

Rating-Agentur Expert RA confirmed at ‘B’ the rating of Belarus. The rating outlook is positive.

Rating-Agentur Expert RA confirmed the sovereign government credit rating (SGC) of Belarus at ‘B’ (Moderately low level of creditworthiness of the government) in national currency and at ‘B’ (Moderately low level of creditworthiness of the government) in foreign currency. The rating outlook is positive which means that in the mid-term perspective there is a high probability of upgrading the rating.

MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:**Positive factors:**

- Despite the failure of the planned receipt of new tranches from Russia and the EFSD¹ in the total amount of USD 800 m, current repayments and servicing of public debt in 2019 were made immediately. In 2020, the expected short-term obligations will amount to BYN 7,6 bn or 5,8% of GDP. In our opinion, given the current accumulated foreign exchange reserves of USD 5,6 bn as of December 2019, and the absence of obstacles to new borrowings in the external markets, Belarus will not experience liquidity problems and will be able to service the public debt;
- After a significant improvement of the fiscal position in 2017-2018 with a consolidated budget surplus² of 3% and 4%, respectively, in 2019, the budget execution was performed in challenging conditions, which included a decline in refining production due to contaminated Russian oil, as well as a decrease in export duties due to the Russian tax maneuver. However, owing to the compensating dynamics of potash prices and conservative execution of expenditures, we estimate that the surplus will remain at 1% of GDP. However, given the planned off-balance expenditures, including the construction of the Belarusian NPP³, the deficit of the adjusted consolidated budget may reach 3-4% of GDP compared to a surplus of 0,2% in 2018. In the medium term 2020-2021, the scope for maintaining the surplus will narrow, considering the existing oil shocks to the economy, as well as the need to support the natural growth of social spending, especially before the presidential elections in 2020;
- Positive signal to mitigate possible external shocks is the steady growth during 2019 of the international reserves due to FX purchases by the National Bank of the Republic of Belarus (NBRB) and higher gold prices. Thus, international reserves increased to USD 9,4 bn as of December 2019 from USD 7,1 bn at the beginning of the year. The accumulated international exchange reserves allow covering 2,5 months of imports and can be partially used to meet short-term government credit obligations;
- Largely due to its close economic integration with Russia, Belarus shows a moderately high level of economic development with GDP per capita in PPP terms USD 20,6 th in 2019 and the level of investment in human capital⁴ at 0,765 in 2018, which is higher than in other non-oil CIS countries.

Restricting factors:

- After several consecutive years of strong growth, the economy of Belarus has recovered

¹ The Eurasian Fund for Stabilization and Development.

² Excluding off-budget expenses (including expenses for NPP construction).

³ Belarusian nuclear power plant.

⁴ Inequality-adjusted Human Development Index.

to the level of 2015 and started to slow down from the end of 2018. At the beginning of 2019, the growth rate was projected to halve from 3% in 2018 down to 1,5% amid weakening external demand for export goods and deteriorating consumer demand. However, a number of factors affected one of the main pillars of the economy – oil production, which led to a slower growth rate of 1,1% for 10M 2019. Accordingly, we have narrowed our estimates to 1,2% for 2019. Moreover, we do not see any potential for faster growth in the medium term due to the absence of an agreement on compensation for the Russian tax maneuver, as well as the structural problems hampering the development of an economy focused on inefficient SOEs;

- Amid the conservative debt policy and strengthening of BYN, the level of gross government debt⁵ declined slightly during the year and, according to our estimates, will not exceed 43% of GDP in 2019, which is lower compared to 47,8% in 2018. Despite the favorable structure and maturity of the debt, most of which fall on bilateral loans from foreign governments and international financial institutions, high concentration risks and foreign exchange risks persist. Russia and its related institutions account for more than 60% of external debt, and tense disputes between countries create uncertainties in the further refinancing of current debt. Additionally, more than 91% of direct government debt is denominated in foreign currency, which may worsen the debt position if external imbalances widen;
- Over the past few years, the monetary authorities have made significant progress in achieving price stability by adhering to inflation targeting, a floating exchange rate regime, liberalization of currency legislation and abandonment of preferential directive lending to SOEs. As a result, the historic inflation levels in 2018 were renewed below the 5% target level. At the end of 2018, inflation has accelerated, largely due to short-term factors: rising food and fuel prices. However, in 2H 2019, inflation has returned to its target, and the NBRB has switched its policy from a neutral measure to an accommodative stance, reducing the refinancing rate twice from 10% to 9%. We expect that in 2020, inflation will be around the 5% target on the back of subdued domestic demand and less external pressure on prices. At the same time, we consider that the transmission mechanism is still ineffective due to the high dollarization of the banking system and underdeveloped domestic capital market. Besides, the NBRB is limited in making key decisions and is subject to political influence;
- The level of institutional development is supported by the moderate quality of the business environment: moderately high 37th position in the Doing Business ranking 2019 and the moderate corruption perception index - 44 (70th place out of 180 countries in 2018). On the other hand, the government's lack of independence from political influence is reflected in the low government effectiveness and rule of law indexes of -0,83 and -0,35 respectively as of 2017.

Negative factors:

- The risk of contingent liabilities' materialization persists. As of September 2019, external debt obligations of legal entities with 50% or more state ownership accounted for 11% of GDP. The state-owned sector, especially banks, continues to dominate the Belarusian economy, concentrating about 50% of the total workforce and value-added. At the same time, SOEs remain inefficient and need to be reformed. Besides, the full-scale launch of privatization is constrained by the lack of political will, weak corporate governance and low transparency of SOEs' reporting. There are plans to sell several state banks' shares to the EBRD, but these projects are insignificant in volume and are still under discussion;
- The local capital market remains weak, characterized by low capitalization: joint-stock companies did not exceed 7% of GDP as of the end of 2019, and concentration remains high, as the 10 largest issuers account for more than 99% of the overall market capitalization. At the same time, the volume of shares' trading fell by 44% y-o-y as of 1H

⁵ Includes direct and guaranteed debt of the central government and local government, and SDRs distributed to the Republic of Belarus.

2019. Capital market development is hampered by the lack of progress in structural reforms of the public sector, as well as the lingering practice of directed lending and subsidizing the economy. The share of corporates bonds remains negligibly small; the volume of trading in 1H 2019 did not exceed 11,5% of the total volume;

- Although banks' assets grew by 8,1% y-o-y as of 3Q 2019 primarily due to active consumer lending, the banking sector is still weak with total assets estimated at around 59% of GDP and domestic credit at 41% of GDP in 2019. The sector is characterized by high concentration risks: the share of the three largest banks is slightly over 60%, the share of SOBs also reached about 60% as of September 2019, which hinders effective development and competition. The level of NPLs increased by 0,9p.p. up to 5,03% y-o-y as of September 2019. In our opinion, the real volume of troubled assets may be higher, as, in the case of SOEs, payments on problem loans tend to be covered by the Government. Besides, the high share of FX loans creates risks of increasing the credit burden in the case of BYN devaluation. However the financial soundness indicators remain robust with capital adequacy ratio at 18,4%, and efficiency metrics ROA and ROE stood at 1,7% and 11,3% as of September 2019 respectively.

Stress factors:

- The risks for the creditworthiness stem from the direct and indirect dependence on the relationships with Russia, as well as the economic and political situation of this major trading partner and creditor (weak stress-factor);
- Although the share of banks' FX-denominated assets and liabilities continues to decline, dollarization in Belarus remains one of the highest among the peers' countries of the region, at 45% and 56,1% for loans and deposits, respectively as of September 2019. The current FX exposure significantly limits the effectiveness of monetary policy and increases the sensitivity of the economy to fluctuations in the exchange rate of the national currency (moderately weak stress-factor).

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Achieving favorable agreements with partners on oil and gas supplies and prices, financial compensation for adverse effects of the tax maneuver in oil industry from the Russia;
- Strengthening and further development of the banking system and mitigation of concentration risks;
- Outstanding and gradual improvement of financial dollarization levels.

The following developments could lead to a downgrade:

- Changes in the format of bilateral relations and agreements on a range of economic issues with Russia, which may lead to economic shocks with a worsening of the budget and external position;
- Deterioration of the fiscal position due to materialization of contingent liabilities or deviations from the restrained fiscal policy.

“The Agency confirmed the credit ratings of the Republic of Belarus at ‘B’ with a positive outlook. These are supported by improved macroeconomic stability, as evidenced by the success in containing inflation, reduced volatility of the exchange rate as a result of the introduction of the floating exchange rate regime and strengthened international reserves. In addition, we observe prudent fiscal policy and reduced government indebtedness.

Nonetheless, economic growth is slowing down with weak medium-term prospects amid the uncertainty about the compensation of losses caused by the Russian tax maneuver. The consequences of higher oil import costs will also weigh negatively on the government budget and

balance of payments. The rating continues to be constrained by a weak local financial market, which, along with still high dollarization levels, limits the monetary transmission mechanism.

We keep a positive outlook on the ratings, reflecting the high probability of an upgrade, while maintaining macroeconomic stability, continued decline in dollarization, and the absence of shocks to the budget and external position in case of changes in the character of the current economic ties with Russia.” – Clarified Denys Anokhov, Rating Analyst of Rating-Agentur Expert RA.

Research report on Belarus is available at:

https://raexpert.eu/reports/Research_report_Belarus_10.01.2020.pdf

Next scheduled rating publication: TBD in December 2019. The full sovereign rating calendar can be found at [Sovereign Rating Calendar 2020](#)

For further information contact:

Responsible expert:

Denys Anokhov, Rating Analyst of Rating-Agentur Expert RA

+49 (69) 3085-45-00, ext. 1210

anokhov@raexpert.eu

Reviewer:

Vladimir Gorchakov, Associate Director of Rating-Agentur Expert RA

+49 (69) 3085-45-00, ext. 1211

gorchakov@raexprert.eu

Rating-Agentur Expert RA GmbH

Walter-Kolb-Strasse 9-11,

60594 Frankfurt am Main, Germany

+49 (69) 3085-45-00

E-mail: info@raexpert.eu

www.raexpert.eu

RATING HISTORY:

Date	Review reason	SGC		Outlook	
		National currency	Foreign currency	National currency	Foreign currency
12.07.2019	Scheduled revision of both types of ratings for the country	B	B	Positive	Positive
18.01.2019	Scheduled revision of both types of ratings for the country	B	B-	Positive	Positive
20.07.2018	Scheduled revision of both types of ratings for the country	B	B-	Positive	Positive
26.01.2018	Scheduled revision of both types of ratings for the country	B	B-	NA	NA
28.07.2017	Scheduled revision of both types of ratings for the country	B	B-	NA	NA
03.02.2017	Scheduled revision of both types of ratings for the country	B	B-	NA	NA
05.08.2016	Scheduled revision of both types of ratings for the country	B	B-	NA	NA
04.03.2016	First assignment of both types of ratings	B	B-	NA	NA

Minute's summary

The rating committee for Belarus was held on 10 January 2020. The quorum for the rating committee was present. After the responsible expert presented the factors, which influenced the rating assessment, the members of the committee expressed their opinions and suggestions within the framework of the Sovereign methodology. The chairman of the rating committee ensured that every member of the committee expressed his/her opinion before proceeding to the voting.

The following methodology was used for the rating assessment: [Methodology for Assigning Sovereign Government Credit Ratings – Full Public Version](#) (from April 2019). Descriptions and definitions of all rating categories can be found under the [Rating scale](#) section. The user of the rating shall read the methodology in order to have a full understanding of the rating procedure.

The definition of default can be found on the Agency's website in the section for [Internal policies](#).

These ratings are unsolicited. The rated entity did not participate in the rating process.

Main sources of information: World Bank, International Monetary Fund, Belstat, National Bank of the Republic of Belarus, Ministry of finance of the Republic of Belarus, BCSE, Börse Frankfurt, Cbonds, CBR, Rosstat, World Federation of Exchanges.

Limits of the Credit Rating

During the rating assignment process, Rating-Agentur Expert RA GmbH (the Agency) used publicly available information that was considered to be reliable, complete and non-biased. The responsible expert performed the rating assessment of the country with information considered as the most reliable and up to date in accordance to the overall position of the country and the Agency's internal criteria for selecting data providers. The information and data used for this specific assessment can be considered as of sufficient quality.

Regulatory use

SGC ratings can be used for regulatory purposes according to the ESMA definition.

Conflict of interest

The responsible expert was neither influenced nor biased by third parties during the rating assessment. All employees involved in the rating assessment and revision of the rated entity have reported absence of conflicts of interests before initiation of the rating process.

Rating-Agentur Expert RA GmbH is completely independent from the activities of other agencies of the RAEX group.

Risk warning

The Agency disclaims all liability in connection with any consequences, interpretations, conclusions, recommendations and other actions directly or indirectly related to the conclusions and opinions contained in the Agency's press-release and research report.

This press-release represents the opinion of Rating-Agentur Expert RA GmbH and is not a recommendation to buy, hold or sell any securities or assets, or to make investment decisions.

Office responsible for preparing the rating

The office responsible for the preparation and issuance of this credit rating is the office of Rating-Agentur Expert RA GmbH in Frankfurt am Main, Germany.

Rating-Agentur Expert RA GmbH is a credit rating agency established in Germany and therefore shall comply with all applicable regulations currently in force in the European Union.

The European Securities and Markets Authority (ESMA), the EU's direct supervisor of credit rating agencies (CRAs), has registered Rating-Agentur Expert RA GmbH as a CRA under Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, with effect from 1 December 2015.

Rating-Agentur Expert RA GmbH applies the Code of Conduct Fundamentals for credit rating agencies issued by the International Organization of Securities Commissions (IOSCO Code) and includes the basic principles of IOSCO Code in its Code of Conduct.