August 2006
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Republic of Belarus: 2006 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for the Republic of Belarus

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2006 Article IV consultation with the Republic of Belarus, the following documents have been released and are included in this package:

- the staff report for the 2006 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on May 26, 2006, with the officials of the Republic of Belarus on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 21, 2006. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its August 4, 2006 discussion of the staff report that concluded the Article IV consultation.

- a statement by the Executive Director for the Republic of Belarus.

The documents listed below have been or will be separately released.

Selected Issues Paper
Statistical Appendix

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

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INTERNATIONAL MONETARY FUND

REPUBLIC OF BELARUS

Staff Report for the 2006 Article IV Consultation

Prepared by the Staff Representatives for the 2006 Consultation
with the Republic of Belarus

Approved by Poul M. Thomsen and Adrienne Cheasty

July 21, 2006

- The discussions were held in Minsk during May 17–29, 2006. The mission met with Deputy Prime Minister Kobiakov, Ministers Korbut (Finance), Zaichenko (Economy), and Zinovsky (Statistics), Governor of the National Bank of the Republic of Belarus (NBRB) Prokopovich, other senior officials in government and the presidential administration, as well as representatives of parliament, banks, research institutes, and the diplomatic community.

- The mission comprised Balázs Horváth (Head), Marco Rossi (both EUR), Serkan Arslanalp (FAD), and Kristian Hartelius (ICM). Resident Representative Office staff, Neven Mates (EUR), Senior Resident Representative in Moscow, and Mr. Kiekens, Executive Director, participated in the discussions.

- Belarus has accepted the obligations of Article VIII, maintains an exchange system free of restrictions on the making of payments and transfers for current international transactions, and has no outstanding purchases. The 2005 Article IV consultation was completed on June 17, 2005.

- President Lukashenko has retained his position after the March 2006 elections and continues to dominate political life.

- Lack of policy convergence precludes the near-term implementation of the planned currency union with Russia.

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EXECUTIVE SUMMARY

Background and outlook. Belarus continues to benefit from very favorable energy import prices. Macroeconomic performance has been strong over the past few years, with real GDP growth averaging 7½ percent and inflation falling to under 8 percent at end-2005. Hefty and increasing terms of trade gains related to cheap imported prices of energy have substantially contributed to these results, but are unlikely to continue. Belarus remains vulnerable to a deterioration of the external environment and still faces challenging tasks in fostering the transition to a market-based economy.

Policy discussions focused on the following key issues:

- the sustainability of Belarus's macroeconomic performance in adverse external conditions;
- how to ensure high and sustainable noninflationary growth while enhancing transition reforms; and
- the need for fundamental policy changes.

The authorities and staff agreed that macroeconomic performance had been strong while acknowledging that external circumstances had been favorable. Common ground was found on the need to implement some structural reforms to foster sustainable growth in the medium term, including on the following objectives: reducing the share of GDP redistributed by the budget and the tax burden, strengthening the financial system, facilitating the development of small and medium-sized enterprises, moderating real wage growth, and attracting foreign investors.

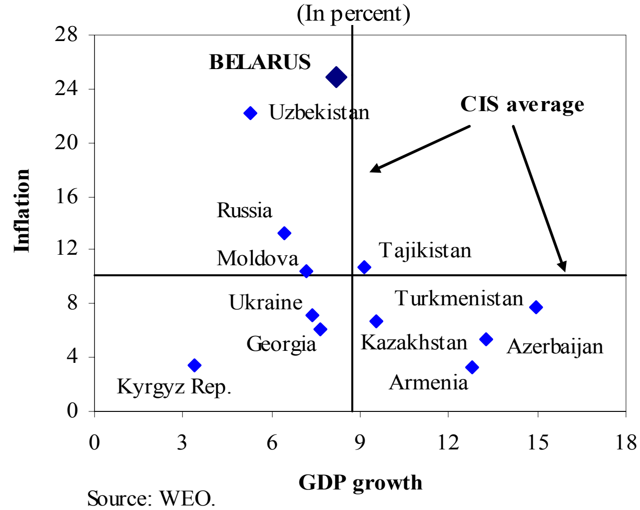
The authorities stressed their achievements in consolidating Belarus's manufacturing base, maintaining a strong social protection element and implementing a unique Belarusian economic development model based on a pragmatic approach to the role of the state and the private sector. They also felt that their reform agenda was sufficient to ensure strong growth over the medium term, even in a less favorable external environment.

Staff, however, stressed that the unfavorable outlook underscored the need for fundamental policy changes. Staff emphasized, in particular, the need for fiscal tightening in anticipation of lower revenues as terms-of-trade gains cease growing or fall, and recommended that the authorities reduce the economy's dependence on fiscal and quasi-fiscal subsidies. Key among the recommended structural reforms are (i) introducing hard budget constraints, including through a significant cut in government subsidies; (ii) phasing out price controls and recommended (directed) lending, (iii) eliminating economywide mandatory wage targets; (iv) revising and limiting the "golden share" rule to a handful of strategic enterprises; and (v) initiating transparent tenders to privatize selected enterprises other than natural monopolies.

I. Background

1. **Belarus's state-dominated economy has performed well over the past few years.** The government's centrally administered, socially oriented policies have facilitated rapid real income growth, near-full employment, and a reduction in poverty to the lowest level in the CIS. GDP growth averaged 8.2 percent in 2002–05, while inflation remained high, but declining—a strong, but not exceptional performance among CIS countries (although Belarus's inflation rate was among the lowest by May 2006). These results were achieved with a dominant role of government in economic activity, while the private sector, subject to pervasive controls and government interference, contributed only one fourth to GDP (*EBRD Transition Report 2005*).

2002-05 macroeconomic performance in CIS countries
(In percent)



Source: WEO.

2. **Favorable energy import prices have supported high growth, particularly in 2005** (Figure 1). A widening gap between world prices for Belarus's energy-intensive exports and prices of energy imports from Russia have provided a large and increasing amount of trading gains—reaching about 12 percent of GDP in 2005.[1] These gains were redistributed through various channels (Box 1), boosting domestic demand—investment and household consumption grew by 13½ and 14½ percent, respectively, in 2005. A measure of growth that excludes the impact of favorable external conditions (Box 2), however, shows that underlying performance has fallen short of headline growth since 2001, especially in 2005.

3. **Other factors also supported growth.** Belarus benefited from strong partner country growth, which, together with the 12¾ percent terms-of-trade improvement, helped swing the current account into a surplus of 1.6 percent of GDP in 2005. Moreover, economic stabilization and rising incomes have strengthened consumer confidence, further contributing to increasing domestic demand. The economy's positive momentum has carried forward into 2006, despite higher imports (Table 1).

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[1] In 2005, Belarus imported gas at US$47 per thousand cubic meters (a quarter of world market levels), and crude oil at US$30/barrel (half of world market prices).

4. **Ample production capacity and price controls have contributed to declining inflation, but some signs of inflationary pressures are emerging** (Figure 2)**.** Owing to a sizable output gap, strong demand has boosted GDP growth beyond potential while headline inflation declined steadily to 6.9 percent in May 2006, aided also by pervasive administrative controls over price formation (Box 3). However, rising unit labor costs, tighter capacity utilization in many sectors, a high and increasing ratio of producer price index (PPI) to CPI inflation, and estimates of underlying inflation suggest a build-up in inflation pressures.

5. **Macroeconomic data may not tell the whole story**. While the statistical system is generally good, state controls and non-market mechanisms permeate economic activity, substantially altering the information content of data. This complicates the assessment of economic developments and of the impact of policy actions.

Box 1. Centralized Redistribution of Terms-of-Trade Gains

Belarus imports energy from Russia at prices below world market levels and exports refined oil products (US$4.9 billion or 55 percent of non-CIS exports in 2005), as well as other energy intensive products, at world market prices. The resulting gains are redistributed into the domestic economy through the budget and through non-budgetary channels.

About a quarter of the terms-of trade gains accrues to the budget by taxing the consumption and export of imported energy, as well as the profits of energy companies. This fiscal windfall feeds budgetary transfers to state-owned enterprises and banks, and to the population (including hikes in budgetary wages). It also supports high budgetary investment.

The remaining gains are redistributed through several non-budgetary channels. First, through economywide mandated wage increases, which, while contributing to raising household demand, further decapitalize enterprises that cannot cover these increases with profits. Second, through large scale recommended (directed) bank lending funded by increasing deposits that reflect higher enterprise profits (mainly those of exporters) and rising household income. Such lending occurs mainly through state-owned banks, which have benefited from a 2005 decree requiring state enterprises to place their deposits with these banks. Finally, the government also mandates significant redistribution through selected state-owned enterprises, notably by keeping domestic energy prices below full cost-recovery levels, and in the form of free gasoline to agriculture.

Box 2. Measures of Underlying Growth

Underlying growth is defined as actual growth minus transient growth effects. Three methods are used to calculate transient effects in 2000–05.

The **terms of trade approach** relies on econometric estimates of the terms of trade elasticity of growth. We combine staff estimates for Belarus with estimates in Broda's (2001) VAR model for developing countries (see Selected Issues Paper, Chapter I for details and references).

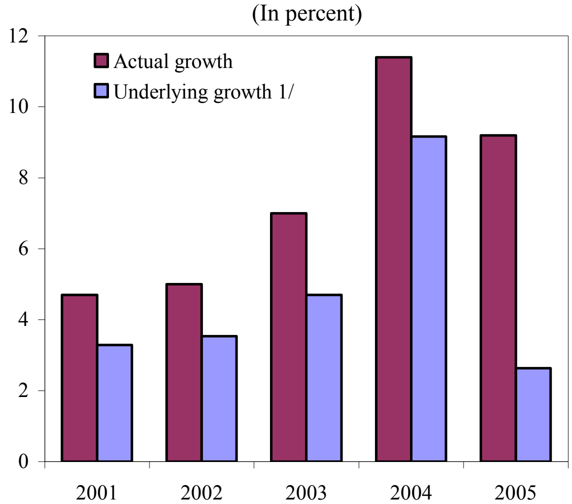
The **trading gains approach** assumes that the real income from terms of trade windfalls has been consumed or invested since 2000. Following SNA (93), we calculate trading gains, the excess of real Gross Domestic Income over real GDP, as

$$T = \frac{X - M}{P} - \left\{ \frac{X}{P_X} - \frac{M}{P_M} \right\},$$

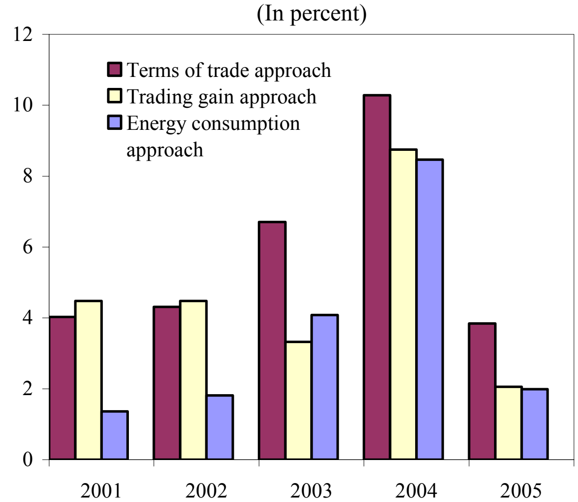
where X and M are export and import values, P_X and P_M the relevant price indices, and P the GDP deflator.

The **energy consumption approach directly estimates** underlying GDP growth, relating it to energy consumption, following Rawski (2001). It assumes a constant energy efficiency of production—not unrealistic since production technologies are unlikely to have changed substantially (over 70 percent of machinery and equipment in Belarus has been fully depreciated in recent years). Input-output tables also show a broadly stable cost share of energy in industrial production during 2001–04. Given its macroeconomic importance, gas consumption is used to proxy underlying GDP.

Actual and Underlying Growth
(In percent)



Estimates of Underlying Growth
(In percent)



Sources: Belarusian authorities; and Fund staff estimates.

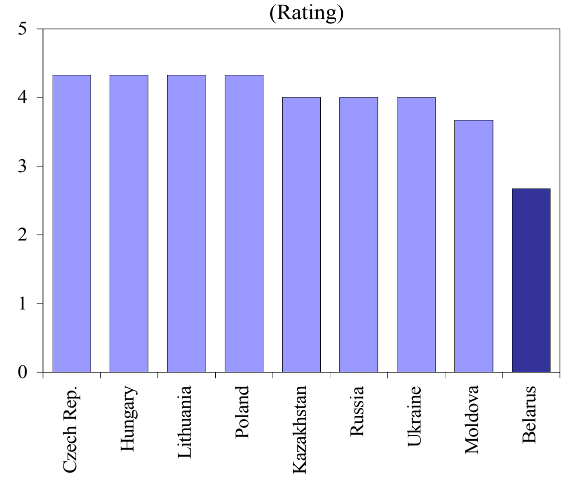
1/ Average of the three approaches.

Box 3. Price Regulation

Direct and indirect interventions in price formation add up to pervasive price controls. Article 394 of the Civil Code stipulates the free formation of prices, but allows the president and state agencies to control them administratively. Wholesale and retail prices are regulated through fixed prices, price caps, markup ceilings, rate of return ceilings, and governmental indicative prices (World Bank's *Doing Business in 2005* survey). They are also subject to norms on manufacturers' trade margins and the Council of Ministers' mandatory exfactory price limits based on the projected inflation rate. If a manufacturer's envisaged price increase exceeds this index, the manufacturer must seek approval from a regional pricing authority—generally forthcoming only if costs are assessed to be in line with established norms.

Price Liberalization

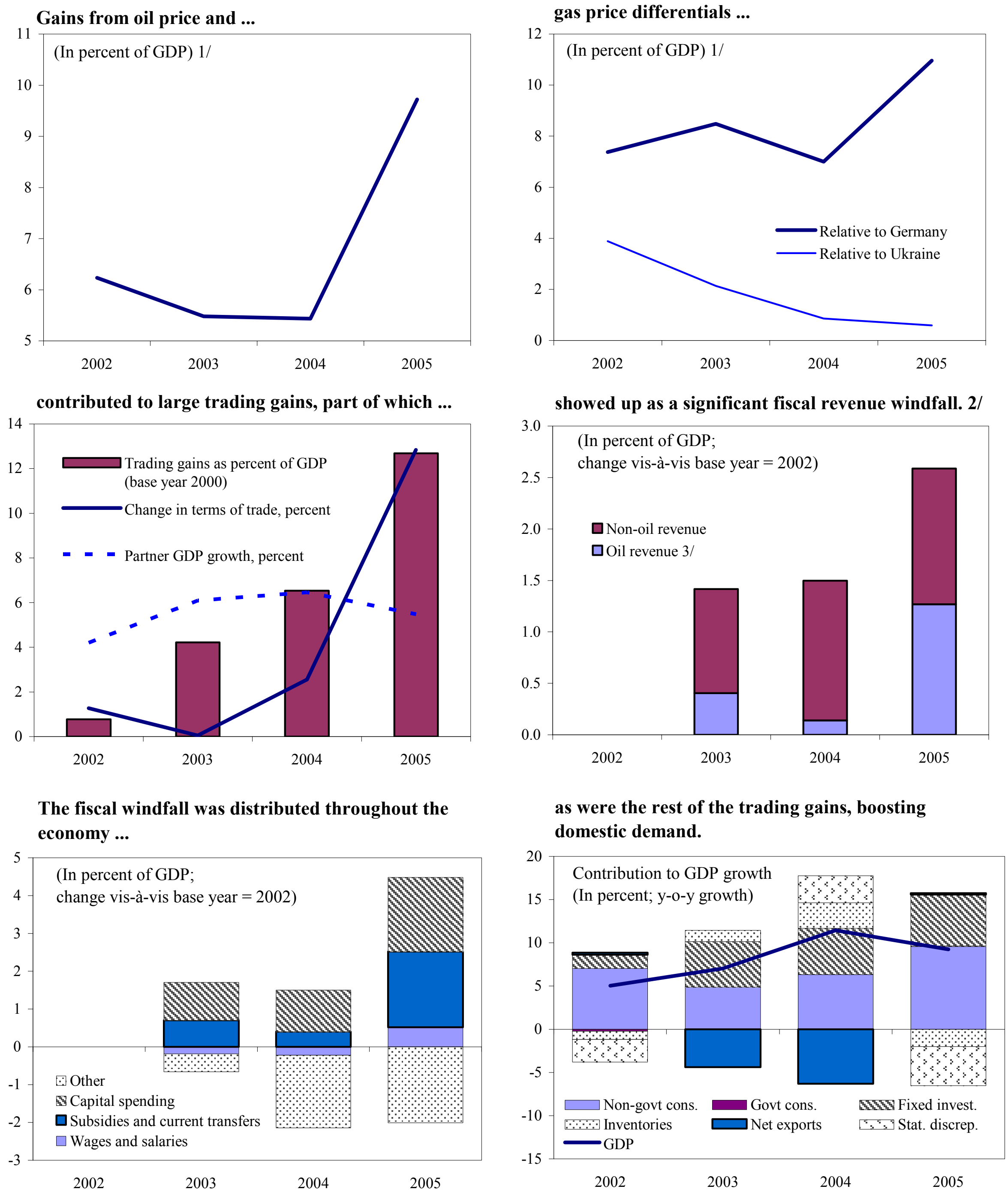
(Rating)



Source: *EBRD Transition Report 2005* .
Note: A rating of 1 indicates most prices formally controlled by the government; 4.33 indicates standards of advanced countries: complete price liberalization with no price control outside housing, transport, and natural monopolies.

Of the World Bank survey's 1,200 respondents, 88 percent had been inspected by the ministry of economy, local authorities, or other price control agencies during 2004, and 39 percent by the State Control Committee. If a price regulation is violated, the authorities seize excess earnings and impose a penalty. Repeat violations can lead to business closure.

Figure 1. Belarus: Determinants of Growth, 2002–05

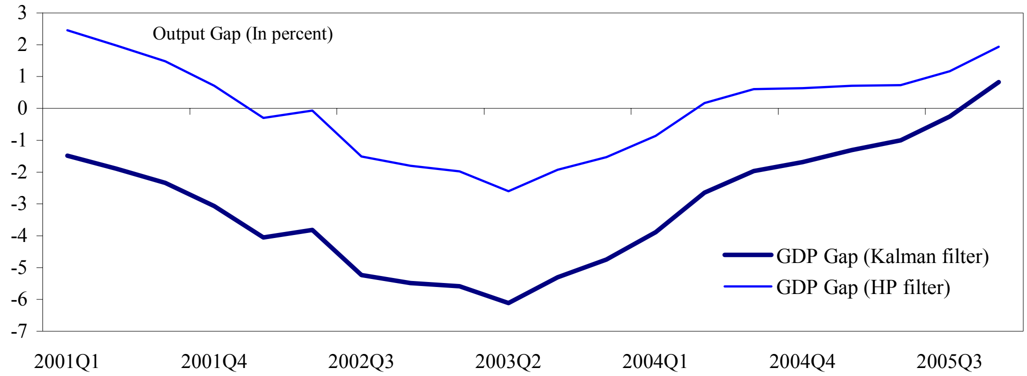


Sources: Ministry of Statistics of Belarus; and Fund staff estimates and calculations.

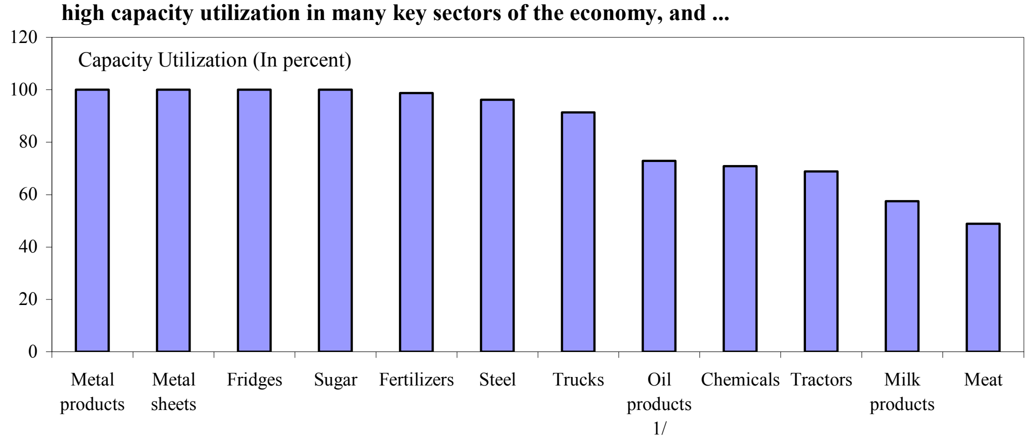
1/ Volume of imports times the price differential.
2/ Revenue windfall is defined as the increase in general government revenue as compared to 2002, excluding the revenue impact of the VAT switch in 2005.
3/ Oil revenue is estimated as the sum of VAT, excises, profit tax, and non-tax revenue collected from domestic sale and export of oil products.

Figure 2. Belarus: Capacity and Inflation

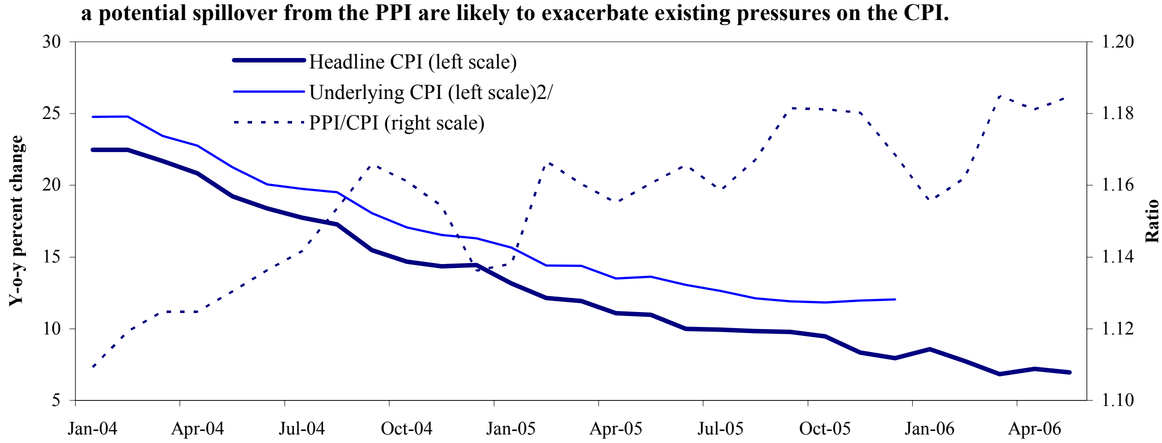
A rapidly closing output gap, ...



high capacity utilization in many key sectors of the economy, and ...



a potential spillover from the PPI are likely to exacerbate existing pressures on the CPI.

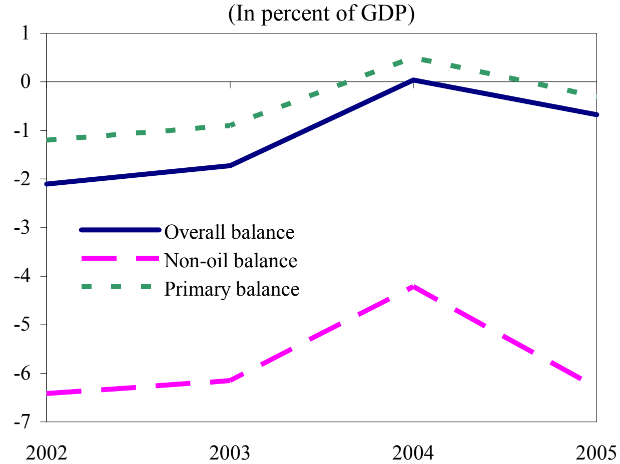


Sources: Ministry of Statistics; Central Bank of Belarus; and Fund staff estimates.

1/ Estimate for early 2005 based on Mozyr refining plant.
2/ Staff estimates from Selected Issues Paper, Chapter 2.

6. **Fiscal policy was gradually tightened during 2004, but relaxed at end-2005 reflecting in part pre-election spending.** After being in broad balance in 2004, the budget—amended 16 times through presidential decrees—recorded a deficit of 0.7 percent of GDP in 2005, despite a 2¼ percent of GDP revenue windfall from the booming energy sector and from the switch to the destination principle for the VAT in trade with Russia from 2005.[2] Excluding oil-related revenues, the 2005 deficit would have been around 6 percent of GDP. The final budget amendment released spending of 2¾ percent of GDP in December, primarily on wages and pensions, subsidies and transfers, and capital spending—including a large recapitalization of two state-owned banks. The 2006 budget recorded a 3.1 percent of GDP surplus through May against a 5.2 percent of GDP surplus during the same period last year and a 3.4 percent of GDP surplus in 2004. The surplus is projected to wind down by end-2006, given the budgeted increase in wages and pensions for the rest of the year, and the expected acceleration of spending by earmarked funds.

General Government Fiscal Indicators, 2002-05
(In percent of GDP)



Sources: Belarusian authorities; and Fund staff estimates.

7. **There has been no change in the exchange rate policy pursued by the NBRB.** De jure, it targets the exchange rate of the Belarusian rubel to the Russian ruble within a horizontal band (plus/minus 2 percent). De facto, the exchange rate of the Belarusian rubel against the Russian ruble is allowed to move in line with market trends outside the established band with a view to limiting daily fluctuations in the exchange rate of the Belarusian rubel vis-à-vis the U.S. dollar. Exchange rate stability vis-à-vis the U.S. dollar has helped anchor inflation expectations, and facilitated further gradual dedollarization and a rapid increase in international reserves in 2005.

8. **Monetary policy has been mildly accommodative** (Figure 3). Rising government deposits in the NBRB and some NBRB intervention largely sterilized the increase in international reserves, and limited broad money growth to about 30 percent through November, despite a reduction of 600 basis points in the refinance rate and of one percentage point in the reserve requirement. The liquidity impact of the large drop in government deposits at end-2005 was broadly neutralized in early 2006 by the subsequent partial

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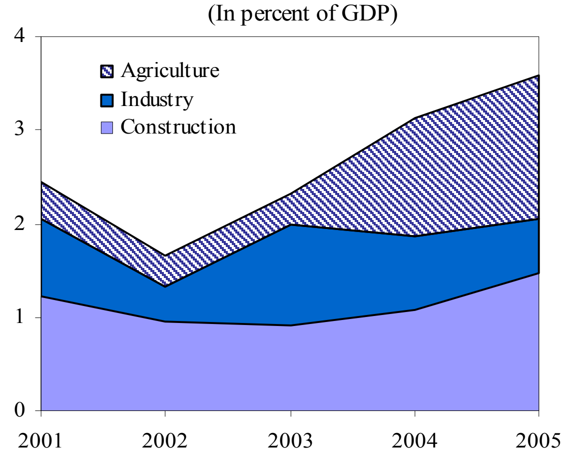
[2] Belarus, a net importer from Russia, experienced a net revenue transfer as a result of zero rating its exports and bringing imports fully into the tax system.

rebuilding of such deposits, and some NBRB interventions in the money markets and in the foreign exchange market to support the currency ahead of the March elections. International reserves remained broadly unchanged in January-June 2006. In June, the NBRB cut the refinance rate by 50 basis points to 10½ percent and the reserve requirement by another percentage point.

9. **Bank recapitalizations have continued amid rapid credit growth (**Figure 4**)**. The largest (mainly public) banks continued to lend at the government's behest for designated purposes—amounting to about 3½ percent of GDP in 2005—mostly at controlled and subsidized interest rates. The resulting decline in these banks' liquidity necessitated budgetary recapitalizations of 1.1 percent of GDP. Central bank credit (mainly to agriculture under presidential directives) has also increased, reaching about ½ percent of GDP at end-2005. The rapid growth in banking system credit to the economy raises concerns about credit quality, even though the share of nonperforming loans (NPLs) fell to below 2 percent at end-2005. A tenth of NPLs remained unprovisioned in May 2006 (an improvement from a year ago), and the few banks still not complying with prudential requirements on liquidity and maximum risk exposure have agreed to an adjustment schedule with the NBRB.

Recommended Credits
(In percent of GDP)



Source: Ministry of Statistics and Analysis.

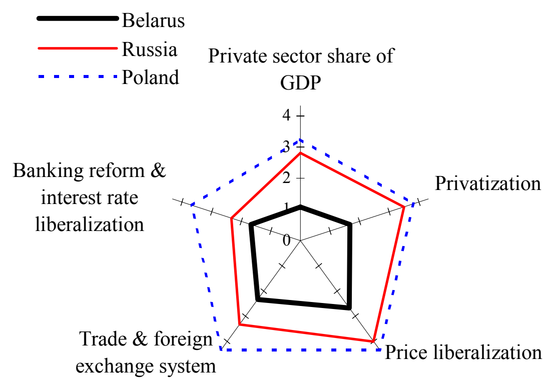
10. **Despite improvements, deep-seated external vulnerabilities remain** (Figure 5). First, while the current account was in surplus in 2005, the non-oil current account deficit is large and growing as export volumes lag behind imports mainly reflecting declining export market share in Russia, a key market.[3] In this regard, Russia has indicated that Belarus's energy import costs may rise substantially from 2007. Second, real wage growth has exceeded productivity gains over most of the last six years by a considerable margin, eroding competitiveness. In particular, the appreciating bilateral real exchange rate vis-à-vis the U.S. dollar and the euro in recent years does not bode well for non-CIS export prospects. Third, gross foreign exchange reserves—while up by two-thirds in 2005—remain low at less than one month of imports and one-third of short-term debt (which comprises 80 percent of

[3] Import volumes spiked at end-2004, in the run up to the introduction of the destination principle for VAT in trade with Russia, then fell substantially. Rival exporters heightened competition in the Russian market and some bilateral trade disputes, suggesting that Belarusian exporters' market share losses may not be temporary.

external debt). Fourth, foreign direct investment (FDI) is extremely low by international comparison at 1 percent of GDP, and negligible from countries other than Russia. Should shocks materialize, the ability of the highly concentrated economy to adjust flexibly remains uncertain.[4]

11. **Structural reforms have not fostered the role of the private sector.** In aiming to refine centralized macroeconomic management, Belarus is further diverging from the liberalization trend in other transition economies. Complex and changing administrative requirements, the state's overarching role in the concentrated economy, an excessive golden share rule (applicable ex post), and residence permit requirements restricting the movement of labor to large cities thwart private sector investment and product and labor market flexibility.

Belarus lags well behind other countries in implementing structural reforms.

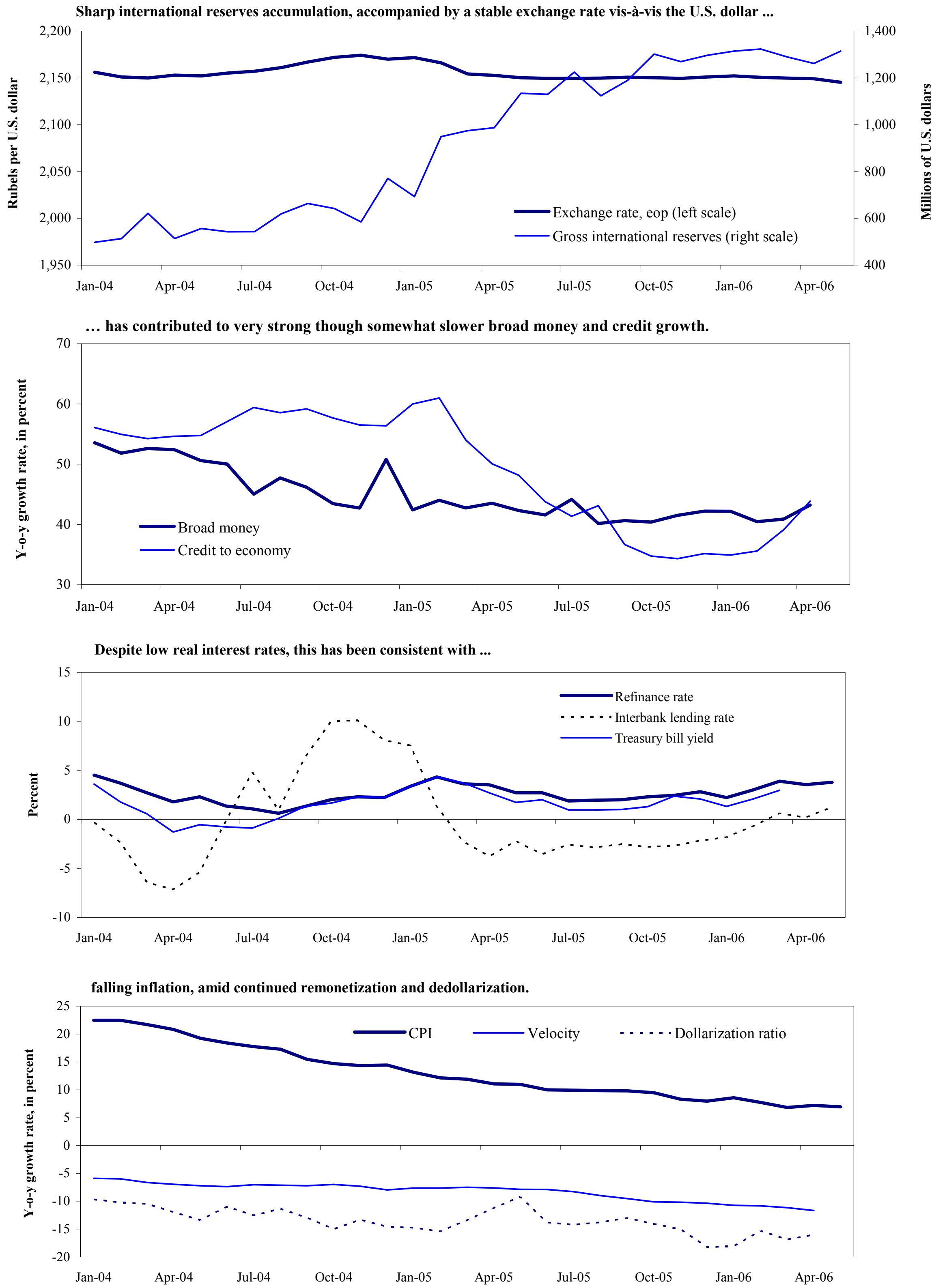


Source: *EBRD Transition Report 2005* .
Note: Transition indicators range from 1 (little change from centrally planned economy) to 4.33 (representing the standards of an industrialized market economy).

12. **Regarding the effectiveness of Fund surveillance, while significant differences remain between the views of the authorities and staff on economic and structural policies, Fund surveillance has contributed to narrowing some differences.** The authorities remain unconvinced about the need to revise their overall policy approach, but indicated that Fund advice and technical assistance had contributed toward formulating some of their policy and reform measures. Their track record in implementing technical assistance (TA) recommendations has been good.

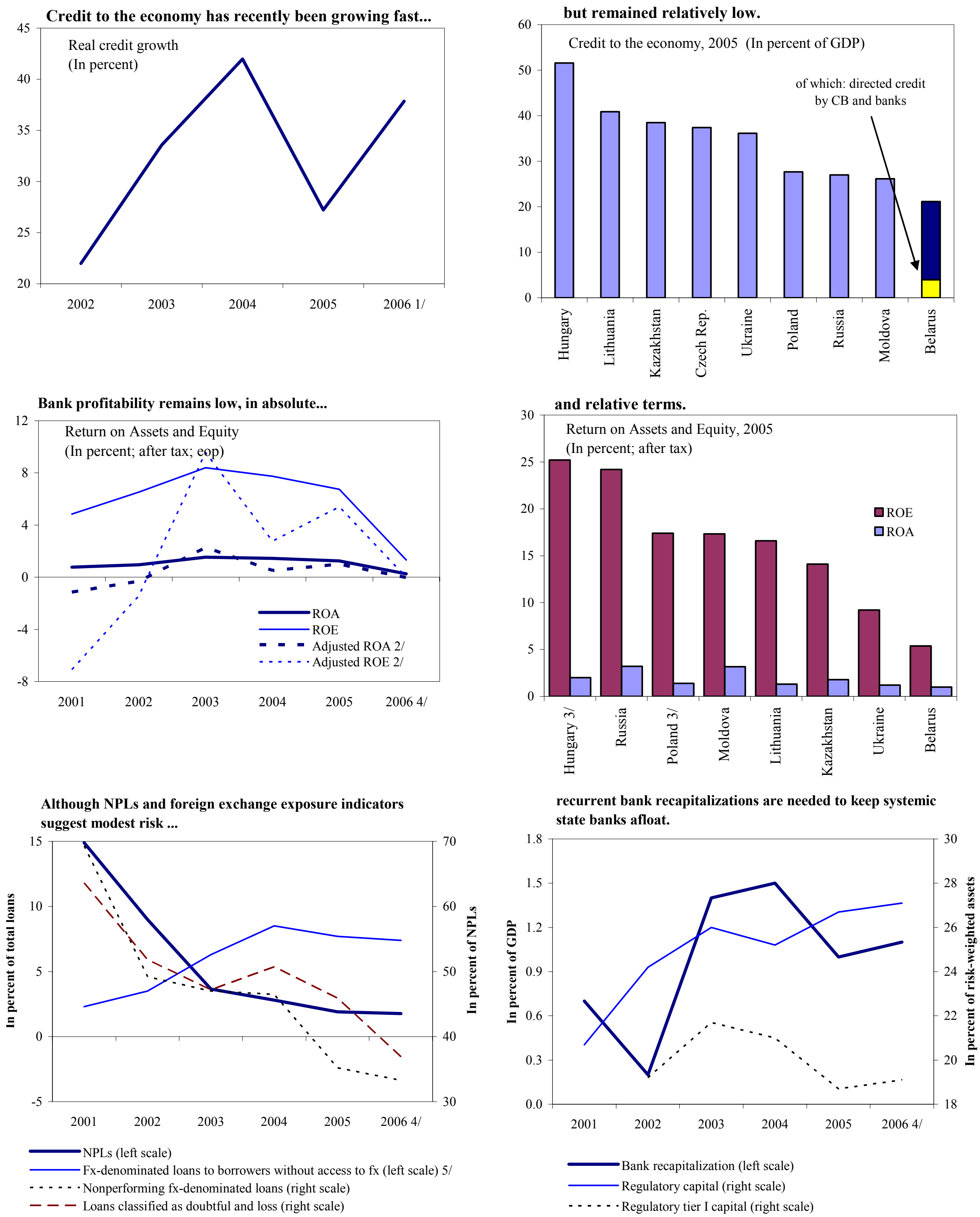
[4] About a hundred—mostly state-owned—enterprises accounted for 14 percent of GDP and 30 percent of republican budget revenues in 2005; they contributed a fifth of GDP growth.

Figure 3. Belarus: Monetary Developments, 2004–06



Sources: Ministry of Statistics; NBRB; and Fund staff estimates.

Figure 4. Belarus: Banking Sector Developments, 2001–06

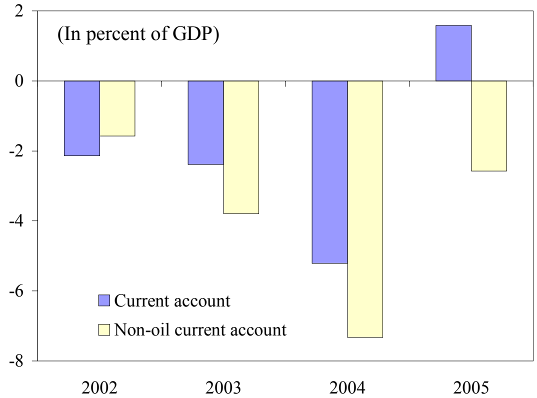


Sources: IFS; WEO; staff reports; and Fund staff estimates.

1/ As of end-March 2006.
2/ With required loan provisioning.
3/ Data are for 2004.
4/ As of end-February 2006.
5/ Sectors with no access to foreign exchange are households, agriculture, and construction.

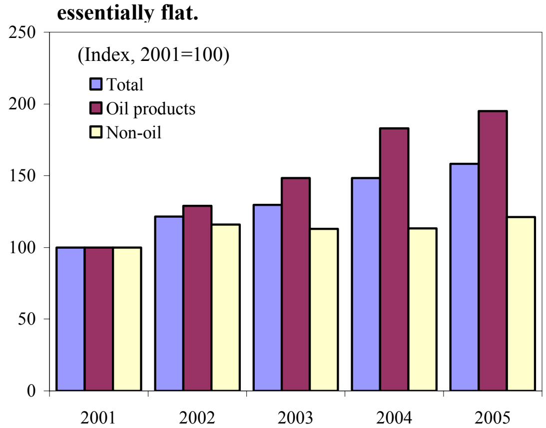
Figure 5. Belarus: External Performance

The non-oil current account shows a less favorable picture than the headline figure 1/...

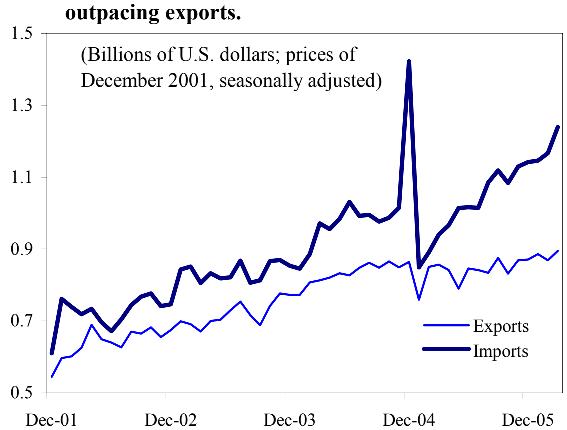


and there are signs that Belarus is losing market share in Russia and ...

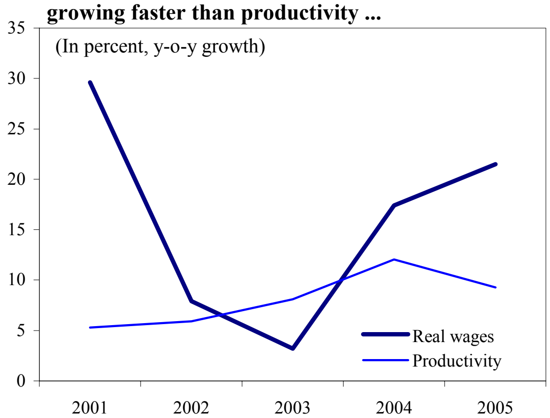
in non-CIS countries, where non-oil exports are essentially flat.



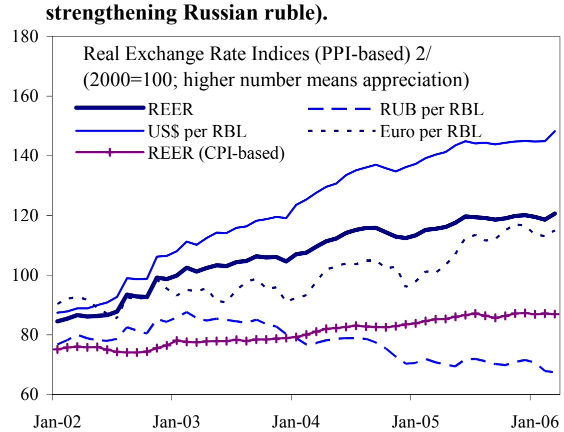
Meanwhile in volume terms, imports are outpacing exports.



Competitiveness is likely to suffer from real wages growing faster than productivity ...



amid some real appreciation (cushioned by the strengthening Russian ruble).



Sources: Belarus authorities; Federal State Statistics Service of Russia; WEO; and Fund staff estimates.

1/ The non-oil current account is used as a proxy for the non-energy current account, owing to data constraints.
2/ Effective exchange rates are weighted according to the breakdown of export proceeds.

II. Policy Discussions

13. **Discussions focused on the sustainability of rapid growth and the attendant policy implications.** In staff's view, recent growth critically benefited from fiscal and quasi-fiscal redistribution of terms-of-trade gains, which facilitated high mandatory wage increases and strong investment growth while enterprise losses have remained high. Even if energy import prices were to remain at current levels, further terms-of-trade gains are unlikely unless world market energy prices continue to rise. In staff's opinion, this suggests (i) markedly lower future GDP growth, since the growth rate of subsidies, investment, and mandatory wage increases experienced in recent years is no longer sustainable; and (ii) a need for policy adjustment. Staff stressed that the possibility of significantly reduced subsidies from Russia—increasingly likely as the horizon lengthens—imparts a significant downside risk to the near-term outlook, further underscoring the need for early policy action**.** Box 4 outlines a possible scenario, which could significantly worsen a medium-term debt outlook that would otherwise appear benign (Figure 6, Tables 6–7). Against this background, staff saw a compelling need for up-front fiscal tightening to mitigate the risk of having to undertake significant pro-cyclical tightening as terms-of-trade gains cease or are reversed. Inevitably, this would involve reductions in subsidies and transfers to loss-making enterprises, making early liberalization of prices and wages, followed by broader structural reforms, a priority.

14. **The authorities did not agree with the thrust of staff's analysis.** In their view, the role of terms-of-trade gains was secondary, so there was no need for significantly altering policies. They were not ready to discuss the risks to the outlook and the policy implications pending the conclusion of talks with Russia on energy prices around end-2006. They argued that in the common economic space, Belarus would continue to benefit from low domestic Russian energy prices, thus avoiding a substantial deterioration in the external environment.

A. Short and Medium-Term Macroeconomic Outlook

15. **The authorities' 2006–10 Socioeconomic Program targets high growth and low inflation assuming a broadly unchanged external environment and economic structure.** The key sources of growth are to be rapidly rising government-led investment and employment. Inflation is envisaged to fall to 5 percent by 2010, and current account surpluses, as well as substantial FDI inflows, are envisaged throughout the period.

Key Objectives of Belarus's 2006-10 Socioeconomic Program
(Midpoints of targeted ranges)

	2006	2007	2008	2009	2010
			Projections		
Real GDP growth (percent growth)	7.8	8.5	8.5	8.5	9.3
Balance of trade in goods and services (U.S. dollar million)	450.2	550.3	650.4	750.5	900
Fiscal deficit (percent of GDP; no range given)	-1.5	-1.5	-1.5	-1.5	-1.5
Investment in fixed capital (percent growth)	13.5	15.8	16.0	16.0	17.0
Employment (percent of labor force)	70.0	70.9	72.5	74.8	77.8
Employment (yoy percent increase)	0.6	1.4	1.6	3.2	4.0

Sources: Social-Economic Development Program for Belarus 2006-10, June 2006; and IMF staff calculations.

Box 4. The Impact of Surging Energy Prices—an Illustrative No Policy–Change Scenario

Belarus—like other CIS energy importers—is likely to face an increase in energy prices toward international levels over the medium term. The baseline scenario is consistent with the authorities' views. A risk scenario assesses the implications of a faster increase in energy prices. Gas prices are assumed to double to $95 per thousand cubic meters in 2007—at par with the 2006 level negotiated for Ukraine and below that for Armenia—and then converge to international prices by 2012. Oil prices are assumed to smoothly converge to international prices during 2007–12.

To quantify the **impact of surging energy prices on baseline growth**, five estimates are averaged. The production function model (Bruno and Sachs, 1985) calculates the direct impact on output using the cost share of energy. The net import model (IEA, 2004) assumes that higher energy prices reduce the wealth of net energy-importing countries. Additional estimates of the impact on growth are obtained from panel regressions in Broda (2004), Becker and Mauro (2006), and Chapter I of the Selected Issues Paper.

The first-round **impact on inflation** is simulated using (i) the CPI weights of energy and utilities prices; (ii) the pass-through rate of energy import prices to utilities prices (gradually increasing from 50 percent in 2007 to full pass-through by 2011); and (iii) the gas intensity of heat and electricity production. Inflation may actually be higher despite slower growth, owing to second-round effects—particularly if profits cannot act as a buffer.

Higher energy prices cause an **equilibrium real exchange rate (ERER) depreciation**, leaving the RER overvalued. The ERER is approximated using the long-term relationship between a real exchange rate index and PPP GDP per capita, estimated on a panel of 100 countries and on a subpanel of transition economies. The scenario uses the average ERER elasticity from these two regressions. In the medium term, higher inflation vis-à-vis trade partners may generate further RER overvaluation.

The **fiscal balance** gradually deteriorates to about 5 percent of GDP by 2011 because revenues fall as enterprise sector profitability drops, and larger subsidies and transfers are needed owing to the incomplete pass-through of energy costs, and the rising share of lossmakers. The **current account** deficit will rise to more than 10 percent of GDP over the medium term as the energy shock unfolds, generating a run-up in external debt. **Banking system** capital adequacy would fall to barely above the regulatory 8 percent level with increasing credit risk (assuming 5 percent of loans to agriculture and 10 percent to other sectors becoming loss, and 20 percent of standard loans becoming substandard). Excluding two large banks, the system appears much more fragile and relatively more exposed to the non-agriculture sector.

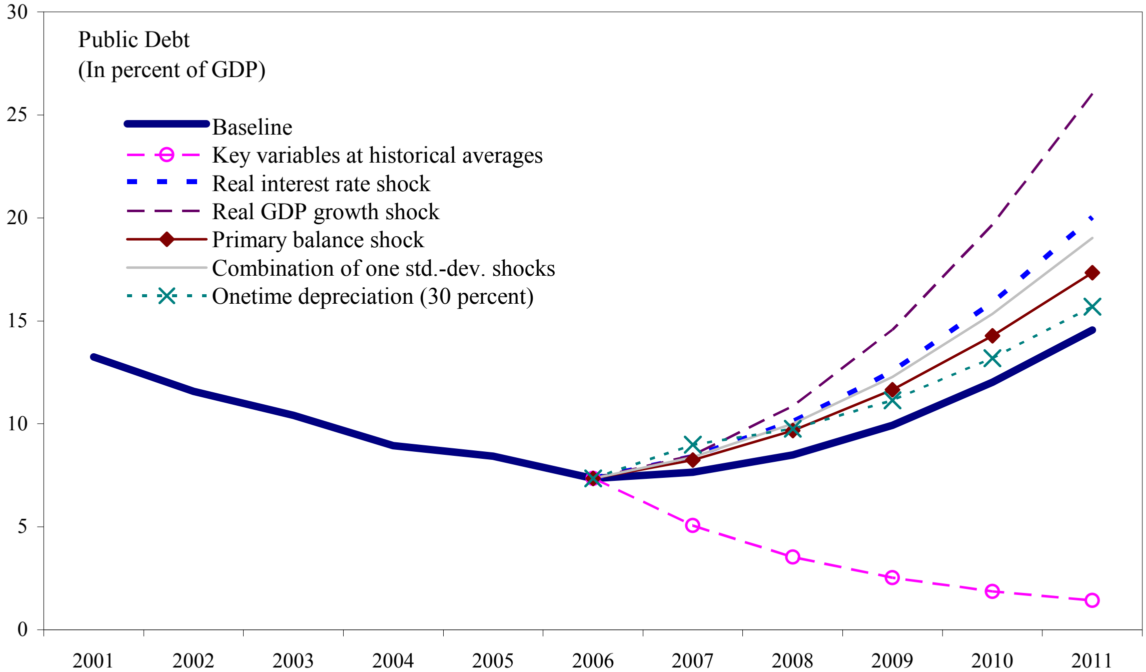
Medium-Term Projections

	2007	2008	2009	2010	2011
	Baseline scenario				
Real GDP growth (in percent)	4.5	3.8	3.6	3.4	3.0
Inflation (eop, in percent)	9.0	8.0	7.0	6.0	5.0
General government balance (in percent of GDP)	-1.2	-1.7	-2.3	-3.0	-3.5
Current account balance (in percent of GDP)	-1.1	-2.1	-3.2	-4.5	-6.3
Memorandum items					
Oil import price (U.S. dollars per ton)	270.0	273.3	277.5	280.0	279.4
Gas import price (U.S. dollars per thousand cubic meters)	51.9	54.5	57.2	60.1	63.1
	Risk scenario				
Real GDP growth (in percent)	-0.7	0.3	0.7	0.9	0.6
Inflation (eop, in percent)	16.4	11.0	10.5	9.0	8.0
General government balance (in percent of GDP)	-2.5	-3.0	-3.6	-4.2	-4.7
Current account balance (in percent of GDP)	-4.6	-6.5	-8.6	-11.1	-14.5
Memorandum items					
Oil import price (U.S. dollars per ton)	270.0	288.7	311.4	336.0	362.5
Gas import price (U.S. dollars per thousand cubic meters)	95.0	110.3	128.0	148.5	172.3

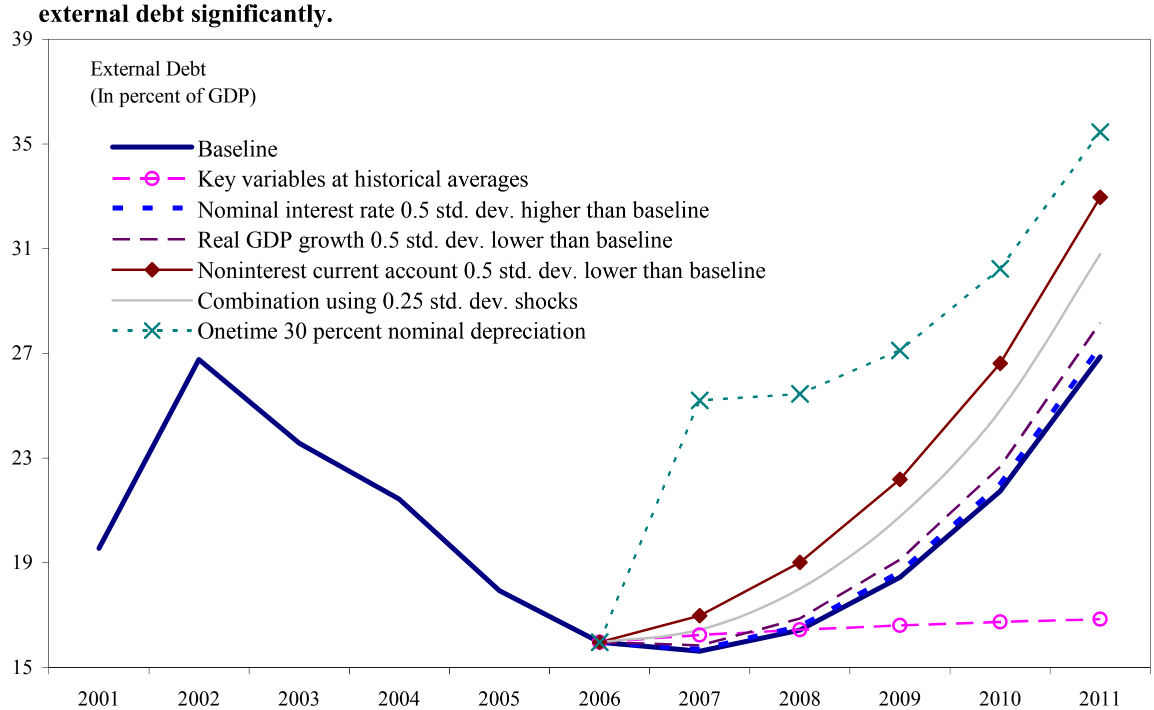
Sources: Belarusian authorities; and Fund staff estimates and projections.

Figure 6. Belarus: Fiscal and External Sustainability Analysis, 2001–11

Public debt sustainability, while vulnerable to various shocks - in particular, to interest rates, GDP growth, the primary balance, and exchange rates - is projected to remain in a comfortable range.



While remaining low by international comparison, external debt is expected to rise significantly in the medium term. Shocks to the exchange rate or the current account would raise the level of external debt significantly.



Sources: Belarusian authorities; and Fund staff estimates.

16. **In staff's view, economic growth is likely to slow down in the medium term in the absence of structural reforms.**

- **Growth in 2006 should remain robust.** Reflecting continued strong growth in Russia, preliminary GDP data for the first six months of 2006, and a sizeable carryover, staff project growth, driven by domestic demand, at around the lower end of the government's projected range of 7–8½ percent.

- **But continued rapid noninflationary growth in 2007 and beyond is increasingly doubtful under current policies.** Terms-of-trade gains are likely to stop increasing, constraining centralized redistribution. Expansionary macroeconomic policies to boost growth above potential will also gradually cease to be a noninflationary policy option as the output gap closes. Moreover, even massive public investment would not necessarily raise productivity rapidly if resources are not allocated efficiently.[5] Panel regressions using a neoclassical growth model—calculated as background to the discussions—suggest annual potential growth of about 3½-4 percent over the next five years (Craft and Kaiser, 2004). Similar results obtain in a growth-accounting framework, with total factor productivity (TFP) calculated as (i) the average Belarusian TFP over recent years; or (ii) the average of transition economy TFP estimates.[6] TFP is unlikely to sustain high growth rates in the medium term given the large share of fully depreciated productive equipment, and policies precluding large, technology-enhancing FDI inflows. Finally, exports' contribution to growth would peter out as Belarusian exports encounter increasing competition.

17. **Staff expressed reservations about some aspects of the authorities' medium-term outlook.** First, the projected current account surpluses, together with the sharp increase in the share of investment in GDP stemming from the government's ambitious investment plan, would imply a considerable contraction in domestic consumption to create room for the necessary sharp rise in savings from its current level of 31 percent of GDP. In contrast, staff projects gradually deteriorating current account deficits after 2006, stemming from weak export volume growth and stagnant terms of trade. Second, the envisaged employment increases would require raising the share of employment in the working-age population by 10 percentage points from an already high 71 percent in 2005, given the demographic trends. Third, projecting substantial increases in FDI would appear overly

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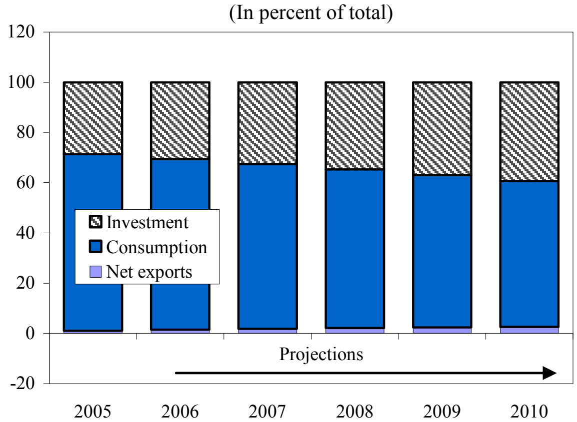
[5] Evidenced by the large share of fiscal subsidies (9.2 percent of GDP); the concentration of public investment on buildings; and the high proportion of lossmakers in the enterprise sector (29½ percent in industry in May 2006).

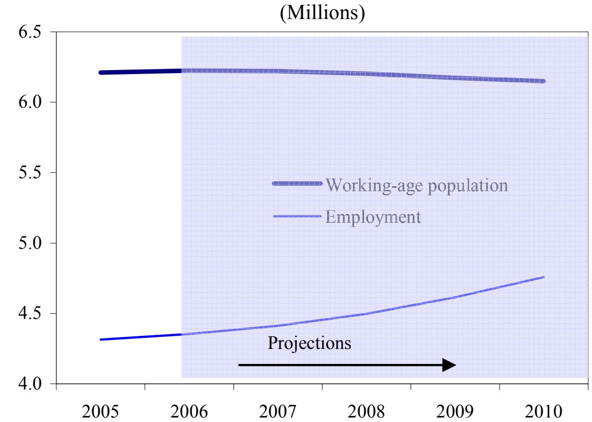
[6] The average of estimates in DeBroeck and Koen (2000) and Mihaljek and Klau (2003) is used.

optimistic in the absence of wide-ranging structural reforms, privatization, and policy changes to enhance the investment climate.

Belarus: Composition of GDP
(In percent of total)



Working-Age Population and Employment
(Millions)



Sources: *Program of Social and Economic Development of Belarus for 2006-10,* and Fund staff calculations.

B. The Need for Structural Reforms

18. **Some common ground has emerged.** The authorities envisaged gradual reforms as part of their multiyear Socioeconomic program, notably some cuts in taxes and subsidies, and measures to strengthen the financial system, facilitate small and medium-sized enterprise development, moderate real wage growth, and attract foreign investors.

19. **Staff argued for deeper and less gradual reforms.** A more rapid withdrawal of state intervention (through the structural reforms described in Box 5) would complement the authorities' own intentions and aim at creating favorable conditions for private sector growth while the economy was still in a period of strength. This would foster an efficient allocation of resources, and ultimately boost productivity and potential growth.

20. **However, the authorities remained unconvinced about the need for, and desirability of, more radical reforms than those envisaged in their Socioeconomic Program.** They pointed to past macroeconomic performance as proof that Belarus's development model was appropriate. The authorities strongly objected to phasing out recommended lending and centrally mandated wage increases, and to wide-ranging privatization, which they saw as putting their social objectives at risk.

C. Fiscal Policy and Reform

21. **Staff argued for fiscal tightening starting in 2006.** The 2006 budget targets an overall deficit of 1.5 percent of GDP, but a broad balance is within reach on current

policies.[7] Staff suggested targeting a moderate surplus of about ½ percent of GDP through expenditure restraint to create fiscal space for future tax cuts and to avoid having to endure lower revenues—notably energy-related ones—while committed to stretched expenditure levels. The authorities, while acknowledging in principle the case for some fiscal savings, were not in a position to commit to a budget surplus this year.

22. **For 2007, the authorities target a fiscal deficit of 1½ percent of GDP.** They were not prepared to discuss the final parameters for the 2007 budget, but discounted the risk that next year's budget would suffer from lower terms-of-trade gains. Pointing to the need to support growth and to the likely availability of financing given low public debt (8.5 percent of GDP), they considered a moderate fiscal deficit appropriate. Staff argued that fiscal policy should be more restrained in 2007 and beyond, stressing that revenues would reflect stagnating terms-of-trade gains, and that expansionary fiscal policy would heighten inflationary pressures and worsen competitiveness. In this context, the quality of expenditure, rather than its quantity, and its ability to enhance productivity were key. Room for maneuver would also be needed to offset contingent liabilities (notably related to cumulative fiscal costs of recommended lending), to finance the cost of structural reforms which may be frontloaded, and—if needed—for smoothing the impact of possible adverse developments in energy prices.

23. **A range of fiscal reforms would need to begin already in 2006 to leave room for future maneuver**. The authorities stressed that tax cuts were continuing in 2006 and that the president had declared that subsidies would be scaled back. While welcoming these plans, staff recommended focusing on (i) identifying permanent expenditure cuts necessary to offset looming revenue losses; (ii) reducing budget rigidities by phasing out earmarking; and (iii) incorporating remaining extrabudgetary funds into the budget and the Treasury Single Account, gradually moving all central budgetary funds to the latter, to enhance expenditure management. Staff also argued for phasing out subsidies and transfers to loss-making enterprises, and discontinuing bank recapitalizations associated with recommended lending.

[7] Under current projections, the state budget deficit would be ½ percent of GDP smaller than budgeted, while the Social Protection Fund (SPF) would record a 1 percent of GDP surplus as in previous years (the budget conservatively assumes that the SPF would be in balance).

Box 5. Structural Reform Agenda

To address the most binding constraints to sustained growth, structural reforms should primarily aim at retrenching the state's pervasive intervention in economic activity, hardening budget constraints, and attracting FDI. While Belarus's savings and investment levels are high and the human capital endowment favorable, potential growth is constrained by the limited efficiency of state-led investment and the low effective returns to private investment evidenced by its low share (both domestic and foreign). Appropriate sequencing and pacing of reforms, together with supporting macroeconomic policies are key to containing potential negative effects on economic activity.

The most urgent reforms would curtail direct government intervention in economic activity, notably by

- sharply reducing entry barriers for private firms and streamlining the regulatory framework;
- phasing out controls on price formation to enhance price signals;
- discarding centrally mandated wage targets to help wages clear the labor market and avoid decapitalizing enterprises; and implementing rules in SOEs to keep wage growth in line with productivity increases;
- phasing out recommended lending to enhance market-based financial intermediation;
- curbing the golden share rule to apply only to a handful of strategic enterprises so as to attract domestic and foreign private investors;[8]
- adopting international accounting standards for enterprises.

This would be followed—after sufficient preparation, but without undue delay—by

- transparently privatizing banks and nonmonopoly enterprises to ensure more efficient use of factors of production;
- curbing subsidies and enforcing the exit of inefficient enterprises to fortify enterprise budget constraints; and
- to complement the latter effect, gradually reducing the tax and regulatory burden financed by cutting state support to enterprises.

Concurrent institutional reforms would round off the transition, including

- putting in place effective regulation of economic monopolies;
- strengthening the social safety net to minimize the social costs of efficient labor reallocation;
- reforming tax administration, public expenditure management, and the pension and health systems to ensure fiscal sustainability.

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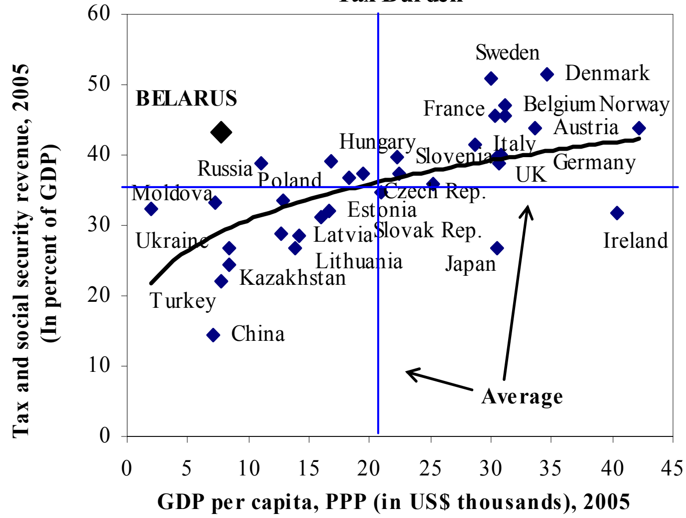
[8]The golden share can be introduced ex post in any enterprise with current or past state ownership, wage arrears, accounting or workers' rights irregularities, allowing the government to take decisions regarding the enterprise's activity. From June 2006, it no longer applies to banks. The authorities claim that they use the golden share rule very selectively.

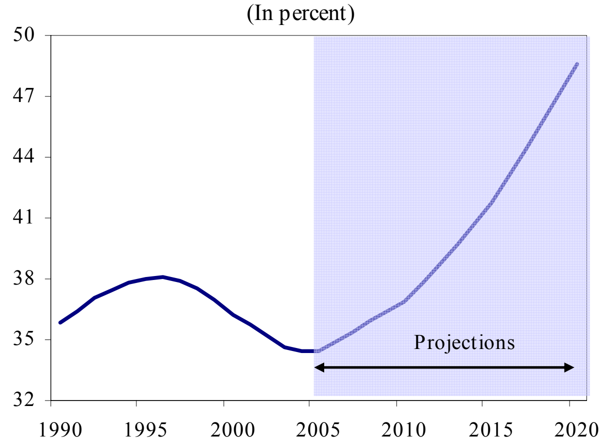
24. **The authorities intend to reduce the very high tax burden by 3–4 percentage points of GDP by 2010 and to streamline tax administration.** To this end, the draft fiscal guidelines propose tax cuts of ¾ percentage point of GDP in 2007, eliminating (i) the Chernobyl tax of 3 percent of the wage bill; (ii) the State Employment Fund contributions of 1 percent of the wage bill; and (iii) the local profit tax of 3 percent of net profits.[9] Staff welcomed this package but advocated an earlier elimination of remaining distortionary taxes—in particular the turnover tax levied concurrently with the VAT—offsetting the revenue impact by reducing discretionary exemptions and concessions to expand the tax base, and simplifying tax rate structures. The authorities agreed in principle that tax cuts should be compensated by expenditure cuts.

Tax Burden



Sources: Belarusian authorities; FAD DEME database; staff reports; Eurostat; WEO; and Fund staff estimates.

Elderly Dependency Ratios 1/
(In percent)



Sources: Historical data from *Statistical Yearbook*, projections from the Population Division of the Department of Economic and Social Affairs of the United Nations Secretariat.

1/ The ratio of population aged 65 years and over to population aged 15-64. Medium fertility variant for projections.

25. **The authorities are considering how to address the economic implications of aging.** Given the low fertility rate of 1.2, Belarus's population is projected to continue falling (by 2.1 percent in 2006–10), triggering a steady rise in the elderly dependency ratio and a consequent decline, starting in 2008, in the ratio of pension system contributors to beneficiaries. Although not ready to discuss reform proposals, the authorities indicated that work on quantifying the problem and the

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[9] Part of the revenue loss from this measure would be compensated by increasing the central government profit tax rate from 24 to 26 percent and unifying local sales tax rates at a higher average level. The first of these changes would reduce the number of taxes levied on the same tax base, as well as revenue earmarking.

gains from possible reform measures had commenced. Staff argued for a pension reform that would raise the effective retirement age (which was falling further behind the nominal retirement ages of 60 for males and 55 for females, owing to early retirements) and enhance the link between lifetime contributions and pension benefits.

D. Monetary and Exchange Rate Policy

26. **The NBRB agreed that its monetary and exchange rate policy should primarily aim at attaining the inflation—rather than exchange rate—objective.** While the NBRB currently sets targets for money supply (M1) and an explicit band for the Russian ruble exchange rate (and an implicit one vis-à-vis the U.S. dollar), these targets can be revised during the year if needed to achieve the inflation objective given developments in money demand. Observing that some exchange rate flexibility would help buffer the economy against real shocks, the NBRB agreed that it should move further toward clearly indicating inflation as the primary monetary policy objective in its 2007 monetary policy guidelines. In this context, while an intermediate target for money supply was needed, staff cautioned against setting further quantitative targets—notably for nominal exchange rates—since this could undermine the credibility of the NBRB's commitment to the inflation objective.

27. **There was agreement that monetary policy needed to remain focused on its target.** Staff agreed that the NBRB's commitment to lower inflation to 7-9 percent in 2006 and to 5 percent by 2010 was attainable. However, given the need to remain vigilant about inflationary pressures, it found the latest reduction in the refinance rate and in reserve requirements somewhat premature. These moves boosted liquidity in a context in which (i) measured inflation might not fully reflect underlying inflationary pressures, and (ii) the preference for foreign currency as a store of value remained high (40 percent of bank deposits were foreign currency denominated). Staff urged the NBRB to discontinue large-scale liquidity support to banks and lending to the economy in support of government programs. Noting that interest rate caps distorted credit allocation and may be largely offset by increased lending fees and commissions, staff advocated their elimination—an objective the NBRB concurred with as a medium-term goal.

28. **The framework for monetary policy and operations has become more transparent.** The NBRB has improved communications to the public of its policy actions and operations. Staff suggested that banks could be allowed to better benefit from reserve requirements averaging to use available liquidity more efficiently. The NBRB could also usefully shorten the maturity of NBRB securities used in liquidity withdrawal operations to coincide with the period for which it could make reliable liquidity forecasts. The NBRB was receptive to both suggestions.

29. **Coordination between the NBRB and government is key for building public confidence in macroeconomic policies.** Enhancing the NBRB's operational independence and further strengthening cooperation with the Ministry of Finance would be key steps

toward bolstering the operational framework of monetary policy. Staff also advocated (i) replacing outstanding NBRB loans to the government with marketable securities that could be used to conduct open market operations and (ii) moving government deposits into the NBRB from banks to facilitate NBRB liquidity management—gradually, to avoid an adverse impact on banking system liquidity.

E. Financial Sector Soundness

30. **The NBRB has improved the supervisory and regulatory framework.** The transparency of bank capital, corporate governance, and risk management has been strengthened and the use of external audits increased. In a welcome recent step, the golden share rule was eliminated for banks to encourage the entry of strategic foreign investors in the banking system. Progress was also made toward adopting a new banking code, and laws on credit bureaus, deposit insurance and mortgages. The authorities indicated that Fund assistance had played a role in several of these accomplishments, and had also helped raise NBRB staff's technical skills. They agreed that continued vigilant oversight was key, particularly of systemic banks that failed to comply with all prudential requirements.

31. **Banking sector soundness has improved but vulnerabilities remain, especially in light of continued rapid credit growth**. Low NPL levels, with a considerable share of loans extended at the government's behest, might not adequately reflect borrowers' repayment capacity (for instance, NPLs exclude loans under central government guarantee). Also, the level of loans written off in 2005 (about 0.35 percent of GDP), which have reduced NPLs, suggested a need for improving banks' risk assessment procedures. Staff noted that high capital adequacy ratios in the banking sector reflected recurrent recapitalizations, and, *per se*, did not provide an adequate forward-looking measure of the system's safety. In this regard, stress tests showed that banking system resilience to shocks had improved since 2004 (when the FSSA stress tests were conducted), but underscored the need for considerable capital injections in case of a severe shock when two large banks were excluded from the test.

32. **Staff emphasized that recommended lending should be phased out as rapidly as feasible.** It argued that such—effectively directed—lending for housing, agriculture, and other purposes increased banks' vulnerabilities as appropriate risk management procedures were not followed; it necessitated large recurrent bank recapitalizations; and it built up potentially large contingent liabilities. Such lending also (i) generated maturity mismatches as affected banks funded themselves at short maturities, increasing systemic liquidity risk; (ii) distorted financial resource allocation; and (iii) precommitted the budget to bear an interest cost during these loans' long life span. The NBRB agreed that eliminating recommended lending could be a medium-term objective.

F. The Trade Regime

33. **Although weighted average tariffs on imports from outside Russia are a moderate 11 percent, the trade regime retains numerous ad-hoc administrative restrictions.** Importers must receive special government permits to import consumer goods considered products of comparative advantage for Belarus. Mandatory shares of domestically produced goods are prescribed for retail outlets, and state procurement favors local firms. Staff argued that these attempts to support inefficient domestic production and compensate for weak export performance hampered growth by (i) reducing competition, (ii) raising domestic prices, and (iii) increasing the cost of producing export goods (to the extent they affected imported inputs).

III. Staff Appraisal

34. **Belarus has enjoyed several years of high growth and falling inflation.** Growth reflected rising labor productivity aided by increasing capacity utilization, with demand benefiting from unfettered access to Russia's expanding market and the redistribution of escalating terms-of-trade gains. The successful exchange rate anchor, administrative intervention in price formation, and a sizable output gap have contributed to lower inflation.

35. **However, once the energy windfall ceases to rise, the Belarusian development model will come under strain.** Continued centralized support to domestic activity will rapidly raise inflationary pressures, given the vanishing output gap. Without policy adjustment and structural reforms—notably liberalizing prices and wages, and curbing the state's role in economic activity—growth will revert toward its lower potential level. The prospect of significantly higher prices of energy imported from Russia imparts considerable further downside risks to the outlook, since the attendant compression of terms-of-trade gains would seriously worsen the external current account and force significant cuts in fiscal subsidies and other forms of demand-supporting redistribution.

36. **Fiscal policy should be tightened, starting in 2006, in anticipation of revenue losses and structural reform costs.** To this end, expenditures—especially recurrent ones—should be constrained to the extent feasible in 2006, and further reduced as a share of GDP in 2007 and beyond. Spending cuts should be focused on subsidies (including to banks), net lending, and transfers to lossmaking enterprises. Remaining elements of earmarking should also be eliminated.

37. **Institutional reforms to enhance fiscal management and sustainability are also needed.** In coordination with the NBRB, central government deposits should be moved gradually to the NBRB, and outstanding NBRB loans to the government converted into marketable securities to enhance liquidity management. Moreover, pension reforms sufficient to address the looming demographic changes should be developed expeditiously.

38. **The NBRB should refocus monetary policy on inflation control.** In this regard, staff noted that the NBRB should stand ready to accept more flexibility in the exchange rate in the event of inconsistency between the inflation and exchange rate targets. Moreover, to enable the NBRB to pursue monetary policy effectively, its operational independence needs to be strengthened, the number of its quantitative targets pruned, its direct lending to the economy discontinued, and interest rate caps eliminated.

39. **Progress in strengthening the supervisory framework and banking system soundness needs to continue.** The NBRB should ensure that future liabilities stemming from remaining directed lending are fully reflected in prudential indicators. By vigilantly enforcing all prudential requirements, it can lower the risk that continued rapid credit growth gives rise to higher NPL levels. Staff welcomes the recent steps toward attracting strategic foreign investors to the banking system, and stresses the importance of ensuring transparency and competition in privatization.

40. **The case for implementing bolder structural reforms while the economy is still in a period of strength is compelling.** It is reinforced by substantial downside risks to the outlook. The policy room built up would help address the diminishing gains from energy trade—notably its impact on fiscal revenues—and support the necessary reduction in fiscal subsidies and transfers. Implementing productivity-enhancing structural reforms while the economy is growing rapidly would also make covering their up-front costs easier. An improved investment climate would help attract FDI, facilitating faster export growth through technology inflows, and enhanced access to foreign markets.

41. **The consequences of piecemeal reforms appear unattractive.** Implementing only moderate changes and retaining state domination of the economy would create increasing macroeconomic and social costs as the external environment worsens and traditional sources of growth fade. While the costs could in principle be financed for some time given the current low external debt, this approach would necessitate larger adjustment down the road.

42. **The key task is to reduce state intervention and improve the business environment.** Directed lending, whose cumulative long-term costs remain partially unaddressed by recurrent bank recapitalizations, should be eliminated as soon as feasible. If subsidies to specific sectors are deemed necessary, these should come directly from the budget. Pervasive controls on price formation should be discontinued, cross-subsidization via state-owned enterprises abolished, and the golden share rule drastically curtailed. Mandatory wage increases should cease.

43. **The quality and timeliness of statistical data are broadly adequate for surveillance, although macroeconomic analysis is encumbered in some areas.** Belarus subscribes to the Special Data Dissemination Standard, publishing extensive statistics. However, administrative controls in the economy may affect the meaning of statistical data

and hence hamper staff's macroeconomic analysis in key areas. Moreover, the weights in the CPI basket remain inaccessible, and the statistical discrepancy in national accounts data is relatively large.

44. The next Article IV consultation is proposed to be conducted under the standard 12-month cycle.

Table 1. Belarus: Selected Economic Indicators, 2003-07

	2003	2004	2005	2006		2007
			Preliminary	Official	Staff	Staff
Output						
GDP (nominal in billions of rubels)	36,565	49,992	63,679	73,650	73,650	83,968
Gross domestic product (in billions of U.S. dollars)	17.8	23.1	29.6	34.3	34.2	38.9
Real GDP 1/	7.0	11.4	9.3	7-8	7.0	4.5
Industrial production	7.1	15.9	10.4	6.5-7.5	...	...
Prices and wages						
GDP deflator (y-o-y)	30.7	22.7	10.3	7.1-8.1	8.0	9.1
Consumer prices, eop (y-o-y)	25.4	14.4	8.0	7.0-9.0	9.0	9.0
Consumer prices, aop	28.4	18.1	10.3	...	8.0	9.1
Producer prices, eop (y-o-y)	28.1	18.8	10.0	...	...	...
Wages (thousands of rubels per month)	250.7	347.5	469.4	...	...	...
Real average monthly wage (1996=100)	238.7	279.0	338.6	355.8	...	...
Average monthly wage (in U.S. dollars)	123.3	162.0	217.4	...	...	...
Exchange rates						
Rubel/USD (average)	2,052	2,160	2,154	...	...	...
Rubel/USD (end-of-period)	2,156	2,170	2,152	2100-2200	...	...
Rubel/Ruble (RUR) (average)	66.92	74.98	76.16	...	...	...
Rubel/Ruble (RUR) (end-of-period)	73.20	77.91	74.86	...	...	...
General government finances 2/						
Revenue	45.9	46.0	48.4	46.1	48.3	47.1
Expenditure (cash)	47.7	46.0	49.1	47.6	48.4	48.3
Expenditure (commitment)	46.9	45.6	49.0	47.6	48.4	48.3
Balance (cash)	-1.7	0.0	-0.7	-1.5	-0.1	-1.2
Balance (commitment)	-1.0	0.4	-0.6	-1.5	-0.1	-4.5
Money and credit						
Annual average broad money velocity (level)	7.3	6.6	6.2	5.6-5.4	6.1	6.4
Annual average rubel broad money velocity (level)	13.5	11.2	9.5	8.2-8.0	7.5	6.6
Reserve money 3/	69.7	41.9	73.7	17.0-21.0	-12.8	32.8
Banking system net domestic credit	68.9	39.1	34.8	20.0-27.0	-7.0	33.8
Rubel broad money	71.0	58.1	59.5	27.5-33.3	30.0	28.0
Refinance rate (percent per annum, end-of-period)	28.0	17.0	11.0	8.0-10.0	...	...
Balance of payments and external debt						
Exports of goods	10,073	13,942	16,095	16,941	17,854	19,066
Imports of goods	-11,329	-16,126	-16,623	-17,073	-18,882	-20,781
Current account balance	-424	-1,206	469	...	57	-440
As percent of 12-month GDP	-2.4	-5.2	1.6	...	0.2	-1.1
Terms of trade index, annual percentage change	0.1	2.6	12.8	...	8.8	-1.5
Gross official reserves	499	770	1,297	1,275	1691	1857
In months of future imports of goods and services	0.3	0.5	0.8	…	0.9	0.9
Medium- and long-term external debt (as percent of GDP)	8.1	4.8	4.2	...	4.8	4.8
Short-term external debt (as percent of GDP)	15.6	16.7	13.8	...	11.2	10.8

Sources: Belarus authorities; and Fund staff estimates.

1/ The Belarusian national accounts have overstated real growth by about 1-2 percent. A new industrial production index, which would improve the estimates is calculated but not published yet.

2/ Consolidates the state government and Social Protection Fund budget.

3/ End period. In 2006, it reflects the jump in December 2005.

Table 2. Belarus: Monetary Accounts, 2003–07
(In billions of Belarussian rubels, unless otherwise indicated; end-of-period)

	2003	2004	2005				2006	2007
	Dec	Dec.	Mar	Jun.	Sep.	Dec.	Dec.	Dec
							Staff projections	
Accounting exchange rate (Rbl/US$)	2,156	2,170	2,153	2,150	2,150	2,152	2,156	2,156
National Bank of Belarus								
Net foreign assets	1,296	1,872	2,357	2,796	2,933	2,978	3,651	3,217
Foreign assets	1,947	2,057	2,455	2,869	2,997	3,009	3,683	3,248
Foreign liabilities	-650	-184	-98	-73	-64	-31	-31	-31
Net domestic assets	390	522	-48	-171	70	1,181	808	2,133
Net domestic credit	872	820	130	18	284	1,405	1,068	2,393
Net credit to government	516	199	-280	-618	-565	325	-175	196
Claims on banks	332	565	384	501	658	818	1,085	2,030
Other claims on economy	24	56	26	135	190	262	157	167
Other items, net	-482	-298	-179	-189	-214	-224	-260	-260
Reserve money	1,687	2,394	2,308	2,625	3,003	4,159	4,459	5,349
Rubel reserve money	1,643	2,281	2,295	2,609	2,988	3,904	4,203	5,093
o/w currency outside banking system	926	1,339	1,374	1,680	1,807	2,016	2,599	3,193
Non-rubel reserve money	44	113	13	16	15	255	256	256
Monetary Survey								
Net foreign assets	1,163	1,523	2,051	2,634	2,976	2,654	2,429	1,577
Foreign assets	2,666	3,044	3,373	3,939	4,479	4,484	5,044	4,615
Foreign liabilities	-1,503	-1,521	-1,322	-1,304	-1,503	-1,830	-2,615	-3,038
Net domestic assets	4,969	7,316	7,195	7,640	8,065	9,916	13,116	17,459
Net domestic credit	7,355	10,234	9,935	10,656	11,474	13,796	17,004	21,347
Net credit to general government	977	259	-355	-463	-779	315	-44	436
Claims on economy	6,378	9,974	10,290	11,119	12,253	13,481	17,049	20,911
Other items, net	-2,386	-2,918	-2,740	-3,016	-3,410	-3,880	-3,888	-3,888
Broad money	6,132	8,839	9,247	10,274	11,041	12,571	15,545	19,036
Rubel broad money	3,408	5,388	5,735	6,657	7,218	8,595	11,173	14,302
Currency outside banks	926	1,339	1,374	1,680	1,807	2,016	2,599	3,193
Domestic currency deposits	2,269	3,949	4,254	4,857	5,297	6,449	8,463	10,986
Bank securities (outside bank circul.), in rubels	213	100	107	120	114	129	112	122
Foreign currency deposits	2,705	3,426	3,498	3,603	3,802	3,952	4,348	4,710
Bank securities (outside bank circul.), in fgn currency	16.3	21	11	12	17	20	20	20
Precious metals in deposits	2.8	3	3	3	3	4	4	4
12-month % change in broad money	56.3	44.1	42.7	41.6	40.6	42.2	23.7	22.5
12-month % change in rubel broad money	71.0	58.1	57.6	55.6	53.6	59.5	30.0	28.0
12-month % change in reserve money 1/	69.7	41.9	21.1	39.3	49.6	73.7	7.2	20.0
12-month % change in rubel reserve money	84.9	38.9	23.1	39.9	50.4	71.1	7.7	21.2
12-month % change in claims on economy	58.9	56.4	54.0	43.8	36.7	35.2	26.5	22.7
Annual rubel broad money velocity 2/	13.5	11.2	11.3	10.3	10.1	9.5	7.5	6.6
Annual broad money velocity 2/	7.3	6.6	6.7	6.4	6.4	6.2	5.3	4.9
Broad money multiplier	3.6	3.7	4.0	3.9	3.7	3.0	3.5	3.6
Rubel broad money multiplier	2.1	2.4	2.5	2.6	2.4	2.2	2.7	2.8

Sources: National Bank of Belarus; and Fund staff estimates.
1/ In 2006, it reflects the jump in December 2005.
2/ Defined as annual GDP divided by average broad (rubel broad) money for the year.

Table 3. Belarus: Fiscal Indicators and Projections, 2002-07
(In billions of rubels, unless otherwise indicated)

	2002	2003	2004	2005	2006		2007
					Official Budget	Staff Projection	Staff Projection
1.State (republican and local) budget							
Revenue	8,651	12,875	17,587	23,420	25,757	26,988	30,348
Personal income tax	773	1,025	1,404	1,882	2,304	2,179	2,485
Profit tax	643	935	1,625	2,366	2,945	2,662	3,147
VAT	2,165	2,897	3,815	5,895	6,700	6,761	7,754
Excises	592	838	1,122	1,368	2,419	1,584	1,873
Property tax	390	731	957	1,149	1,076	1,330	1,588
Customs duties	524	957	1,095	1,682	1,965	1,948	2,297
Other	1,651	2,609	3,662	4,008	8,349	4,599	5,456
Revenue of budgetary funds 1/	1,912	2,884	3,910	5,071	...	5,926	6,756
Expenditure (cash)	9,123	13,495	17,758	24,521	26,887	27,765	31,358
Defense	260	377	472	698	922	868	962
Law, order and security	461	656	921	1,262	1,720	1,328	1,938
Agriculture	179	523	767	1,180	2,959	1,305	1,786
Housing and communal services	612	946	1,175	1,349	1,607	1,502	1,965
Education	1,738	2,352	3,020	4,060	4,732	4,745	5,410
Health	1,270	1,692	2,240	3,183	4,179	3,720	4,241
Social policies	443	615	821	1,396	10,611	1,595	1,818
Interest due	154	175	210	215	277	266	303
Budgetary loans	382	168	47	368	...	430	622
Other	1,830	3,304	4,343	5,874	...	6,488	7,495
Expenditure of budgetary funds 1/	1,794	2,687	3,743	4,894	...	5,719	6,520
Expenditure (accrual) 2/	9,154	13,228	17,587	24,478	26,887	27,765	31,358
Wages and salaries	2,061	2,848	3,880	5,290	6,502	6,502	7,826
Social protection fund contributions	581	780	1,064	1,478	1,776	1,770	2,188
Goods and services	2,108	3,063	3,990	5,013	7,623	5,979	7,237
Interest	143	186	243	229	...	266	337
Subsidies and transfers	1,880	2,881	3,792	5,864	...	6,200	7,489
Capital expenditures	1,999	3,154	4,367	6,088	4,722	6,643	7,153
Net lending	362	336	258	559	73	688	951
Balance (cash) 3/	-472	-620	-170	-1,101	-1,130	-777	-1,010
Balance (accrual) 2/	-503	-354	0	-1,058	-1,130	-777	-1,010
2. Social Protection Fund							
Revenue	2,985	3,921	5,417	7,405	8,182	9,005	9,257
Expenditure	3,061	3,931	5,226	6,735	8,182	8,287	9,257
Balance (cash)	-76	-10	191	669	0	718	0
3. General government							
Revenue	11,636	16,796	23,004	30,825	33,940	35,642	39,604
Expenditure (cash)	12,185	17,426	22,984	31,257	35,070	35,701	40,614
Expenditure (accrual) 2/	12,216	17,160	22,813	31,214	35,070	35,701	40,614
Balance (cash) 3/	-549	-630	21	-432	-1,130	-60	-1,010
Balance (accrual) 2/	-580	-364	191	-389	-1,130	-60	-1,010
4. Statistical discrepancy 3/	34	-113	-53	-263	0	0	0
5. Financing (cash) 3/	583	517	-73	168	1,130	60	1,010
Privatization	427	36	40	45	1	50	150
Foreign financing, net	29	-50	273	218	726	362	360
Domestic financing, net	126	531	-386	-94	403	-353	500
Banking system	-4	453	-718	56	...	-433	480
Central bank (incl. IMF)	-256	257	-318	126	...	329	370
Deposit money banks (incl. SPF)	252	196	-400	-70	...	-762	110
Nonbank	131	78	332	-150	...	80	20
Memorandum items:							
Change in expenditure arrears	19	-105	-8	-43	0	0	0
Stock of expenditure arrears	332	227	220	176	176	176	176
GDP (trillions of rubels)	26	37	50	63.7	73.7	74	84

Source: Ministry of Finance, SPF, and Fund staff estimates.

1/ Includes innovation funds from 2002, formally incorporated into the state government budget from 2005.

2/ Includes changes in expenditure arrears.

3/ The actual deficits from above the line include all the closing expenditure for the year carried out in January of the following year and correspond to the authorities fiscal year reports. The deficit values from the financing side include January closing expenditure in the year they were actually paid.

Table 4. Belarus: Fiscal Indicators and Projections, 2002-07
(In percent of GDP, unless otherwise indicated)

	2002	2003	2004	2005	2006		2007
					Official Budget	Staff Projection	Staff Projection
1.State (republican and local) budget							
Revenue	33.1	35.2	35.2	36.8	35.0	36.6	36.1
Personal income tax	3.0	2.8	2.8	3.0	3.1	3.0	3.0
Profit tax	2.5	2.6	3.2	3.7	4.0	3.6	3.7
VAT	8.3	7.9	7.6	9.3	9.1	9.2	9.2
Excises	2.3	2.3	2.2	2.1	3.3	2.1	2.2
Property tax	1.5	2.0	1.9	1.8	1.5	1.8	1.9
Customs duties	2.0	2.6	2.2	2.6	2.7	2.6	2.7
Other revenue	6.3	7.1	7.3	6.3	11.3	6.2	6.5
Revenue of budgetary funds 1/	7.3	7.9	7.8	8.0	...	8.0	8.0
Expenditure (cash)	34.9	36.9	35.5	38.5	36.5	37.6	37.3
Defense	1.0	1.0	0.9	1.1	1.3	0.9	1.1
Law, order and security	1.8	1.8	1.8	2.0	2.3	1.8	2.3
Agriculture	0.7	1.4	1.5	1.9	4.0	1.8	2.1
Housing and communal services	2.3	2.6	2.3	2.1	2.2	2.0	2.3
Education	6.6	6.4	6.0	6.4	6.4	6.4	6.4
Health	4.9	4.6	4.5	5.0	5.7	5.0	5.0
Social policies	1.7	1.7	1.6	2.2	14.4	2.2	2.2
Interest due	0.6	0.5	0.4	0.3	0.4	0.4	0.4
Budgetary loans	1.5	0.5	0.1	0.6	...	0.6	0.7
Other	7.0	9.0	8.7	9.2	...	8.8	8.9
Expenditure of budgetary funds 1/	6.9	7.3	7.5	7.7	...	7.7	7.7
Expenditure (accrual) 2/	35.0	36.2	35.2	38.4	36.5	37.6	37.3
Wages and salaries	7.9	7.8	7.8	8.3	8.8	8.8	9.3
Social protection fund contributions	2.2	2.1	2.1	2.3	2.4	2.4	2.6
Goods and services	8.1	8.4	8.0	7.9	10.4	8.1	8.6
Interest	0.5	0.5	0.5	0.4	...	0.4	0.4
Subsidies and transfers	7.2	7.9	7.6	9.2	...	8.4	8.9
Capital expenditures	7.6	8.6	8.7	9.6	...	9.0	8.5
Net lending	1.4	0.9	0.5	0.9	...	0.9	1.1
Domestic	1.3	1.0	0.6	1.0	...	1.1	1.2
Foreign	0.1	-0.1	-0.1	-0.1	...	-0.1	-0.1
Balance (cash) 3/	-1.8	-1.7	-0.3	-1.7	-1.5	-1.1	-1.2
Balance (accrual) 2/	-1.9	-1.0	0.0	-1.7	-1.5	-1.1	-1.2
2. Social Protection Fund							
Revenue	11.4	10.7	10.8	11.6	11.1	12.2	11.0
Expenditure	11.7	10.8	10.5	10.6	11.1	11.2	11.0
Balance (cash)	-0.3	0.0	0.4	1.1	0.0	1.0	0.0
3. General government							
Revenue	44.5	45.9	46.0	48.4	46.1	48.3	47.1
Expenditure (cash)	46.6	47.7	46.0	49.1	47.6	48.4	48.3
Expenditure (accrual) 2/	46.7	46.9	45.6	49.0	47.6	48.4	48.3
Balance (cash) 3/	-2.1	-1.7	0.0	-0.7	-1.5	-0.1	-1.2
Balance (accrual) 2/	-2.2	-1.0	0.4	-0.6	-1.5	-0.1	-1.2
4. Statistical discrepancy 3/	0.1	-0.3	-0.1	-0.4	0.0	0.0	0.0
5. Financing (cash) 3/	2.2	1.4	-0.1	0.3	1.5	0.1	1.2
Privatization	1.6	0.1	0.1	0.1	0.0	0.1	0.2
Foreign financing, net	0.1	-0.1	0.5	0.3	1.0	0.5	0.4
Domestic financing, net	0.5	1.5	-0.8	-0.1	0.5	-0.5	0.6
Banking system	0.0	1.2	-1.4	0.1	...	-0.6	0.6
Central bank (incl. IMF)	-1.0	0.7	-0.6	0.2	...	0.4	0.4
Deposit money banks (incl. SPF)	1.0	0.5	-0.8	-0.1	...	-1.0	0.1
Nonbank	0.5	0.2	0.7	-0.2	...	0.1	0.0
Memorandum items:							
Change in expenditure arrears	0.1	-0.3	0.0	-0.1	0.0	0.0	0.0
Stock of expenditure arrears	1.3	0.6	0.4	0.3	0.2	0.2	0.0
Government debt/GDP	11.6	10.4	8.9	8.4	...	7.3	7.1
o/w: external debt/GDP	5.7	4.3	3.2	2.6	...	2.8	2.6
GDP (trillions of rubels)	26.1	36.6	50.0	63.7	73.7	73.8	84.2

Source: Ministry of Finance, SPF, and Fund staff estimates.

1/ Includes innovation funds from 2002, formally incorporated into the state government budget from 2005.

2/ Includes changes in expenditure arrears.

3/ The actual deficits from above the line include all the closing expenditure for the year carried out in January of the following year and correspond to the authorities fiscal year reports. The deficit values from the financing side include January closing expenditure in the year they were actually paid.

Table 5. Belarus: Balance of Payments, 2003-11
(In millions of U.S. dollars, unless otherwise indicated)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
			Prel.	Projections					
Current account balance	-424	-1,206	469	57	-440	-921	-1,568	-2,422	-3,717
Merchandise trade balance	-1,256	-2,184	-527	-1,028	-1,715	-2,357	-3,044	-3,877	-5,072
Exports	10,073	13,942	16,095	17,854	19,066	19,768	20,636	21,581	22,579
Imports	-11,329	-16,126	-16,623	-18,882	-20,781	-22,126	-23,680	-25,458	-27,651
Services (net)	585	712	824	884	1,040	1,142	1,234	1,309	1,413
Income (net)	25	-19	16	40	65	111	46	-68	-292
Transfers (net)	222	285	157	161	170	183	195	214	234
Capital and financial accounts	484	1,371	242	337	606	1,041	1,707	2,582	3,915
Capital account	69	58	41	61	62	62	61	60	60
Financial account	415	1,313	200	276	544	980	1,646	2,522	3,855
Direct investment (net)	170	163	303	272	225	221	217	213	209
Portfolio investment (net)	6	63	-42	-42	-42	-42	-42	-41	-40
Trade Credits (net)	183	577	-353	-124	171	286	359	391	482
Loans (net)	90	379	367	343	379	649	1,245	2,090	3,333
Other (net)	-35	132	-75	-175	-189	-134	-135	-133	-130
Errors and omissions	-14	277	-139	0	0	0	0	0	0
Overall balance	46	442	571	394	166	120	139	161	198
Financing	-46	-442	-571	-394	-166	-120	-139	-161	-198
Gross official reserves	14	-256	-539	-394	-166	-120	-139	-161	-198
Use of Fund resources	-32	-17	-9	0	0	0	0	0	0
Exceptional financing	-28	-169	-23	0	0	0	0	0	0
o/w: Central Bank of Russia	12	-167	-53	0	0	0	0	0	0
Memorandum items:									
Current account (as percent of GDP)	-2.4	-5.2	1.6	0.2	-1.1	-2.1	-3.2	-4.5	-6.3
Trade balance (as percent of GDP)	-7.1	-9.4	-1.8	-3.0	-4.4	-5.4	-6.2	-7.2	-8.7
Overall balance (as percent of GDP)	0.3	1.9	1.9	1.2	0.4	0.3	0.3	0.3	0.3
Y-o-y growth in exports of goods (in percent)	26.5	38.4	15.4	10.9	6.8	3.7	4.4	4.6	4.6
Y-o-y growth in imports of goods (in percent)	27.6	42.3	3.1	13.6	10.1	6.5	7.0	7.5	8.6
Gross official reserves	499	770	1,297	1,691	1,857	1,977	2,116	2,277	2,475
In months of future imports of goods and services	0.3	0.5	0.8	0.9	0.9	0.9	0.9	0.9	...
Medium and long-term debt (as percent of GDP)	8.1	4.8	4.2	4.8	4.8	5.5	7.3	10.3	15.0
Short-term debt (exc. portfolio) (as percent of GDP)	15.6	16.7	13.8	11.2	10.8	10.9	11.1	11.4	11.8
Debt service ratio (as percent of exports of goods and services, incl.arrears)	5.3	3.8	3.4	3.1	3.4	3.8	5.1	7.2	7.4
Public and publicly-guaranteed debt service ratio (as percent of exports of goods and services)	2.2	2.3	0.8	0.2	0.2	0.2	0.2	0.2	0.2
External arrears	448	288	326	326	326	326	326	326	326
In percent of GDP	2.5	1.2	1.1	1.0	0.8	0.7	0.7	0.6	0.6

Sources: Belarusian authorities; and Fund staff estimates.

Table 6. Belarus: Public Sector Debt Sustainability Framework , 2001-2011
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	**Debt-stabilizing primary balance 9/**
Baseline: Public sector debt 1/	13.2	11.6	10.4	8.9	8.4	**7.4**	**7.7**	**8.5**	**9.9**	**12.0**	**14.6**	**-0.4**
o/w foreign-currency denominated	6.3	5.7	4.3	3.2	2.6	2.3	2.4	2.7	3.1	3.8	4.6	
Change in public sector debt	-1.8	-1.7	-1.2	-1.5	-0.5	-1.1	0.3	0.8	1.4	2.1	2.5	
Identified debt-creating flows (4+7+12)	0.8	0.2	-1.5	-2.6	-1.7	-1.0	0.5	0.9	1.5	2.1	2.6	
Primary deficit	2.4	1.4	0.6	-0.5	-0.2	-0.3	0.8	1.2	1.8	2.5	2.9	
Revenue and grants	44.9	44.6	45.8	45.7	48.4	48.3	47.1	46.6	46.1	45.6	45.1	
Primary (noninterest) expenditure	47.3	45.9	46.4	45.1	48.2	48.0	47.9	47.8	47.9	48.0	48.0	
Automatic debt dynamics 2/	-1.6	-2.8	-2.2	-2.1	-1.6	-0.8	-0.5	-0.4	-0.4	-0.4	-0.4	
Contribution from interest rate/growth differential 3/	-6.3	-4.0	-2.8	-2.3	-1.6	-0.8	-0.5	-0.4	-0.4	-0.4	-0.4	
Of which contribution from real interest rate	-5.9	-3.6	-2.2	-1.4	-0.9	-0.3	-0.2	-0.1	-0.1	-0.1	0.0	
Of which contribution from real GDP growth	-0.4	-0.4	-0.6	-0.9	-0.7	-0.5	-0.3	-0.3	-0.3	-0.3	-0.3	
Contribution from exchange rate depreciation 4/	4.7	1.2	0.6	0.2	0.0	...	...	...	...	...	...	
Other identified debt-creating flows	0.1	1.6	0.1	0.1	0.1	0.1	0.2	0.1	0.0	0.0	0.0	
Privatization receipts (negative)	0.1	1.6	0.1	0.1	0.1	0.1	0.2	0.1	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other (specify, e.g. bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes (2-3) 5/	-2.6	-1.9	0.3	1.1	1.2	-0.1	-0.2	-0.1	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	29.5	26.0	22.7	19.6	17.4	15.2	16.3	18.2	21.6	26.4	32.3	
Gross financing need 6/	4.5	3.1	2.2	0.9	1.0	0.8	2.0	2.5	3.3	4.2	5.0	
in billions of U.S. dollars	0.6	0.4	0.4	0.2	0.3	0.3	0.8	1.1	1.6	2.3	2.9	
Scenario with key variables at their historical averages 7/						**7.4**	**5.1**	**3.5**	**2.5**	**1.9**	**1.4**	**-0.5**
Scenario with no policy change (constant primary balance) in 2005-10						**7.4**	**6.6**	**6.0**	**5.4**	**5.0**	**4.5**	**-0.1**
Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
Real GDP growth (in percent)	4.7	5.0	7.0	11.4	9.3	7.2	4.5	3.8	3.6	3.4	3.0	
Average nominal interest rate on public debt (in percent) 8/	9.1	6.3	6.1	6.4	5.1	4.9	6.2	7.1	6.7	6.0	5.3	
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	-70.5	-38.7	-24.5	-16.3	-11.4	-3.2	-2.9	-1.3	-0.8	-0.5	-0.2	
Nominal appreciation (increase in US dollar value of local currency, in percent)	-48.2	-22.5	-13.1	-5.1	0.4	...	...	...	...	...	...	
Inflation rate (GDP deflator, in percent)	79.6	45.0	30.7	22.7	16.6	8.1	9.1	8.5	7.5	6.5	5.5	
Growth of real primary spending (deflated by GDP deflator, in percent)	8.2	1.9	8.2	8.4	16.7	6.8	4.2	3.6	3.8	3.8	2.9	
Primary deficit	2.4	1.4	0.6	-0.5	-0.2	-0.3	0.8	1.2	1.8	2.5	2.9	

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.
2/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).
3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi (1+g)$ and the real growth contribution as -g.
4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.
5/ For projections, this line includes exchange rate changes.
6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.
7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.
8/ Derived as nominal interest expenditure divided by previous period debt stock.
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 7. External Debt Sustainability Framework (Baseline), 2001-11
(In percent of GDP, unless otherwise indicated)

	Actual							Projections							
	2001	2002	2003	2004	2005			2006	2007	2008	2009	2010	2011		
										I. Baseline Projections					**Debt-stabilizing non-interest current account 6/**
External debt	19.5	26.8	23.6	21.4	17.9			**16.0**	**15.6**	**16.4**	**18.4**	**21.7**	**26.9**		**-1.1**
Change in external debt	2.9	7.2	-3.2	-2.1	-3.5			-2.0	-0.3	0.8	2.0	3.3	5.1	0.0	
Identified external debt-creating flows (4+8+9)	2.9	-1.7	-3.2	-8.1	-6.8			-3.1	-1.2	0.0	1.2	2.5	4.3	0.0	
Current account deficit, excluding interest payments	2.7	1.7	2.0	-2.4	-1.9			-0.4	0.6	1.7	2.7	3.8	5.3	1.1	
Deficit in balance of goods and services	4.1	3.3	3.8	6.5	-1.0			0.4	1.7	2.8	3.7	4.8	6.2		
Exports	68.2	63.5	64.9	67.8	61.4			58.8	55.4	51.2	48.2	45.9	44.4		
Imports	72.3	66.8	68.7	74.3	60.4			59.2	57.1	54.0	51.9	50.6	50.7		
Net non-debt creating capital inflows (negative)	-0.7	-0.9	-0.8	-0.6	-0.5			-0.4	-0.4	-0.4	-0.3	-0.3	-0.3	-0.3	
Automatic debt dynamics 1/	1.0	-2.6	-4.3	-5.1	-4.3			-2.2	-1.5	-1.4	-1.2	-1.0	-0.7	-0.9	
Contribution from nominal interest rate	0.5	0.4	0.4	0.4	0.3			0.3	0.5	0.4	0.5	0.7	1.0	1.3	
Contribution from real GDP growth	-0.8	-0.8	-1.5	-2.1	-1.6			-1.1	-0.6	-0.5	-0.5	-0.6	-0.6	-0.7	
Contribution from price and exchange rate changes 2/	1.3	-2.1	-3.2	-3.3	-3.1			-1.3	-1.3	-1.2	-1.1	-1.1	-1.1	-1.4	
Residual, incl. change in gross foreign assets (2-3)	0.0	8.9	0.0	6.0	3.2			1.1	0.9	0.8	0.8	0.8	0.8	0.0	
External debt-to-exports ratio (in percent)	28.6	42.1	36.3	31.6	29.2			27.2	28.2	32.1	38.3	47.4	60.5		
Gross external financing need (in billions of US dollars) 3/	1.8	1.9	3.4	2.8	3.9			4.6	4.8	5.8	7.3	9.3	11.2		
in percent of GDP	14.8	13.1	19.1	12.1	13.3			13.3	12.3	13.3	15.0	17.2	19.1		
Key Macroeconomic Assumptions						10-Year Historical Average	10-Year Standard Deviation							For debt stabilization	Projected Average
Real GDP growth (in percent)	4.7	5.0	7.0	11.4	9.3	6.9	3.1	7.2	4.5	3.8	3.6	3.4	3.0	3.0	3.7
Exchange rate appreciation (US dollar value of local currency, change in percent)	-48.2	-22.5	-13.1	-5.0	0.3	-34.1	27.4	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
GDP deflator in US dollars (change in percent)	-7.0	12.4	13.6	16.5	16.9	5.0	16.8	8.1	8.9	8.5	7.5	6.5	5.5	5.5	7.4
Nominal external interest rate (in percent)	3.0	2.3	1.9	2.0	1.9	2.8	1.0	1.6	3.4	2.5	3.2	4.1	5.2	5.2	3.7
Growth of exports (US dollar terms, in percent)	10.9	9.8	24.4	35.4	15.8	14.1	14.6	11.0	7.3	4.2	4.7	4.9	5.2		5.3
Growth of imports (US dollar terms, in percent)	11.1	9.0	25.1	40.3	4.0	13.2	17.1	13.6	9.9	6.5	7.0	7.5	8.7		7.9
Current account balance, excluding interest payments	-2.7	-1.7	-2.0	2.4	1.9	-2.0	2.7	0.4	-0.6	-1.7	-2.7	-3.8	-5.3		-2.8
Net non-debt creating capital inflows	0.7	0.9	0.8	0.6	0.5	1.3	1.0	0.4	0.4	0.4	0.3	0.3	0.3		0.3
										II. Stress Tests for External Debt Ratio					**Debt-stabilizing non-interest current account 6/**
A. Alternative Scenarios															
A1. Key variables are at their historical averages in 2006-10 4/								**16.0**	**16.2**	**16.4**	**16.6**	**16.7**	**16.8**		**-2.7**
B. Bound Tests															
B1. Nominal interest rate is at baseline plus one-half standard deviation								**16.0**	**15.7**	**16.6**	**18.6**	**22.0**	**27.2**		**-1.0**
B2. Real GDP growth is at baseline minus one-half standard deviations								**16.0**	**15.8**	**16.9**	**19.1**	**22.7**	**28.2**		**-0.8**
B3. Non-interest current account is at baseline minus one-half standard deviations								**16.0**	**17.0**	**19.0**	**22.2**	**26.6**	**33.0**		**-1.3**
B4. Combination of B1-B3 using 1/4 standard deviation shocks								**16.0**	**16.4**	**18.0**	**20.8**	**24.8**	**30.8**		**-1.0**
B5. One time 30 percent real depreciation in 2006								**16.0**	**25.2**	**25.4**	**27.1**	**30.2**	**35.4**		**-1.6**

1/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.
2/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).
3/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.
4/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.
5/ The implied change in other key variables under this scenario is discussed in the text.
6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Table 8. Belarus: Banking Sector Indicators, 2001-06

	2001	2002	2003	2004	2005	2006 1/
I. Asset quality						
NPLs (in percent of total loans)	14.9	9.0	3.7	2.8	1.9	1.8
NPLs net of provision (in percent of regulatory capital)	32.9	31.2	13.1	11.4	6.3	8.3
Fx-denominated loans (in percent of total loans)	50.7	52.7	50.4	43.8	37.0	36.6
Non performing fx-denominated loans (in percent of NPLs)	69.3	49.2	47.0	46.5	35.2	33.3
Fx-denominated loans to borrowers without access to fx (in percent of total loans) 2/	2.3	3.5	6.3	8.5	7.7	7.4
Loans classified as doubtful and loss (in percent of total NPLs)	63.6	51.8	47.2	50.7	45.9	36.9
Required provisions (in percent of NPLs)	67.9	55.5	58.0	56.6	57.2	51.4
Actual provisions (in percent of NPLs)	37.7	15.8	29.9	32.4	48.4	41.4
Actual provisions to required provisions	55.5	28.5	51.6	57.2	84.6	80.5
II. Capital adequacy						
Regulatory capital (in percent of risk-weighted assets)	20.7	24.2	26.0	25.2	26.7	27.1
Regulatory Tier I (in percent of risk-weighted assets)	n.a.	19.2	21.7	21.0	18.7	19.1
Total capital (in percent of total assets)	15.1	18.7	20.4	20.1	19.8	20.5
III. Liquidity						
Liquid assets to total assets 3/	13.9	16.0	28.7	27.7	30.4	24.5
Liquid assets to short-term liabilities 4/	n.a.	67.2	60.9	63.0	95.9	85.5
Long-term assets to long-term liabilities 5/	1.5	2.4	3.9	4.1	3.8	3.9
Loans to deposits	114.1	112.7	111.7	123.2	119.9	124.5
Foreign exchange loans to foreign exchange deposits	87.8	96.7	103.3	116.0	116.7	118.1
Foreign exchange deposits to total deposits	65.9	60.5	54.5	46.5	38.0	38.6
Foreign exchange liabilities to total liabilities	47.6	44.6	42.1	42.8	37.1	35.4
NBB credit to banks (in percent of liabilities)	3.8	3.7	3.2	3.5	3.6	3.8
Average maturity of deposits (in months)	4.9	3.6	3.6	4.2	5.3	5.2
Average maturity of assets (in months)	6.0	7.3	8.2	8.4	8.7	9.5
IV. Profitability						
Return on assets (after tax: in percent, end-of-period)	0.8	1.0	1.5	1.5	1.3	0.3
Return on equity (after tax: in percent, end-of-period)	4.9	6.5	8.4	7.8	6.8	1.3
Adjusted ROA (with required loan provisioning)	-1.1	-0.3	2.3	0.5	1.0	0.0
Adjusted ROE (with required loan provisioning)	-7.1	-1.4	9.5	2.8	5.4	0.0
Noninterest income to gross income	46.5	46.3	35.4	40.8	n.a.	43.1
Noninterest expenses to gross income	66.3	67.7	61.5	64.3	n.a.	63.8
Administrative expenses to noninterest expenses	18.0	19.5	30.7	19.2	n.a.	33.7
Net interest margin (in percent of total assets)	5.3	5.6	4.8	3.9	n.a.	0.6
Interest rate spreads (in percentage points, end-of-period)						
Loans/deposits in local currency	13.1	10.1	6.5	4.0	2.2	1.7
Loans/deposits in foreign currency	7.9	8.2	6.9	5.5	5.1	5.2
Loans in local currency/deposits in foreign currency	39.6	30.5	18.3	11.7	5.8	3.8
Loans in foreing currency/deposits in local currency	-18.6	-12.2	-4.9	-2.2	1.5	3.1
V. Market risk						
Net open positions in foreign currency (in percent of regulatory capital)	n.a.	-7.2	-3.6	-5.2	-14.5	-4.6
Share of private securities in total assets	0.6	1.1	0.8	0.7	0.5	0.4
Memorandum items						
Number of banks	25.0	28.0	31.0	32.0	30.0	30.0
Private	20.0	24.0	27.0	27.0	25.0	25.0
Domestic	11.0	12.0	10.0	8.0	7.0	7.0
Foreign	9.0	12.0	17.0	19.0	18.0	18.0
Public	5.0	4.0	4.0	5.0	5.0	5.0
Concentration						
Assets in private banks (in percent of total assets)	46.8	38.1	38.4	29.8	24.8	24.7
Assets in public banks (in percent of total assets)	53.2	61.9	61.6	70.2	75.2	75.3
Assets in largest 6 banks (in percent of total assets) 6/	86.1	85.0	85.3	86.1	87.5	87.4
Share of loans to state-owned enterprises in total loans 7/	42.2	45.3	35.7	31.7	26.3	26.7

Sources: National Bank of the Republic of Belarus; and staff estimates.
1/ As of 01.03.2006.
2/ Sectors with no access to fx are: households, agriculture, and constructions.
3/ The definition of liquid assets was broadened from 1/1/2004 to include assets with a remaining maturity of less than 1 month.
4/ Assets and liabilities with a remaining maturity of less than 1 month.
5/ Assets and liabilities with a remaining maturity of over 1 year.
6/ These are all public banks.
7/ State-owned enterprises are defined as enterprises with a 100 percent state ownership.

Appendix I. Fund Relations

As of May 31, 2006

I. **Membership Status:** Joined July 10, 1992; Article VIII

II.	**General Resources Account:**	**SDR million**	**Percent of Quota**
	Quota	386.40	100.00
	Fund holdings of currency	386.40	100.00
	Reserve position in Fund	0.02	0.01

III.	**SDR Department:**	**SDR million**	**Percent of Allocation**
	Holdings	0.02	N/A

IV. **Outstanding Purchases and Loans:** None

V. **Financial Arrangements:**

Type	Approval Date	Expiration Date	Amount Approved (SDR million)	Amount Drawn (SDR million)
Stand-by	09/12/1995	09/11/1996	196.28	50.00

VI. Projected Obligations to the Fund (SDR million; based on existing use of resources and present holdings of SDRs): None

VII. **Safeguards Assessments:**

As there is no arrangement in place, under the Fund's safeguards assessments policy, the National Bank of Belarus (NBB) is not subject to a full safeguards assessment. However, as a potential borrower, the NBB requested a voluntary safeguards assessment, and an on-site assessment was conducted in December 2003. The assessment concluded that significant vulnerabilities existed in the safeguards framework, especially in the areas of the legal structure and independence, external and internal audit, and in financial reporting. The assessment made specific recommendations to correct the identified shortcomings. The authorities have begun to address some of these issues, and are considering appropriate measures to address the remaining concerns.

VIII. Exchange Arrangements:

As of August 20, 1994, the rubel (Br) became the unit of account replacing the Belarusian ruble, which was formally recognized as the sole legal tender only on May 18, 1994. The conversion took place at the rate of 10 Belarusian rubles = 1 rubel. The authorities decided to drop three zeroes from the rubel denomination as of January 1, 2000. The exchange rate for the U.S. dollar was Br 2149 on April 18, 2006.

In mid-September 2000, the official exchange rate was unified with the market-determined rate resulting from daily auctions at the Belarus Currency and Stock Exchange. Since then, the official rate on any day is equal to the closing rate of the previous trading day. In line with the objective to reach monetary union with Russia, the authorities adopted a crawling band vis-à-vis the Russian ruble in January 2001, with monthly rates of devaluation that are revised quarterly and a band of currently 5 percentage points around central parity. On November 5, 2001, Belarus accepted the obligations of Article VIII, Sections 2, 3, and 4 of the IMF's Articles of Agreement. During the same month, the NBB suspended all ad hoc exemptions from the 30 percent surrender requirement.

IX. UFR/Article IV Consultation:

Belarus is on a 12-month consultation cycle. The 12th Article IV consultation was concluded on June 17, 2005. Visits since have included:

Staff visit	September 13–21, 2005
2006 Article IV consultation mission	May 17–30, 2006

X. FSAP Participation, ROSCs, and OFC Assessments:

The fiscal ROSC was published on http://www.imf.org/external/pubs/cat/longres.cfm?sk=17839.0 and the data ROSC on http://www.imf.org/external/pubs/cat/longres.cfm?sk=18013.0. Two FSAP missions took place in 2004 and an FSSA report was published on http://www.imf.org/external/pubs/cat/longres.cfm?sk=18367.0.
The detailed FSAPs were disseminated in May 2006 for the Basel Core Principles for Effective Banking Supervision on http://www.imf.org/external/pubs/cat/longres.cfm?sk=19246.0, for the Transparency of Monetary Policy and Banking Supervision on http://www.imf.org/external/pubs/cat/longres.cfm?sk=19248.0, and the Technical Note - Deposit Insurance on http://www.imf.org/external/pubs/cat/longres.cfm?sk=19250.0.

XI. Technical Assistance, 2000–05:

	Department Counterpart	Subject	Timing
Missions			
	MFD	Banking Supervision	February 6–10, 2006
	MFD	Monetary Policy Transmission Mechanism	December 12–16, 2005
	MFD	International Accounting Standards	October 24–28, 2005
	STA	Monetary and Financial Statistics	October 19–November 1, 2005
	MFD	Improving Monetary Policy	June 20–July, 10, 2005
	FAD	Government Finance Statistics	April 28, May 12, 2005
	MFD	Banking Supervision Issues	April 11–20, 2005
	MFD	Monetary Policy and Monetary Operations	February 26–March 10, 2005
	FAD/MFD	Improving debt management	October 6–20, 2004
	FAD	Budget code and other issues in public expenditure management	March 1–12, 2004
	FAD	Tax policy	March 19–April 1, 2003
	FAD	Public expenditure management	June 12–27, 2001
	FAD	Treasury development	January 15–26, 2001
	MFD	Banking supervision issues	April 11–20, 2005
	MFD	Monetary policy and monetary operations	February 26–March 10, 2005
	MFD	FSAP	September, November, and December 2004
	MFD/LEG	Anti-money laundering and combating the financing of terrorism legislative issues	June 17, 24, 2004
	MFD	Bank supervision and restructuring	December 1–12, 2003
	MFD	Issues in Monetary Unification with Russia	April 2–11, 2003
	MFD	Assessment of foreign exchange markets and operations and reserve management	June 2–10, 2002
	MFD	Assessment in monetary and foreign exchange policy and operations and central bank organization	April 10–22, 2002
	FIN	Safeguards Assessment	December 9–19, 2003
	STA	National Accounts Statistics	January 10–21, 2005
	STA	Data ROSC and SDDS subscription	March 2004
	STA	SDDS subscription	December 2004
	STA	Balance of payments	August 20–September 3, 2003
	STA	Balance of payments	November 13–24, 2000

	STA	Money and banking statistics	October 25–November 7, 2000
	STA	Multisector statistics (report of the resident advisor)	August 7, 1996–August 6, 2000
	STA	National accounts statistics	August 23–September 6, 2000
Resident Advisors	STA	Mr. Umana (General Statistics Advisor)	August 1996–August 2000

APPENDIX II. RELATIONS WITH THE WORLD BANK

Partnership in Belarus' development strategy

1. According to the recent Country Assistance Strategy for Belarus the World Bank Group aims to advance cooperation in critical areas, help the country open up its economy and society, minimize social and environmental risks, and address global public good concerns.

IMF-World Bank collaboration in specific areas

2. The Bank and Fund teams work closely in Belarus and maintain an extremely good relationship. The IMF plays a key role at the macro level, while the World Bank focuses on the structural agenda, social and environmental issues. The Bank and the Fund teams carry out joint activities on the key fiscal and structural issues. The joint work on the Public Expenditure Review (PER), Financial Sector Assessment Program (FSAP) and the Country Economic Memorandum (CEM) - are examples of excellent cooperation between the two institutions.

Areas in which the World Bank leads

3. **Social sphere.** The World Bank technical engagement with Belarus has generated a significant amount of analysis in areas of relevance to the assessment of poverty and living conditions in the country. A strong platform for technical collaboration on poverty issues was provided by technical assistance under the *IDF grant for Strengthening of the Capacity of the Ministry of Social Protection in Policy Formulation and Analysis* for preparation and introduction of Targeted Social Assistance Program (TSAP). The Grant was implemented successfully during 2000-2003 and completed in June 2003. In 2004 the Bank presented study "Poverty Assessment. Can Poverty Reduction and Access to Services Be Sustained?" offering a number of improvements to the methodology for measuring poverty and living conditions in Belarus and contributing an in-depth analysis of the multiple dimensions of poverty. Driven by demographic and socio-economic factors, Belarus faces a need for deep pension system reform. To analyze current situation and discuss possible reform options the World Bank team conducted a *Pension Policy Dialogue* with the Government during FY 2004.

4. **Energy sector.** The *Social Infrastructure Retrofitting Project* (US$22.6 million) aims to assist in the rehabilitation of the heating system, thermal insulation, and lighting in over 450 public buildings across the country. The project targets schools, hospitals, orphanages, and community homes for the elderly and the disabled. It also includes measures to increase energy efficiency.

5. *Energy Sector Management Assistance Program (ESMAP) grant* (US$50.0 thousand, completed in 2005). The project helped the Committee on Energy Efficiency explore market mechanisms to improve energy efficiency through operation of Energy Servicing Companies (ESCOs) and options of strengthening the energy efficiency program by learning experience of neighboring countries that have managed to weather the impact of multi-fold energy prices increases.

6. *Private-Public Infrastructure Advisory Facility project* (US$350.0 thousand) was approved in 2005**.** The project will help to advance the transition to market principles and encourage private sector involvement in the Belarus energy sector by providing regulatory, institutional and other support to create an environment that is conducive to private investment. While recognizing that the environment for private investments is not conducive in Belarus, the government has considered some reform scenarios that draw on experience gained by neighboring countries, and is seeking technical assistance in the evaluation and implementation of such scenarios.

7. **Environment.** Belarus has made good progress in the protection of environment. However, the country is still facing many environmental problems, including coping with the legacy of the Chernobyl accident. The *Post-Chernobyl Recovery Project* (approved on April 18, 2006) is designed to revitalize selected regions of the country, affected by the Chernobyl accident, by improving local people's living conditions, reinforcing the energy efficiency and environmental safeguards. The project is based on the recommendations of the *Chernobyl Review* (2002) and also intended to spearhead greater support of the international community to the affected regions of the country.

8. *PHRD Climate Change Pilot Project* (US$1.0 million, approved in 2003) is aimed at demonstrating opportunities for greenhouse gas (GHG) emission abatement through energy efficiency and renewable energy utilization in the supply of heat and hot water to social sector buildings, and assisting the Belarusian Government with the development and implementation of emission standards for biomass-fired boilers, thereby removing an institutional barrier to broader introduction of energy supply based on biomass fuel.

9. *GEF POPs Enabling Activity Project* (US$499,300). After a two-year dialogue and preparation activities in cooperation with UNEP, Belarus ratified the Stockholm Convention on Persistent Organic Pollutants (POPs) and selected the World Bank as a GEF Implementing Agency for the POPs activities**.** The project objective is to develop a National Implementation Plan (NIP) for POPs to reduce volume and ultimately eliminate the persistent organic pollutants stockpiles, consistent with the protection of human health and the environment. Preparation of a follow-up GEF investment project is under consideration**.**

Areas of shared responsibility

10. **Economic development.** The Bank team cooperated closely with the IMF on the issues related to the preparation of the *Country Economic Memorandum (CEM)*, with one chapter - "Macroeconomic policies and risks," prepared jointly. This chapter reviews the country's macroeconomic developments since 1996, the sources and structure of growth, and analyzes the role of macroeconomic policies in Belarus's growth performance. Special attention was paid to the risks associated with Belarus's current macroeconomic position, and how these risks might be addressed effectively through adjustments in monetary policy, fiscal policy, and debt management.

11. **Private sector development.** The most challenging reform agenda for Belarus is in the area of structural reforms and private business development. The Bank Group seeks to improve the general environment for the creation and operation of private business in Belarus through technical assistance, policy dialogue and ESW. The Bank and the IFC conducted a number of studies including *Improving the Business Environment* and *Costs of Doing Business Surveys* to track the developments in this area, define impediments to private business expansion and provide policy recommendations. The Fund focuses on macroeconomic policies aimed at sustainable growth and encouraging private sector development. The Fund also provides technical assistance to improve taxation, banking regulations and banking supervision.

12. **Public expenditure management**. The current CAS attaches great importance to fiscal issues, emphasizing the goals of greater effectiveness, transparency, and accountability in the use of public resources. In 2003 the World Bank with the IMF participation completed the first *Public Expenditure Review* (PER) for Belarus.

13. The IMF and the Bank provide continuous technical assistance to Belarus in the area of public expenditure management. The Government has determined the following priority areas: modernization of budget classification, Budget Code preparation, MTEF, reform of inter-budgetary fiscal relations, and development of sector strategies. During FY2004 the Bank provided technical assistance to the Ministry of Finance for Budget Code preparation. In FY2005 efforts have been focused on assisting the Government in the area of intergovernmental fiscal relations, in particular, in clarification of revenues and expenditures assignments for different level of the Government and in the development of formula for intergovernmental fiscal transfers. In FY 2006 the assistance has been provided for preparation of budget programs' description and other basic documents required for the introduction of performance-based budgeting (PBB).

14. **Financial sector.** The FSAP for Belarus (2005) has been centered on assessments of the banking system, including deposit insurance, securities markets, insurance industry, payment system and transparency in conducting monetary policy. Regulations, oversight and governance arrangements has been reviewed also. The Bank and the IMF also carry out joint responsibility for providing assistance to Belarus in the prevention of money laundering and combating financing of terrorism.

In the context of the CIS Payments and Securities Settlement Initiative (CISPI), the World Bank-lead mission visited Minsk in spring 2006 to review the payment and securities settlement systems of the Republic of Belarus. The CISPI is a cooperative effort lead by the World Bank. Its objective is to describe and assess the payments systems of the countries of the CIS with a view to identifying possible improvement measures in their safety, efficiency and integrity.

15. **Statistical capacity-building.** The IMF and the World Bank provide technical assistance in the area of statistics to the Ministry of Statistics and Analysis, National Bank and the Ministry of Finance. Trust Fund for Statistical Capacity Building (TFSCB) grant (US$108.0 thousand, 2005) was designed to assist the GOB in the design of the National Strategy for the Development of Statistics (NSDS), which will provide Belarus with the strategy for strengthening statistical capacity across the entire national statistical system.

Areas in which the IMF leads

16. The IMF is actively engaged with the Authorities in discussing the macroeconomic program providing them with technical assistance and related support, including on economic and financial statistics, tax policy, monetary operations and fiscal transparency. The IMF is leading the dialogue on setting the objectives for monetary and exchange rate policies, public debt management, overall budget envelope and tax policy.

17. The IMF analysis in these areas serves as an input to the Bank policy advice. The Bank and the IMF teams have regular consultations and the Bank staff takes part in the IMF Article IV Consultation missions. This helps to ensure consistency of the policy recommendations by the two institutions.

The World Bank Group Strategy

18. Belarus joined the World Bank in July 1992. Bank relations with Belarus have generally paralleled those of the IMF. Under the 1999 CAS, liberalization of the exchange rate was set as a trigger for moving to a *low case* lending (one project per year) scenario. The unification of the exchange rate in September 2000 allowed the Bank to proceed with the preparation of a US$22.6 million Social *Infrastructure Retrofitting Project*, approved on June 5, 2001. An improved technical dialogue between the World Bank Group and the Belarus authorities preceded the preparation of the 2002-04 CAS. In the *low case*, the CAS focused on the areas compatible with government priorities and the Bank's corporate mandate—global public goods and interventions with a high social content. The CAS left the

door open for a broader assistance by spelling out triggers for a *base case*, should the Government advance in public expenditure reform and improve business environment.

19. The Country Assistance Review (2004) recommended completing the key elements of latest CAS before initiation of the new strategy of engagement. This included, completion of ongoing ESW, particularly the CEM and the FSAP; continuation of the environment initiatives, and finalization of the Chernobyl Project. The next CAS for Belarus will be prepared in the first half of FY07.

20. To date, the Bank has committed the total of US$240.6 million, and US$15.0 million has been provided in the form of grants. The IBRD Belarus active portfolio has one ongoing operation – *Social Sector Energy Retrofitting Project* totaling US$22.6 million. The *Post-Chernobyl Recovery Project* (US$50.0 million) was approved by the Executive Board on April 18, 2006.

21. Non-lending activities include extensive analytical work. The most recent work includes the report entitled *Belarus: Chernobyl Review* (2002), a Public Expenditure and Institutional Review (*Belarus: Strengthening Public Resource Management,* 2003) and a Poverty Assessment Update (*Belarus Poverty Assessment: Preparing for the Future*, 2004), Country Economic Memorandum (*Belarus: Window of Opportunity to Enhance Competitiveness and Sustain Economic Growth*, 2005) and *Financial Sector Assessment Program* (2005)

22. **The IFC activities in Belarus.** The International Finance Corporation has been actively involved in advisory work in Belarus since 1993. The work began with the advisory services on privatization of small businesses. Currently IFC focuses its efforts on small and medium enterprise development and improvement of the business environment.

23. In December 2004 IFC has launched a Business Enabling Environment Project funded jointly with the Swedish International Development Cooperation Agency (SIDA). This two-year technical assistance effort will aim at reducing the regulatory burden on small and medium enterprises and improving their access to information and business support services.

24. In addition to the advisory services the IFC is also pursuing investment activities in Belarus. It has invested a total of US$71 million in four projects in the financial and manufacturing sectors, including credit lines extended to *Priorbank* and *Belgazprombank* for on-lending to private enterprises and providing loan and equity for the refurbishment, modernization and expansion of *Dednovo* brewery. Despite the difficult investment

environment in Belarus, IFC continues to seek opportunities for investment projects with the participation of the strategic investors.

Questions may be referred to Sergiy Kulyk (202) 458-4068

APPENDIX III. BELARUS: STATISTICAL ISSUES

1. The quality and timeliness of statistical data are broadly adequate for surveillance, although macroeconomic analysis is encumbered in some areas. While weaknesses remain in the statistical system of Belarus, the authorities, with the help of technical assistance from the Fund, have made significant efforts and improvements over the past years in a number of key areas, as described below. The Ministry of Statistics and Analysis of the Republic of Belarus (Minstat) publishes a large amount of data and has a predetermined publication schedule. The provision of data over the last year has generally been adequate for the analysis of economic developments on a regular basis.

2. The country's *IFS* page was published since November 1996 and is updated regularly on a monthly basis. A Statistics Law was signed by the President in February 1997. A multisector statistical advisor sponsored by the Fund was in place from August 1996 to August 2000.

3. The data ROSC mission that visited Minsk in early 2004 found that all statistical agencies face the challenge of increasing users' confidence in the accuracy and reliability of official statistics.

4. The authorities subscribed to the IMF's Special Data Dissemination Standard (SDDS) on December 22, 2004: http://www.belstat.gov.by/homep/en/specst/np.htm.

National Accounts

5. National accounts are compiled in accordance with the System of National Accounts of 1993 (SNA 1993). GDP is compiled by the production, the expenditure and the income approaches, and covers the entire economic territory of the Republic of Belarus. Data on GDP are disseminated on a quarterly basis (in national currency) in current and constant market prices (2000=100) expressed as absolute values.

6. GDP figures are likely to be distorted by the underreporting of newly emerging sectors—in particular services—and an active informal sector. A systematic upward bias in measuring industrial output has also led to significant inaccuracies in GDP estimates. In addition, problems remain in calculating holding gains from inventories. Problems continue to exist in measuring the capital stock and consumption of fixed capital. Estimates of GDP by expenditure categories are still uncertain. The authorities have prepared an alternative series on industrial output that corrects some of the above problems, and these data, and the requisite revisions to GDP, have been published from January 1, 2006.

Prices

7. Data on Consumer Price Index (CPI) and the Producer Price Index (PPI) are being reported to the Fund monthly on a timely basis. Both indices were developed with substantial technical assistance from the Fund. As regards the PPI, in January 1995 a Laspeyres formula recommended by the Fund was adopted. Other recommendations, such as inclusion of exports, adequate specification of items, and better selection of representative products and prices, have either been adopted or are in the process of being adopted. Since January 2001, the PPI has been compiled using the 1999 weights; and beginning with 2003 data, with 2001 production weights.

Government Finance Statistics

8. Since the 2004 data ROSC mission, the MOF has made progress in different areas of collection, compilation, and dissemination of fiscal data. The authorities have extended the coverage of the general government (republican and local government) operations by including data for innovation funds, included the Social Protection Fund's operations in the budget, increased the number of officials involved in the GFS compilation work, established a close coordination with the National Bank of the Republic of Belarus (NBRB) for the reconciliation of fiscal and monetary datasets, and increased provision of detailed budgetary metadata and methodological descriptions on the MOF's website. In addition to these improvements, the MOF has prepared new budgetary classifications codes for revenue, expenditure, and financing data that will align them to the *GFSM 2001* analytical framework.

9. At the end of April 2005, a GFS technical assistance (TA) mission visited Minsk. This mission found that the existing fiscal, accounting, and statistical systems have a sound basis for migrating to the *GSFM 2001*. Nonetheless, several areas were identified that will need further work before satisfactory implementation of the *GFSM 2001.* In order to provide assistance in this area, the GFS TA mission collaborated with the authorities on the preparation of a migration plan for a gradual implementation of this analytical framework.

10. The authorities have reported GFS for 2003 and 2004 under the *GFSM 2001* analytical framework for publication in the *GFS Yearbook* and started disseminating, through the MOF's website, fiscal data according to the IMF's Special Data Dissemination Standard.

Monetary Statistics

11. The balance sheet of the NBRB and the monetary survey are usually provided with a lag of no more than two weeks; the bank monthly balance sheet is available on or about the fifth of the month following the reference period, but monetary data for publication in *IFS* are reported with a lag of about six weeks.

12. Interest rate data on bank deposits and credits, as well as data on NBRB credit auctions and the placement of NBRB and government securities, are provided with a one-month lag. Exchange rate data are readily available on the NBRB's web site, and periodically reported to the Fund in electronic file.

13. Following the TA mission of October 2005, the NBRB has compiled and submitted to STA a pilot set of monetary data for December 2004 – November 2005 using the framework of the new Standardized Report Forms (SRF). Subsequent STA review of the data validated the resulting monetary aggregates and the authorities initiated regular reporting of current monetary data in the SRF framework to EUR and STA. Also, the authorities and STA have been working on converting historic monetary database beginning from December 2001 into the SRF format for inclusion in the STA database and publication in on forthcoming *IFS Supplement*.

Balance of Payments Statistics

14. The overall quality and timeliness of external sector data is satisfactory. The International Transactions Reporting System employed by the NBRB has been broadened to permit a more accurate classification of external transactions, while coverage and reporting forms for enterprise surveys were also improved. The NBRB publishes quarterly balance of payments and international investment position statements in the *BPM5* format on a timely basis. Scheduled interest and amortization payments on public sector debt are tracked by the MoF and reported to the Fund, and timely information is available on arrears on government and government-guaranteed debt.

15. Belarus has started to disseminate historical data on the reserves template on the IMF's website: http://www.imf.org/external/np/sta/ir/colist.htm. Monthly time series start with November 2004 data.

APPENDIX IV: BELARUS: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE
(AS OF JULY 14, 2006)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of publication[6]	Memo Items[7]: Data Quality – Methodological soundness[8]	Memo Items[7]: Data Quality – Accuracy and reliability[9]
Exchange Rates	7/12/06	7/12/06	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	07/01/06	7/07/06	W	W	W		
Reserve/Base Money	06/2006	7/14/06	M	M	M	O, O, LO, LO	O, O, O, O, O
Broad Money	6/2006	7/14/06	M	M	M		
Central Bank Balance Sheet	6/2006	7/14/06	M	M	M		
Consolidated Balance Sheet of the Banking System	6/2006	7/14/06	M	M	M		
Interest Rates[2]	7/13/06	7/14/06	D	M	M		
Consumer Price Index	6/2006	7/12/06	M	M	M	O, LO, O, LO	O, O, LO, LO, O
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	3/2006	6/23/06	M	M	M	LO, LNO, O, O	O, O, O, O, NO
Revenue, Expenditure, Balance and Composition of Financing[3]– Central Government	6/2006	6/26/06	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	5/2006	6/23/06	M	M	M		
External Current Account Balance	3/2006	06/16/06	Q	Q	Q	O, O, LO, LO	LO, O, O, O, O,
Exports and Imports of Goods and Services	4/2006	06/21/06	M	M	M		
GDP/GNP	03/2006	6/21/06	Q	Q	Q	O, O, LO, O	LO, LNO, LO, O, LO
Gross External Debt	03/06	6/23/06	Q	Q	Q		

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Including currency and maturity composition.
[6] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).
[7] These columns should only be included for countries for which a Data ROSC (or a Substantive Update) has been prepared.
[8] Reflects the assessment provided in the data ROSC (published on February 1, 2005, and based on the findings of the mission that took place during March 23–April 7, 2004) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).
[9] Same as footnote 8, except referring to international standards concerning source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.

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Washington, D. C. 20431 USA

IMF Executive Board Concludes 2006 Article IV Consultation with the Republic of Belarus

On August 4, 2006, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Republic of Belarus.[1]

Background

Belarus's centralized, state-dominated economy has performed well over the past few years. The government's centrally administered, socially oriented policies have facilitated rapid real income growth, near-full employment, and a reduction in poverty to the lowest level in the CIS.

GDP growth averaged 8.2 percent in 2002–05. Favorable energy import prices have supported high growth, particularly in 2005. A widening gap between world prices for Belarus's energy-intensive exports and prices of energy imports from Russia have provided a large and increasing amount of trading gains. These have been distributed throughout the economy—including through transfers and subsidies to state-owned enterprises, high budgetary investment, as well as economy-wide mandated wage increases, and recommended lending—supporting domestic demand. Belarus also benefited from strong partner country growth, which, together with terms-of-trade improvements, helped swing the current account into a surplus of 1.6 percent of GDP in 2005. Moreover, economic stabilization and rising incomes have strengthened consumer confidence, further contributing to increasing domestic demand. The economy's positive momentum has carried forward into 2006.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

Ample production capacity has allowed twelve-month inflation to decline steadily over the past few years, to 6.9 percent in May 2006. However, rising unit labor costs, tighter capacity utilization in many sectors, a high and increasing ratio of Producer Price Index to Consumer Price Index inflation, and estimates of underlying inflation suggest a build-up in inflation pressures. Low inflation also reflects, in part, administrative controls over price formation.

Macroeconomic data may not tell the whole story. While the quality of statistics is generally good, extensive state controls over the economy—notably on prices— complicate the assessment of economic developments and of the impact of policy actions.

After a broad balance in 2004, the 2005 budget recorded a deficit of 0.7 percent of GDP, despite a 2¼ percent of GDP revenue windfall from the booming energy sector and from the switch to the destination principle for the value added tax in trade with Russia from the beginning of 2005. The 2005 deficit excluding oil-related revenues of around 6 percent of GDP suggests continued fiscal sensitivity to energy pricing. The 2006 budget recorded a—largely seasonal—3.1 percent of GDP surplus through May against a budgeted full-year deficit of 1½ percent of GDP.

While officially targeting the Russian ruble, the National Bank of the Republic of Belarus (NBRB) has maintained a stable exchange rate vis-à-vis the U.S. dollar, which facilitated further gradual dedollarization and rapid increases in international reserves in 2005. The refinance rate was reduced by 600 basis points in 2005 and by a further 50 in June 2006. Reserve requirements were also lowered twice in 2005 and 2006, by one percentage point each time. These developments triggered an increase in liquidity that the NBRB sterilized to a large extent, in a context of further remonetization.

State banks continued to lend at the government's behest for designated purposes mostly at controlled and subsidized interest rates. The resulting decline in these banks' liquidity and profitability necessitated budgetary recapitalizations of 1.1 percent of GDP. NBRB credit to the nonfinancial nongovernment sector has also increased, reaching ½ percent of GDP in April 2006. As a result, credit to the economy has continued growing, while the share of nonperforming loans fell to below 2 percent at end-2005. Banks have improved provisioning, covering about 90 percent of the requirement as of May 2006.

Progress with structural reforms has been limited. The remaining significant role of the state in the economy and administrative restrictions on the movement of labor and in other areas hamper market flexibility and private investment.

Executive Board Assessment

Executive Directors noted that Belarus has enjoyed several years of relatively strong macroeconomic performance. In particular, growth has been rapid since 2003, and inflation has declined further, remaining in single digits since the second half of 2005. This economic performance has reflected broadly the authorities' pursuit of prudent fiscal and monetary policies, as well as strong growth in partner countries, although price controls have also contributed to declining inflation.

Most Directors observed that the strong growth of recent years owed much to energy imports from Russia at markedly below-market prices, while prices for Belarus's energy-intensive exports had grown considerably. The resulting large and increasing terms-of-trade gains had been redistributed, financing rapid wage increases, budgetary support to enterprises, and large-scale investment projects that had underpinned the policy of strong government interference in the economy.

Directors emphasized that the outlook seems much less favorable than recent trends. They noted that current World Economic Outlook energy price projections suggest that terms-of-trade gains are set to halt from 2007. Indeed, the possibility of significantly less subsidized energy imports could impart a considerable downside risk to the outlook. Directors also pointed to Belarus's declining market share in the CIS, the large and growing non-oil current account deficit, the low level of international reserves, and the diminishing output gap. In light of these considerations, most Directors called for a fundamental change of course in policies, notably in the structural and fiscal areas. In particular, they stressed the importance of an up-front fiscal tightening, calling for early liberalization of prices and wages, followed by broader structural reforms.

Directors welcomed the authorities' intentions to implement fiscal and structural measures by 2010, especially to curb budgetary transfers and subsidies, reduce the tax burden, strengthen the financial system, moderate real wage increases, and attract foreign investors. However, Directors noted that a more rapid withdrawal of state intervention, including early liberalization of prices and wages, would help to underpin strong noninflationary growth in the medium term. They stressed that structural reform measures should be implemented without delay, while the economy is still in a position of strength. In this context, several Directors noted the importance of improving the institutional framework and governance, and several Directors pointed to the need to build social consensus for the reforms. Directors welcomed the authorities' strong track record regarding the implementation of technical assistance from the Fund, and endorsed the provision of further technical assistance in support of the reform agenda.

In particular, Directors argued for rapidly phasing out directed bank lending, bringing all remaining state support to enterprises on-budget, ensuring that budgetary and public sector wages grow in line with productivity, and curtailing the golden share rule to apply to only a handful of preannounced strategic enterprises. Directors cautioned against using privatization proceeds or increased foreign borrowing to sustain an unaltered state-dominated economic structure—a strategy that would only postpone the inevitable macroeconomic adjustment, while increasing its costs.

Directors argued that fiscal tightening, starting already in 2006, is necessary to cope with the impact on the budget of a stabilization of the terms of trade. The case for this policy stance is reinforced by the risk that the terms of trade might weaken, heightening the possibility that a relatively loose fiscal policy would prompt inflationary pressures and undermine competitiveness. Fiscal savings—primarily in the form of expenditure retrenchment—are also required to finance the cost of structural reforms and offset the planned reduction in Belarus's high tax burden. With a view to safeguarding the effective social safety net and productivity growth, these cuts should focus on phasing out subsidies and transfers to loss-making enterprises, and discontinuing bank recapitalizations associated with directed lending. Directors also noted the need to reduce budget rigidities by phasing out earmarking.

Turning to monetary policy, Directors believed the NBRB should clarify that controlling inflation is its primary objective. In this regard, most Directors stressed that the NBRB should accept more flexibility in the exchange rate in the event of inconsistency between the inflation and exchange rate targets. They also found that further policy interest rate cuts should be contingent on clear signs of lasting declines in inflationary pressures. Directors noted that to enhance the credibility of the NBRB's commitment to the inflation objective, its operational independence would need to be strengthened, the number of its quantitative targets pruned, its direct lending to the economy discontinued, and interest rate caps eliminated.

Directors commended the NBRB on the progress in strengthening the supervisory framework. However, they emphasized that, against the backdrop of continued rapid credit growth, the NBRB needs to remain vigilant in enforcing all prudential requirements. Directors welcomed the recent steps toward attracting strategic foreign investors to the banking system, while stressing the importance of transparent and competitive privatization procedures. It was also suggested that anti-money laundering legislation should be improved to meet international best practices.

Directors noted that the quality of the statistical system and the timeliness of data are broadly adequate.

Republic of Belarus: Selected Economic Indicators

	2002	2003	2004	2005 Preliminary
	(Annual change in percent, unless otherwise indicated)			
Real economy				
GDP (nominal in billions of rubels)	26,138	36,565	49,992	63,679
Real GDP	5.0	7.0	11.4	9.3
Industrial production	4.5	7.1	15.9	10.4
CPI (average)	42.6	28.1	18.1	10.3
Real average monthly wage (1996=100)	231.9	238.7	279.0	338.6
Average monthly wage (in U.S. dollars)	107.3	123.3	162.0	217.4
Money and credit				
Reserve money	32.0	69.7	41.9	73.7
Rubel broad money	59.6	71.0	58.1	59.6
Banking system net domestic credit	53.7	68.9	39.1	34.8
Refinance rate (percent per annum, end-of-period)	38.0	28.0	17.0	11.0
	(In percent of GDP)			
General government finances 1/				
Revenue	44.5	45.9	46.0	48.4
Expenditure (cash)	46.6	47.7	46.0	49.1
Expenditure (commitment)	46.7	46.9	45.6	49.0
Balance (cash)	-2.1	-1.7	0.0	-0.7
Balance (commitment)	-2.2	-1.0	0.4	-0.6
	(In millions of U.S. dollars unless otherwise indicated)			
Balance of payments and external debt				
Current account balance	-311	-424	-1,206	469
As percent of GDP	-2.1	-2.4	-5.2	1.6
Gross international reserves	477.8	499.0	770.2	1,297
In months of future imports of goods and services	0.6	0.3	0.5	0.8
Medium- and long-term debt (as percent of GDP)	9.9	8.1	4.8	4.2
Short-term debt (as percent of GDP)	17.0	15.6	16.7	13.8
	(Rubels per U.S. dollar)			
Exchange rates				
Average	1,784	2,052	2,160	2,154
End-of-period	1,920	2,156	2,170	2,152

Sources: Data provided by the authorities and IMF staff estimates.
1/ Consolidates the state government and Social Protection Fund budgets.

Statement by Willy Kiekens, Executive Director for Republic of Belarus and Mikhail V. Nikitsenka, Advisor to Executive Director
August 4, 2006

Economic Developments

The cooperation between the authorities and the staff has been constructive and has enabled further convergence of views. The authorities share staff's general assessment on the sources of growth and medium-term policy goals. These include structural reforms, reducing the size of the budget, strengthening the financial system, facilitating the development of small and medium-size enterprises, wage moderation and improving the business climate. The authorities are grateful for the technical assistance and advice, which was helpful for designing and implementing economic policies and reforms.

The staff has analyzed the sources of growth in Belarus, which has enabled them to project growth more accurately. In the past years, staff projections significantly underestimated actual growth. Real growth in 2005 was 9.2 percent, or 2.1 percent above the staff projection. For the first half of 2006, annualized growth has been already in excess of 10 percent. For the year as a whole, growth is projected by the staff to be 7 percent.

The authorities agree that in Belarus, as elsewhere, macro-economic data must be assessed in light of the specifics of the given economy. Nonetheless, they believe that par. 5 and par. 43 of the staff report and par. 5 of the background section of the draft PIN exaggerate the difficulties for assessing Belarus' economic developments and policies on the basis of what are widely considered good quality statistical data. The Fund's technical assistance report on national accounts, finalized in April 2005, confirms that the methodology for compiling national accounts is based on "*sound techniques and procedures*", and that "*regarding GDP growth rates, the mission's opinion is that the methods and procedures applied by the Minstat are in accordance with international standards and the GDP data are consistent with the source data*". At the same time, the report points to a possible upward bias in recorded growth rates, in the order of 1 percentage point, because of methodological shortcomings.

The staff concludes that high growth and falling inflation reflect rising labor productivity, increased capacity utilization and favorable terms of trade. The authorities would like to stress that the country's favorable growth record is primarily the result of policies directed at high savings and investments to upscale the country's industrial potential and to make the economy more energy efficient. In this respect, Belarus compares favorably with Russia and Ukraine.

GDP growth is mainly export driven. Exports in U.S. dollar terms doubled in the last four years. Belarus is now the most open economy among CIS countries. Exports to non-CIS countries, mainly EU countries, have been growing fast and have now reached 52 percent of total exports. While exports of fertilizers have dropped dramatically in the first quarter of 2006, exports of finalized goods, such as trucks, grew in the same period at the brisk pace of 66 percent.

Monetary and Exchange Policies

The decline in inflation, which is now among the lowest in the CIS countries, has greatly enhanced Belarus' external competitiveness. The central bank agrees with the staff that low inflation, rather than the exchange rate, should be its principal policy objective. The 2007 monetary guidelines are consistent with this priority. However, the authorities continue to believe that the crawling band exchange rate regime during the past years was instrumental in reducing inflation, increasing external reserves and reducing the level of dollarization.

Low inflation, exchange rate stability, and robust growth, all have enhanced confidence and demand for money. In parallel, bank assets have continued to grow at a brisk pace.

The Fund's technical assistance was instrumental in improving bank regulation and supervision. Financial soundness indicators for the banking system improved substantially. The ratio of non-performing loans fell from 14.4 percent at the end of 2001 to 1.5 percent in May of this year. At the same time, the authorities are aware that the country's banking system is still underdeveloped and must be further improved.

Fiscal Policy

Belarus continues to pursue a disciplined fiscal policy. Last year it showed a budget deficit of 0.7 percent of GDP. Buoyant revenue collection contributed to a budget surplus of 3.1 percent of GDP during the 5 first months of this year.

Transparency in the budget process has improved. In 2004, the extra budget pension fund was integrated in the overall budget. Last year the innovation fund was also integrated in the budget. Both operations increased the overall budget by 12.6 percent of GDP. As recommended by the Fund, the government now considers its annual budgets within a medium-term framework.

Belarus has borne a financial burden in relation to the Chernobyl catastrophe, and will do so in the foreseeable future. On top of all the human suffering come the total financial costs, which according to international experts, exceed 10 times the country's GDP.

Structural Policies

Since the last Article IV consultation, the authorities have continued to improve institutions and the business environment. An IFC study of the business environment in Belarus, published in June 2006, highlights several improvements. The average number of inspections of SMEs has dropped from 10 in 2004 to 7 in 2006. The average time required to issue a license has also dropped from 45 days to 27 days.

Technical assistance provided by the IFC was helpful in preparing regulations on business registration. The regulation, issued last April, provides for a one stop procedure and reduces both expenses and time needed to complete the procedure. To give an example, the number of documents required for registration will be reduced from 13 to 4. The IFC estimates that the overall cost of a registration will be reduced by 21 percent. The decree also provides that all formalities will not take more than 30 days. Moreover, it eliminates all penalties for not complying with the time limits for submitting documents.

In order to improve the access of SMEs to information, an Internet portal "*Belarus SME Toolkit*" (www.bel.biz.url) was launched in May 2006. The website covers a multitude of business related issues: legislation, support services, etc. The portal is updated daily and contains all the administrative information which an entrepreneur might require for running the business.

In the most recent five year plan, the government envisages to cut taxes and subsidies, to facilitate the functioning of SMEs, to strengthen the financial system and to attract foreign capital. Belarus has already nine banks that are now fully owned by foreigners. The so called "Golden Share" no longer applies to banks. This should encourage the entry of strategic foreign investors. Today the golden share rule applies in only 14 enterprises for a limited period of 1 to 5 years. This year, the government's golden share will lapse in eight enterprises, thereby only leaving six enterprises with the golden share.

The authorities made a strong effort to reduce the level of cross subsidization. Utility cost recovery ratios increased from 21.7 percent in 2001 to 50.7 percent in 2006. The recent World Bank Report "*Belarus: Addressing Challenges Facing the Energy Sector*", concludes that cost-recovery tariffs allowed enterprises to finance their investment programs, fully pay current bills, and significantly reduce the stock of debt related to energy imports from Russia. In April 2006, less than 20 percent of enterprises were loss making, compared to the 26.2 percent one year earlier.

Wage increases are no longer mandatory for the economy as a whole. Every enterprise now has its own wage policy, according to financial affordability.

Relations between Belarus and the Fund

In Belarus gradualism proved conducive to economic stability and maintaining high social standards. The country has the lowest level of poverty among the CIS countries.

The authorities recognize the difference of views with the staff, and would have preferred these differences to be resolved by a more intense dialogue. The authorities believe that both, an IMF resident representative in Belarus and a greater continuity in the IMF staff team working on Belarus, would be beneficial in this regard. They would like to benefit from the high quality of technical assistance and would prefer full-fledged consultations rather than streamlined staff visits.

In conclusion, we would like to convey the intention of the Belarusian authorities to continue with disciplined monetary and fiscal policies and to improve the business climate so as to sustain economic growth. The authorities are confident that the Board will recognize the positive macroeconomic developments and encourage management to provide capacity building assistance to help the country strengthen its policies, reforms and economic performance.