

Belarusian Monthly Economic Review

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- Belarus signed the Kyoto Protocol.
- Wages grew faster than labor productivity.
- Belarus adopted the Concept of Energy Security.
- The export of ferrous metals fell by 7.4% yoy in the 2nd quarter of the 2005.
- Government deposits in the NBB decreased.
- The legal requirement to provide collateral by guarantor for loans was abolished.

Politics: Belarus joined the Kyoto Protocol

On August 12, Belarus joined the Kyoto protocol. President Lukashenko signed the requisite edict. The Kyoto Protocol defines the rules for the international trade in greenhouse gas emissions, which is a mechanism to fight global warming. According to some estimates, joining the Kyoto Protocol will enable Belarus to receive revenues of at least of USD 325 m for selling free quotas for greenhouse gas emission. Moreover, the Kyoto protocol will create opportunities for the country to get additional investment revenues in the form of Joint Implementation projects in the fields of energy savings or technologies aimed at emission reductions.

On August 26–27, the 40th CIS Summit was held in Kazan, Russia. At this summit the presidents of Belarus, Kazakhstan, Russia, and Ukraine discussed several issues leading to the implementation of the Single Economic Space (SES). Ukraine, unlike its partners who are ready to sign 29 agreements of the package of documents required to set up the Free Trade Area, agreed to sign only 15 agreements. It stated that other documents need to be further analyzed and worked out. At a bilateral meeting the presidents of Belarus and Ukraine agreed to draft a document that would regulate the relations between Belarus and Ukraine. The prime ministers of the two countries will discuss the details of the draft at the meeting to be held in September.

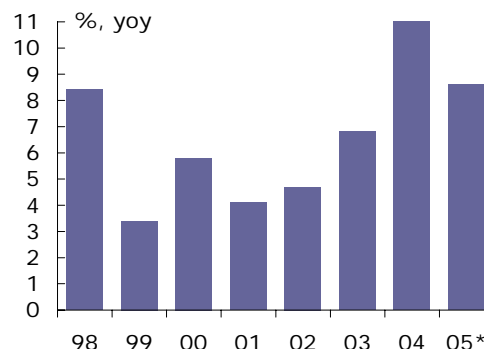
Real sector: The wage growth rate is higher than the labor productivity growth rate

Between Jan-Jul the GDP grew by 8.8% yoy, which is 0.1% less than for Jan-Jun. As in previous months, the slowing of the GDP growth was mainly due to a lower growth rate in industry. Industrial production grew by 5.0% yoy in July whereas it had grown by 9.6% yoy between Jan-Jul. The growth rates dropped most in the fuel industry (due to a slower growth of exports of oil products) and light industry (due to a low demand for the goods of this sector).

The slowing down of economic growth was accompanied by a lower growth rate of labor productivity. Labor productivity growth began to slow in the 4th quarter of 2004, while the real wage growth slowed only slightly during the 2nd quarter of 2005. The real wage growth rate (22% yoy for the 2nd quarter of 2005) was more that twice as high as the labor productivity growth rate. The difference between the growth rates of the two indicators is to a large extent due to the differing deflators that are used to calculate them. In the 2nd quarter of 2005 the GDP deflator was 19.5% yoy, while the CPI deflator was just 10.7% yoy. However, even when adjusted to the deflator difference, the real wage growth rate in the second quarter of 2005 was almost 5 percentage points higher than the labor productivity growth rate. The same situation was observed in 2000–2001. It led to a deterioration

Population: 9.8 m
Industry/GDP: 26.8%
Agriculture/GDP: 8.9%
Investment/GDP: 20.7%
Export destination: Russia 47%, EU 37%
Import origin: Russia 68%, EU 20%

Real GDP Growth



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

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of the financial status of enterprises. Hence, if the gap in the growth rates between real wages and labor productivity is not scaled down in the near future one can expect the number of loss making enterprises to increase.

Structural trends: The Concept of Energy Security for Belarus was adopted

Energy sector. The President issued an edict adopting “the Concept of Energy Security” and “Ensuring Higher Energy Independence”. The document was adopted because Belarus is very dependant on Russian gas supplies. According to this concept the share of local fuels in the fuel and energy balance should be at least 25% by 2010. The document also states that the fixed capital of the energy system should be modernized. The option of building a nuclear power station was also considered. However, a final decision on its construction will depend on opinion poll results and on finding a foreign investor. Most of activities that are described in the Concept will be financed with state fund and with internal investment funds of the energy enterprises.

External trade: Exports of ferrous metals fall

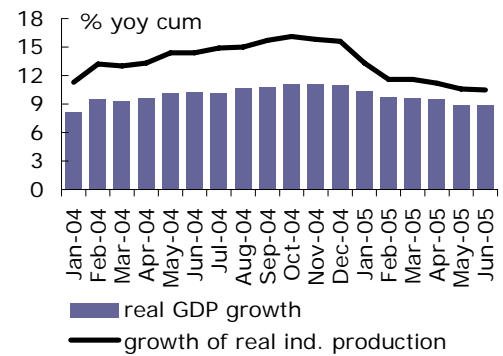
According to data from the Ministry of Statistics and Analysis, the merchandize trade surplus was USD 294.4 m for the first half of the year. For the 1st quarter of the 2005 the surplus amounted to USD 447.1 m, while in the second quarter there was a deficit of USD 152.7 m. The situation in merchandize trade deteriorated in the 2nd quarter of 2005 due to slower export growth and some acceleration of import growth compared to the first quarter.

The lower export growth rate was due to a considerably slower growth of oil products exports and to decreased ferrous metal exports. The lower growth rate of oil products exports was mainly due to a slower growth of the volume of their exports. The decrease of ferrous metal exports (by 7.4% yoy for the 2nd quarter of the 2005) was due to changes in the world metals market. The demand for ferrous metal products in the 1st quarter of 2005 was lower than supply, which led to falling prices. However, in 2005 iron ore prices soared, which decreased the profitability of ferrous metallurgy enterprises. It forced the Belarusian metallurgical plants to cut imports and exports of ferrous metal.

Public finance: Exporters are paid back more VAT

In June and July the growth rate of the general government revenues was lower than the growth rate of the nominal GDP for the first time this year. As a result, the share of consolidated revenues in July decreased by 0.8 percentage points and amounted to 50.5% of GDP for Jan-Jul. This lower growth rate of the consolidated revenues was mainly due to increased VAT amounts being paid back to exporters based on the zero rate of this tax (exporters are freed from paying this tax, and VAT paid on operations inside the country is compensated). In July the share of VAT revenues within the consolidated revenues dropped by 0.3% of GDP. In spite if this, revenues execution remained favorable. For Jan-Jul, the general government revenues amounted to 62.4% of the annual plan (58.8% of the annual plan a year ago). All main revenue sources generated more revenues than planned. The consolidated expenditures for Jan-Jul amounted to 47.8% of GDP, or 56.2% of the annual plan (55.7% of the annual plan a year ago). The fiscal surplus of the general government was 2.7% of GDP. In July the general government faced a deficit in the amount of 0.6% of GDP. The deficit was financed by selling government securities.

GDP and Industrial Production



Source: Ministry of Statistics and Analysis.

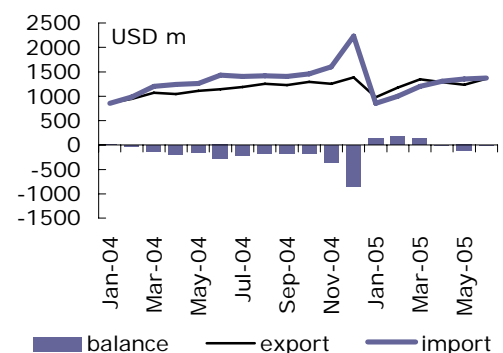
Contribution to industrial output growth

	Jan-Jul 2005	
	growth rate*	contribution**
Industry	9.6	9.6
including industries:		
electric power	-5.9	-0.4
fuel	10.8	2.2
ferrous metallurgy	9.9	0.4
chemical and petrochemical industry	5.4	0.6
machinery and metalworking	14.0	2.8
logging, woodworking, pulp and paper	7.4	0.3
building materials	9.1	0.3
light	1.6	0.1
food	13.0	1.8
other	14.3	1.6

* % yoy; ** percentage points.

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

Merchandise Trade



Source: Ministry of Statistics and Analysis.

Merchandise Trade Structure

	Exports Imports		Balance, USD m
	growth rate, % yoy		
Total			
Jan-Mar 05	21.8	0.6	447.1
Apr-Jun 05	17.7	2.6	-152.7
Russia			
Jan-Mar 05	-8.0	-9.0	-668.8
Apr-Jun 05	-9.3	-9.1	-964.1
Non-CIS countries			
Jan-Mar 05	49.3	17.7	1061.7
Apr-Jun 05	35.9	23.6	712.4

Source: Ministry of Statistics and Analysis.

In August some indicators of the central budget for 2005 were amended again. According to the presidential edict of August 9, the government gave banks guarantees for BYR 272.5 bn on preferential loans, in order to allow them to purchase grain of the 2005 harvest. According to the edict of August 10, the expenditure part of the budget (Republican Fund for Agricultural Producers and Agrarian Science Support) was increased by BYR 204 bn. Financing of additional expenditures is planned to be at the expense of higher than planned revenues of the Fund in 2005 (BYR 179.2 bn) and resources that were accumulated by the Fund in 2004 (BYR 24.8 bn).

Monetary policy: Reduction of government deposits in the NBB

In July the monetary authorities considerably increased the money supply to stimulate business activities. Following June's tendency, the main channel for the money supply increase was a reduction of the government deposits in the NBB, though earlier this channel had been used to cut the money supply. Increased net foreign assets of the NBB contributed to the money supply increase, too. In July the money base increased by 11.2% mom. In annual terms its growth continued to accelerate, rising by 49.8% yoy in July (39.3% yoy in June).

The slowing down of economic growth led to a further decrease of the crediting growth rate. With the higher money supply this led to an increase of banking liquidity. A certain part of the free resources of banks was placed on deposit with the NBB or invested in short-term NBB bonds. Interest rates on the inter-bank market remained low. The liquidity growth contributed to a further reduction of interest rates for national currency credits and deposits. This interest rate policy – under conditions of growing household incomes – led to a considerable increase of cash in circulation (7.6% mom in July).

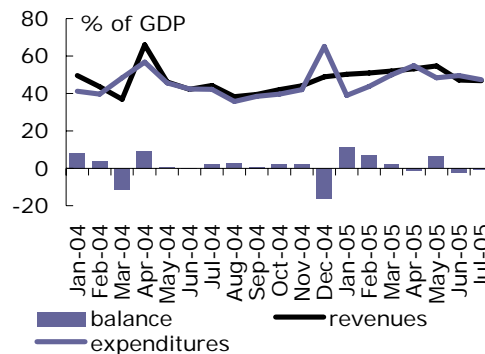
The stability of the exchange rate of the Belarusian ruble led to a further reduction of the gap between the deposit interest rates in hard currency and in national currency. Nevertheless, ruble deposits remained the main form of saving. Enterprises reduced their current ruble deposits in banks, because they faced a turnover capital deficit and falling interest rates. Ruble money increased by 5.7% mom and broad money rose by 3.9% mom in July.

In spite of seasonal factors, this significant money supply increase led to a substantial price growth in July. In July consumer prices went up by 0.9% mom. In annual terms inflation amounted to 9.9% yoy. The Belarusian ruble devalued vis-à-vis the US dollar by 0.14%. As of August 31, its exchange rate was 2151 BYR/USD.

Banking sector: The legal requirement to provide collateral by guarantor for loans was abolished

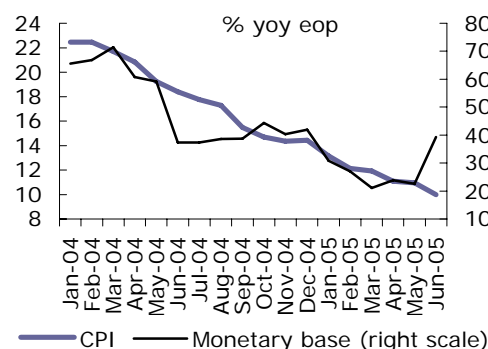
The president signed an edict abolishing the legal requirement to provide collateral for loans. Previously a collateral was nearly always required, except for getting small loans and for some loans at authorized banks. This norm greatly restricted the access to loans for small enterprises, which could not provide collaterals. Abolishing this norm should create more favorable conditions for micro lending in Belarus. Additionally, it removes a big obstacle on the way toward creating guarantee funds in Belarus, which are an important tool for small and medium business development.

Consolidated Budget*



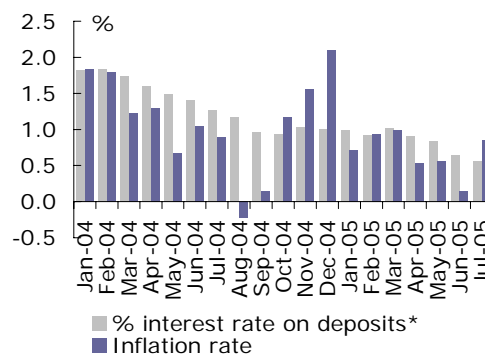
* 2004 – without innovation funds.
Source: own calculations based on the Ministry of Statistics and Analysis and the NBB data.

Monetary Base and CPI



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

Monthly Inflation and Interest Rates



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

Economic Trends		Q3 03	Q4 03	Q1 04	Q2 04	Q3 04	Q4 04	Q1 05	Q2 05	May 05	Jun 05	Jul 05
GDP growth	% yoy	7.2	8.8	9.3	11.0	11.6	11.6	9.6	8.3	--	--	--
GDP growth	% yoy cum.	6.0	6.8	9.3	10.3	10.8	11.0	9.6	8.9	8.9	8.9	8.8
Industrial production	% yoy cum.	6.5	7.1	13.0	14.4	15.7	15.6	11.6	10.5	10.6	10.5	9.6
Agricultural production	% yoy cum.	4.4	6.6	4.3	5.7	10.2	12.9	12.5	10.1	11.1	10.1	11.6
CPI	% yoy eop	28	25	22	18	15	14	12	10	11	10	9.9
PPI	% yoy eop	36	29	27	27	22	24	14	12	13	12	11.1
Merchandise export (USD)*	% yoy	21.3	25.0	27.7	36.9	44.6	42.2	21.8	--	9.3	--	--
Merchandise import (USD)*	% yoy	22.8	24.6	21.5	43.1	42.9	53.4	0.5	--	5.7	--	--
Merchandise trade balance (NBB data)	USD m cum.	-714	-1256	-58	-541	-931	-2066	533	--	505	--	--
Current account	USD m cum.	-131	-424	164	-58	-186	-1043	762	--	935	--	--
Current account	% GDP cum	-1.0	-2.4	3.7	-0.6	-1.1	-4.6	13.5	--	9.1	--	--
International reserves	USD bn eop	459	474	617	539	664	770	975	1130	1134	1130	1225
Monetary Base	% yoy eop	52	51	71	37	39	42	21	39	23	39	50
Lending rate**	% p.a. aop	33	31	29	24	19	18	19	--	15	14	--
Exchange rate (official)	USD aop	2082	2135	2156	2155	2161	2173	2164	2151	2150	2150	2150
Exchange rate (official)	EUR aop	2342	2541	2695	2617	2640	2810	2840	2713	2734	2619	2590

* 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		1998	1999	2000	2001	2002	2003	2004
Nominal GDP*	BYR trn	0.702	3.026	9.134	17.173	26.613	36.565	49.445
Nominal GDP	USD bn	7.1	5.4	8.9	12.1	14.5	17.7	22.9
GDP growth	% yoy	8.4	3.4	5.8	4.7	5.0	7.0	11.0
Industrial production	% yoy	12.4	10.3	7.8	5.9	4.5	7.1	15.6
Agricultural production	% yoy	-0.7	-8.3	9.3	1.8	0.7	6.6	12.9
CPI	% yoy aop	73	294	169	61	43	29	18
CPI	% yoy eop	182	251	108	46	35	25	14
PPI	% yoy aop	72	355	186	72	41	38	24
PPI	% yoy eop	197	245	166	41	42	29	19
Exports (gs, USD)	% yoy	-10.8	-8.5	17.6	10.4	8.6	24.0	38.3
Imports (gs, USD)	% yoy	-7.8	-19.0	21.0	8.2	9.1	27.1	41.4
Current account	USD m	-1017	-194	-338	-394	-311	-424	-1043
Current account	% GDP	-14.9	-3.6	-3.9	-3.2	-2.1	-2.4	-4.6
FDI (net)	USD m	201	443	119	96	453	170	168
International reserves	USD m	339	305	357	347	457	474	770
Fiscal balance**	% GDP	-1.4	-2.9	-0.6	-1.6	-0.2	-1.6	0.1
Internal public debt	% GDP eop	4.9	5.7	4.5	4.5	4.6	6.0	5.6
External debt (total)	% GDP eop	51	42	24	20	20	19	17
Monetary base	% yoy eop	102	204	52	225	32	50	42
Exchange rate (official)*	USD aop	151	572	1035	1394	1784	2075	2160
Exchange rate (official)*	USD eop	430	925	1213	1580	1920	2156	2170
Spread***	% aop	224.0	128.2	44.4	0.8	0.0	0.0	0.0
Spread***	% eop	301.9	189.1	2.8	0.2	0.0	0.0	0.0
Exchange rate (official)*	EUR aop	--	270	651	1239	1690	2353	2686
Exchange rate (official)*	EUR eop	--	323	1097	1392	1989	2695	2956

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

** The fiscal balances for 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		