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## Ratings

Sovereign Government Credit (LC)	<b>B</b>
Sovereign Government Credit (FC)	<b>B-</b>
Country Credit Environment (LC)	<b>CCC+</b>
Country Credit Environment (FC)	<b>CCC</b>

\* These ratings are unsolicited

## Main Economic Indicators of Belarus

Macro indicators	2013	2014	2015
Gross gov. debt, BYR trln	247,1	315,2	384,4 <sup>f</sup>
Nominal GDP, BYR trln	649,1	778,4	952,2 <sup>f</sup>
Real GDP growth, %	1,0	1,7	-3,9
Gross gov. debt/GDP, %	38,1	40,5	40,4 <sup>f</sup>
Deficit (surplus)/GDP, %	-0,9	0,2	-2,4 <sup>f</sup>
Inflation rate, %	16,5	16,2	16,9 <sup>f</sup>
Current Account Balance/GDP, %	-10,4	-6,7	-7,0 <sup>f</sup>
External debt, USD bn	-	-	38,2*
Development indicators	2015		
Inequality adj. HDI	0,74		
GDP per capita, USD th	17,9		
Default indicator	04.03.2016		
10Y Gov Bond Yield, %	7,26		

Source: RAEX (Europe) calculations based on data from the WB, IMF, Belstat, National Bank of Republic of Belarus, Börse Frankfurt.

\* Gross external public sector debt and publicly guaranteed private sector debt as of 01.10.2015.

## Summary

Belarus' ratings reflect a weak external position, inconsistent policies and acceptable levels of government debt. While fiscal and monetary policies have improved over the last year, they remain distorted by widespread off-budget operations and high levels of financial dollarization. Spillover effects from the economic slowdown in Russia and internal structural imbalances have had a strong adverse effect on the country's macroeconomic stance.

**Total debt remains tolerable, key risks are related to the amount of FX-denominated debt.** Gross government debt accounted for 40,4% of GDP and 97,5% of budget revenues according to IMF's estimates for 2015 (see graph 1). These figures pose moderately low risks to the country's creditworthiness.

The maturity and creditor structure of the public debt contributed positively to the government's creditworthiness. External short-term debt as of December 2015 was equal to 7,5% of GDP and 18,1% of budget revenues. The Russian government (RG) and Russian banks have remained the largest creditors over the last two years: combined, they provided 72% of external funds in 2015 (87% in 2014, 36% in 2013<sup>1</sup>). The Agency assesses the probability of this debt restructuring as high based on previous agreements between the Russian and Belarussian governments. However, the high dependence on the RG as the largest creditor is an additional risk factor, especially taking into account deteriorated fiscal position of Russia.

The amount of FX-denominated debt had a strong adverse effect on the country's creditworthiness. Around 70% of the government obligations are denominated in foreign currency according to the Agency's estimations as of the end of 2015. Taking into account the decline in FX reserves (see graph 2) and volatile and depreciating local currency (see graph 3), the debt repayment risks and needs of additional external financial support the increase.

**The government continues to aim for fiscal consolidation, but off-budget operations persist.** The Ministry of finance of Republic of Belarus (MFRB) maintains a fiscal policy focused on consolidation. The government approved the increase of some tax rates (personal income tax rate was increased from 12% to 13%, profit tax rate was increased from

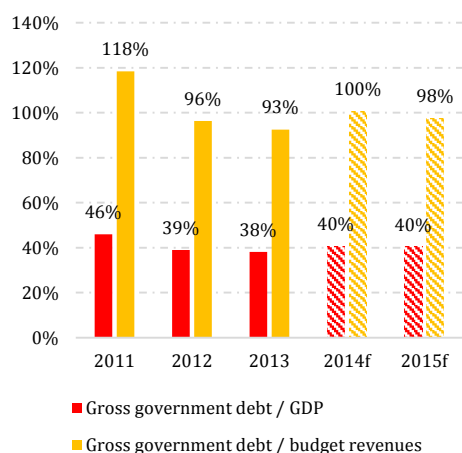
<sup>1</sup> Eurasian Fund of stabilization and development (EURASEC Anti-crisis fund) led mostly by Russia was the largest source of external funds in 2013 (36,2% of raised funds).

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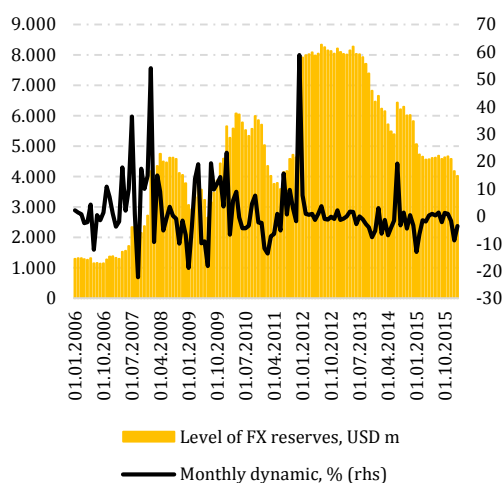
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**Graph 1: Gross government debt, % of GDP**



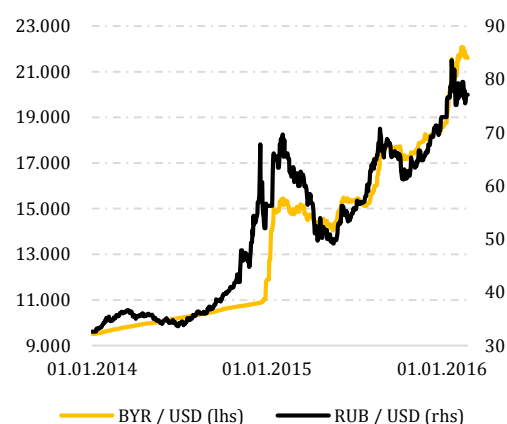
Source: RAEX (Europe) calculations based on data from the IMF.

**Graph 2: FX reserves dynamic**



Source: RAEX (Europe) calculations based on data from the NBRB.

**Graph 3: Comparative dynamics of the exchange rates of BYR and RUB**



Source: RAEX (Europe) calculations based on data from the NBRB, CBR.

18% to 25% for banks and insurance companies, etc.) and tax control has been strengthened (for simplified tax system in particular). Furthermore, in 2015 the Belarusian government reached an agreement with the RG on retention of duties on refined oil sales (before the agreement, most of the duties was transferred to the Russian budget). This translated in unplanned revenues from foreign trade (FT) operations which increased by 112% in nominal terms in the past year.

Both factors contributed positively to the dynamic of fiscal revenues of the consolidated budget of Belarus in 2015 (MFRB data), despite lower growth of revenues from corporate profit tax and VAT.

At the same time, the government eased the policy of wage increases and reduced total expenditures in real terms.

As a result, the Belarusian government ended 2015 with a positive fiscal balance at 1,3% of GDP in the MFRB's definition (compared with a surplus of 1,1% GDP in 2014), and announced further spending cuts and tax increases for 2016. The augmented balance of the government for 2015 (including outlays for bank recapitalizations, guaranteed debt and directed lending) was projected by the IMF at -3,0% of GDP (0,4% for 2014) (see graph 4).

**Monetary policy remains inconsistent while the exchange rate regime is becoming more flexible.** As mentioned in previous research report<sup>2</sup>, in the beginning of 2015, the National Bank of Republic of Belarus (NBRB) modified the exchange rate regime to provide more flexibility. This measure eased pressures on FX reserves. The level of reserves continued to decline over 2015, but at a lower pace: -1,5% per month on average for 2015, compared with -2% per month in 2014 (see graph 2). Nonetheless, this measure increased the volatility of the exchange rate (see graph 3).

The NBRB has maintained the refinancing rate at moderately high levels in 2015 (25%), at the same time it lowered its standing facilities rates (SWAP overnight, deposits overnight) several times during 2015. The latest can be considered as a risky policy taking into account the still high and volatile inflation.

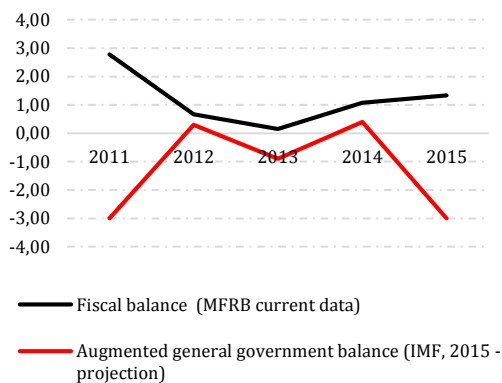
Extremely high levels of financial dollarization (see graph 5) are key factors limiting monetary policy transmission mechanism. The share of FX-loans and FX-deposits shows an upward trend over the past year despite the set of restrictions imposed by the government and NDRB. In addition, monetary policy transmission mechanism is distorted by still high levels of directed lending (4% of GDP in 2014 according to IMF's estimations).

<sup>2</sup> Research report on Belarus from 11 September 2015 ([http://raexpert.eu/reports/Research\\_report\\_Belarus\\_11.09.2015.pdf](http://raexpert.eu/reports/Research_report_Belarus_11.09.2015.pdf))

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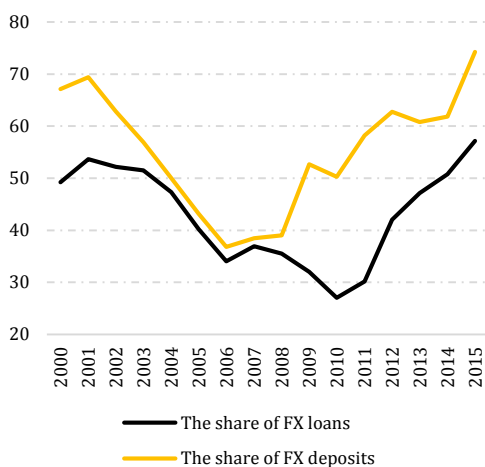
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**Graph 4: Fiscal balance of Belarus, % of GDP**



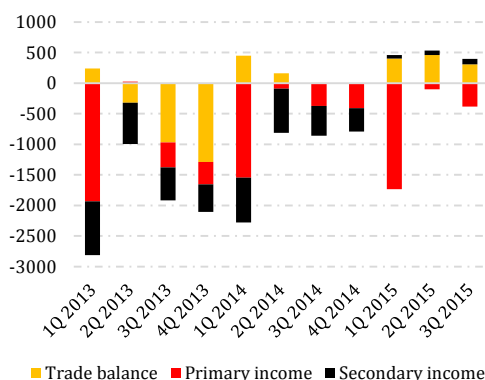
Source: RAEX (Europe) calculations based on data from the IMF Country Report (May 2015), MFRB.

**Graph 5: Financial dollarization in Belarus, %**



Source: RAEX (Europe) calculations based on data from the NBRB.

**Graph 6: Current account of Belarus, USD m**



Source: RAEX (Europe) calculations based on data from the NBRB.

**Important note for sovereign ratings**

This Research Report shall be treated as a supplementary part of the published Press Release included in the following link:

[http://raex.eu/reports/Press\\_release\\_Belarus\\_04.03.2016.pdf](http://raex.eu/reports/Press_release_Belarus_04.03.2016.pdf)

Both documents shall be treated as essential parts of each other.

For further information on the factors, their weights, methodologies, risks and limitations of these ratings, and other regulatory disclosures, please refer to the Press Release and the website of the Agency.

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**Spill-over effects from Russia are key external risks for the country.**

Russia, Belarus' main trading partner, provided 53% of total imports (mostly formed by crude oil and gas) and received 38% of total exports (formed by agricultural goods, recycled oil and transport means) in 2014. In addition, Russia contributes with approximately 60% of FDI.

A sharp appreciation of the BYR against the RUB led to growth of imports from Russia (total trade balance in 4Q 2014 was negative, see graph 6). Further slowdown in the Russian economy in 2015 combined with trade restrictions from the RG reduced the total amount of export from Belarus (-24,8% for 11 months 2015 compared with the same period of 2014). Current estimates made by the NBRB show a surplus for foreign trade of goods and services in 2015 at USD 205,7 m (compared with a deficit of USD 483,8 m in 2014). However, these projections are based on data for 11 months 2015, and shall be kept on watch.

Real GDP of Belarus declined by 3,9% in 2015 (according to preliminary data of Belstat) as a result of slowdown of exports, combined with stagnated internal consumption and decline in investments in fixed assets (-15,2% in 2015 y-o-y). Estimations for 2016 GDP growth continue this trend (-2,2% according to IMF).

**Structural imbalances remain in place.** Belarus' inefficient economic model, based on extremely high share of government-owned enterprises, and centralized planning, makes resource allocation inefficient, constrains companies' business flexibility and limits the general competitiveness of the economy. The progress in structural reforms was negligible over the last years and privatization plans are often stalled.

**Contingent risks of the banking system present long-term risks.** The banking sector structure provides contingent risks for the government. The three largest government owned-banks ("Belarusbank", "Belagroprombank", "Belinvestbank") accounted for 60,5% of total assets as of the end of 3Q 2015. In addition, the government is a minority shareholder in several private banks. Widespread directed lending through the state-owned banks includes subsidized interest rates, loan prolongations (which could be "hidden defaults") and underestimation of credit risks of borrowers. This means that the officially disclosed indicators of the banking system (positive ROA, capital adequacy ratio at 12,2% in 2015) do not reflect its actual weakness.