



- *Improvements in the business environment, implemented since 2006, have helped the private sector to expand, but post-recession recovery remains weak, especially in terms of corporate lending.*
- *Private firms continue to identify access to finance as one of the key binding constraints to their growth.*
- *To improve access to finance, systemic policy measures are needed, first of all improving the legal frameworks for insolvency and secured creditors' rights protection, setting up a framework to resolve non-performing loans in line with best international practices, and developing non-banking financial sectors.*

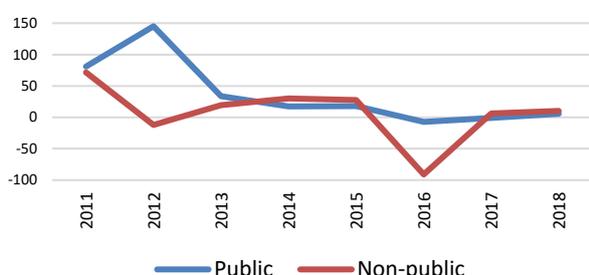
Business Environment, Credit Supply, and the Private Sector Development

While the public sector dominates the economy and employment in Belarus, the share of the private sector has gradually been increasing. The share of the private sector (firms with full and majority of private ownership) in GDP has increased from roughly 30 percent in 2008-2010 to more than 40 percent from 2016 onwards, while the share of private sector employment (excluding individual entrepreneurs) grew by 1.9 percentage points annually to reach 31.6 percent in 2016 and further in 2017-2018. During 2011-2016, the number of registered private companies¹ was growing on average by 3.4 percent per year to account for 82.2 percent of all legal entities by 2016. Between 2012 and 2018, the number of micro- and small-sized companies (MSEs), which are nearly all private, has increased by 12 percent, falling during the recession, but resuming growth afterwards.

Improvements in the business environment, introduced since 2006 have supported the expansion of the private sector. Quantitative estimates establish a strong positive association between simpler conditions for opening and running a new private company and the creation of new micro- and small-sized enterprises. In particular, during the pre-recession period of 2006-2014, broader liberalization measures, captured by the progress in the World Bank's *Doing Business* (DB) rankings and the distance-to-frontier scores, were positively correlated with the number of MSEs. Since then, most progress has been achieved in the areas of business and property registration, licensing and inspections, and especially in the reduction of the costs of tax administration. As a result, in 'Paying Taxes', Belarus moved from the bottom of the list in 2010 to the 99th place in the 2020 rating.

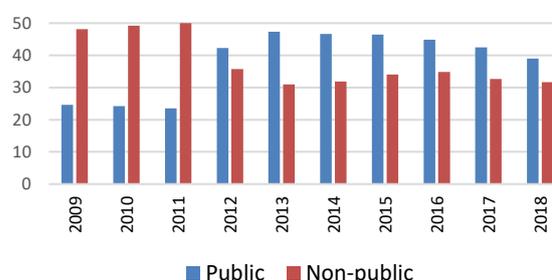
During the 2015-2016 recession, lending to the private sector fell more sharply than to the public sector, and both are recovering at low rates (Figure 1). With decelerating inflation and falling real interest rates, credit supply has been skewed towards the public sector. The share of private credit to GDP was as low as 23 percent in 2018. The share of the public sector in the stock of outstanding loans increased from about one-fourth in 2011 to almost 40 percent by 2018 (Figure 2). These dynamics were partially driven by the effects of BYN depreciation vis-à-vis USD in 2011 and 2014, which increased the nominal value of loans denominated in foreign currency. Often, such loans have been provided to State-Owned Enterprises (SOEs) within the framework of "state programs" for upgrading production facilities from 2009 onwards. Although the flow of directed lending has gradually reduced from BYN 2.8 billion in 2016 (3 percent of GDP) to BYN 1.24 billion in 2018 (1 percent of GDP), subsidized loans to SOEs still account for about one-third of the total credit stock. These loans do not only entail credit, but also currency risks.²

Figure 1. Change in the stock of outstanding loans in nominal terms, y/y percent



Source: Calculations on the basis of NBRB data (Statistical Bulletin)

Figure 2: Sectoral shares in the stock of outstanding loans, percent



Source: Calculations on the basis of NBRB (Statistical Bulletin)

Access to Finance in Belarus: Perceptions and Policy Options

According to recent survey results,³ access to finance remains the second biggest obstacle for private firms in Belarus. In the 2018 Business Environment and Enterprise Performance Survey (BEEPS), while only 6.1 percent of surveyed firms mentioned access to finance as a constraint in 2008, this share increased to 18 percent on average by 2013, being

higher among manufacturing firms – 23.7 percent. In 2018, this pattern changed marginally – to reach 17.1 and 22.1 percent, respectively. However, business environment reforms have resulted in a dramatic drop in the percentage of firms highlighting issues with business licensing and permits – from 14.6 percent in 2008 to just 6.7 percent in 2013.

While the majority of firms in Belarus indicate the need for commercial loans, they tend to finance their investments internally, using lending to scale up their working capital. A snapshot of the BEEPS results show that about 40 percent of firms have a loan or rely on a credit line, which is close to the Europe and Central Asia (ECA) average of 37/6 percent. Almost a half of surveyed firms – 45.7 percent – indicated they need a loan to finance working capital (31.1 percent), rather than investment (23.5 percent). At the same time, the vast majority of companies' investments – 83.4 percent – are funded internally, significantly above the ECA average of 74.8 percent. Also, some non-standard financing instruments, such as supplier or customer credit, are practically not used in Belarus – only 8 percent of surveyed firms mentioned the use of such an instrument, in contrast to 24.4 percent in ECA countries.

Statistical data on financing of investment support BEEPS results. Over 2016-2018, about 40 percent of investments were funded by companies themselves, while the share of bank lending fell from 26.5 percent in 2012 to 13.9 percent in 2018. At the same time, the share of budget financing (central and local budgets) increased from 16 percent in 2012 to 25 percent in 2017. The share of investment funded from loanable funds of other economic entities also tends to be very small and falling – from 1.5 percent in 2012 to just 0.8 percent in 2018.

Among firms, SMEs are most credit-constrained, indicating a need to further facilitate financial intermediation for this segment. The domestic surveys, conducted by the IPM Research Center,⁴ confirm – during 2010–2018 and 2019 – that a large share of SMEs, and especially young firms, are credit-constrained, with high interest rates mentioned as the main obstacle (40 percent of surveyed companies). Young firms often do not have enough collateral and may operate in unfamiliar areas, bringing in information asymmetries and risks, discouraging bank lending. While direct government interventions in improving access to finance is more limited than often believed, a properly-designed and priced credit guarantee scheme can be broadly considered catalytic and a useful tool in supporting SME financing.

Limited access to finance, and especially long-term finance, is a byproduct of structural rigidities in the economy. Private SMEs – about 44.3 percent of surveyed firms in 2019 – point to the absence of a level-playing field, stemming from a policy bias towards SOEs. This is also due to the legacies of directed lending, mostly through state-owned banks, which distorted the operation of the financial system by splitting it into subsidized and non-subsidized parts. While in the past commercial banks could partially cover their losses from lending to SOEs below market rates by charging higher interest rates from non-privileged borrowers, the current context of lower real interest rates and reduced volumes of directed lending weaken such capacity.

Access to finance in Belarus can be facilitated by strengthening legal protection of secured creditors' rights, improving legislation on insolvency and secured transactions, along with setting up a framework to resolve non-performing loans in line with best international practices. It is becoming important to improve legal protection of rights of secured creditors, including by the means of prioritizing claims within enforcement and insolvency procedures as well as banning collateral seizure in case debtors have other property, along with improvements of debt collection procedures. Also, a workable framework for the resolution of non-performing loans – established in line with best international practices – may lead to a reduction of provisions applied to risky loans by commercial banks to cover possible losses, as well as limit the practice of loan evergreening. Taken together, these measures can create more enabling conditions for the expansion of bank lending through lower interest rates.

Furthermore, developing the non-banking sector can further enable access to finance. This sector includes insurance, leasing, and factoring, which can introduce alternative sources of funds for private firms. Building capacity of domestic institutional investors, such as pension funds and insurance companies, and facilitating the entry of foreign institutional investors will increase the availability of long-term finance and support the development of the capital market. An active and sizable capital market can play a bigger role in mobilizing domestic resources to finance long-term needs for private firms; unlocking more investment opportunities for all firms, in particular SMEs.

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¹ Private companies include 100 percent privately-owned firms, without mixed ownership enterprises. However, it includes foreign companies and mixed private-foreign ownership companies. Accordingly, the public sector includes companies fully and partially owned by the state.

² GET Belarus, Issue No. 58 | May – June 2019.

³ 'Business Environment and Enterprise Performance Surveys' (BEEPS), conducted jointly by the World Bank and the European Bank for Reconstruction and Development. Business owners and top managers in 600 firms were interviewed from October 2018 through April 2019. The survey focus on perception of factors that can be accommodating or constraining for firms and play an important role for an economy's private sector.

⁴ <http://www.research.by/publications/surveys-of-business/>.