

**Republic of Belarus: Financial System Stability Assessment,
including Reports on the Observance of Standards and Codes on
the following topics: Banking Supervision, Payment Systems, and Anti-Money
Laundering and Combating the Financing of Terrorism**

This Financial System Stability Assessment on the Republic of Belarus was prepared by a staff team of the International Monetary Fund and the World Bank as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed on June 2, 2005. The views expressed in this document are those of the staff team and do not necessarily reflect the views of the government of the Republic of Belarus or the Executive Board of the IMF.

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Financial System Stability Assessment

Prepared by the Monetary and Financial Systems and European Departments

Approved by Stefan Ingves and Susan Schadler

June 2, 2005

This Financial System Stability Assessment (FSSA) is based on work of the Financial Sector Assessment Program (FSAP) team, whose two main missions to the Republic of Belarus were in September and December 2004. The FSAP findings were further discussed with the authorities during the Article IV consultation mission in March 2005.

The FSAP team comprised Paula Perttunen (mission chief, World Bank), Mark O'Brien (deputy mission chief, IMF), John Abbott, Terrence Donovan, Vassili Prokopenko, Jerome Vacher, and Sibel Yelten (all IMF/MFD); Veronica Bacalu (IMF/EUR); Antonio Hyman Bouchereau (IMF/LEG); Claire Grose and Ulle Lohmus (both World Bank); Árpád Király (Hungarian Financial Supervisory Authority), Walter Zunic (World Bank banking expert), Tom Kokkola (European Central Bank), Lorenzo Savorelli (World Bank insurance expert); and Maria Koreniako (administrative assistant, World Bank). In addition, Andrea Nicolai (independent AML/CFT expert, Italian Guardia di Finanza, Italy) helped undertake the AML/CFT assessment. The FSAP team received excellent cooperation from the authorities and market participants. The main findings of the FSAP are:

- Although significant progress has been made in upgrading the financial system's technical infrastructure and the regulatory and supervisory framework, financial sector structural reform has been slow overall.
- The centralized approach to economic management continues to dominate the financial system. The major banks, which are with one exception government owned or controlled, are frequently requested to lend to priority enterprises and sectors. The impact of this lending on banking system liquidity and capital has necessitated periodic recapitalizations and other supportive measures for the largest banks.
- Given the still high dollarization of banks' balance sheets and low levels of official foreign reserves, the banking system would be vulnerable in the event of a shock which undermined confidence in the rubel. In the absence of this kind of shock, however, immediate stability concerns are limited so long as the government is prepared to continue its financial support to the banks.
- This approach is nevertheless costly, and more rapid progress with structural reform is a prerequisite for achieving an efficient financial system with substantial private sector and foreign ownership.

The main authors of this FSSA are Messrs. O'Brien and Prokopenko, with contributions from the rest of the FSAP team.

FSAPs are designed to assess the stability of the financial system as a whole and not that of individual institutions. They have been developed to help countries identify and remedy weaknesses in their financial sector structure, thereby enhancing their resilience to macroeconomic shocks and cross-border contagion. FSAPs do not cover risks that are specific to individual institutions such as asset quality, operational or legal risks, or fraud.

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GLOSSARY

AML/CFT	Anti Money Laundering and Combating the Financing of Terrorism
BSD	Banking Supervision Directorate
BC	Banking Code of the Republic of Belarus
BCP	Basel Core Principles for Effective Banking Supervision
BCSE	Belarus Currency and Stock Exchange
BISS	Belarus Interbank Settlement System
BYR	Belarus Ruble
BAS	Belarusian Accounting Standards
CAR	Capital Adequacy Ratio
CC	Criminal Code
CPC	Criminal Procedure Code
CPSIPS	Core Principles for Systemically Important Payment Systems
CT Law	Law No. 77-3 of January 3, 2002 “On combating terrorism”
DFM	Department of Financial Monitoring of the State Control Committee
DNFBP	Designated Non-Financial Businesses and Professions
EAG	Eurasian Group Against Money Laundering
FID	Financial Investigations Department
FIU	Financial Intelligence Unit
FSAP	Financial Sector Assessment Program
FT	Financing of Terrorism
GDO	Government long-term bonds
GKO	Government short-term bonds
GDP	Gross Domestic Product
IFRS	International Financial Reporting Standards
LOLR	Lender Of Last Resort
MIA	Ministry of Internal Affairs
ML	Money Laundering
MLA	Mutual Legal Assistance
MOF	Ministry Of Finance
MOJ	Ministry of Justice
MTD	Ministry of Taxes and Duties
NBRB	National Bank of the Republic of Belarus
NPLs	Non Performing Loans
OJSC	Open Joint Stock Company
PGO	Prosecutor General’s Office
RTGS	Real Time Gross Settlement
ROSC	Report on Observance of Standards and Codes
SC	State Committee for Securities Supervision
SCC	State Control Committee
SDF	Special Data Form
VGDO	Government bonds denominated in foreign currency

EXECUTIVE SUMMARY

The reform of the Belarusian financial system has been slow overall, with the centralized approach to managing the economy still dominating the financial system. Nevertheless, the Government has laid out, in its Banking Concept, its intention to move toward an efficient financial system with substantial private sector and foreign ownership over the coming years, and progress has been made in a few areas. The National Bank of the Republic of Belarus (NBRB) has stabilized the value of the Belarusian rubel, and the financial system's technical infrastructure and the regulatory and supervisory framework has been significantly upgraded toward international standards.

With one exception, the major banks are still government owned or controlled and they play a key role in economic management. These banks are frequently requested by the authorities to lend to priority enterprises and sectors (for example, long term funding for housing construction) irrespective of whether or not the recipients of these loans are profit-making. Banks are also encouraged to lend at close to the official refinance rate, so as to keep interest rates reasonably low. This approach has contributed to liquidity shortages and undermined profitability, especially in the two largest banks—the liquidity situation was particularly tight at the end of 2004, due to the rapid increase in bank loans during the year. Consequently, there has been a need for repeated recapitalization and liquidity injections in the two largest banks by the government.

The playing field in the banking sector is far from level, which works directly against the long term financial sector development objectives set down in the Banking Concept. Several measures which have been taken at least in part to offset the impact of the recommended lending policies on the liquidity positions of the two largest banks have contributed, e.g., the recent direction that the deposits of some state controlled enterprises (most recently state controlled insurance companies) be shifted to the government-owned banks. The two largest banks have also received supervisory forbearance at times—undermining the supervisory framework—and they benefit from not having to contribute to the deposit insurance system. The other four large banks, which are affected by official lending recommendations although to a lesser extent, also receive some preferential treatment under the deposit insurance scheme.

The nonbank financial sector remains underdeveloped. The regulatory environment for nonbanks also remains unpredictable due to frequent changes and ad hoc administrative measures. In particular, the extensive and recently tightened golden share rule deters private sector participation in both currently, and previously, state-owned companies. In the meantime, the securities market lacks good investment opportunities despite progress in market infrastructure. There have also been some backward steps in the insurance sector.

Due to the financial policy approach, there are significant structural weaknesses in the banking system. In addition to the periodically tight banking system liquidity situation, bank profitability is low, several banks have been underprovisioned at times, and interbank markets are underdeveloped. Non-performing loans (NPLs) may also be higher than official

statistics indicate. Furthermore, despite some de-dollarization resulting from the stabilization of the rubel, a significant proportion of bank loans and deposits are in foreign currency while the level of official foreign reserves is low. Stability issues could thus quickly become of concern, for example in the event of a significant shock affecting confidence in the rubel and resulting in a run on foreign exchange deposits.¹

In the absence of this type of shock, however, the banking system should be able to continue operating as it currently does for some time, despite its weaknesses. So long as the Government is willing and able to continue periodic financial support to the banking system, the needed restructuring can be deferred. On the other hand, recapitalization and liquidity support to the system will do nothing by themselves to resolve the underlying structural issues, or help to move the financial system in the direction set out in the Banking Concept. Furthermore, the size of injections needed to keep the system going in its current form may well increase over time, making its ongoing stability increasingly linked to fiscal support.

Fundamental restructuring of the financial system should therefore commence sooner rather than later, with a first step of cessation, or at least a significant phasing back, of directed lending. In the absence of this step, it will not be possible to develop the kind of banking system which is set out in the Banking Concept. To the extent that government influence over bank lending continues, the lending could be centralized in only one or two institutions. These institutions should focus only on these activities so that they are not in a position to compete unfairly and so inhibit financial system development. In particular, they should not take be able to take deposits but instead should be funded directly from the budget.

Further, government ministers and NBRB officials should cease sitting on the boards of commercial banks even if the government is the major shareholder. While the ultimate goal would be privatization, in the short run moves should be made to achieve more autonomous bank managements and boards, comprised of professionals with incentives to focus solely on viable banking activities.

Financial sector reform will have to go hand in hand with enterprise restructuring. Loss-making enterprises are a source of much of the banking sector's problems, and a comprehensive program of corporate sector reform is required in order to limit the role of banks in supporting unprofitable sectors and enterprises. The government funding which is currently provided in the form of periodic bank recapitalizations could be shifted to direct enterprise subsidies to those sectors which the government wished to continue to support.

¹ Many of the large Belarusian enterprises remain under state control. The authorities would be able to offset the impact of such a shock to a degree by influencing the timing of these enterprises' foreign currency transactions.

Box 1 summarizes the assessment's main recommendations. A number of other technical recommendations are discussed in the main body of this report and in the standards assessments that were carried out as part of the FSAP work.² While implementation of these technical recommendations will help to improve the financial system at the margin, the fundamental reforms that are proposed in this assessment are required in order to achieve a more self-sufficient, diversified and efficient financial system.

Box 1. Summary of Key Recommendations

A. High Priority

- Commence fundamental financial sector reform, with an essential first step of stopping, or at least winding back, the policy of recommended lending.
- Develop a plan for bank restructuring, incorporating:
 - the removal of non-performing recommended loans from bank balance sheets;
 - changing the composition of government banks' boards;
 - refraining from measures that create moral hazard and distort the financial markets, such as directing deposits of state owned entities for liquidity provision purposes; and
 - elimination of caps on lending rates and informal recommendations to banks to lend at close to the refinance rate.
- Increase NBRB independence, and provide banking supervision with greater autonomy.
- Enhance and better enforce the system of supervisory remedial measures.
- Increase the awareness of bank borrowers of the risks implied in unhedged foreign currency lending.

B. Medium Term and Developmental

- Accelerate the transition to International Financial Reporting Standards (IFRS), especially in the banking sector.
- Approve the proposed new structure of the deposit insurance system.
- Phase out the golden share rule.
- Consolidate all substantive legal provisions in the Law on Securities and Stock Exchanges and remove inconsistencies with other laws, such as the Civil Code.
- Implement a phased opening of the insurance sector to domestic and foreign private competition, reduce excessive regulation, relax licensing, tariff setting and controls, and implement a more level playing field in taxation of insurance premiums.
- Strengthen the role and independence of the insurance supervisory authority to ensure adequate on- and off-site supervision.

² Many of the technical recommendations in the supervisory area are expected to be addressed when the new supervision law is finalized.

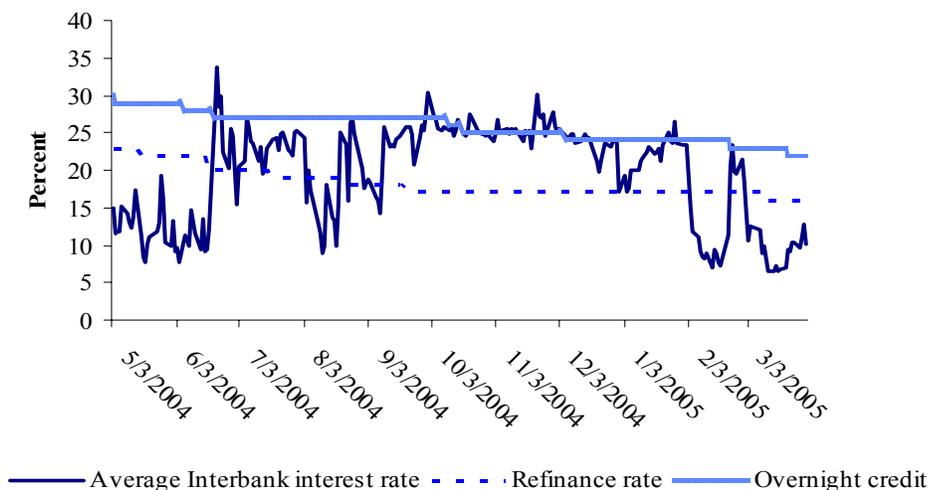
I. STABILITY ISSUES

1. **Financial system stability issues in Belarus arise almost entirely in the banking system.** The capital market is still only in the early stages of development, and the insurance sector is small and has not been growing in real terms.

2. **The continuation of many aspects of a centrally managed economy has had a profound impact on the banking system.** The major banks have continually been “recommended” to expand lending to priority enterprises and sectors irrespective of whether or not the borrowers are profit-making (Box 2). This has contributed to intermittent liquidity shortages and undermined profitability, especially in the two largest banks. The aggregate ratio of liquid assets (assets with a maturity of less than one month) to short term liabilities (liabilities with a maturity of less than one month) was 63 percent in December 2004, below the prudential minimum of 70 percent (Table 1). This aggregate ratio masked a wide variation in the liquidity of individual banks, ranging from 29 percent to 112 percent across the ten largest banks.

3. **As a result, interbank interest rates have been volatile at times.** Due to the limits that are imposed on banks’ access to overnight credit with the NBRB, the interbank rate has at times exceeded the overnight credit interest rate when liquidity was particularly tight (Figure 1). One recent instance of this coincided with the market unrest in Russia at the end of June 2004, which led to the withdrawal of some Russian banks from the Belarusian interbank market. This withdrawal was short-lived, however, and the high interbank rates later in 2004 seem to be due solely to the very tight domestic liquidity situation

Figure 1. Belarus. Daily Interbank Rates in Rubels and Main NBRB Interest Rates



Source: Belarusian authorities.

Box 2. Belarus: Recommended Lending

The Belarusian financial system is dominated by six commercial banks. These banks, of which five are state owned or controlled, are “authorized for participation” in state programs involving lending to priority sectors, programs and companies, often on preferential terms.

Loans under the state programs are recommended, rather than being mandatory, via Presidential or Government decrees and resolutions. While not all the recommendations are fully implemented by the banks, they can nevertheless be regarded as having the impact of directed lending in terms of their influence on banks’ lending decisions.

For example, in early February 2005, the Belarusian government recommended that the country’s commercial banks provide 1.8 trillion Belarusian rubles worth of long-term investment loans for the real sector of economy, of which 1.34 trillion Belarusian rubles were to service state programs. Of the total, investment loans in foreign currency were to amount to the equivalent of 700 billion Belarusian rubles, with 510 billion rubles provided by the banks that service state programs.

Recommended lending, in flow terms, reached 3.4 percent of GDP in 2004 or about half of all new lending by banks, with two thirds of it extended to agriculture. At the end of 2003, the loans extended by Belagroprombank and Belarusbank under Government programs for housing construction and for support to agriculture amounted to 19 percent of the total credit to the economy. As of October 1, 2004, these loans were estimated to account for about 70 percent of Belagroprombank’s, and for 23 percent of Belarusbank’s, credit portfolios, and for 24 percent of total bank lending to the economy.

Such loans are often guaranteed by central or local governments and/or recommended by official decrees and resolutions. Central Government guarantees to support bank credits increased sharply in 2004. While the annual limit for central government guarantees on loans extended by banks in 2004 was initially set at the same level as for 2003 (BYR 100 billion or 0.3 percent of GDP), a Presidential Decree subsequently increased the amount by another BYR 500 billion (1.1 percent of GDP). A limit of BYR 200 billion for central government guarantees has been included in the 2005 budget.

Table 1. Belarus: Financial Soundness Indicators for the Banking Sector
(In percent, unless otherwise indicated)

	Dec-00	Dec-01	Dec-02	Dec-03	Dec-04
<i>Capital Adequacy</i>					
Regulatory capital to risk-weighted assets	24.4	20.7	24.2	26.0	25.2
Regulatory Tier I capital to risk-weighted assets	n.a.	n.a.	19.2	21.7	21.0
Capital (net worth) to total assets	n.a.	15.1	18.7	20.4	20.0
<i>Asset composition and quality</i>					
Sectoral distribution of loans to total loans	100.0	100.0	100.0	100.0	100.0
Industry	49.5	46.0	45.3	41.1	35.9
Agriculture	9.9	11.1	11.3	11.3	12.6
Trade	8.7	8.0	7.1	6.7	7.2
Construction	1.0	1.4	1.7	1.5	2.1
Households	9.8	11.2	13.6	18.1	21.2
Others	21.1	22.3	21.0	21.3	21.0
Share of state-owned enterprises in total loans 1/	39.4	42.2	45.3	35.7	31.7
Foreign exchange loans to total loans	54.9	50.7	51.9	50.4	43.8
NPLs to gross loans	10.8	13.4	10.8	6.2	4.6
Required Provisions to NPLs	n.a.	67.9	55.5	58.0	56.6
Actual Provisions to NPLs	n.a.	37.7	15.8	29.1	32.4
Actual Provisions to Required Provisions	n.a.	55.5	28.5	50.2	57.2
NPLs net of provisions to capital	n.a.	32.9	27.3	12.3	11.4
Annual growth in loans	219.1	66.1	56.4	57.6	59.3
Annual growth in assets	224.3	62.7	53.0	57.8	45.7
<i>Earnings and Profitability</i>					
ROA (after tax)	1.0	0.8	1.0	1.5	1.4
ROE (after tax)	4.8	4.9	4.4	6.4	6.3
Noninterest income to gross income	23.7	46.5	46.3	35.4	40.8
Noninterest expenses to gross income	45.0	66.3	67.7	61.5	64.3
Administrative expenses to noninterest expenses	n.a.	18.0	19.5	30.7	19.2
<i>Liquidity</i>					
Liquid assets to total assets 2/	13.2	13.9	16.0	29.1	27.7
Liquid assets to short-term liabilities 3/	n.a.	n.a.	n.a.	60.9	63.0
Long-term assets to long-term liabilities 4/	1.8	1.5	2.4	3.9	4.1
Loans to deposits	106.8	114.1	112.7	111.7	123.2
Foreign exchange loans to foreign exchange deposits	81.2	87.8	96.7	103.3	116.0
Foreign exchange deposits to total deposits	72.2	65.9	60.5	54.5	46.5
Foreign exchange liabilities to total liabilities	54.2	47.6	44.6	42.1	40.4

Source: NBRB and staff estimates.

1/ State-owned enterprises are defined as enterprises with a 100 percent state ownership.

2/ The definition of liquid assets was broadened from 1/1/2004 to include assets with a remaining maturity of less than 1 month.

3/ Assets and liabilities with a remaining maturity of less than 1 month.

4/ Assets and liabilities with a remaining maturity of over 1 year.

4. **To address the liquidity problem, the Government has repeatedly provided funds to the two largest banks.** Some of these injections have effectively been book transactions, either converting the funds previously provided for recommended loans into capital or providing capital injections from the proceeds of government securities placed in the same bank.³ These approaches do not add liquidity in the system. Several other measures have also been taken in part to help alleviate the major banks' liquidity situation. These included directions that the deposits of state controlled insurance companies be shifted to the government owned banks. The two largest banks have also received preferential supervisory treatment at times.
5. **Foreign currency lending also poses challenges.** Despite increased confidence in the domestic currency, with rubel deposits growing faster than foreign currency deposits, the banking system remains highly dollarized; foreign currency deposits in the banking system currently amount to close to 40 percent of broad money.⁴ At the same time, official foreign reserves are relatively low, at two weeks of imports, which limits the NBRB's ability to maneuver or to absorb shocks. Further, net foreign assets of commercial banks are negative, so a sudden, unexpected withdrawal of foreign currency liquidity could be disruptive for the financial system.
6. **While the interest rates for foreign currency deposits and loans have been less volatile and lower than domestic currency interest rates, the high dependence on nonresident banks to provide liquidity entails risks.** In particular, the significant role of Russian banks at times in providing liquidity to the Belarusian interbank market means that any disruption in the Russian banking system could rapidly spill over to Belarus.
7. **Foreign currency loans also expose banks to increased credit risk due to the foreign exchange risk faced by the borrowers.** Borrowers without foreign currency hedges, either natural or synthetic, may have difficulty servicing their loans in case of a substantial depreciation of the rubel.
8. **Trade concentration of the highly open Belarusian economy is also a potential source of risk for the financial system.** While the traditional trade links with Russia—the main trading partner of Belarus—have helped to maintain growth, the reliance on one trading partner makes Belarus susceptible to external shocks.
9. **Many of the large banks have a high sectoral lending concentration.** At end-2004, over 50 percent of loans by Belagroprombank were for agriculture while loans to the industrial sector constituted about 70 percent of Belpromstroybank's and

³ These recapitalization costs have averaged close to 1 percent of GDP over the last five years.

⁴ In *Monetary policy in Dollarized Economies*, IMF Occasional Paper 117, an economy is regarded as highly dollarized if the ratio of foreign currency deposits to broad money exceeds 30 percent, and Belarus is shown as consistently among the most dollarized of the former Soviet countries.

Belvnesheconombank's loan portfolios.⁵ Data on the portfolio concentrations at the enterprise level are not available, but they are felt likely to be considerable, at least for some banks, given the regulations that required that enterprises could have BYR denominated accounts with only one bank. The periodic issuance of exemptions by the NBRB on the maximum legal lending limit to a single client is also indicative of probable loan concentration.

10. **Banks' are also affected by administrative measures restricting interest rates** and thus their ability to adequately price risk, especially at the longer end of the interest rate curve. Interest rates on loans in foreign currency are capped, and interest margins for loans in rubel are limited by a general recommendation to lend at the refinance rate plus 3 percentage points. Banks seem to be able to compensate for these restrictions to some extent with added fees and commissions. However, this in turn leads to non-transparent pricing, with borrowers not being easily able to determine the true cost of funds.

11. **Reflecting the restrictions on interest rates, overall banking sector profitability is low.** In 2004, the average reported return on assets was 1.4 percent, and the return on equity was 6.3 percent. These ratios are amongst the lowest for emerging European countries; return on assets typically ranged between 1.2 percent to and 2.5 percent in 2004, while return on equity was typically between 10 percent and 25 percent. Furthermore, several Belarusian banks are under-provisioned, which implies that profitability is overstated.

12. **The reported ratio of nonperforming loans (NPLs) to total loans has been declining.** Following high level attention to the level of NPLs, the NBRB issued an instruction for banks to reduce their NPL to total loan ratio below 5 percent by end-2004. As a result, NPLs were significantly reduced to 4.6 percent by end-2004, down from 13.4 percent in December 2001. According to the authorities, the decline in NPLs partly reflected the rapid growth in the bank lending, and was also facilitated by the mid-2002 amendment by NBRB to the loan classification and provisioning rules, enabling banks to clear the stock of the old NPLs more aggressively.⁶

13. **However, other important factors have also contributed to the decline in the reported NPLs, including (i) 'evergreening' (rolling over) of loans, and (ii) issuance of government guarantees, which doubled in nominal terms in 2003 and has further increased in 2004.** Presidential decrees mandating lending or restructuring also allow loss loans to be provisioned only partially. The loan classification regulations and practices are lax; reclassification of a loan is generally required only after the second roll-over. For long-term (more than 1 year) loans, only the overdue portion is classified. This results in

⁵ These high concentration ratios reflect that some of the large banks in Belarus still retain a degree of the focus on specific sectors that characterized the structure of the financial system during the Soviet period, whereas in other neighboring countries the banks have diversified their operations to a greater extent.

⁶ NPLs were required to be written off after 1 year from the time of being classified as losses.

substantial underprovisioning by banks and an over-capitalization bias in the reported soundness indicators, although it is difficult to quantify it with precision.

14. **Despite the recent high economic growth, the financial situation of the enterprise sector remains difficult, providing a further indication that NPLs may be higher than reported.** The high share of loss-making enterprises and the scale of inter-enterprise arrears in the economy cast doubt on the reported low level of overdue bank loans. Large administratively determined real wage increases also put additional pressure on enterprises; the Government mandated that wages should reach a minimum equivalent to US\$190 by end-2004. Reaching the official wage target of US\$250 by end-2005 could create pressures on enterprises as well as on the budget, and could potentially translate into increased non-performing loans for banks and further need for recapitalization. Finally, the considerable share of non-monetary payments between enterprises also implies a persisting lack of liquidity, at least in some sectors.

15. **Irrespective of the true state of the banks' loan portfolios, the rapid loan growth in 2003 and 2004 raises concern about future NPLs.** Loans grew in real terms by in excess of 40 percent in both 2003 and 2004, at the top end of real loan growth rates for central and eastern European countries (the average loan growth rate for this group of countries in the 2003-04 period was around 25 percent).

II. INSTITUTIONS AND MARKETS

A. Banks

Performance

16. **The Belarusian financial system is dominated by six commercial banks, with 31 banks in total.** The six systemically important banks constitute about 85 percent of total assets and the total capital of the banking system. The largest is Belarusbank which has its origins as the domestic savings bank under the Soviet system and which accounts for about 40 percent of banking system assets and over 60 percent of retail deposits.

17. **The state strongly dominates the banking sector.** As of September 2004, the share of the government and state agencies (including the NBRB) in the capital of the banking system was around 80 percent, and state-owned banks accounted for 70 percent of total banking assets. Only one of the six largest banks, Priorbank, is foreign controlled (Austria's Raiffeisen group has a majority shareholding) although the number of small foreign banks has been increasing in recent years (Table 2).⁷ All of the systemically important banks, including Priorbank, have government ministers and/or senior NBRB officials on their boards.

⁷ The sharp jump in 2003 in the share of assets in the banking system which are foreign-controlled resulted from the entry of the Austrian Raiffeisen group into the system.

Table 2. Belarus: Financial System Structure

	2000	2001	2002	2003	2004
Number of licensed banks	28	25	28	31	32
of which state-controlled	7	5	5	6	6
of which with the majority of foreign participation	6	9	12	18	19
Number of bank branches	529	509	478	473	463
Assets of commercial banks (percent of GDP)	29.5	25.5	25.7	29.5	31.2
of which percent state-controlled	65.2	63.9	63.8	70.6	72.8
of which percent with foreign participation	4.4	7.5	8.1	20.4	20.0
Number of exchange bureaus	983	1427	1998	2443	2914
Number of licensed insurance companies	42	37	35	33	n.a.
Gross Written Premiums (BYR billion)	55.0	120.8	165.4	215.4	n.a.
of which state-controlled (>50% stake, percent)	NA	55.7	55.0	54.1	n.a.
of which with foreign participation	NA	26.7	28.1	28.1	n.a.
of which by the top 5 largest	75.3	74.9	72.8	72.0	n.a.
of which by the top 10 largest	91.3	87.9	86.2	88.0	n.a.
(%) Penetration Ratio: Gross written premiums/GDP	0.64	0.70	0.63	0.60	n.a.
Number of professional participants in the securities market 1/	142	114	117	126	n.a.
Number of attested specialists	2002	2696	3232	3632	n.a.
Number of transactions in government securities		19428	22776	32477	n.a.
Value of transactions (BYR billion)		1811	3646	5097	n.a.
Number of transactions in shares on BCSE		18	408	4776	n.a.
Value of transactions (BYR billion)		0.09	0.80	11.90	n.a.
Number of transactions in shares on OTC		3585	3982	4147	n.a.
Value of transactions (BYR billion)		10.79	9.57	12.10	n.a.

Source: Belarusian authorities and staff estimates.

1/ Market capitalization not available due to low trading level that leads to lack of price information.

18. **The reported average capital adequacy ratio (CAR defined as capital to risk-weighted assets) was 25.2 percent as of end-2004.** This ratio declined slightly in the first half of 2004 reflecting a growing share of loans to the private sector. As a result of the recent Government capital injections, some state-owned banks report a higher capital adequacy ratio than other banks. With the exception of one small bank that is being restructured, all banks comply with the capital requirements.

19. **Belarusian accounting and asset classification practices give an upward bias to reported CARs** (see Appendix I on the stress testing exercise for a discussion of the various factors which potentially contribute to this bias). Staff estimated that adjusting for these could result in a reduction in the average CAR of the banking sector by 25 percent (to around 19 percent), with several of the largest banks potentially having CARs below 10 percent. The

estimate is very approximate, based on several *ad hoc* assumptions, as the mission did not have sufficient information to determine the scale of the adjustments with great accuracy.

Stress tests

20. **The FSAP team conducted stress tests to investigate the potential vulnerabilities of the banking system.** In particular, the tests assessed the impact of: a deterioration in the quality of credit portfolio; exchange rate and interest rate fluctuations; and liquidity withdrawals. The specific shocks and their magnitudes were decided after consultations with the NBRB.

21. **The tests were conducted on balance sheet data which had been adjusted, as discussed above, to compensate for the over-capitalization biases arising from Belarusian accounting and asset classification practices.** While the approximate nature of the adjustments lowers the accuracy of the stress tests, they should still give a reasonable indication of the likely direction and size of the impact of a presumed shock.

22. **The stress tests found that several of the systemically important Belarusian banks are vulnerable to credit and liquidity shocks** (Appendix I). The special features of the banking sector and the economy (large share of loss-making enterprises, large share of foreign-currency-denominated loans, and large share of assets with long-term maturities) could substantially amplify the impact of a disturbance.

B. Insurance and Securities Markets

23. **A series of policy measures implemented recently by the Government and Presidential administration have reversed the positive trends in the insurance market, limiting competition and prompting private (especially foreign) companies to leave the market.**⁸ Private sector participants have seen their business dramatically reduced as these measures effectively prevent private companies from accessing the currently most profitable segment of the market—compulsory lines of insurance. These companies' ability to deduct from taxation voluntary insurance premiums collected was also abolished. Local and foreign private companies are prevented from providing certain products and barriers to the entry of foreign companies have been erected.

24. **Capital market activity is still in a nascent stage.** The basic technical infrastructure for the securities market is reasonable though the overall regulatory environment for the protection of property, contractual and other economic rights is lacking which impedes the development of a well-functioning securities market. There are also some impediments to

⁸ In spring 2002 a Presidential resolution established that State owned companies could be the only providers of motor third party liability insurance (MTPL), with effect from 2004, thereby restricting almost half of the market to State companies. Similar provisions on other lines of compulsory insurance were subsequently introduced.

secondary market trading and some of the current practices in Government debt issuance are not conducive to capital market development. In particular, transparency in the direct placement of Government bonds could be improved and foreign exchange denominated Government long-term securities are not tradable and can be called before maturity at the issuer's discretion.

25. **The golden share rule, which was strengthened considerably in March 2004 by a Presidential Decree, represents a serious deterrent for potential investors.** The share can be applied to any company (including 100 percent privately owned) which was previously owned or created by the State. There is no limit to the duration of the golden share. Reportedly the share would only be applied in limited circumstances, including anti-competitive conduct on the part of a company, possible liquidation, failure to pay tax, and failure to pay employees' salaries for a period of 6 months.

26. **The voucher privatization program has not yet been a success.** The pace of privatizations has been slow and no strategically important state assets have been included in the scheme. The contingent liability to the Government from redemption of unused vouchers at present face value is about 800 billion rubels (around US\$400 million) or approximately 12 percent of the annual budget. By law at the end of the privatization program unused vouchers may be redeemed for cash at the face value. Originally, the program was to finish at the end of 2003, however in 2003 it was extended by a year to December 31, 2004 and it has recently been extended again till December 31, 2005.

III. FINANCIAL STABILITY POLICY FRAMEWORK

A. Financial Regulation and Supervision

27. **The mission undertook detailed assessments of the supervisory and regulatory framework for banking and payment system supervision.** Due to the currently limited role of the insurance and securities markets, only informal assessments of the supervisory and regulatory framework were undertaken.

28. **Significant progress has been made in recent years in upgrading the regulatory and supervisory framework, and the NBRB's supervisory capacity, towards international standards.** For the most part banking supervision in Belarus is converging with the Basel Core Principles (BCP). Since 2001, there has been an ongoing program in the NBRB to streamline and improve the oversight process, and since 2003 the NBRB has moved from the transaction testing supervision approach to a more risk-focused approach, based on a qualitative assessment of the financial condition of, and prospects for, a bank.

29. **Specific recommendations to further strengthen banking supervision are given in the Annex to this report.** The main recommendations are, however, that the NBRB should:

- provide banking supervision with more autonomy through strengthening the institutional standing within the NBRB of the Director of the Bank Supervision Directorate;
- make the current system of remedial measures more specific;
- strengthen the licensing process to grant the NBRB the right to conduct a deeper analysis of a proposed bank's ownership structure, and to reveal the true beneficial owners of a bank and assess their potential influence on the bank's activities;
- introduce specific legislative provisions to protect the NBRB supervisory staff against law suits for measures taken in good faith against a financial institution;
- move ahead expeditiously with the introduction of international financial reporting standards (IFRS) for banks' financial statements; and
- introduce a comprehensive Manual of Examination Procedures.

30. **Conflict of interest issues potentially arise as the NBRB is both the supervisor of banks and has shareholdings in four banks.** Senior ministers and members of the Board of NBRB are also seated on the boards of the larger banks. To limit actual or apparent conflicts of interest, the NBRB should dispose of its bank shareholdings. Further, government ministers and National Bank of Belarus officials should cease sitting on the boards of commercial banks even where the government is the major shareholder. While the ultimate goal would be privatization, the near term objective should bank managements and boards that are comprised of professionals with incentives to focus solely on viable banking activities.

31. **While the payment system was found to be technically well functioning,** improvements in a number of areas are needed to achieve full compliance with the Core Principles for Systemically Important Payment Systems. Effective and transparent governance for the payment system need to be established. Furthermore, it is recommended that an oversight function be introduced and, subsequently, that the NBRB define and make publicly available its main payment system oversight objectives and policies. Technical security and business continuity measures should be further elaborated and the system should be subject to regular risk analysis.

32. **The Law on Insurance issued in June 1993 is comprehensive and modern.** It defines insurance, insurance-related concepts, products and market participants. It also provides the legal basis for the establishment of insurance companies, brokers and intermediaries, licensing procedures, financial reporting and solvency criteria and sanctions. The regulatory system includes many key norms foreseen by international best practice, including a definition of solvency margin according to EU directives. It still lacks, amongst other things, the requirement for the application of IFRS, norms on corporate governance, safe custody and segregation, discount rates and mortality tables for mathematical reserves calculation, rules for group consolidated control and treatment of derivative products. The

regulatory system foresees a strict licensing process for all new insurance products, and strict controls and guidelines for tariffs and commissions, which are set by law.

33. **While originally established as a separate body the insurance supervisory authority was downsized in 2002**, its staff reduced, and it was converted into a department of the Ministry of Finance (MOF). Its main functions are to: register and license insurers, re-insurers, brokers, intermediaries; ensuring compliance with the law of all participants; providing accounting and reporting rules; supervising tariff rates and reserving levels; regulating foreign insurance activity. This department is currently too small. It should be reinforced, and be made more autonomous, so as to cope successfully with more developed market.

34. **The legal and regulatory regime for securities market supervision and regulation has undergone fairly constant change.** The securities market in Belarus is governed by a plethora of laws, rules and regulations. The uncertainty created by continuing change, the heavy layers of regulation, and the lack of clarity in the drafting of legal provisions and their implementation, limits the confidence of investors, issuers and intermediaries in the securities market. The primary regulator of the securities market, the State Committee for Securities Supervision (SC) under the auspices of the Council of Ministers, lacks operational independence, has limited enforcement powers, and does not have the skills and resources to be able to respond quickly to the market or regulatory requirements of an active securities market. While the Chairman has day-to-day responsibility for decisions taken by Committee, all important matters are apparently referred to the Council of Ministers for decision.

B. Safety Nets

Systemic liquidity

35. **The NBRB has a sufficient range of instruments to enable it to manage banking system liquidity.** It chiefly relies on Lombard auctions and standing facilities, with foreign exchange swaps and mutual placement of foreign exchange deposits now rarely used. Repo auctions were introduced earlier, but they have been used only since October 2004 because of technical difficulties in setting up the auctions.

36. **The interbank market is, however, still fairly shallow and segmented.** Two of the largest banks represented two thirds of the borrowing at times in late 2005, reflecting the tight liquidity resulting from the governments recommended lending programs. This resulted in upward pressure on interbank interest rates and significant access to NBRB funds. Due to limited collateral, there were quantity constraints at times on access to NBRB funding, so that interbank rates occasionally exceeded the NBRB's overnight credit rate during the period of tightest liquidity in the second half of 2004.

37. **The lack of secondary markets further limits the liquidity of banks' assets.** The secondary market for government bonds (GKO and GDO) is shallow, and the primary market for these instruments does not appear to respond to market signals or to the banks' liquidity needs. Government bonds denominated in foreign currency (VGDO) placed with

banks, primarily in Belarusbank, amounting to US\$135 million by end-September 2004, pose a specific problem as they are not tradable and cannot be used as collateral for operations with the NBRB.

38. **There is currently a structural limitation on liquidity available in the payment system.** One approach to improving the functioning of the payment system could be for a greater share of reserve holdings to be available intraday for payments purposes. In considering this issue, the NBRB would need to examine carefully any potential impact of the present structural liquidity shortage in the banking system.

39. **The interbank foreign exchange market is less segmented and relatively less volatile than the interbank market in rubels.** There is still a relatively wide dispersion of interest rates as some banks can borrow at low rates while other (mostly smaller) banks have to pay higher rates. About three quarters of the liquidity on the market is provided by foreign banks, with Russian banks representing the majority of those involved. Despite the prominent role played by Russian banks, the impact of the Russian banking crisis on the Belarusian interbank foreign exchange market in the summer 2004 was limited. After initially withdrawing some funds, Russian banks returned fairly promptly to the market.

Deposit insurance

40. **The NBRB is currently drafting a new deposit insurance law, aimed at overcoming the shortcomings with the present system.** The current system provides preferential treatment to the authorized banks, with Belarusbank and Belagroprombank receiving an even greater advantage than the other four authorized banks (Box 3). This lowers the cost of funding for these banks, giving them a competitive advantage in attracting deposits.

41. **The proposed new law aims to level the competitive playing field between the state-owned banks and their privately owned rivals.** The proposed law would be an improvement over the current system and does incorporate most best practices of a sound deposit insurance scheme. The envisioned premium of a quarterly 0.3 percent of deposits is high by international standards. A higher premium can be perhaps justified while the deposit insurance fund builds up its resources from the currently low base. However, contribution rates should probably not be held so high for an extended period.

42. **If implemented as currently envisioned—it is expected that there may be resistance to changing the system from some banks—the new scheme would reduce the Government's contingent liabilities in the event of a major bank failure** and thus reduce moral hazard. However, the proposed maximum coverage per individual is high relative to other CIS countries. Given that the average size of a household deposit in the major banks is still fairly small, the proposed scheme would still imply substantial moral hazard.

Box 3. Belarus: Current and Proposed Deposit Insurance Schemes

Key features of the current scheme

- Under the current deposit insurance system in Belarus, two of the authorized banks, Belarusbank and Belagroprombank benefit from a full guarantee on all their deposits. However, they are not required to pay any contributions to the Guarantee Fund.
- Foreign currency deposits are fully guaranteed in the four other authorized banks, Belpromstroybank, Belinvestbank, Belvnesheconombank, and Priorbank. Local currency deposits in those banks are covered up to US\$1,000 equivalent. These four banks pay monthly 0.1 percent of the household deposits to the Guarantee Fund.
- All other banks are covered up to US\$1,000 equivalent both for their local and foreign currency deposits and they pay monthly contributions according to the total deposit levels: (i) 0.1 percent if deposits do not exceed the capital of the bank; (ii) 0.2 percent if the deposits are between one and two times the capital of the bank; and (iii) 0.3 percent if the deposits are greater than two times bank capital.

Key features of the proposed scheme

- State and non-state owned banks will be treated equally, with membership of the scheme being mandatory
- Foreign and local currency deposits will be treated equally, hence reducing possible incentives for dollarization.
- Contributions will be an initial 0.5 percent of a bank's capital, with ongoing quarterly contributions of 0.3 percent of deposits.
- Deposits will be covered in full up to Euro 2,000 equivalent with 80 percent coverage for the next Euro 3,000 equivalent.

43. **The structural liquidity shortage in Belarus means that the authorities will need to be careful to sequence the changes in deposit insurance with other banking sector reforms.** It would be necessary to put in place transitional arrangements to address potential concerns Belarusbank's and Belagroprombank's depositors may have while moving from full to partial coverage. The lessons learned from the current experience in Russia would be useful in planning a transition.

Crisis resolution and contingency planning

44. **The bank resolution process in Belarus should be made more efficient.** Experience shows that bank liquidations, even with smaller banks, proceed slowly. The NBRB needs to be able to react consistently and promptly to information indicating that a bank is in violation of prudential and regulatory requirements. Failure by a bank to rectify a problem upon NBRB instruction and without delay should lead to increasingly onerous

penalties. If a bank fails to take adequate action, the NBRB should be clearly empowered to take corrective action, for example, by replacing the management, seeking a take-over, or eventually closing the bank. Bank resolution should be guided by principles of corrective action, least-cost reorganization, deposit safety, and systemic stability. Any recapitalization of a seriously under-capitalized bank should be accompanied by a solid restructuring program.

45. **The NBRB has no formalized contingency planning and its management of any crisis situation is case-by-case basis, as admittedly is the case in many other countries.** The NBRB should aim to put in place an early warning system and contingency plans for handling problems in individual banks. Best practice would be to have a clear sequencing of actions and criteria for their application. Currently, liquidity provision for troubled banks is ad hoc, and on occasion without collateral. Safeguards are needed to ascertain that liquidity provision is limited over time and does not impact monetary operations.

C. Monetary Policy Transparency

46. **An informal assessment was undertaken of monetary policy transparency in Belarus,** using the IMF's *Code of Good Practices on Transparency in Monetary and Financial Policies* as a guide. Belarus appears to observe many aspects of monetary policy transparency. The responsibilities of the NBRB are specified in legislation, and the legislation also establishes the NBRB's authority in using monetary policy instruments to attain the policy objectives. It is notable that the legislation also allows for a relatively heavy role for the state in monetary policy. In particular, rather than being solely based on the identified goals of price or exchange rate stability, the Banking Code states that monetary policy is a component part of a single state economic policy.

47. **Improvements could be made to the NBRB's monetary policy transparency and accountability practices.** These include: (a) clarification of the NBRB's autonomy;⁹ (b) further clarification of the institutional relationship between monetary and fiscal operations; (c) greater clarity regarding the role, if any, of the U.S. dollar in anchoring monetary policy;¹⁰ (d) distribution of NBRB profits according to international best practice; (e) adoption and disclosure of specific standards of NBRB staff conduct, and granting legal

⁹ As was pointed out in the safeguards assessment, which was produced by the IMF Safeguards mission which visited Minsk from December 9–19, 2003, “The NBRB is accountable to the President, the Chairman of the Board is a member of the Government, the property of the NBRB is owned by the Republic of Belarus, and although “managed” by the NBRB cannot be disposed of without permission of the President; similarly, the approval of the NBRB's annual budget must be confirmed by the President. This impacts the transparency of monetary policy.”

¹⁰ While the official monetary policy anchor is the Russian ruble exchange rate, and expected movements in this exchange rate are pre-announced on an annual basis, indicative expected movements against the U.S. dollar are also officially announced at the same time. Further, at times in the past, exchange rate policy has seemed to be aimed at stabilizing the U.S. dollar exchange rate rather than the Russian ruble rate.

protection for its staff; and (f) publishing of the detailed audited financial statements in accordance with IFRS.

D. AML/CFT Issues

48. **An assessment of the anti-money laundering (AML) and combating the financing of terrorism (CFT) regime** of Belarus was based on the Forty Recommendations 2003 and the Eight Special Recommendations on Terrorist Financing 2001 of the Financial Action Task Force (FATF), and was prepared using the AML/CFT Methodology 2004.

49. **Belarus has many of the elements of a modern AML regime.** Money laundering is criminalized. Financial institutions must monitor and report financial transactions subject to special control and take other measures to deter ML. Compliance supervision is detailed with a strong culture of on-site examination. Two agencies exercise financial intelligence responsibilities. ML offenses are investigated and successfully prosecuted. Some capacity exists to cooperate internationally.

50. **Nevertheless, gaps and misalignments in the current legal and institutional arrangements, as well as incomplete implementation, undermine the full effectiveness of the AML/CFT regime.** On several key points arrangements fall well short of the standards called for in the FATF Recommendations. Legislation needs to be updated; functions of relevant agencies need to be streamlined and better coordinated; supervisors need to place more emphasis on detection, deterrence, and reporting of truly suspicious transactions; financial intelligence needs to be centralized in a single agency; and provisions for international cooperation need to be strengthened. The authorities are aware of the need to update and reshape the present AML/CFT regime and they are well advanced on a reform agenda.

OBSERVANCE OF FINANCIAL SECTOR STANDARDS AND CODES—SUMMARY ASSESSMENTS

The annex contains summary assessments of international standards and codes relevant for the financial sector. The assessments have helped to identify the extent to which the supervisory and regulatory framework is adequate to address the potential risks in the financial system.

The following detailed assessments of financial sector standards were undertaken:

- The *Basel Core Principles for Effective Banking Supervision* (BCP), by Messrs. Árpád Király (Hungarian Financial Supervisory Authority) and Walter Zunic (World Bank Supervision expert);
- The Committee on Payment and Settlement Systems *Core Principles for Systemically Important Payment Systems* (CPSIPS), by Tom Kokkola (European Central Bank); and
- The FATF Recommendations for Anti-Money Laundering Combating the Financing of Terrorism (AML/CFT), by Messrs. John Abbott and Terrence Donovan (both IMF/MFD); Antonio Hyman Bouchereau (IMF/LEG), and Andrea Nicolai (independent AML/CFT expert, Italian Financial Intelligence Unit).

The BCP and CPSIPS assessments were carried out during a mission to Belarus from November 1–18, 2004, while the AML/CFT assessment was carried out from December 2–16, 2004. All the assessments were based on the laws, regulations, policies and practices in place at the time the assessments were made.

The assessments were based on several sources including:

- Self-assessments by the supervisory authorities;
- Reviews of relevant legislation, decrees, regulations, policy statements and other documentation;
- Detailed interviews with the supervisory authorities;
- Meetings with other authorities and independent bodies, including the National Bank of Belarus, the Ministries of Economy, Finance, Foreign Affairs and Internal Affairs, The State Control Committee, the State Security Committee and the Prosecutor General's Office; and
- Meetings with the financial sector firms and associations, including banks and accounting and auditing firms.

BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

Main findings

Objectives, autonomy, powers and resources

51. The legal framework for the regulation and supervision of the financial sector has undergone significant reform during the last decade. The result has been the adoption of a series of laws and regulations that are reasonably comprehensive and broadly consistent with international best practices. Belarusian regulatory policies are formulated on two levels. At the first level is the Law of the Republic of Belarus of October, 2000 *On the Banking Code of the Republic of Belarus*. This is the main legislative act which regulates banks, providing the NBRB with responsibility for authorization, supervision and regulation of financial institutions' operations in Belarus. This level also include decrees issued by the President. At the second level and on more technical policy, the NBRB has the powers to issue prudential regulations for enforcing provision of the Banking Code (BC). The NBRB issues Regulatory

Legal Acts jointly with the Government, as well as Rules and Instructions, which complete the framework of minimum prudential standards that banks must meet.

52. The present governance arrangements the operational independence of the NBRB in banking supervision. A member of the government and a representative of the banking sector are both seated in the main decision making body of the NBRB. Various official directives and requests can also have implications for the supervisors. Further, the government can significantly influence the budget of the NBRB. Finally, coordination among different agencies—including the NBRB, the State Securities Commission and Insurance Supervisory Department of the MOF—could be better formalized, and the meetings and information exchange between the two authorities could be on a regular basis.

53. The legal protection for supervisors is currently not addressed. The law does not provide for legal protection for the supervisory agency and its staff for actions taken while discharging their duties in good faith. There is no formal NBRB indemnification policy protecting employees against the costs of defending their actions while discharging their duties.

Licensing and structure

54. The BC clearly specifies that the name of a bank must include the word “bank”. Prior to engaging in banking operations, each institution is required to obtain a license from the NBRB which is the sole authority for granting banking licenses. The BC grants the NBRB the right to request information about the founders of the institution , to assess their financial condition and to evaluate the professional fitness of executive bodies and the chief accountant. Under the provisions of the BC, the NBRB has the authority to grant authorization for acquisitions or increases of qualifying holdings in an existing bank. However, the legislation does not explicitly grant the NBRB the right to conduct a full analysis of a bank’s ownership structure. Bank ownership approval by the NBRB is limited to shareholdings of 10 percent or higher, but the NBRB may not be able to detect if buyers are acting in concert, causing a situation where the NBRB may not be aware of the full extent of financial interests of some shareholders. Finally, the BC does not define “controlling interest”.

Prudential regulation and requirements

55. Rules and regulations regarding capital adequacy generally conform to the Basel Capital Accord 1988, and as of January 1, 2005 will include a capital charge for market risk, country risk, foreign exchange risk and other material risks. Rules and regulations covering requirements of criteria, practices and procedures for extension of credit are adequately addressed by the regulations issued by the NBRB. The procedure for classifying the assets of a bank exposed to credit risk and the procedures for establishing special loss reserves for assets exposed to credit risk are mandated by regulations issued by NBRB.

56. Decision making by banks in credit operations is evaluated by the NBRB to ensure compliance with the BC, according to which banks must be independent in their activities and they must independently determine the condition of transactions not conflicting with the legislation. However, in practice, banks often are not completely independent in their decisions to issue credits. Frequently, regulations signed by the President and Government of the Republic of Belarus request banks to allocate their resources to official programs.

57. The NBRB has issued regulations covering criteria for identifying a bank's related customers in accordance with the dispositions of the BC, and for the most part banks conduct investment operations within the limits of the Regulations. However there have been instances where Agencies of the Government have opted not to take corrective actions against a bank for violations of the Regulations. Again, these decisions are made in connection with the importance to the State of the measures to which these credits are granted.

58. The NBRB has issued regulations and recommendations requiring banks to have in place systems that accurately measure and monitor country risk, market risk, foreign exchange risk and all other material risk. These regulations became effective, however, from January 1, 2005, after this BCP assessment was undertaken. Consequently, the effectiveness of its implementation could not be assessed.

59. The Law of the Republic of Belarus "On Measures To Prevent Legalization of Criminal Proceeds" (AML Law) issued in May 2002 requires persons carrying out financial operations, including banks, to develop the regulations and measures of internal control of financial operations that are subject to special control and are associated with legalization (laundering) of criminal proceeds. The main functions of controlling compliance with requirements of the AML Law are not assigned to the NBRB but to the Ministry of Taxes and Duties and the State Control Committee of the Republic of Belarus. Bank supervisors need to place more emphasis on detection, deterrence, and reporting of suspicious transactions. Financial intelligence should also be centralized in a single agency and provisions for international cooperation need to be strengthened.

Methods of ongoing supervision

60. An effective banking supervisory system should have some form of both on-site and off-site supervision. The NBRB conducts full scope on-site examinations of banks including their larger branches on a two year basis. The examination process is comprehensive and covers a wide range of banking areas, including risk management systems, internal controls, management systems, compliance with prudential requirements, and asset quality and provisioning. Two examination reports are prepared at the completion of each full scope examination and forwarded to management. A comprehensive system of off-site monitoring of banks, is based on the analysis of a wide range of information provided to the NBRB by banks on a daily, weekly, monthly and quarterly basis.

61. However, the legislation does not currently codify the possibility of conducting supervision on a consolidated basis. The NBRB has prepared a draft in order to introduce amendments to the BC which provides definitions of a banking group and a bank holding company, and allows NBRB the possibility for supervising such groups and holding companies on a consolidated basis.

62. The NBRB is implementing International Financial Reporting Standards for financial institutions on a stage-by-stage basis and so far has introduced eleven standards. It is anticipated that the process of implementing international standards will be accomplished by 2008.

Formal powers of supervisors

63. The BC empowers the NBRB to issue decisions to restore the rightful conditions and remove abuses, develop a practice of corrective action and early intervention. The BC provides a range of remedial actions, including the removal of the bank's governor and withdrawal of the bank's license. However, the powers of the supervisor could be more flexible. The NBRB does not have the right to apply several corrective actions simultaneously for one violation, or to apply supplemental measures if prior ones have not had sufficient impact. The appropriate changes to the BC have been proposed in order to rectify the situation.

Cross-border banking

64. Under the BC, the supervisory responsibilities of the NBRB apply equally to Belarusian and foreign banks. Prior to issuing a license to a bank that is a subsidiary of a foreign owned bank, the NBRB ensures that the home supervisor has issued an approval. In accordance with MOUs that have been signed with most of the relevant home country supervisors, the NBRB also shares information on a reciprocal basis, and gives on-site access to home country bank supervisors.

65. The BC does not currently provide the NBRB with the means to conduct the supervision of credit institutions on a global consolidated basis over banking entities. Currently no cross border operations of Belarusian banks exist, so that this issue is not significant. However, this situation could change rapidly. Draft amendments to the BC to provide the NBRB with the ability to supervise banking groups and holding companies on a consolidated basis have been prepared.

Table 3. Recommended Actions in the Area of Banking Supervision

<i>Reference Principle</i>	<i>Recommended Action</i>
<i>Independence CP 1(1)</i>	Increase the level of independence in the budgetary process.
<i>Legal protection CP 1(5)</i>	Provide legal protection to the supervisors against legal actions. Provide indemnification of supervisors for legal costs incurred.
<i>Information sharing CP 1(6)</i>	Formalize the coordination among different agencies involved in financial sector regulation and supervision
<i>Licensing criteria CP 3</i>	Amend legislation in order to permit a deeper analysis of ownership structure including indirect ownership.
<i>Ownership CP 4</i>	Decrease the current limit for authorization of purchases of shares transferred from original owner to subsequent owners.
<i>Investment criteria CP 5</i>	Authorize the NBRB to conduct deeper analysis of the impact of investments on a bank's financial position.
<i>Large exposure limits CP 9</i>	Give the NBRB discretionary power in the interpretation of what constitutes closely related groups.
<i>Connected lending CP 10</i>	Grant bank supervisors the discretion to make judgments about the existence of connections between a bank and other parties.
<i>Country risk CP 11</i>	Ensure that individual banks have established country exposure limits and transfer risk limits on their operations. Ensure the effectiveness of implementation of Instruction 92 dated June 2004, that become effective in January 2005, regarding country risk.
<i>Market risk CP12</i>	Ensure the effectiveness of implementation of Instruction 92 dated June 2004, that become effective in January 2005, regarding market risk. Bank supervisors should reach a more proficient level of understanding market risks and require additional training in order to analyze and monitor the actual level of complexity in the market activities of the banks.
<i>Other risks CP 13</i>	Establish an operational risk management procedure and a procedure for calculating aspects of interest-rate risks. The effectiveness of implementation of Instruction on Economic Standards for banks due to become effective on January 1, 2005 regarding other material risks.
<i>Consolidated supervision CP 20</i>	Adopt and implement the proposed amendment to the BC to allow the NBRB to develop and introduce the necessary mechanisms to supervise the activities of banking groups and holding companies on a consolidated basis.
<i>Accounting standards CP 21</i>	Take steps to introduce International Financial Reporting Standards to the full extent more rapidly than the current timetable envisages.
<i>Globally consolidated supervision CP23</i>	Adopt and implement the proposed amendments to the BC that introduce definitions of a banking group and a bank holding company, and grant the NBRB the possibility for supervising such groups and holding companies on a consolidated basis.

Authorities' responses

66. The NBRB broadly agreed with the assessment and found it objective and useful for the purpose of further improvement of banking supervision in Belarus, although the NBRB felt that the ratings of several principles (CPs 5, 6, 9, and 21) could have been higher. The NBRB noted that the authorities continue working on the implementation of international standards of banking supervision, including the application of procedures to monitor and to limit country risks, operational risks, and market risks, and that several steps have already been done to implement recommendations formulated by the present assessment.

CPSS CORE PRINCIPLES FOR SYSTEMICALLY IMPORTANT PAYMENT SYSTEMS

General

67. This section summarizes the degree of observance of the Belarus Interbank Settlement System (BISS), which provides real-time gross settlement facilities for transactions in Belarusian rubels, with the *Core Principles for Systemically Important Payment Systems* (CPSIPS) and includes recommendations for several further improvements. The assessment was conducted based on information provided by the NBRB including a self-assessment of BISS based on the CPSIPS, a document outlining the NBRB's plans for further development of the payment system, and other documents and statistics relevant for the assessment. Extensive meetings were held with officials from the NBRB (during which oral information was received on a large range of issues), supplemented by discussions with representatives of three banks participating in BISS.

Institutional Setting

68. The core elements of the Belarusian payment system are owned and managed by the NBRB. In particular, all interbank transfers of funds in Belarus are settled through payment systems managed by the NBRB, within the framework of the Automated System of Interbank Settlements, which consists of two components:

- the BISS, which provides real-time gross settlement, in central bank money, primarily for high-value (credit) transactions in Belarusian ruble. There are currently 36 participants in BISS; and
- the National Bank clearing system, providing for net settlement of large volumes of low-value interbank transactions. The clearing system has 35 participants.

69. In addition, the Currency and Stock Exchange operates a clearing and settlement system for securities. Payments for transactions using plastic cards issued in Belarus under the BelCard scheme are handled within the BelCard scheme (payments for transactions using cards of international systems are processed by the processing centers of those systems). Net interbank balances arising in the securities clearing and settlement system and from all plastic card transactions are settled in BISS.

70. Once a valid payment request is submitted to BISS, the system checks whether sufficient funds are available in the correspondent (settlement) account of the ordering bank. If yes, funds are debited in the account of the ordering bank and credited to the account of the receiving bank (as from this moment, the payment is final). The payment message is then automatically released to the receiving participant. If a payment cannot be settled due to a lack of funds, it is put in a waiting queue. Once funds become available, queued payments are processed first by priority, then by time of input to the queue.

71. Payment requests can be prioritized by the originating bank. A real-time information management system allows participants, *inter alia*, to continuously monitor their account balance, payments queued (both their own outgoing payments and incoming payments from other participants), to change the priority of queued payments and to request funds to be reserved for different purposes.

72. In 2003, some 92 percent of all interbank payments, in value terms, were settled in the BISS. However, in terms of volume, only some 8 percent of the total traffic was settled through the BISS. This division of volume and value between the RTGS system and the net settlement system is in line with the situation in other countries. The six biggest banks account for some 80 percent of both value and volume of payments. The intraday pattern of payment flows is currently unbalanced, with around some 50 percent of the payments value being processed toward the end of the day.

73. In May 2004, the Board of the NBRB approved by way of a Resolution the *Concept Document for the Development of the National Payment System of the Republic of Belarus until 2010 with an Account for Global Trends*. The “concept document” identifies development opportunities in the payment system in general. Individual development initiatives, when addressed, are elaborated in more detail in separate documentation.

74. The most important project under way is the implementation of a new upgraded BISS system, expected to start live operations as from April 2005. In the new version of BISS, the payment flow will be divided into two categories of payments: one for large value and/or time sensitive and the other (new) for non-time sensitive payments. To facilitate the flow of payments, the system will attempt to settle queued payments by means of a frequently applied (automated) queue optimization procedure.

Main findings

75. While the BISS has proved to be generally a technically well functioning system, improvements in a number of areas are needed to achieve full compliance with the CPSIPS. Effective and transparent governance for the payment system, including overall economic efficiency, needs to be established. To improve intraday liquidity conditions and the functioning of the payment system, a greater share of reserve holdings should be available intraday for payments purposes and the current limitations to the intraday credit facility should be reconsidered. Technical security and business continuity measures should be further elaborated and the system should be subject to regular risk analysis. Furthermore, it is recommended that an oversight function be introduced and, subsequently, that the NBRB defines and makes publicly available its main payment system oversight objectives and policies.

76. **Legal foundation (CP I).** The Belarusian payment system is governed by a two-tier legislative framework, complemented by contractual agreements. The first tier comprises laws and presidential decrees, most notably the BC of the Republic of Belarus which provides that the main functions of the NBRB include “arranging interbank settlements and

specifying and adopting procedures, forms and rules relating to non-cash settlements in the national economy". The second tier comprises regulatory documents issued by the NBRB under the BC. While the legal basis for the BISS is well-founded, it is also complex (albeit understood by system participants), as is the technical, operational and organizational documentation. In view of the further modifications to the system which are envisaged, a simplification of the documentation would be welcome. It is understood that the NBRB has already initiated work aiming at a consolidation of the documentation.

77. **Understanding and management of risks (CPs II–III).** As the BISS is an RTGS system with settlement in central bank money, credit risk does not arise for participants in the system. The NBRB is subject to credit risk to the extent it provides credit to participants, however this risk is mitigated by the NBRB requiring collateral (to which haircuts are applied) for any credit provided. As a result, the main risks to which participants are exposed are legal risk, operational risk and liquidity risk. The rules and procedures as regards credit and liquidity risk management, information on the system's design, its work schedule, and the procedures of technical and operational risk management are well documented.

78. It is evident that there is currently a structural limitation on liquidity available in the RTGS system. Liquidity available from the central bank is limited and, as a consequence, banks have only limited possibilities to raise (re-allocate) liquidity in the market. The above restrictions in the availability of liquidity could be resolved by allowing banks to use a larger share of their reserve holdings for transaction purposes during the day. The NBRB should also make available an instrument and procedures for the provision of intraday credit to participants. Intraday credit should ideally not be subject to any other restrictions than the availability of eligible collateral. Further, while limits on net positions in clearing systems set by pre-blocking of funds in the RTGS system constitute an effective way to ensure successful settlement of such balances, the disadvantage of this risk management measure is that it can restrict efficiency in terms of liquidity. The NBRB may wish to consider replacing the current procedure with other, more liquidity efficient, risk management arrangements.

79. **Settlement (CPs IV–VI).** Individual payments are settled on a real-time gross basis, in central bank money, in the BISS. Any payment that cannot be settled due to a lack of funds is put in a waiting queue. Once funds become available, queued payments are processed first by priority, then by time of input to the queue.

80. **Security and operational reliability and contingency arrangements (CP VII).** The BISS is a stable and reliable system with a very good track record as regards availability. Technical security has been improved over time and a secondary site established recently. There are nevertheless opportunities for further improvement. A comprehensive risk analysis and management framework should be elaborated, documented and implemented. Business continuity and contingency procedures should be defined, documented and, subsequently, regularly tested. Moreover, change management procedures should usefully be refined and the test system upgraded.

81. **Efficiency and practicality of the system (CP VIII).** In principle, the NBRB follows an approach according to which the running (but not investment) costs of the BISS should be recovered. However, there are large differences in fees for differing payments. Moreover, as the BISS and the NBRB clearing system are operating on a shared hardware platform, it is unclear whether costs are appropriately allocated to the two. There also appears to be some overstaffing in payment system-related activities, which implies a loss in cost efficiency. The system could usefully close earlier and, to achieve a more balanced (and disciplined) payments traffic throughout the day, the NBRB could consider introducing some throughput guidelines to banks.

82. **Criteria for participation (CP IX).** Access to the BISS is granted to banks and nonbank credit and financial institutions (all current participants are classified as banks). The access criteria are set out in an NBRB Board of Directors Resolution. Some streamlining of the agreements which must be signed by participants is possible.

83. **Governance of the payment system (CP X).** Banks are informed in advance on upcoming changes to the system and NBRB meets regularly with the banking community—at the level of both senior management and payment system experts—to discuss issues related to payment systems. Reports on BISS activities are published annually and statistics are available on the NBRB website and in its monthly statistical report. The main content of the “concept document” has been published. While it is recognized that the BISS is a technically well functioning system, appreciated by the banks, it should also be noted that the overall organization and governance of the BISS is not very easy to understand. Cost recovery arrangements are also unconventional. The roles, duties and the controls thereof could be further clarified in detailed service level agreements with the NBRB payment system subsidiaries.

84. **Central Bank responsibilities in applying the CPSIPS.** The payment systems objectives of the NBRB derive from the Banking Code and the NBRB Statute, which note that one of the (three) main objectives of the NBRB shall be “ensuring efficient, reliable and secure functioning of the payment system”. While some informal oversight-like activities have started, the NBRB has not yet formally defined and established an oversight function. As a consequence, oversight objectives and policies are yet to be formulated. While the BISS does not yet comply with all Core Principles, the NBRB has shown a clear interest in identifying areas for improvement.

Table 4. Recommended Actions in the Area of Payment Systems

<i>Reference principle</i>	<i>Recommended action</i>
Understanding and management of risks <i>CPs II-III</i>	<i>Make available an instrument and procedures for the provision of intraday credit to participants. Allow a greater share of reserve holdings to be used intraday for payments purposes.</i>
Security and operational reliability, and contingency arrangements <i>CP VII</i>	<i>A comprehensive risk analysis and management framework should be elaborated, documented and implemented and a risk analysis should be made regularly. Business continuity and contingency procedures should be defined, documented and subsequently, regularly tested. Security and performance requirements for communication services should be further elaborated and adherence control strengthened.</i>
Efficiency and practicality of the system <i>CP VIII</i>	<i>Elaborate on the justification for the large difference in fees and ensure consistency in fees applied. Assess accuracy of cost allocation between BISS and the NBRB clearing system. Develop the cost calculation methodology further and consider including at least some of the investment costs (e.g. software development) in the costs to be recovered. Shorten the operating time and consider introducing some throughput guidelines to banks.</i>
Criteria for participation <i>CP IX</i>	<i>Introduce explicit rules for (voluntary and enforced) exit.</i>
Governance of the payment system <i>CP X</i>	<i>Critically assess and strengthen the governance arrangements for the BISS. The roles, duties and the controls thereof could be further clarified in detailed service level agreements between the NBRB and its payment system subsidiaries. Address overstaffing in the Belarusian Interbank Settlement Center and the Center for Banking Technologies, and administrative overhead in general.</i>
Central Bank Responsibilities in applying the CPs <i>Responsibilities A-D</i>	<i>The NBRB should formally establish an oversight function (separated from the operational function) and, subsequently, ensure sufficient training in building up oversight competence. Define and make publicly available the main NBRB payment system oversight objectives and policies. Establish an Action Plan for addressing the shortcomings identified in the assessment of BISS against the Core Principles.</i>

Authorities' response

85. The authorities generally agree with the assessment. At the same time it should be noted that even though the National Bank does not have a formally defined task to supervise payment systems, it does engage in a broad set of measures associated with the fulfillment of that function.

FATF RECOMMENDATIONS FOR ANTI-MONEY LAUNDERING AND COMBATING THE FINANCING OF TERRORISM

Introduction

86. This Report on the Observance of Standards and Codes for the FATF Recommendations for anti-money laundering and combating the financing of terrorism (AML/CFT) is based on the Forty Recommendations 2003 and the Nine Special Recommendations on Terrorist Financing 2001, as amended, and was prepared using the AML/CFT Methodology 2004. The assessment team reviewed the institutional framework, the relevant AML/CFT laws, regulations, guidelines and other requirements, and the regulatory and other systems in place to deter money laundering (ML) and the financing of terrorism (FT) through financial institutions and designated non-financial businesses and professions (DNFBP), as well as examining the capacity, the implementation, and the effectiveness of all these systems.

87. This report provides a summary of the AML/CFT measures in place in Belarus at the date of the on-site visit or immediately thereafter. It describes and analyzes the measures and provides recommendations for improvement (see Table 5).

Main findings

88. Belarus has many of the elements of a modern AML regime. Money laundering is criminalized. Financial institutions must monitor and report financial transactions subject to special control under the AML Law and take other measures to deter money laundering. Compliance supervision is detailed with a strong culture of on-site examination. Two agencies currently exercise financial intelligence responsibilities. Money laundering offenses are investigated and some have been successfully prosecuted. Some capacity exists to cooperate internationally.

89. Nevertheless, the assessment identified gaps and misalignments in the current legal and institutional framework, as well as incomplete implementation which undermine the full effectiveness of the AML/CFT measures. The AML/CFT legal and institutional framework needs to be updated and reorganized and all relevant government agencies should coordinate their efforts to ensure that the legislative and regulatory changes to be put into place will be implemented effectively. The authorities are aware of the need to update and reshape the present measures and are well advanced on a reform agenda.

General

Situation of Money Laundering and Financing of Terrorism

90. While the situation is difficult to assess independently, Belarusian officials identified a variety of predicate offenses which they believe are linked to money laundering either in or through Belarus, most of which are typical for the region. In their view, tax evasion, customs

violations, and contraband are frequent predicate offenses. Fraud and other white-collar crime was noted as a source of illegal proceeds. Officials observed that proceeds from crimes related to drugs, trafficking in people, and illegal arms dealing could also be significant. Cross-border cash movements were cited as a concern, particularly across the Russian border where there are no controls. Such examples are illustrative, as there is no centralized agency systematically collating this information.

Overview of Financial Sector and DNFBPs

91. Banks dominate financial activity in Belarus. The National Bank of Belarus (NBRB), the central bank, is the regulator of banks. The banking sector is comprised of 31 active banks with the six largest banks making up about 85 percent of the total assets of the banking system. Of the six largest banks, five are exclusively or mainly state owned. Foreign participation is largely confined to smaller banks, primarily through joint ventures in Belarus banks. Money exchange is a separately licensed activity which, to date, has only been authorized for banks. Only banks may be authorized to be agents for money remitters and Western Union is the largest money remitter. The internal security authorities expressed confidence that no significant informal transfer activity takes place.

92. The insurance sector is small, consisting of 34 companies, 31 of which are currently licensed and operational, of which three are government owned. The largest (government owned) accounts for approximately 60 percent of the market. Auto, health, and property business predominates. No firms specialize in reinsurance. The Ministry of Finance (MOF) is the regulator of insurance.

93. The securities sector is small with 131 firms licensed to operate in the sector, a number of which are dormant. Activity is dominated by transactions in government securities and NBRB securities; banks dominate trading in these securities. The securities sector is regulated by the Committee on Securities at the Council of Ministers (SC).

94. The most important DNFBPs are lawyers, notaries, auditors, real estate agents, and casinos, all of which are governed by specific legislation and regulation. Company formation is not a distinct profession, with services provided by lawyers, notaries and accountants. Trust activity is not well developed and asset management appears to be largely confined to banks. Dealings in precious metals and stones are conducted on a limited scale, primarily by banks under a special license from the NBRB, and nonbank dealers licensed by the MOF. There are approximately 25 casinos, none on a large scale.

Legal Systems and Related Institutional Measures

Criminalization of ML and FT

95. Belarus criminalized ML in June 1999 through Article 235 of the Criminal Code (CC). The predicate offenses for ML include criminal, civil and administrative offenses, but do not cover all offenses required by the Vienna and Palermo conventions (insider trading

and securities market manipulation are not yet covered), or provide for self-laundering. The very high evidentiary standard for prosecuting ML, which requires proving both the intent to legalize illegal proceeds and specific knowledge of the predicate offense, needs to be reduced. A prior conviction for the predicate offense is also required in order to prove that the funds are proceeds of crime.

96. Law No. 77-3 of January 3, 2002 “On combating terrorism” (CT Law) outlines the legal and institutional framework for combating terrorism, but does not criminalize FT as a separate, autonomous offense. FT can only be prosecuted as a form of complicity in terrorism-related crimes. The AML Law does not cover terrorist financing; a draft law amending the CC would criminalize FT separately.

Confiscation, freezing, and seizing of proceeds of crime

97. Belarus legislation provides broad powers of seizure, and for law enforcement agencies to identify and trace property. The confiscation system in Belarus is conviction-based and is available for all serious criminal offenses in the CC, including ML, and confiscation is generally applied upon conviction to the assets seized in the course of the judicial procedure. Confiscation from third parties appears to be possible under Belarus law, but the rights of bona fide third parties are not expressly provided for in the legislation.

The Financial Intelligence Unit and its functions

98. The Department of Financial Monitoring of the State Control Committee (DFM) is the designated FIU for Belarus. However, the typical FIU functions are carried out, in practice, by both the DFM and the Ministry of Taxes and Duties (MTD). The DFM only receives Special Data Forms (SDFs)¹¹ regarding foreign currency transactions, while the MTD receives SDFs for both local and foreign currency transactions. Each of these authorities then processes and disseminates the resulting intelligence to the appropriate law enforcement agencies. The DFM's operational independence is not specifically provided for in legislation, but appears to be effective in practice. There is a need to expedite the enactment of legislation to consolidate the DFM as the single, centralized FIU for Belarus. The DFM represents Belarus in the Eurasian Group Against Money Laundering (EAG)¹² and has applied for membership of the Egmont Group of FIUs, but has yet to be accepted. Comprehensive statistics on SDFs (including in domestic currency) are not yet compiled. There is a need for adequate funding, staffing and resources for the DFM, as well as resources for an enhanced electronic database for analysis to DFM.

¹¹ SDFs are a form of criteria-linked threshold reporting.

¹² EAG is a newly established FSRB whose membership comprises Belarus, China, Kazakhstan, the Kyrgyz Republic, Tajikistan, and Russia.

Law enforcement, prosecution, and other competent authorities

99. The investigation of economic crimes in Belarus is carried out under the supervision of the Prosecutor General's Office (PGO) and its investigatory divisions, the Ministry of Internal Affairs (MIA), the Financial Investigations Department (FID) of the SCC and the Economic Security Directorate of the State Security Committee (SSC), each within the area of responsibility assigned in the Criminal Procedure Code (CPC). The Anti-Terrorism Centre of the SSC is responsible for the coordination of the preliminary investigations of terrorism-related offenses. The specific areas of responsibility of each investigatory agency are not clearly established by the legislation, nor is a precise mechanism through which the AML/CFT actions should be coordinated.

100. The law on state security agencies provides adequate powers to search and compel production of materials. A variety of investigative techniques, such as controlled delivery, surveillance, infiltration, and wire-tapping, are available. There is a need for additional staff and more training, experience and expertise to fight organized crime and serious economic crime. Comprehensive AML/CFT statistics are not maintained on seizure and confiscation of property, mutual legal assistance (MLA), or extradition requests. Controls on cross-border movements of cash need to be reviewed for effectiveness and extended to cover negotiable instruments.

Preventive Measures—Financial Institutions

101. Under the AML Law, the preventive measures required to be implemented by banks, nonbank financial institutions, and certain DNFBPs include: recording and reporting of financial operations subject to special control; customer identification, retention of records related to foreign exchange transactions for 10 years, retention of other records related to domestic currency transactions for periods specified by relevant supervisors; and development of internal policies and controls as necessary to comply with the AML Law. The scope and content of these preventive measures need to be spelled out in more detail in legislation. Oversight of preventive measures falls to several agencies: the SCC, the MTD, and the primary functional regulators. Legally binding regulations have been issued with respect to financial transactions subject to special control, with compliance procedures specified by the MTD. The NBRB has issued AML/CFT implementing recommendations to the institutions it supervises. Although not binding legally, they are treated as mandatory in practice. The other functional regulators have not as yet issued guidance on implementation of preventive measures.

102. In addition to banks, the preventive measures obligations imposed by the AML Law also apply to persons engaged in financial operations in the following sectors: securities, insurance, investment funds, a range of money service businesses, notaries, and casinos. The post office, attorneys, real estate agents, or dealers in precious metals and stones are not subject to preventive measures requirements.

103. *Suspicious transaction reporting.* The AML Law requirement to report “financial operations subject to special control” stresses threshold reporting and could not be considered as providing for suspicious transactions reporting in line with the FATF standard. The Law lists categories of transactions that must be reported where they exceed one of the specified thresholds (2,000 base units for individuals and 20,000 for legal entities, equivalent to approximately US\$23,000 and US\$230,000, respectively). The authorities and reporting institutions were unclear whether suspicion needs also to be taken into account or whether exceeding the threshold value is the sole determinant for reporting.

104. *Financial Institution secrecy or confidentiality.* The reporting obligation under the AML law supersedes other confidentiality requirements. Some transactions below the thresholds in the AML Law are reported and it is unclear whether the exemption from confidentiality obligations would also apply to them. Moreover, the extension of the reporting requirements to a broader range of DNFBPs would require clarification of the professional secrecy obligations of various professions, particularly for lawyers.

105. *Customer Due Diligence.* The requirement in Article 3(4) of the AML Law for customer identification is scant. However, under other tax and legal provisions there are strict registration requirements for legal entities and individual entrepreneurs which require a number of layers of identification by financial institutions. The AML Law gives broad authority to supervisors to adopt implementing regulations. For banks the NBRB’s KYC recommendations set out detailed identification provisions for both individuals and legal entities. These include face-to-face account opening with identity verification based on passport for individuals or registration documents and tax records for legal entities. Normally an individual may not open an account on behalf of another. There are no requirements for politically-exposed persons, foreign or domestic. Requirements for correspondent banking are being updated.

106. While banks are instructed to identify the founders of legal entities, identification of beneficial owners is not addressed in the NBRB recommendations. Banks are advised to assess the level of risk on the basis of information provided and to question the sources of funds and type of business in high-risk cases. Anonymous accounts are not accepted and, although bearer accounts are still legally provided for, they do not exist in practice. The NBRB recommendations do not address one-time transactions but they do suggest that for transactions below mandatory reporting threshold passport identification is sufficient.

107. Compliance with customer identification procedures is systematically reviewed by the NBRB during on-site examinations. Interviews with banks indicated a high level of awareness of CDD requirements and well-established routines for ensuring compliance.

108. *Internal controls, compliance, training and audit.* The NBRB’s recommendations provide useful guidance on developing banks’ AML internal control systems. Although not legally binding, they are treated as mandatory in practice and are the subject of on-site and off-site checking and review by the NBRB. Internal audit is mandatory. While officials and financial institutions showed a keen awareness of the requirements, the focus seemed to be

on compliance with centralized control and taxation needs. Additional training is needed to develop an overall awareness of the risks and implications of AML/CFT.

109. *Supervisory and oversight system.* Banks in Belarus are licensed and supervised by the NBRB, which is well staffed and has comprehensive enforcement powers. Fit and proper tests are applied to shareholders above a 10 percent threshold. Through its active on-site and off-site supervision, the NBRB checks compliance in the implementation of the AML Law and its AML recommendations. On-site inspections include a review of relevant policies and procedures and sample transaction testing.

Insurance

110. Under Presidential Decree No. 17, last amended in 2003, insurance businesses are registered, licensed, and supervised by the MOF, which is adequately resourced and has an active program of on-site inspections for the legislative obligations of the insurance acts, though not for AML/CFT. The MOF does not carry out specific fit and proper testing for ownership of insurance companies and has not issued any specific AML/CFT guidance.

Securities

111. Other than dealings in government securities, securities operations are small. Within the limits of its resources, the SC carries out active supervision of the market and its participants. Although securities firms are subject to the AML Law, the SC has not issued guidance or taken any specific steps to ensure that AML/CFT measures are applied.

112. Additional training in AML/CFT is needed for all supervisory authorities, particularly for implementation of the FATF Recommendations.

Preventive Measures—Designated Non-Financial Businesses and Professions

113. *Customer due diligence and record keeping.* DNFBPs are subject to customer identification and record-keeping requirements. In most cases, these obligations are imposed under professional or administrative laws and regulations. For individuals, passport identification is the norm. For legal entities, registration documentation, including details on founders and controllers, is the norm. Identification of beneficial owners is rare. Face-to-face identification is standard, although by exception notarized documents may be accepted. A statement of business purpose may be requested. There is no provision for enhanced due diligence for high-risk transactions. Record keeping requirements meet or exceed a minimum five-year retention period. Reidentification is not addressed. For casinos, customer identification is required only for winnings above 1,000 base units (approximately US\$11,500). Regulators should issue CDD guidance for their sectors.

114. *Monitoring of transactions and relationships.* For lawyers, notaries, and auditors, monitoring of client transactions does not typically arise since these professions are prohibited from engaging in commercial activities, and they do not normally execute

transactions on behalf of clients. Where continuing relationships are involved, regulations and professional norms typically call for annual update of client information.

115. *Suspicious transaction reporting.* Under the current AML Law, the post office, lawyers, auditors, real estate agents and dealers in precious metals and stones are not expressly required to report financial operations subject to special control. Of the FATF list of DNFBPs, only notaries and casinos are required to report suspicious transactions.

116. *Internal controls, compliance, and audit.* DNFBPs in Belarus are subject to internal control requirements, although typically not imposed explicitly for AML/CFT. While casinos are subject to the AML Law and are required to have stringent financial controls for tax purposes as well as to prevent employee theft, not for AML purposes.

117. *Regulation, supervision and monitoring.* Each category of DNFBP is regulated in some form. Attorneys, notaries, and real estate agents are under the MOJ. Auditors and insurance are under the MOF. Casinos are regulated by the Ministry of Sports and Tourism. The Post Office is the responsibility of the Ministry of Communications. Dealers in precious metals and stones are regulated by the NBRB (for banks) or the MOF (others). The Law on the Legal Profession delegates responsibility for regulation and oversight of lawyers, including sanctioning, to the Republican Bar.

International Cooperation

118. Belarus is a party to the Vienna Convention, the Palermo Convention and the Terrorist Financing Convention and to 11 U.N. treaties concerning terrorism-related crimes. Belarus also is a party to the U.N. Convention Against Corruption. Belarus is making efforts to implement the UNSCRs 1267, 1373 and successor Resolutions. Resolution No. 10 of January 28, 2002 of the NBRB provides for the suspension of credit and debit transactions in respect of accounts belonging to terrorists, terrorist organizations, and persons associated therewith. There has not yet been a case in practice where terrorists' assets have been frozen or identified by the banks in Belarus. Coordination of counter-terrorism is conducted by the Interdepartmental Counter-Terrorism Commission.

119. MLA in criminal matters may be provided based on multilateral or bilateral treaties to which Belarus is a party, or case by case on condition of reciprocity as determined by the PGO and the Supreme Court. Belarus normally does not apply a dual criminality condition. Financial secrecy or taxation issues would not be grounds for refusal of assistance.

120. All crimes are extraditable offenses under the CC, including ML and the FT-related offenses. Belarus does not consider terrorist acts to be political offenses for which extradition can be refused. There is no extradition law in Belarus, but provision is included in the CC. Belarusian nationals may not be extradited to a foreign state. The CC does not mention any specific grounds for the refusal of extradition, other than those specified in each of the bilateral treaties. Belarus has signed extradition treaties with the 15 FSU countries and with four other countries.

121. All authorities are authorized to share information spontaneously with their foreign counterparts in relation to ML and predicate offenses, subject to reciprocal treatment and within the limits established in the legislation. The performance of inquiries on behalf of foreign counterparts is also authorized.

Summary assessment against the FATF Recommendations

122. The current AML/CFT measures in Belarus were designed mainly for purposes other than specific compliance with the FATF Recommendations. As a result, many changes and improvements are needed to achieve such compliance. Nonetheless, many of the current measures are reasonably effective for their purpose. The following table sets out the recommended actions in relation to the FATF 40+9 Recommendations:

Table 5. Recommended Action Plan to Improve the AML/CFT System

FATF 40+9 Recommendations	Recommended Action (listed in order of priority)
Legal System and Related Institutional Measures	
Criminalization of Money Laundering (R.1 & 2)	<ul style="list-style-type: none"> • Reduce excessive burden of proof for prosecuting ML and criminalize all the types of ML offenses under the Vienna and Palermo Conventions. • Allow prosecution for “self-laundering” and that intention of ML may be inferred from objective factual circumstances. • Establish criminal liability of legal entities for ML
Criminalization of Terrorist Financing (SR.II)	<ul style="list-style-type: none"> • Criminalize FT as a separate offense from terrorist acts and introduce preventive measures against FT.
Confiscation, freezing and seizing of proceeds of crime (R.3)	<ul style="list-style-type: none"> • Make confiscation obligatory for ML or FT, including for legal entities. • Extend provisional measures to include ML and FT.
Freezing of funds used for terrorist financing (SR.III)	<ul style="list-style-type: none"> • Require freezing of terrorist assets without delay or prior notice. Allow for unfreezing. Clarify powers of authorities in relation to suspected terrorist assets.
The Financial Intelligence Unit and its functions (R.26, 30 & 32)	<ul style="list-style-type: none"> • Enact draft AML Law to provide for DFM as the centralized FIU for Belarus, with adequate resources. • Expedite implementation of steps needed to gain admission to the Egmont Group.
Law enforcement, prosecution and other competent authorities (R.27, 28, 30 & 32)	<ul style="list-style-type: none"> • Improve coordination between investigating agencies. • Provide training for judges and prosecutors. • Compile and maintain relevant statistics.
Cash couriers (SR IX)	<ul style="list-style-type: none"> • Provide AML/CFT training to customs officers. • Improve border controls for movements of cash and include bearer negotiable instruments.
3. Preventive Measures–Financial Institutions	
Customer due diligence, including enhanced or reduced measures (R.5 to 8)	<ul style="list-style-type: none"> • Explicitly prohibit anonymous and bearer accounts. • Specify in AML Law the basis for, nature, and timing of CDD and the identification of beneficial owners. • Require in the AML Law ongoing due diligence for all

	<p>transactions, not just special control list.</p> <ul style="list-style-type: none"> • Introduce enhanced due diligence for foreign PEPs. Consider extending to domestic PEPs. • Proceed with more detailed requirements for correspondent banking.
Record keeping and wire transfer rules (R.10 & SR.VII)	<ul style="list-style-type: none"> • Provide clearly for five-year record retention and for originator information for all wire transfers.
Monitoring of transactions and relationships (R.11 & 21)	<ul style="list-style-type: none"> • Require special attention for complex or unusual transactions and for countries with weak AML/CFT.
Suspicious transaction reports and other reporting (R.13-14, 19, 25 & SR.IV)	<ul style="list-style-type: none"> • Require reporting to the DFM of all suspicious transactions, regardless of size or currency and provide a clearer prohibition on tipping off. • Issue AML/CFT guidance to all reporting entities. • Enact an FT Law.
Internal controls, compliance, audit and foreign branches (R.15 & 22)	<ul style="list-style-type: none"> • Require additional employee training programs.
Shell banks (R.18)	<ul style="list-style-type: none"> • Presence and control of banks to be within Belarus.
The supervisory and oversight system—competent authorities and SROs (R. 17, 23, 29 & 30).	<ul style="list-style-type: none"> • Specify the role of the SC in supervising AML/CFT for the securities sector.
Financial institutions—market entry and ownership/control (R.23)	<ul style="list-style-type: none"> • Apply fit-and-proper tests to owners (and ultimate beneficial owners) of financial institutions.
AML/CFT Guidelines (R.25)	<ul style="list-style-type: none"> • Update NBRB guidance and provide firm legal basis. • Issue guidance for the insurance and securities sectors.
Ongoing supervision and monitoring (R.23, 29 & 32)	<ul style="list-style-type: none"> • Collect and analyze comprehensive statistics.
4. Preventive Measures—Nonfinancial Businesses and Professions	
Customer due diligence and record-keeping (R.12)	<ul style="list-style-type: none"> • Apply CCD, record-keeping requirements, and preventive measures to lawyers, auditors, real estate agents, and dealers in precious metals and stones. • Issue CDD guidance, simplified if ML/FT risk is low. • Apply five-year record-keeping requirements.
Monitoring of transactions and relationships (R.12 & 16)	<ul style="list-style-type: none"> • Require all DNFBPs to monitor all transactions for suspicious characteristics. Issue guidance. • For each DNFBP category, issue AML/CFT guidance. For lawyers, both the MOJ (for “public” lawyers) and the Republican Collegium (for “private” lawyers) should issue such guidance.
Suspicious transaction reporting (R.16)	<ul style="list-style-type: none"> • Amend the AML law to extend suspicious transactions reporting to all DNFBPs. • Training on identification of suspicious transactions should be provided to all DNFBPs.
Internal controls, compliance & audit (R.16)	<ul style="list-style-type: none"> • Require: internal policies, and controls, employee screening and training; and an audit function.
Regulation, supervision and monitoring (R.17, 24-25)	<ul style="list-style-type: none"> • Apply AML Law to lawyers, auditors, real estate agents, and dealers in precious metals and stones. • Assign AML/CFT compliance responsibility to the functional regulator, the DFM, or both. • Provide training to both regulators and regulated.

Other designated nonfinancial businesses and professions (R.20)	<ul style="list-style-type: none"> Require settlement of real estate transactions between individuals by bank transfers or check.
5. Legal Persons and Arrangements & Nonprofit Organizations	
Legal Persons–Access to beneficial ownership and control information (R.33)	<ul style="list-style-type: none"> Improve completeness and accuracy of company registration information, to include verification of beneficial ownership, including for nonresidents.
6. National and International Cooperation	
National cooperation and coordination (R.31)	<ul style="list-style-type: none"> Include DNFBPs in interdepartmental agreements with an AML/CFT coordinating committee.
The Conventions and UN Special Resolutions (R.35 & SR.I)	<ul style="list-style-type: none"> Ensure full implementation of UNSCRs. Review FT Convention; amend legislation as needed.
Mutual Legal Assistance (R.32, 36-38, SR.V)	<ul style="list-style-type: none"> Enact draft law on international legal assistance. Adopt administrative procedures to prevent MLA requests from being unduly delayed.
Extradition (R.32, 37 & 39, & SR.V)	<ul style="list-style-type: none"> Enact draft law to render international legal assistance. Ensure that extradition requests are not delayed

Authorities’ response to the assessment

123. The Authorities were broadly in agreement with the assessment.

STRESS TESTING SHOCKS AND SCENARIOS

Methodology

124. The stress tests of the Belarusian banking system were conducted using detailed balance sheet data for all thirty-one commercial banks which operated in Belarus as at June 2004. The purpose of these tests was to examine the potential effects of a set of specified changes in risk factors, corresponding to exceptional but plausible events, on banks' financial condition. Historical and hypothetical scenarios based in part on the rest of the FSAP analysis were used to calibrate the shocks. The stress tests gauged the vulnerabilities of banks to a deterioration in the quality of credit portfolio, exchange rate and interest rate fluctuations, and liquidity withdrawals.¹³ In accordance with confidentiality requirements in Belarus, the data on individual banks did not identify any of the banks.

125. The stress tests were performed for each individual bank as well as for five different groups of banks. Group 1 included six largest banks; Group 2 included state-owned commercial banks (6 banks); Group 3 included local private banks (7 banks); Group 4 included foreign banks (18 banks); and Group 5 included all commercial banks (31 banks). Prior to undertaking the tests, the balance sheet data for the banks were adjusted to correct the existing over-capitalization bias of the Belarusian accounting and asset classification practices.¹⁴ The adjustments resulted in a reduction of capital adequacy ratio (CAR) of the banking sector as at June 2004 from 24.9 percent to 18.6 percent, or by approximately 25 percent (Box 4).

Results

126. The stress tests found that the Belarusian banks are vulnerable to credit and liquidity shocks (Table 6). The special features of the banking sector and the economy (large share of loss-making enterprises, large share of foreign-currency-denominated loans, and large share of assets with long-term maturities) could substantially amplify the impact of a disturbance:

- **Credit risk.** Three separate stress test scenarios for credit risk were performed: a deterioration in the quality of 50 percent of loans issued to agricultural enterprises, a deterioration in the quality of 5 percent of loans issued to non-agriculture sectors, and a shift by one category in classified loans (due for example, to a decline in the value of

¹³ No stress tests were performed for equity price risk as the exposure of Belarusian banks to this type of risk is negligible. As of end-June 2004, private sector securities accounted on average for less than 5 percent of the total bank holdings of securities and 0.4 percent of the banking sector assets. A hypothetical assumption of a stock market crash would therefore have no major direct impact on banks.

¹⁴ The precise scale of the adjustments made was approximate only, as the mission did not have sufficient information to determine them with great accuracy.

collateral held by banks).¹⁵ The results indicate that all five groups of banks would be able to withstand such shocks.

- **Market risk.** Overall, the banks were found to be sufficiently capitalized to withstand the direct effects of a substantial volatility of the exchange rate or interest rate. However, the regulatory capital in two large banks would decline below the required minimum in case of a hypothetical parallel increase in the rubel yield curve by 10 percentage points.¹⁶ The indirect exposure of banks to exchange rate fluctuations represents a serious concern for many banks. A depreciation of the rubel by 20 percent, with a deterioration in the quality of unhedged foreign-currency-denominated loans (assuming a 50 percent provisioning)¹⁷ would substantially affect the solvency of many Group 1, 3, and 4 banks, given that foreign currency denominated loans in these banks account for a substantial portion of total loans (more than 80 percent of all loans issued by Group 3 and Group 4 banks were denominated in foreign currency as of June 2004).
- **Combined credit and market risk.** Simultaneous shocks on credit quality, exchange rate, and interest rate would have a substantial impact on the capital position of banks, especially for Group 1 and Group 3 banks. A depreciation by 20 percent, a deterioration in the quality of unhedged loans in foreign currencies (with 50 percent provisions), and an increase in interest rates of short-term maturities would reduce the CAR of Group 1 banks to 9.2 percent. A capital injection of approximately BYR610 billion would be required to restore the capital adequacy of these banks.
- **Liquidity risk.** The results of stress tests for liquidity risk show that a 20 percent run on liquid liabilities would further worsen the liquidity condition of state-owned banks. The liquidity ratio of these banks would fall from 50.1 percent to 37.6 percent. Such a shock would not however result in a significant liquidity shortage in private banks and foreign banks; the liquidity coverage as measured by the ratio of liquid assets to liquid liabilities would remain adequate in these banks (above 70 percent).

127. The reported and adjusted aggregate CAR for Group 1, 2, and 5 banks as well as the aggregate stress test results for these banks are substantially affected by the ongoing recapitalization of large banks. As a result of these recapitalizations, the CAR of one bank

¹⁵ A relatively large deterioration in credit quality for agricultural loans was assumed due to the significant evergreening of loans that has taken place in this sector in the past, indicating that the sector is not very profitable and thus likely to be highly impacted by an adverse shock.

¹⁶ The interest-rate sensitive assets and liabilities are smaller than banks' assets and liabilities distributed by different maturity brackets—hence the interest rate exposure of Belarusian banks is likely to be smaller than the results of the stress test would suggest—because some medium- and long-term loans issued to their customers are at floating rates.

¹⁷ All loans issued to agriculture, construction, and households, and 20 percent of loans issued to industry, trade, and other sectors were estimated as being unhedged.

was very high as of end-June 2004. The exclusion of this bank from Group 1, 2, and 5 banks significantly reduces the aggregate CAR for these groups of banks. For example, the adjusted CAR for Group 1 banks would be reduced from 17.6 percent to 10.5 percent when this bank is excluded from the sample.

Box 4. Stress Tests: Adjustments to the Reported Data

Prior to undertaking the stress tests, the banks' balance sheet data were adjusted to correct the existing over-capitalization bias arising from the Belarusian accounting and asset classification practices. The precise scale of the adjustments was approximate only, using several *ad hoc* assumptions, as the mission did not have sufficient information to determine these adjustments with great accuracy. The following adjustments were made:

- ***Establishment of general provisions.*** According to the Belarusian banking regulations, banks are not required to maintain general provisions against nonperforming loans. Although banks distribute a portion of their profits in reserves which can subsequently be used to write-off loan losses, the amount of these reserves is not related to the amount of total loans, and these reserves are fully included in the calculation of the regulatory capital. In line with existing international practice, Belarusian banks were assumed to form general provisions equal to 2 percents of their total loans, which were then subtracted from the amount of regulatory capital.
- ***Increase in specific provisions for loans prolonged by official decrees.*** In recent years, at least five different Presidential decrees have ordered Belarusian banks to reschedule loans distributed to enterprises of specific economic sub-sectors, which were in weak financial position. The loans were mainly to enterprises in the agricultural and industrial sub-sectors, provided by three large state-owned banks. It was assumed that 70 percent of these rescheduled loans are in fact loss, which should be fully provisioned for, whereas they are currently classified as substandard and are provisioned for at 30 percent (no information was available on the precise classification of these loans, which are actually distributed across all four classification categories).
- ***Increase in specific provisions for the estimated amount of underreported NPLs.*** An estimate of underreported NPLs (and hence underprovisioning) was based on the results of inspections conducted by the NBRB in eleven banks in the first nine months of 2004. With one exception, all small banks were confirmed to be adequately implementing asset classification and provisioning rules. The on-site inspections in large banks, however, typically revealed that a part of loans needed to be reclassified. Indications are that there is also substantial underprovisioning due to underreported NPLs in the largest bank in the country. Therefore, it was assumed that the six largest banks need to increase their provisions for bad loans by 10 percent.
- ***Increase in specific provisions for unclassified long-term NPLs.*** The rules on the formation of provisions for loan losses authorize banks to establish specific provisions for loans with a remaining maturity of over one year only for the amount of payment overdue. It was assumed that specific provisions for long-term NPLs should be increased by 12 times. This assumption was borne out by the estimation of the average remaining maturity of long-term loans (3 years) and the average number of annual payments scheduled for bank loans (4 times, or quarterly payments).
- ***Reduction in the amount of revaluation accounts included in the regulatory capital.*** In a relatively high inflation environment, revaluation of fixed assets has been an important factor affecting the capital position of banks, with several banks reporting revaluation accounts substantially higher than their equity capital. Large surpluses on the revaluation accounts should, however, be seen with caution in Belarus due to the problems in using an appropriate valuation technique for these assets and also because these surpluses may be quickly absorbed by significant market reversals (e.g., in case of a major fall in fixed asset prices). Currently, Belarusian banks are allowed to fully include their revaluation accounts in the calculation of Tier II capital. It was assumed that only 50 percent of these revaluation accounts are included in the regulatory capital.

Table 6. Belarus: Summary of Stress Test Assumptions and Results 1/

	Group 1	Group 2	Group 3	Group 4	Group 5	Group 1 without one large bank	Group 2 without one large bank	Group 5
Reported Capital Adequacy Ratio	24.1	26.0	22.0	23.2	24.9	16.5	16.6	18.5
Adjusted Capital Adequacy Ratio	17.6	18.7	16.2	18.5	18.5	10.5	10.0	12.7
Capital Adequacy Ratio After Shocks								
A. Credit Risk								
50 percent of loans to agriculture become loss	13.0	13.4	15.8	17.5	14.6	9.2	8.6	11.5
5 percent of loans to nonagriculture sectors become loss	14.6	15.8	13.5	15.9	15.7	7.1	6.4	9.5
Shift in classified loans by one category 2/	12.4	13.3	12.3	14.6	13.6	5.7	4.9	8.1
B. Exchange Rate Risk								
Depreciation by 20%	17.5	18.8	15.8	18.2	18.5	10.4	9.9	12.5
Depreciation by 20%; deterioration in the quality of all unhedged FX loans (50% provisions) 3/	12.1	13.9	9.8	10.8	13.0	4.3	4.3	6.5
Appreciation by 20%	17.6	18.7	16.6	18.7	18.6	10.7	10.1	12.9
C. Interest Rate Risk								
Increase in BLR yield curve by 1000 basis points	13.8	14.2	15.8	18.3	15.3	7.5	6.1	10.1
Increase in FX interest rates by 500 basis points	16.6	17.7	16.1	17.8	17.7	9.4	8.7	11.7
Increase in interest rates of short-term maturities	14.7	15.4	15.8	17.6	15.9	7.9	6.8	10.4
D. Combined Scenario								
Depreciation by 20%; deterioration in the quality of all unhedged FX loans (50% provisions); increase in BLR short-term interest rates 3/	9.2	10.5	9.4	10.0	10.4	1.6	1.1	4.2
E. Liquidity Risk								
Reported Liquidity Ratio (BYR and FX) 4/	53.1	50.1	78.5	80.1	59.1	48.8	44.4	55.8
Reported Liquidity Ratio (BYR) 4/	50.3	48.4	82.8	78.7	55.4	44.1	41.0	50.5
Reported Liquidity Ratio (FX) 4/	56.8	52.8	75.4	81.0	63.9	54.6	49.4	62.1
Liquidity Ratios After Shocks								
A 20% withdrawal in liquid liabilities (BYR and FX)	41.4	37.6	73.1	75.1	48.9	36.0	30.4	44.8
A 20% withdrawal in liquid liabilities (BYR)	37.9	35.5	78.5	73.4	44.2	30.1	26.3	38.1
A 20% withdrawal in liquid liabilities (FX)	46.0	41.0	69.2	76.2	54.8	43.2	36.7	52.6

1/ Group 1 includes 6 largest commercial banks. Group 2 includes state-owned commercial banks (6 banks). Group 3 includes local private banks (7 banks). Group 4 includes foreign banks (18 banks). Group 5 includes all commercial banks (31 banks).

2/ 20 percent of standard loans are assumed to become substandard.

3/ The share of unhedged loans is estimated based on the sectoral distribution of foreign currency loans. All loans issued to agriculture, construction, and households, and 20 percent of loans issued to industry, trade, and other sectors are estimated as being unhedged.

4/ Liquidity ratio is defined as the ratio of liquid assets (assets with a maturity of less than 1 month) to liquid liabilities (liabilities with a maturity of less than 1 month). The prudential minimum required for this ratio is 70 percent.