

Belarusian Monthly Economic Review

- The Russian ruble will not be introduced in Belarus in 2005.
- Gazprom and Beltransgaz signed a contract for gas deliveries to Belarus in 2004.
- Imports of investment goods grew at a slow pace.
- The Ministry of Finance is planning to restructure its debt to the NBB.
- The NBB's purchases of hard currency became the main money supply source.
- Collateralized credit auctions will become the main means for regulating banking liquidity.

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Politics: Belarus will not introduce the Russian ruble as its currency in 2005

After the June 5 meeting in Sochi, the presidents of Belarus and Russia stated that they had reached agreements on practically all issues including gas deliveries to Belarus. Both stated that no further important problems remained between their countries, only disputes between some economic entities. Also, President Putin stated that the plan to introduce a single currency in Belarus and Russia in 2005 would not likely be implemented. The presidents met again on June 27 (the fourth time in five weeks), suggesting that a number unresolved issues in their bilateral relations still exist.

Real sector: Acceleration of economic growth continues

The GDP and output growths continued to accelerate in Jan-May. According to the official statistics, GDP grew by 10.2% yoy (i.e. 6% more than in Jan-May 2003). Industrial output grew by 14.4% yoy (8.5% more than last year). This economic growth was demand-driven.

Machine building and metal working, fuel and food processing contributed most to the industrial output growth (3.3, 2.4 and 2.1 percentage points respectively). External and internal demand for the products of these sectors grew considerably. Substitution of electric energy imports caused the power sector to contribute 1.5 percentage points more to the industrial output growth than in Jan-May 2003. The financial status of enterprises also continued to improve. The share of loss making enterprises decreased by 9.2 percentage points. Obviously, such real sector dynamics will lead to increased fiscal revenues and improvements in the labor market (unemployment decreased by 0.7% compared to May 2003, reaching 2.6%).

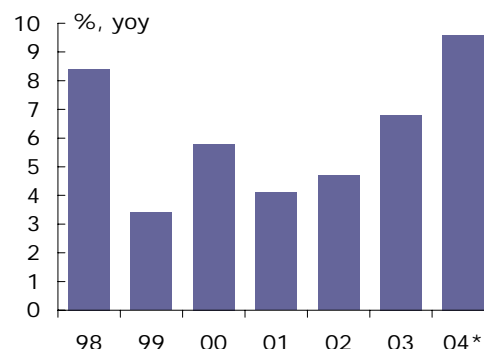
Structural trends: A contract has been signed with Gazprom

Energy. On June 8, after six months of negotiations between Gazprom and Beltransgaz the parties finally signed a contract to deliver gas to Belarus. In 2004 Gazprom will sell Belarus 10.2 bn m³ of gas. The price will be USD 46.68 per 1000 m³ (last year it was about USD 30). The transit price through the Beltransgaz pipeline will be USD 0.75 per 1000 m³ of gas per 100 km (compared to about USD 0.55 in 2003). The contract terms show that Gazprom has made a concession, as earlier on it had insisted on a transit price of USD 0.67. Compared to last year, Belarus will have to pay to Gazprom an additional USD 170 m. Gazprom will pay about USD 45 m more for gas transit than in 2003, according to expert estimates.

Agriculture. The president issued an edict according to which the price of the assets of a loss making agricultural enterprise will be 20% of net value of its assets. If this price is zero or negative, then the collective farm can be bought for one base

Population: 9.8 m
Industry/GDP: 25.5%
Agriculture/GDP: 6.1%
Investment/GDP: 18.6%
Export destination: Russia 49%, EU 23%
Import origin: Russia 66%, EU 15%

Real GDP Growth



* Own estimates.
Source: Ministry of Statistics and Analysis.

unit (BYR 19,000). However, the edict also introduces additional conditions for a buyer, namely to pay off all debts of the loss making enterprise, to keep everybody employed while the debts are being paid off (within 5 years), and finally to continue the agricultural production. The Belarusian legislation also contains certain conditions regulating the procedures for buying and evaluating the assets, which, taken together, make such an investment unattractive. Thus, one can hardly expect a significant demand for the assets of loss making agricultural enterprises.

Utilities. On June 16, the deputy minister of the Housing and Utility Ministry stated that the government set the limit for housing and utility services price increases at USD 5 for 2004. Since the beginning of the year these services (without monthly indexation) became more expensive by USD 3.7. The government plans to index the tariffs for the remaining USD 1.3 to keep the total within the USD 5 limit. If energy purchase prices remain stable, the level of cost coverage by households will be no more than 55% by the end of the year, which is 5 percentage points below the limit set forth in the Budgetary Law for 2004. As a result, the government will spend about BYR 65 bn to compensate producers for the losses in the housing and utility services area. These losses might be partially offset by raising tariffs for enterprises. It appears that all these decisions are driven by the coming parliamentary elections in autumn. In the short-term these measures will restrain price growth, but the state will face heavier burdens and an inefficient redistribution of resources.

External sector: Slow growth of capital goods imports

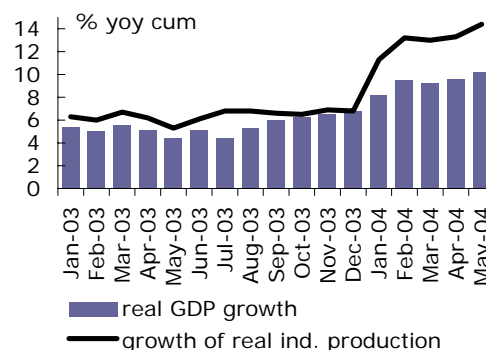
The merchandise trade deficit in Jan-Apr was still lower than for the same period of 2003. The export exceeded the import growth rate by 3.2 percentage points. However, in March and April the merchandise trade deficit grew by USD 53 and 67 m, more than during the same months last year. Thus, it is likely that the improvement in the foreign trade balance was temporary and was due to short-term effects.

In the long-term, export growth prospects are vague. In order to achieve sustainable export growth it is necessary to modernize the enterprises and install new equipment, which requires attracting foreign direct investment and importing capital goods. However, at present these two indicators give little rise for optimism. The share of capital goods imports decreased from 9.3% to 8.5% in Jan-Apr. Its growth rate was 15.4% yoy, which is 10 percentage points lower than the import growth rate in general. According to preliminary data, the net foreign direct investment inflow dropped by 9.2% yoy.

Public finance: The Ministry of Finance is planning to restructure its debts to the NBB

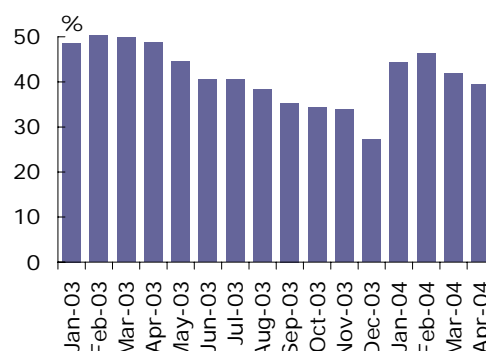
The fiscal situation continued to be favorable. In Jan-May consolidated revenues reached 107.1% of the amount planned in the consolidated budget. The percentages of central and local revenues were 103.5% and 111.4% respectively. The consolidated revenues were BYR 6182.7 bn (without the Social Security Fund), or 37.7% of GDP, which is 1.2% higher than for the same period of the previous year. At the same time, the higher GDP growth rate compared to general state revenue growth led to a lowering of the tax burden in May by 0.4%. The structure of revenues did not change much. The major source of fiscal revenues was still the VAT (8.6% of GDP) and profits (3.9% of GDP) taxes. The revenues from these taxes ensured that the revenue plan was met and exceeded. The improved financial status of enterprises led to reduced fiscal arrears in May. As of June 1, they amounted to 304 bn. VAT

GDP and Industrial Production



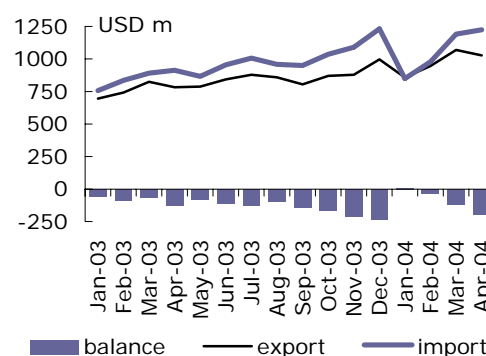
Source: Ministry of Statistics and Analysis.

Share of Loss Making Enterprises



Source: Ministry of Statistics and Analysis.

Merchandise Trade



Source: Ministry of Statistics and Analysis.

Import of Capital, Consumer, and Intermediate Goods

Merchandise import:	Jan-Apr 2003	Jan-Apr 2004	Change, % yoy
	USD m	USD m	
Capital	312.9	361.2	15.4
Intermediate	2495.5	3162.7	26.7
Consumer	540.8	686.6	27.0
Total:	3382.4	4242.8	25.7

Source: Ministry of Statistics and Analysis.

arrears were the biggest (32.6% of the total), followed by excises debts (23.5%) and sales tax arrears (16.7%). In May the volume of extended tax credits grew by 0.3%, amounting to BYR 245.3.

The Ministry of Finance drafted an edict to restructure debts on NBB loans issued between 1991 and 2003 to finance the fiscal deficit. They amount to more than BYR 800 bn or 35% of the domestic debt. It is planned to implement the restructuring by issuing long-term government bonds and transfer them to the NBB. Thus, the NBB will have an additional tool to regulate the liquidity of the banking system.

Monetary policy: The NBB's purchases of hard currency became the main money supply source

The hard currency revenues of Belarusian exporters continued to grow in May. This caused the NBB to become a net buyer of hard currency again. Its net foreign assets (NFA) grew by 8.3% in May, reaching BYR 1482.2 bn. This NFA increase became the main channel of money supply growth. As a result, the money base grew by 3.2% mom, and the coverage of the money base by net foreign assets increased by 3.5 percentage points to reach the level of 74.7%.

In spite of the high level of liquidity in the banking system, the NBB did not take measures to reduce it. This led to a lowering of credit interest rates to banks and to increased crediting of the economy, increasing by BYR 335.2 (4.8%) in May. However, since the beginning of the year the interest rate spread decreased by only 0.4 percentage points.

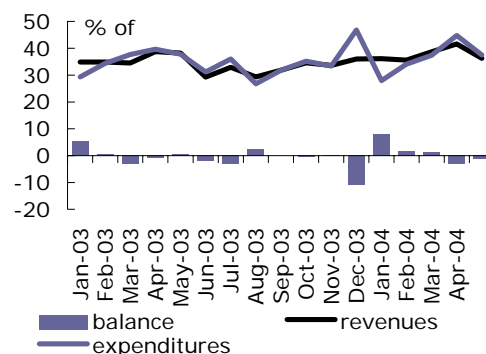
Lowering the ruble deposit interest rates did not result in their reduction in real terms. Besides, the yield of these financial tools was much higher than the yield on hard currency financial tools. This made it easier to support the high demand for Belarusian ruble deposits. They became the main component of money creation. The ruble monetary aggregate M2 grew by 4.5% in May. Transferable deposits of legal entities increased by 7.3%. This made a 1.6 percentage point contribution to the increase of the monetary aggregate M2. Time deposits by individuals increased by 5.5% (1.7 percentage points of the M2 increase). Keeping a high operational demand on the Belarusian ruble contributed to further disinflation. In May consumer prices grew by 0.7%.

The growing hard currency supply on the domestic currency market led the NBB to keep the nominal exchange rates of the Belarusian ruble against the US dollar and the Russian ruble practically unchanged in June. As of July 1, the exchange rates of the Belarusian ruble were 2156 BYR/USD and 74.2 BYR/RUB.

Banking sector: Credit auctions will become a means to regulate banking liquidity

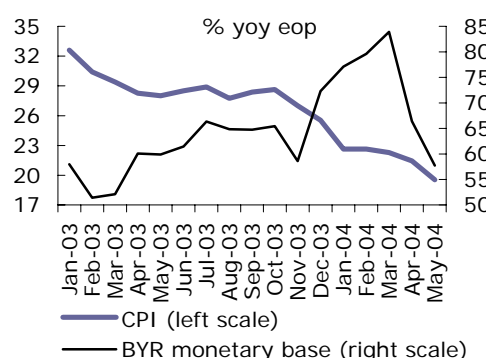
On June 24, the NBB for the first time in its history held a collateralized auction to place BYR 15 bn for 6 days at the annual interest rate of 22%. The NBB stated that it intends to use such auctions as its main strategy in maintaining banking liquidity. At the same time, the NBB is going to stop the rediscounting of legal entities' bills. The main reason for this is the high requirements to creditworthiness of promisers, which limited the availability of this tool. This changed approach to regulating banking liquidity will lead to more transparency on the inter-bank market and will increase the competition among commercial banks. In turn, this will increase the effectiveness of allocation of their resources.

Consolidated Budget*



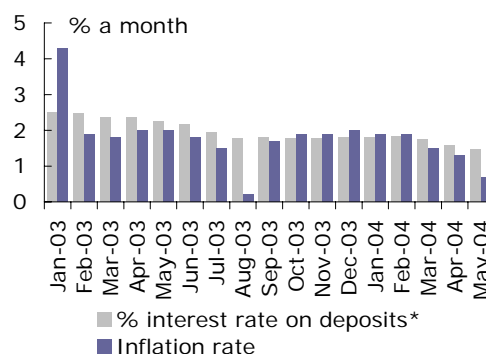
* Without Social Security Fund.
Source: Own calculations based on the Ministry of Statistics and Analysis and the NBB data.

Ruble Monetary Base and CPI



Source: Own calculations based on the Ministry of Statistics and Analysis and the NBB data.

Inflation and Interest Rates



* Interest rates on new household deposits in BYR.
Sources: NBB, own calculations.

Economic Trends		Q2 02	Q3 02	Q4 02	Q1 03	Q2 03	Q3 03	Q4 03	Q1 04	Mar 04	Apr 04	May 04
GDP growth	% yoy	5.7	4.6	5.5	5.6	4.7	7.2	8.8	9.3	--	--	--
GDP growth	% yoy cum.	4.9	4.8	5.0	5.6	5.1	6.0	6.8	9.3	9.3	9.6	10.2
Industrial production	% yoy cum.	4.0	3.9	4.5	7.0	6.3	6.5	6.8	13.0	13.0	13.3	14.4
Agricultural production	% yoy cum.	3.2	2.8	0.7	1.2	-1.5	3.8	6.8	4.3	4.3	5.5	5.5
CPI	% yoy eop	44	42	35	29	29	28	25	22	22	21	20
PPI	% yoy eop	38	44	42	43	42	36	29	27	27	27	27
Merchandise export (USD)*	% yoy	8.4	10.2	24.1	39.2	20.0	22.2	25.3	25.2	30.0	34.2	--
Merchandise import (USD)*	% yoy	2.9	12.9	19.4	39.0	29.8	21.4	21.5	20.5	30.1	40.9	--
Merchandise trade balance (NBB data)	USD m cum.	-179	-441	-914	-165	-398	-695	-1234	-91	-101	-285	--
Current account	USD m cum.	137	-23	-337	-32	-44	-174	-505	77	97	-24	--
Current account	% GDP cum	2.1	-0.2	-2.3	-0.7	-0.6	-1.4	-2.9	1.3	1.6	-0.4	--
International reserves	USD bn eop	257	251	457	463	526	459	474	617	617	511	552
Monetary Base	% yoy eop	58	55	40	52	61	65	72	84	84	66	58
Lending rate**	% p.a. aop	67	55	51	47	41	33	31	29	28	25	24
Exchange rate (official)	USD aop	1753	1837	1893	1960	2031	2082	2135	2156	2152	2152	2154
Exchange rate (official)	EUR aop	1613	1808	1891	2105	2311	2342	2541	2695	2639	2586	2586

* Since 2003 – the data of the Ministry of Statistics and Analysis. Other external trade indicators – NBB data.

** Nominal rate of commercial banks for new loans for legal entities in national currency.

Sources: Ministry of Statistics and Analysis, NBB, own calculations.

Key Economic Indicators		1997	1998	1999	2000	2001	2002	2003
Nominal GDP*	BYR trn	0.367	0.702	3.026	9.134	17.173	26.613	35.930
Nominal GDP	USD bn	12.7	9.4	6.3	8.9	12.2	14.5	17.5
GDP growth	% yoy	11.4	8.4	3.4	5.8	4.7	5.0	6.8
Industrial production	% yoy	18.8	12.4	10.3	7.8	5.9	4.5	7.1
Agricultural production	% yoy	-4.9	-0.7	-8.3	9.3	1.8	0.7	6.6
CPI	% yoy aop	64	73	294	169	61	43	29
CPI	% yoy eop	63	182	251	108	46	35	25
PPI	% yoy aop	88	72	355	186	72	41	38
PPI	% yoy eop	90	197	245	166	41	42	29
Exports (gs, USD)	% yoy	19.5	-10.8	-8.5	17.6	10.4	8.6	26.9
Imports (gs, USD)	% yoy	20.5	-7.8	-19.0	21.0	8.2	9.1	27.2
Current account	USD m	-859	-1017	-194	-338	-435	-337	-505
Current account	% GDP	-6.8	-10.8	-3.1	-3.8	-3.6	-2.3	-2.9
FDI (net)	USD m	350	201	443	119	96	453	169
International reserves	USD m	394	339	305	357	347	457	474
Fiscal balance**	% GDP	-5.8	-5.0	-2.9	-0.6	-1.3	-0.6	-1.3
Internal public debt	% GDP eop	4.3	4.9	5.7	4.5	4.5	4.6	6.0
External debt (total)	% GDP eop	20	51	42	24	20	20	19
Monetary base	% yoy eop	96	102	204	52	225	32	50
Exchange rate (official)*	USD aop	34	151	572	1035	1394	1784	2075
Exchange rate (official)*	USD eop	42	430	925	1213	1580	1920	2156
Spread***	% aop	31.1	224.0	128.2	44.4	0.8	0.0	0.0
Spread***	% eop	35.5	301.9	189.1	2.8	0.2	0.0	0.0
Exchange rate (official)*	EUR aop	--	--	270	651	1239	1690	2353
Exchange rate (official)*	EUR eop	--	--	323	1097	1392	1989	2695

* On January 1, 2000 the Belarusian ruble was devalued (1:1000). All figures are given in "new" Belarusian rubles.

** The fiscal balances for 1996-1998 included quasi-fiscal financing through commercial banks. Negative values refer to fiscal deficits.

*** Spread between the black market and official (NBB) exchange rates.

Sources: Ministry of Statistics and Analysis, Ministry of Finance, NBB, own calculations.

Notes:

aop	average of period	mom	month-on-month change
avg	average	trn	Trillion
bn	billion	NBB	National Bank of Belarus
cum.	cumulative	p.a.	per annum
eop	end of period	yoy	year-on-year change
gs	goods and services	ytd	year-to-date
m	million		

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