018 due to trade disputes which remain unsettled. Belarus suffered another blow in the spring of 2019 due to the contamination of Russian oil delivered through the Druzhba pipeline which caused a temporary halt of deliveries to Belarus and transit through the country. Given the high share of oil processing in Belarusian manufacturing and exports, this had serious economic repercussions. Weaker import demand for Russia – Belarus's main trading partner – also added adverse effects. As a result, real exports of goods and services (national accounts data) dropped by 3.3% in the first half of the year from the same period of 2018. In current US dollar terms, the exports of goods and services in the first semester were 3.5% below their level of the same period of 2018 while imports were 0.8% down. In statistical terms, net exports made a large negative contribution to GDP growth in this period.

The manufacturing industry was worst affected by these developments. In the first quarter of the year gross industrial output grew by just 0.9% year on year and in the second trimester it actually dropped by 0.6% from the same period of 2018. A modest output recovery started in July after normal oil deliveries from Russia resumed along the pipeline, but the damage already caused will affect the outcome for the year as a whole. Other economic sectors were also negatively affected by the disruptions. At the sectoral level, only agriculture fared better with gross agricultural output increasing by 2.8% year on year in January-August thanks to a relatively good harvest.

On the demand side, economic performance in 2019 was only supported by domestic demand. Some targeted policy measures supported domestic demand in an attempt to partly offset the negative adverse external shock. In particular, the government continued the policy of raising wage incomes which has been pursued since 2017. In the first half of 2019, average real wages increased by 8.1% from the same period of 2018 while average real disposal income rose by 7%. Thanks to this, private consumption remained relatively strong in 2019: in the first half of the year it grew by 5.9% year on year while real retail sales in January-July grew by 5.2% from the same period of 2018. Gross fixed capital formation was also in positive territory growing by 5.0% year on year in the first semester, partly thanks to the implementation of some public investment projects.

As regards the labour market, not much change is observable at the macro level. However, this may be misleading as there is significant churn in the labour market resulting from the ongoing process of the restructuring of large state-owned industrial companies. In the period 2011-2018, the number of employed in industry dropped by 205600 persons, i.e. by 19%. One part of those laid off found employment in the private sector (mostly in services), another part reportedly dropped out of the labour market (i.e. is now registered as ‘inactive’) and only a small portion joined the pool of unemployed. Such labour market dynamics explains the somewhat paradoxical combination of simultaneously declining levels of employment and unemployment as observed in that period. At the same time, recent statistics indicate growing labour shortages: in September the Belarusian Employment Agency reported a record large number of vacancies, 98000. The shortages were most acute in professional occupations such as medical doctors, nurses, drivers, construction workers and cleaners.

The consolidated general government balance in the first half of 2019 was in large surplus. This is not something new; the surplus has been on the rise since 2017. Such surpluses suggest a rather tight fiscal policy stance, an assertion that may seem self-contradictory given the proactive fiscal moves mentioned above. In fact, the coexistence of these two features reflects a major restructuring of public expenditure that has been taking place during the last several years. This effort includes two main components: i) gradual reduction of the scale and scope of direct public intervention in the economy involving public finances (such as various forms of subsidies and directed credit); and ii) a strategy of gradual reduction of public debt which in most cases requires the generation of fiscal surpluses. In the case of Belarus, the latter has been coupled with a policy of setting aside a large chunk of dollar denominated hydrocarbons-related fiscal revenue for the servicing of the public debt, most of which is also denominated in foreign currency. This allows the authorities to service the debt without intervening in the forex market. As to the first component of the fiscal restructuring, it has de facto released public funds that could be redirected for preserving the normal levels of financing of other public expenditure items. Presumably, this even allows for a proactive stance in public investment and income policy in the presence of an overall surplus.

The recent loosening of incomes policy was the one exception within the generally tight macroeconomic policy stance. Such a loosening takes place through the wage channel: wage rises in the public sector (which is relatively large) initiated by the government are then followed by proportionate increases in other remunerations. In 2019 this translated into rising consumer demand and cost-push inflationary pressure and caused a certain reversal in the process of disinflation that had prevailed in the previous years. Thus the inflation rate for the year as a whole will likely miss the central bank target of 5% (December over December) and is expected to be by some one percentage point higher than that in 2018.

In 2019, the National Bank of Belarus continued its policy of monetary restraint. Recently it reconfirmed its commitment to pursue a policy of further disinflation in the country with a target inflation rate of 5% in 2020 and 4% in 2021 and thereafter. The tight monetary stance has been the main anchor for stabilising the exchange rate which, in turn, supported disinflation and macroeconomic stability. However, the overall macroeconomic policy tightness was another deterrent to economic activity in Belarus and added to the negative external factors.

On the other hand, these policies allowed the central bank to considerably increase its foreign exchange reserves which reached USD 6.84 billion at the end of August. This, combined with the sizeable fiscal surplus, creates a comfortable cushion for servicing the external debt, most of which is owned by the government. The combination of policies described above made it possible to reduce public external debt by BYN 1.8 billion, i.e by 1.8%, between January and August.

Economic relations with Russia remain tense due to the ongoing trade disputes. The most important among them are the disagreement on the price of Russian gas supplies and the implications of the Russian energy tax reform. The so-called Russian 'tax manoeuvre' resulted in a change in the redistribution of import and export duties within the Eurasian Economic Union which results in lower revenue for Belarus. According to local estimates, in 2019 Belarus is expected to lose some USD 400 million directly as a result of this 'tax manoeuvre'. In 2018 and 2019, Belarus benefited from a 2-year transitional customs agreement with Russia according to which Belarus could withhold a portion of the oil export duty revenue for oil transported through Belarus as a cushion for increased gas prices. This agreement generated some USD 500 million annually for the Belarusian budget; however, it is due to be phased out at the end of 2019.

For months, Belarus has been trying to agree with Russia some new forms of compensation for the 'tax manoeuvre' and the end of the transitional customs agreement. However, several rounds of negotiations, including at the highest level, did not produce results satisfactory for Belarus. So at this point in time, these changes in the trade relations with Russia can be considered to have the effect of a lasting negative external shock.

In recent months, the downside risks have increased and the short-term economic prospects have deteriorated further. In the most likely combination of a negative external environment and continued policy restraint, only domestic demand will be providing an impetus to economic activity. In these circumstances, GDP growth in 2019 can be expected to be around 1% or a little higher. If some of the above restraints are relaxed, growth could accelerate slightly in 2020 and 2021. Sustaining macroeconomic stability seems to have become a lasting policy priority for the Belarusian authorities. Therefore, after a temporary reversal in 2019, disinflation in the country should continue in the next years. Belarus has been managing its external debt rather skilfully and its servicing should not pose problems in the foreseeable future.

Table 5.2 / Belarus: Selected economic indicators

	2015	2016	2017	2018 1)	2018 January-June	2019 January-June	2019 Forecast	2020 Forecast	2021 Forecast
Population, th pers., average	9,490	9,502	9,498	9,484	.	.	9,470	9,450	9,430
Gross domestic product, BYN mn, nom.	89,910	94,949	105,748	121,568	55,910	60,765	130,500	139,800	149,300
annual change in % (real)	-3.8	-2.5	2.5	3.0	4.5	0.9	1.3	1.5	1.7
GDP/capita (EUR at PPP)	13,800	13,200	13,400	14,100	.	.	.	.	.
Consumption of households, BYN mn, nom.	47,006	51,122	56,843	64,684	30,600	34,314	.	.	.
annual change in % (real)	-2.4	-3.2	4.8	8.3	9.7	5.9	4.8	3.0	3.0
Gross fixed capital form., BYN mn, nom.	25,763	24,155	27,662	31,461	12,780	14,739	.	.	.
annual change in % (real)	-15.5	-14.5	5.5	4.9	11.5	5.0	4.0	2.0	1.5
Gross industrial production									
annual change in % (real)	-6.6	-0.4	6.1	5.7	7.8	0.1	1.5	1.5	1.0
Gross agricultural production									
annual change in % (real)	-2.5	3.3	4.2	-3.3	2.2	0.5	.	.	.
Construction industry									
annual change in % (real)	-11.3	-14.8	-3.7	2.2	5.4	1.3	.	.	.
Employed persons, LFS, th	.	4,862	4,902	4,897	.	.	4,920	4,900	4,880
annual change in %	.	.	0.8	-0.1	.	.	0.5	-0.4	-0.4
Unemployed persons, LFS, th	273	302	293	245	250	227	226	231	230
Unemployment rate, LFS, in %	5.2	5.8	5.6	4.8	4.9	4.4	4.4	4.5	4.5
Reg. unemployment rate, in %, eop	1.0	0.8	0.5	0.3	0.4	0.3	0.3	0.3	0.3
Average monthly gross wages, BYN	671.5	722.7	822.8	971.4	909	1,040	1,110	1,240	1,380
annual change in % (real, gross)	-2.3	-3.8	7.5	12.5	13.3	8.1	8.0	6.0	6.0
Consumer prices, % p.a.	13.5	11.8	6.0	4.9	4.7	5.9	6.0	5.5	5.0
Producer prices in industry, % p.a. 2)	17.2	12.0	9.8	6.8	7.1	7.1	7.0	6.5	6.0
General governm.budget, nat. def., % of GDP									
Revenues	41.3	40.9	40.5	41.8	43.6	42.6	42.0	41.0	41.0
Expenditures	39.9	39.4	37.6	37.7	37.6	38.5	39.0	39.0	39.0
Deficit (-) / surplus (+)	1.4	1.5	3.0	4.0	6.1	4.1	3.0	2.0	2.0
General gov.gross debt, nat. def., % of GDP 3)	53.0	53.5	53.4	44.0	.	.	42.0	41.0	41.0
Stock of loans of non-fin.private sector, % p.a.	19.4	-6.2	7.2	12.7	10.3	12.2	.	.	.
Non-performing loans (NPL), in %, eop 4)	6.8	12.8	12.9	5.0	3.7	5.8	.	.	.
Central bank policy rate, % p.a., eop 5)	25.0	18.0	11.0	10.0	10.0	10.0	9.5	9.0	9.0
Current account, EUR mn 6)	-1,669	-1,464	-843	-29	-604	-683	-200	-700	-800
Current account, % of GDP	-3.3	-3.4	-1.7	-0.1	-2.6	-2.7	-0.4	-1.2	-1.4
Exports of goods, BOP, EUR mn 6)	23,854	20,988	25,405	28,409	13,556	13,834	29,000	29,000	29,300
annual change in %	-13.2	-12.0	21.0	11.8	8.5	2.1	2.1	0.0	1.0
Imports of goods, BOP, EUR mn 6)	25,807	23,270	28,043	30,536	14,599	15,166	31,700	32,100	32,600
annual change in %	-12.6	-9.8	20.5	8.9	9.6	3.9	3.8	1.3	1.6
Exports of services, BOP, EUR mn 6)	6,099	6,255	7,000	7,493	3,486	3,852	8,000	8,200	8,400
annual change in %	-1.2	2.6	11.9	7.0	4.6	10.5	6.8	2.5	2.4
Imports of services, BOP, EUR mn 6)	4,025	3,981	4,274	4,584	2,086	2,234	4,800	4,900	5,000
annual change in %	-10.0	-1.1	7.4	7.3	7.7	7.1	4.7	2.1	2.0
FDI liabilities, EUR mn 6)	1,506	1,133	1,130	1,212	923	943	1,300	.	.
FDI assets, EUR mn 6)	97	112	60	47	12	-55	100	.	.
Gross reserves of NB excl. gold, EUR mn 6)	2,510	3,071	4,502	4,561	4,259	5,352	.	.	.
Gross external debt, EUR mn 6)	34,996	35,930	33,363	34,307	33,584	35,215	34,600	34,100	33,400
Gross external debt, % of GDP	69.4	83.3	68.9	67.8	66.3	62.1	61.0	58.5	57.0
Average exchange rate BYN/EUR	1.7828	2.2010	2.1833	2.4008	2.3969	2.3917	2.3	2.4	2.6

1) Preliminary. - 2) Domestic output prices. - 3) Including publicly guaranteed debt. - 4) From 2018 NPL definition comprises doubtful, bad and small part of supervised assets (before that doubtful and large part of supervised assets were considered). - 5) Refinancing rate of NB. - 6) Converted from USD.

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