

BELARUSIAN MONTHLY ECONOMIC REVIEW



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- President of the Parliamentary Assembly of the Council of Europe has visited Belarus.
- The rate of economic growth in 2006 amounted to 9.9%.
- Conditions of oil supply to Belarus are settled.
- Merchandise trade deficit reached USD 1.9 bn.
- Excise taxes on oil products have been cut by 60%.
- The volume of household time ruble deposits decreased.

Politics: President of the Parliamentary Assembly of the Council of Europe has visited Belarus

In January, the Chairman of the Parliamentary Assembly of the Council of Europe, Mr. Renee van der Linden, has visited Belarus and conducted a number of meetings with officials and representatives of the opposition. Prospects for widening of Belarus-EU cooperation have been discussed, including the opening of the EU's Commission office in Minsk. According to van der Linden, if Belarus opts for democratization, the PACE has strong reasons to expect that the Parliament of the country will restore its special guest status with the organization. This might be an important step towards the development of political and economic cooperation between Belarus and the EU.

Real sector: The rate of economic growth in 2006 amounted to 9.9%

According to the Ministry of Statistics and Analysis data, the rate of GDP growth was 9.9% in 2006 (9.4% in 2005). The economic boom in manufacturing can explain these high rates of growth over the last two years. According to our estimates, manufacturing contributed to GDP rate of growth at a level of 4.6 percentage points in 2006 (4.1 percentage points a year ago). In its turn, more than 40% of rate of industrial output growth was provided by the contribution of the fuel industry. Apparently, this makes the economy dependent on the situation in the oil sector. In case of output stagnation in oil processing, the rate of GDP growth could decline by 2 percentage points.

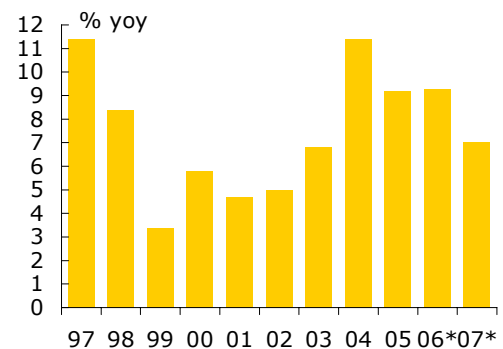
In 2006, contribution of investment to GDP growth has increased. According to the official statistics, investment increased by 31.4% in real terms (by 20% a year ago). However, the rate of investment growth in nominal terms was lower than in real terms although prices for the means of production went up by 9%. As for the financial sources of investment, the share of state expenditures and bank loans went up from 40.8% in 2005 to 44.5% in 2006. Nevertheless, given the expected repercussions of higher energy prices also for the public and the banking sectors, these sources of investment could become more constrained.

Structural trends: Conditions of oil supply to Belarus are settled

Energy sector: After a January oil supply conflict between Belarus and Russia, on January 12, the governments of two countries signed up a bilateral agreement on supply of crude oil and exports of processed oil. The Agreement stipulates collection of export duties by Belarus like it is done in Russia. In turn, the Russian Federation applies a duty on crude oil exported to Belarus. However, the duty is adjusted for a correction coefficient. In 2007, it is set at 0.293, in 2008 – 0.335, and in 2009 – 0.356. It is in this way the revenues from oil product duties exported to Belarus are to be distributed among the parties (Russia insisted on that during the

Population: 9.71 m
Industry / GDP: 27.6%
Agriculture / GDP: 7.5%
Investment / GDP: 24.3%
Export destination: Russia 35%, EU 46%
Import origin: Russia 59%, EU 22%

Real GDP growth



* Estimate for 2006 and forecast for 2007: IPM Research Center.

Source: Ministry of Statistics and Analysis.

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negotiations). However, Russia would have its share of revenues in advance when crude oil is supplied to Belarus.

On January 30, Belarus agreed with oil suppliers from Russia to use a new oil price formula. Now oil price for Belarus consists of world price plus oil duty set for Belarus. It is expected that the Russian budget would gain more than USD 1 bn by collecting this duty. In fact, windfall profit of Russian oil suppliers would be redirected to the Russian budget. For Belarus, the formula means that new oil price appears to be equal to the last year's price (due to the reduction of world prices of oil). Therefore, the introduction of oil duty in 2007 might not lead to higher imports prices in 2007.

Foreign trade: Merchandise trade deficit reached USD 1.9 bn

In Jan-Nov 2006, exports of goods increased by 23.5% yoy, while imports by 34.0% yoy. As a result, merchandise trade deficit reached the level of USD 1.9 bn (USD 0.5 bn in Jan-Nov 2005). More than 90% of the volume of the deficit comes from 'other intermediate goods', including raw materials and component parts. One of the major causes here is the reduction of the volume of exports of key intermediate goods, such as potash fertilizers and timber against the background of growing imports of intermediate goods.

Gas price hike and changing of conditions of oil supply imply a rise in the costs of imports of intermediate goods in 2007. But this can hardly be compensated by growing exports at a full scale. Therefore, merchandise trade deficit is very likely to increase over 2007. In order to finance this deficit, inflow on capital account could be required, such as foreign borrowing or foreign investment.

Public finance: Excise taxes on oil products have been cut by 60%

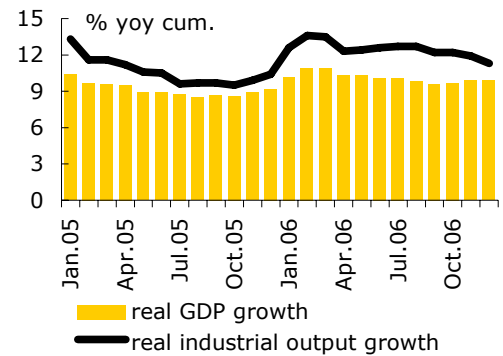
Over Jan-Nov 2006, an annual plan on revenues of the general government has been fulfilled at 97.7% (93.7% a year ago). The revenues amounted to BYR 34.5 trn, or 48.8% of GDP, and this is 0.4 percentage points more than over the same period of 2005. The share of expenditures has decreased by 0.6 percentage points, amounting to 45.4% of GDP (BYR 32.1 trn). The fiscal surplus reached 3.4% of GDP (2.3% a year ago).

The new conditions of oil supply imply that the Belarusian budget could gain from higher oil products export duties up to USD 1.9 bn in 2007 (USD 0.2 bn in 2006). A fraction of these revenues (USD 0.6 bn) would be refunded by the state to exporters via VAT refund schemes. Nevertheless, exporters would face a heavier tax burden. As a result, the government has introduced some changes into the tax system aimed at reduction of tax burden for exporters of oil products. Since January 1, 2006 excise taxes on oil products are cut by 60%, while some compulsory payments deducted from oil products revenues were terminated (such as contributions to the National Support Fund of Agricultural Producers and a tax on highway users). Thus, on the one hand, the budget revenues would grow at the expense of export duties, but on the other hand, they would decrease because of lower excise taxes and VAT refund. Even in case the overall volume of expenditures in 2007 is higher, the situation with execution of the budget can not be improved because of higher energy prices that lead to higher expenditures on the state budget.

Monetary policy: The volume of household time ruble deposits decreased

In December 2006, foreign currency market experienced agiotage-driven demand for foreign currency, partially caused

GDP and Industrial Output



Source: Ministry of Statistics and Analysis.

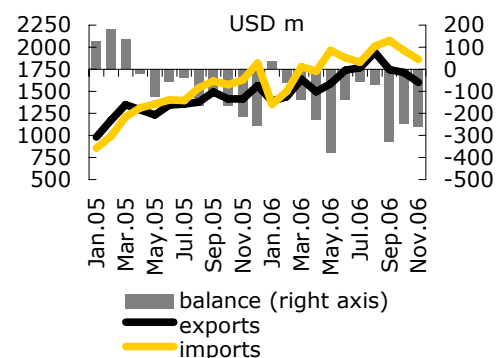
Contribution to Industrial Output Growth

Branches of industry:	2006	
	Growth rate*	Contribution**
Electric power	3.1	0.2
Fuel	23.1	4.7
Ferrous metallurgy	11.2	0.4
Chemical and petrochemical industry	6.9	0.7
Machinery and metalworking	10.0	2.2
Logging, woodworking, pulp and paper	2.9	0.1
Building materials	14.7	0.4
Light	2.6	0.1
Food	6.7	1.0
Other	12.4	1.4
Industry, total	11.3	11.3

* % yoy, ** percentage points.

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

Merchandise Trade



Source: Ministry of Statistics and Analysis.

Exports and Imports of Merchandise Groups in Jan-Nov 2006, USD bn

Merchandise groups:	exports	imports	balance
Investment goods	2.2	2.1	0.1
Intermediate goods	12.8	14.3	-1.5
Energy goods	6.8	6.6	0.2
Other intermediate goods	5.9	7.7	-1.7
Consumer goods	3.0	3.3	-0.3
Food and meal	1.3	1.3	0.0
Non-food goods	1.7	2.0	-0.3
Total	18.1	19.9	-1.9

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

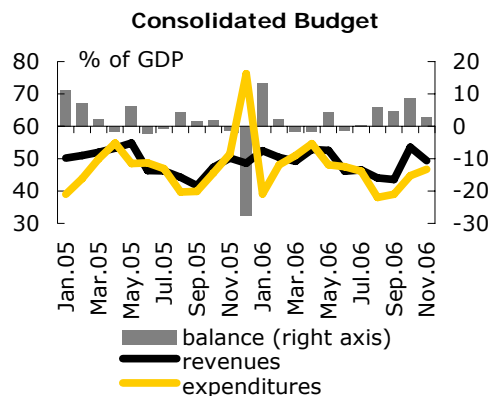
by the energy conflict between Belarus and Russia. As in the course of previous months, commercial banks played the major role in satisfying this growing demand for foreign currency by reducing the volumes of foreign assets and increasing currency supply at the domestic market. In turn, net foreign assets (NFA) of banks decreased by USD 691 m, while the volume of NFA of the monetary authorities went down by just USD 15 m (1% mom). In December, the traditional cause of growth of money supply was the reduction of government ruble balances held at the NBB (by 33.2% mom) caused by growing state expenditures at the end of the year. However, in December 2006, the volume of government deposits in the NBB reduced at a lesser scale than in December 2005. As a result, over December, monetary base increased by 18.0% mom, but in annual terms its change was much more moderate than in November or in 2005, namely 19.8% yoy (41.0 and 73.7% yoy in November 2006 and in 2005, respectively).

A seasonal boost in business activity in December informed a high demand for loans. Rate of loan growth had been increasing to reach 57.2% yoy (55.4% yoy in November). At the same time, expanding business activity provided an increase for the banks' resource base at the expense of transferable enterprise deposits. Besides that, an important source of bank liabilities were funds returned from abroad. Accordingly, at loan and deposit market, only some minor adjustments of interest rates were recorded. However, against the background of negotiations with Russia, the households reduced its demand for Belarusian rubles, preferring to save in foreign currency. As a result, time ruble deposits of the households decreased in December by 1.3% mom, while in annual terms, their rate of growth slowed down to 47.9% yoy (54.6% yoy in November). In contrast, the rate of foreign currency deposit growth was 33.5% yoy (29.9% in November). Next, the growth rate of cash in circulation amounted to 39.8% yoy (46.0 yoy in November). The ruble money supply increased in November by 8.5% mom, while the broad money went up by 7.5% mom. In annual terms, their growth rates amounted to 44.5 and 39.3% yoy, respectively (51.3 and 42.2% yoy in November).

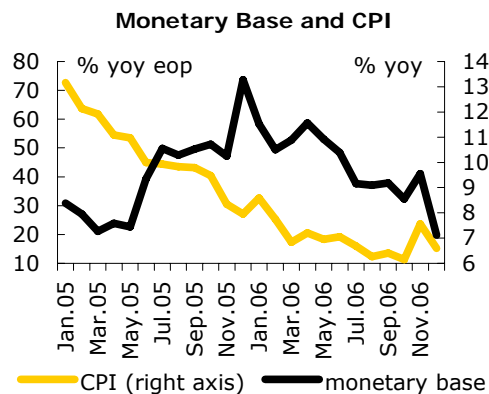
Consumer prices in December increased by 0.8% mom, while in annual terms inflation rate was 6.6% yoy, thereby returning to its October level. Gasoline price increase has been the most notable and much higher than recorded inflation rate: by 4.7% mom in December or by 22.4% yoy. The exchange rate remained unchanged at the level of 2140 BYR/USD.

Banking sector: Three commercial banks from free economic zones are deprived of their licenses

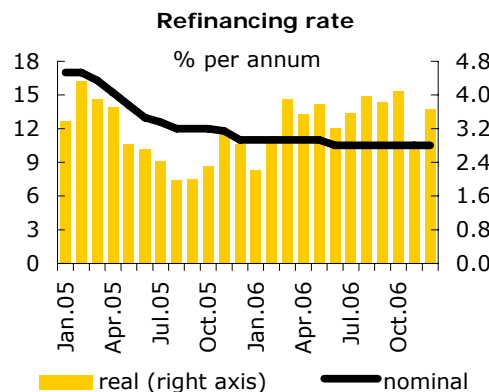
At the end of December – early January, the NBB recalled the general licenses of three banks from free economic zones: 'Atombank' JSC, 'Meszdunarodnyi Rezervnyi Bank' JSC, and 'Investprombank' JSC. The reason behind that was non-compliance with own capital minimum requirements set at the level of EUR 5 m. Prior to that requirement, banks with EUR 0.5 m of own capital were allowed to register in free economic zones. However, this preferential treatment was abolished at the end of 2005 and general regulations of banking activity were applied by the NBB. The activity of these banks was focused on serving resident companies of free economic zones, while only 'Meszdunarodnyi Rezervnyi Bank' JSC had a deposit license. Since these three banks had not been playing any notable role in the banking system as a whole and only conducted some small-scale operations at the inter-bank market, their liquidation does not produce any serious impact on the financial sector of the country.



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



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



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

Economic Trends		Q1 05	Q2 05	Q3 05	Q4 05	Q1 06	Q2 06	Q3 06	Q4 06	Oct 06	Nov 06	Dec 06
GDP growth	% yoy	9.9	8.4	8.7	10.7	11.0	9.6	8.6	10.8	--	--	--
GDP growth	% yoy cum.	9.9	9.1	9.0	9.4	11.0	10.3	9.6	9.9	9.7	9.9	9.9
Industrial Production	% yoy cum.	11.7	10.3	9.7	10.5	13.5	12.6	12.2	11.3	12.2	11.9	11.3
Agricultural Production	% yoy cum.	12.5	10.1	3.0	2.1	10.1	6.9	2.2	6.1	3.7	5.6	6.1
CPI	% yoy eop	11.9	10.0	9.8	8.0	6.8	7.0	6.4	6.6	6.2	7.6	6.6
PPI	% yoy eop	14.2	12.1	10.5	10.2	8.3	8.1	8.0	8.5	7.7	7.8	8.5
Merchandise export (USD)*	% yoy	21.8	17.2	15.1	11.5	27.5	24.9	29.3	--	21.5	13.2	--
Merchandise import (USD)*	% yoy	0.6	3.6	7.8	-5.3	51.3	37.0	30.0	--	24.6	14.2	--
Merchandise trade balance (NBB data)	USD m cum.	452	345	43	-527	-134	-785	-1220	--	-1449	-1683	--
Current account	USD m cum.	723	945	989	469	126	-305	-492	--	--	--	--
Current account	% GDP cum	12.1	7.3	4.6	1.6	1.7	-1.9	-1.9	--	--	--	--
International reserves	USD bn eop	975	1130	1189	1297	1290	1154	1155	1383	1279	1369	1383
Monetary base	% yoy eop	21	39	50	74	53	48	38	20	32	41	20
Lending rate**	% p.a. aop	19	15	14	12	12	11	12	12	12	12	12
Exchange rate (official)	USD aop	2164	2151	2150	2150	2151	2146	2142	2141	2141	2140	2140
Exchange rate (official)	EUR aop	2840	2713	2623	2558	2587	2694	2729	2761	2701	2755	2827

* Growth rates in value terms (source: Ministry of Statistics and Analysis).

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

Sources: Ministry of Statistics and Analysis, NBB.

Key Economic Indicators		2000	2001	2002	2003	2004	2005	2006
Nominal GDP*	BYR trn	9.134	17.173	26.613	36.565	49.991	65.067	79231
Nominal GDP**	USD bn	8.7	12.1	14.5	17.7	23.1	30.2	36.9
GDP Growth	% yoy	5.8	4.7	5.0	7.0	11.4	9.4	9.9
Industrial production	% yoy	7.8	5.9	4.5	7.1	15.9	10.5	11.3
Agricultural production	% yoy	9.3	1.8	0.7	6.6	12.6	1.7	6.1
CPI	% yoy aop	168.6	61.1	42.6	28.4	18.1	10.3	7.0
CPI	% yoy eop	107.5	46.1	34.8	25.4	14.4	8.0	6.6
PPI	% yoy aop	185.3	72.1	41.4	37.5	24.1	12.1	8.3
PPI	% yoy eop	166.4	40.9	42.7	28.1	18.8	10.0	8.5
Exports (gs, USD)	% yoy	17.6	10.4	8.6	24.0	38.3	15.6	--
Imports (gs, USD)	% yoy	21.0	8.2	9.1	27.1	41.4	4.0	--
Current account	USD m	-338	-394	-311	-424	-1206	469	--
Current account	% GDP	-3.9	-3.2	-2.1	-2.4	-5.2	1.6	--
FDI (net)	USD m	119	96	453	170	163	303	--
International reserves	USD m	357	347	457	474	770	1297	1383
Fiscal balance	% GDP	-0.6	-1.6	-0.2	-1.6	0.0	-0.6	--
Domestic public debt	% GDP eop	4.5	6.1	5.4	5.5	5.7	5.8	6.5
External dent (total)	% GDP eop	24.4	24.8	27.0	23.7	21.4	17.9	--
Monetary base	% yoy eop	52	225	32	50	42	74	20
Exchange rate (official)*	USD aop	1035	1394	1784	2075	2160	2154	2145
Exchange rate (official)*	USD eop	1213	1580	1920	2156	2170	2152	2140
Spread***	% aop	44.4	0.8	0.0	0.0	0.0	0.0	0.0
Spread***	% eop	2.8	0.2	0.0	0.0	0.0	0.0	0.0
Exchange rate (official)*	EUR aop	651	1239	1690	2353	2684	2681	2692
Exchange rate (official)*	EUR eop	1097	1392	1989	2695	2956	2550	2817

* On January 1, 2000 the Belarusian ruble was denominated 1:1000. All figures for 1999 are given in 'new' Belarusian rubles.

** For the period of 1999–2000, GDP in USD is calculated by using the market (unofficial) exchange rate (source: IPM Research Center).

*** Spread between the black market and official (NBB) exchange rates (source: IPM Research Center).

Sources: Ministry of Statistics and Analysis, Ministry of Finance, NBB, IPM Research Center.

Notes:

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