

Macro Notes – Belarus: Political Stalemate



August 26, 2020

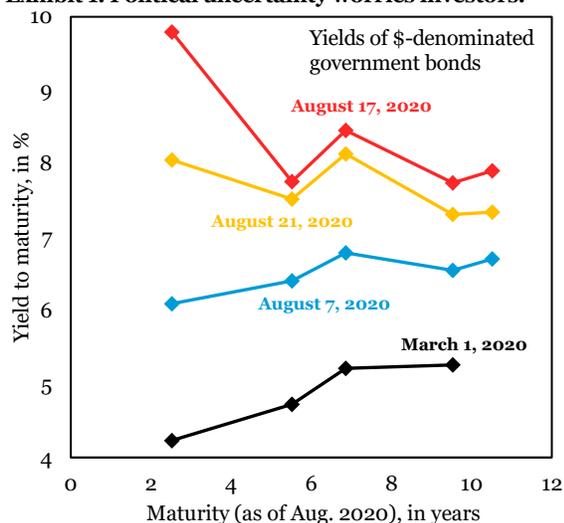
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- Widespread demonstrations and strikes followed the presidential election on August 9.
- Political uncertainty, together with the COVID-19 shock, weigh on the economic outlook.
- Belarus' economy is highly dependent on Russia's energy subsidy and domestic SOEs.
- The disputed election results mean that international financial support is very unlikely.

In this **Macro Notes**, we focus on recent political and macroeconomic developments in Belarus in light of large and persistent protests following the August 9 presidential election. The official election results published by the Belarusian central election committee, according to which incumbent President Alexander Lukashenko won 80% of votes, were rejected by the opposition as well as, among others, the European Union and the United Kingdom. Protests have spread across the country since election day, and importantly, employees of major state-owned enterprises have gone on strike. According to media reports, more than 7,000 protestors have been arrested—of which more than 5,000 remain incarcerated—and two persons are dead. Moreover, evidence of police brutality and torture has emerged. Opposition leader Svetlana Tikhonovskaya left the country due to fears for the safety of herself and her family and established a coordination committee for the transition of power out of Lithuania.

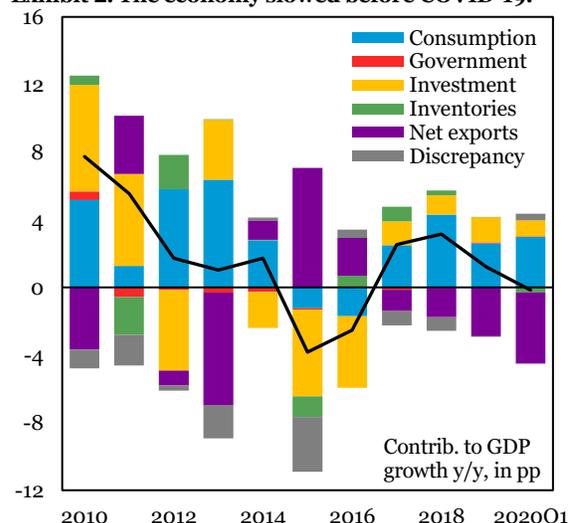
While Belarusian authorities—and the Russian government—allege foreign interference, most countries, including the United States and many in Europe, did not recognize the results of the election. The European Union has promised to impose sanctions on individuals responsible for the regime's violent response. As protests are now entering their third week, a political stalemate is setting in and an immediate solution to the conflict appears elusive. Markets reacted sharply to the initial emergence of the conflict and have not bounced back in a meaningful way since the election (Exhibit 1).

Exhibit 1. Political uncertainty worries investors.



Source: Bloomberg, IIF

Exhibit 2. The economy slowed before COVID-19.



Source: Haver, IIF

The Belarusian economy more broadly had been struggling even before the COVID-19 shock and disputed presidential election (Exhibit 2). The failure to reach an agreement on energy supplies from Russia resulted in a sharp reduction in oil imports in 2020Q1 and a deterioration in balance-of-payments inflows (Exhibit 3), which are highly reliant on Belarus' eastern neighbor (Exhibit 4). The COVID-19 pandemic, and the government's extremely poor response, worsened the situation, in turn fueling public discontent with President Lukashenko ahead of the election. The president had largely dismissed the public health emergency and few containment measures were taken, resulting in the fifth highest number of infections in Eastern Europe.

The Belarusian economy is dominated by SOEs, including the banking system where they make up 76% of capital. At the same time, some sectors driven by SMEs, including IT, have become increasingly competitive. While inflation appears under control (5.2% in July vs. the "less than 5%" target) despite substantial wage increases ahead of the election and the recent BYR devaluation of roughly

20% year-to-date, high dollarization is a financial stability concern, particularly given low reserves of \$4.3 bn (or 1.2 months of imports). An additional vulnerability lies in the high share of FX in corporate lending (over 50%) and public debt (~80%).

Exhibit 3. Significant c/a deterioration in 2020.

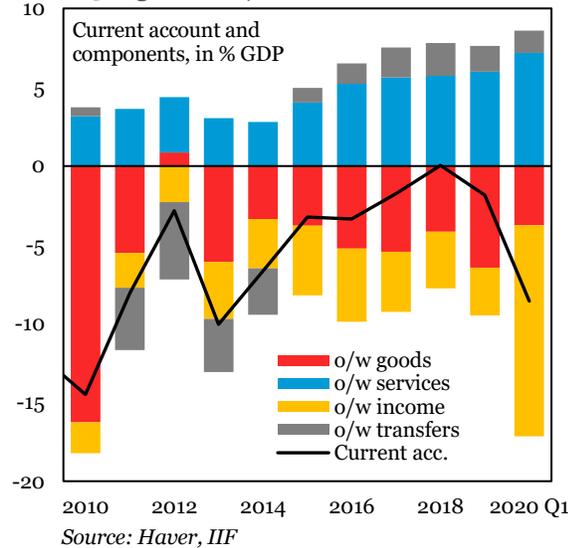
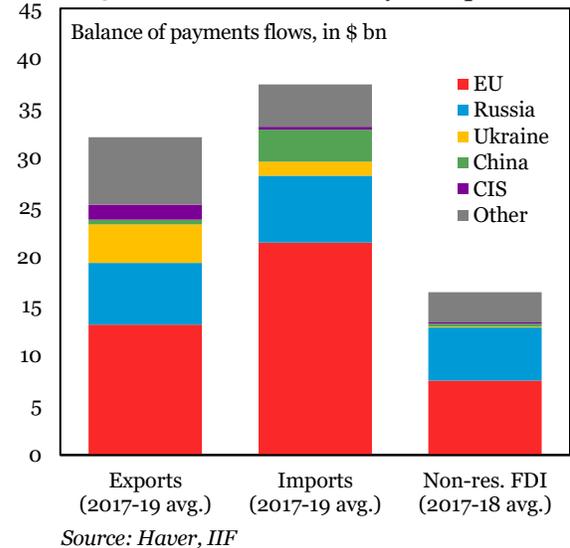


Exhibit 4. Russia and the EU are key trade partners.



Belarus is highly dependent on Russia’s energy subsidy. The country receives around 24 mn tons of oil per year free of import duties as well as a transfer from Russia’s budget for the re-export of refined oil. The transfers will expire in 2024, when Russia introduces a new energy taxation system (“tax maneuver”), where export duties are being phased out and a revised extraction tax remains. The loss to the Belarusian budget could be as high as 2% of GDP and the BoP impact around 4%. As negotiations with Russia broke down and COVID-19 led to a sharp drop in external demand, the current account deteriorated markedly.

Government debt is likely to reach 60% of GDP due to the economic slowdown and BYR devaluation (Exhibit 5). While Belarus successfully issued \$1.25 bn in Eurobonds in June, market access is now limited due to political uncertainty. In addition, negotiations with the IMF appear to have broken down, and EU support is not tenable in the current environment. There are now five different maturities on the Eurobond sovereign curve plus the Belarus Development Bank bond and a bond by the largest domestic retailer. While repayments are still a few years off (Exhibit 6), total external amortization needs are about 25% of GDP.

The overall macroeconomic outlook for Belarus is challenging, mostly due to its reliance on Russia’s energy subsidy, high share of SOEs, and significant dollarization. In the next note, we will look at external financing needs and political scenarios.

Exhibit 5. Public debt has been increasing lately.

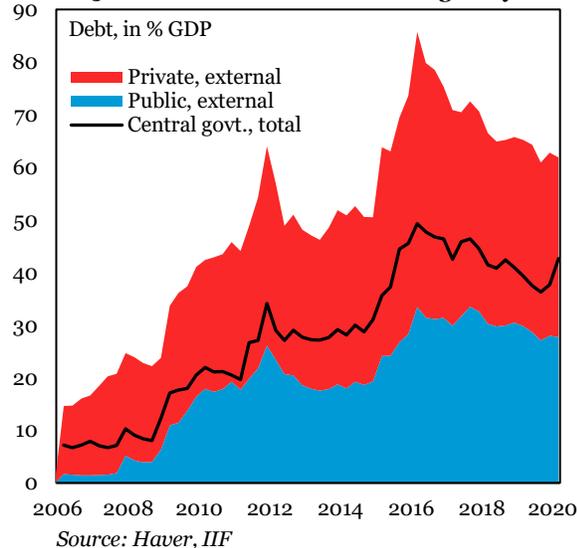


Exhibit 6. Eurobond amortization is not imminent.

