



- **Recession in Russia and low commodity prices have had a major impact on Belarus's economy, which contracted by 3.9 percent in 2015, the first recession in two decades.**
- **Real GDP is projected to decline in both 2016 and 2017 in light of the weak external environment and structural rigidities, while significant vulnerabilities arise from external financing needs going forward.**
- **The poverty impact of the recession has remained muted so far, although households' disposable incomes are expected to deteriorate.**

Recent Economic Developments

Real GDP contracted by 3.9 percent in 2015, the first recession in two decades. The external environment has deteriorated considerably, leading to a sharp reduction in total exports of goods and services by 24.1 percent, while imports contracted by 25.4 percent. In particular, exports of goods to the Russian market dropped by 26 percent due to the slowdown in Russia, contributing to a decline in Belarusian industrial output, which fell by 6.6 percent. Given faltering exports and sizeable debt repayments in foreign currency coming due, macro policies have been tightened to narrow external and fiscal imbalances. Gross fixed investment fell by 15.2 percent due to cuts in public capital expenditures and containment of directed lending.

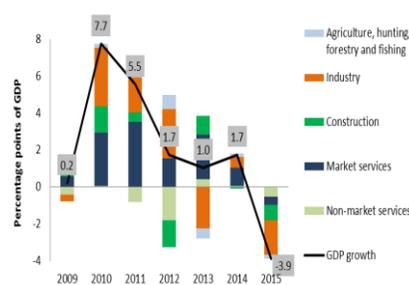
The Belarusian Ruble has depreciated considerably, helping to maintain external balances in the face of faltering exports. During 2015, the Belarusian Ruble (BYR) depreciated by 36 percent against the US dollar and by 19 percent vis-à-vis the Russian Ruble (RUR). The current account deficit narrowed from 6.7 percent of GDP in 2014 to 3.8 percent of GDP in 2015. Exchange rate policy has responded to deteriorating conditions in Russia, where the RUR has depreciated considerably in tandem with oil prices. Foreign reserves, excluding gold, stood at \$2.5 billion at end-March 2016, covering 0.9 months of imports of goods and services.

The recession in 2015 helped contain inflationary pressures, although nominal broad money growth exceeded the 30 percent target set by the National Bank of the Republic of Belarus. Annual inflation stood at 13.5 percent in 2015, well below the 18±2 percent target and also lower than the 18.1 percent inflation observed in 2014. Twelve-month inflation slowed further to 12.4 percent by March 2016.

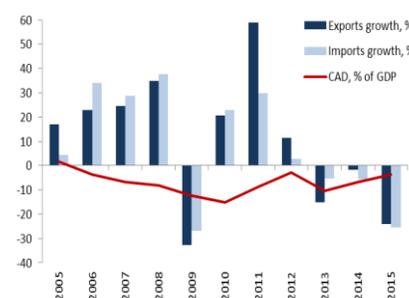
Capital expenditures were cut sharply in 2015 to maintain a budget surplus and meet repayment obligations. Revenues from corporate income tax, VAT, and excise taxes fell due to economic weakness, but were more than offset by foreign trade tax gains from the reintroduction of export duties on potash fertilizer and from an agreement with Russia to retain export duties on oil products. Nevertheless, fiscal pressures persisted due to debt service obligations and current expenditures. Foreign debt payments (of \$2 billion) were refinanced in part by new loans from the Russian government and commercial banks. In light of the constrained financing environment, capital expenditures were cut sharply (by 26 percent in real terms) to maintain a budget surplus. As a result, the general government surplus in 2015 was 1.5 percent of GDP.

The labor market is under stress due to weak performance of the construction, industrial and agricultural sectors. State-owned enterprises (SOEs) as a whole did not shed labor, but rather shortened the working week. Reduction of real wages and incomes, by 3.1 and 5.9 percent, respectively, led to a contraction in private consumption by 3.3 percent. Yet, the Government has prevented a rise in poverty by spending more on targeted social assistance as the number of applicants increased. Measured at the international standard of PPP \$ 5/day, poverty in Belarus remains low at below 1 percent of the population.

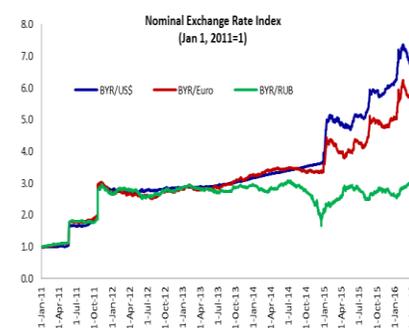
Contribution to GDP Growth in percent



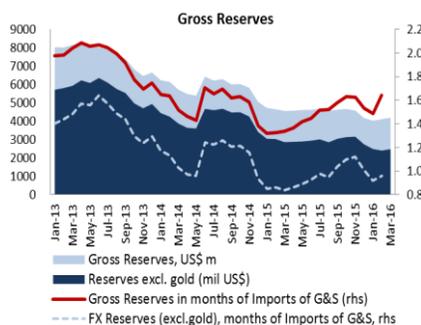
Nominal Growth of Exports and Imports and Current Account Deficit



Index of Nominal Exchange Rates



International Reserves and Reserves in Months of Imports of Goods and Services



Source: World Bank Staff calculations based on Belstat and NBRB data.

Medium-term Outlook

The economic outlook is affected by low oil prices, weaker prospects for growth in Russia and other trading partners, and structural bottlenecks in Belarus. The external shocks will continue to have an enduring impact on the Belarusian economy, with real GDP projected to contract by 3 percent in 2016 and by 1 percent in 2017. This is based on an oil price forecast of \$41 per barrel in 2016 and \$50 in 2017 and a continued weak outlook for the Russian economy. Progress on structural reforms would bolster medium-term prospects in Belarus, but growth is unlikely to pick up immediately because of lags in diversifying products and markets, particularly for SOEs. Risks remain considerable. A steeper slowdown in foreign markets could lead to a sharper recession, particularly since mineral products and fertilizers account for more than a third of total exports.

Further monetary and fiscal tightening may be necessary to adjust to external shocks, adding to contractionary pressures. Limited access to external financing and increasing losses in the SOE sector constrain the space for countercyclical policies. Continued distress in the SOE sector will constrain employment creation and job transition. Existing unemployment benefits are low, while the Government plans on expanding them have not yet been clarified.

External financing needs are substantial because of maturing foreign liabilities, low reserves, and weak exports. The current account deficit is projected to average 3 percent of GDP in 2016-2017 compared to 5.2 percent in 2014-2015. Repayments of foreign currency-denominated public debt is estimated to be \$3.3 billion in 2016, of which one-third is due to domestic residents. As the level of international reserves is low, identifying adequate levels of external financing will be critical. The Government recently signed a \$2 billion program with the Eurasian Fund for Stabilization and Development and is seeking official financing assistance from the IMF (up to \$3 billion) to support international reserves and debt service obligations.

Growth can be spurred by appropriately sequenced reforms, supported by international partners and investors. Restructuring the SOEs is essential to reduce distortive state interventions and improve firms' performance. Companies in the public sector should move away from imposed quantitative and employment targets toward productivity and profitability, with their managerial autonomy strengthened by appropriate corporate governance arrangements. More enabling policies for the development of the private sector can help to raise productivity and employment growth in the Belarusian economy.

Structural reforms will need to be accompanied by improved unemployment benefits and social assistance. A reduction in government directed lending and enterprise restructuring will likely increase layoffs in the short term, for which revamping the current unemployment benefits system will be important. Furthermore, additional targeted social assistance will be important in helping relatively poorer households cope with increases in utility tariffs. Appropriate modalities of support have yet to be designed and implemented.

Key Macroeconomic Indicators

	2013	2014	2015	2016f	2017f	2018f
<i>GDP by components, annual growth in constant prices unless otherwise stated</i>						
GDP, at constant market prices	1.0	1.7	-3.9	-3.0	-1.0	0.3
Private Consumption	10.8	4.4	-3.0	-1.5	-0.5	0.2
Government Consumption	-2.0	-1.8	-1.8	0.0	0.3	0.1
Gross Fixed Capital Investment	3.8	-8.8	-8.6	-9.2	-2.0	0.8
Inflation (Consumer Price Index)	18.3	18.1	13.5	14.0	13.0	11.5
Merchandise exports, % change (nominal \$)	-13.7	8.2	-24.1	-21.9	-2.9	-1.6
Merchandise imports, % change (nominal \$)	-8.6	-7.5	-25.6	-12.0	-7.0	1.3
Current Account Balance, % of GDP	-10.4	-6.7	-3.8	-2.8	-3.0	-3.1
General Government Revenues, % of GDP	41.1	40.5	42.6	41.5	41.9	43.8
General Government Expenditures, % of GDP	41.0	39.4	41.1	41.3	41.5	43.1
Fiscal Balance, % of GDP 1/	0.1	1.1	1.5	0.2	0.4	0.7
Poverty rate (\$5.00 a day, PPP terms)	0.44	0.31	0.36	0.37	0.38	0.37

Source: Belarusian authorities and World Bank staff projections.

Annual percentage change, unless otherwise noted; f=forecast

1/Fiscal Balance does not include extra-budgetary and quasi-fiscal expenditures.

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