Eurasian Development Bank

Resources Manager of Eurasian Fund for Stabilisation and Development

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Progress Report on Compliance with Conditions for the Sixth Tranche of the Reform Programme of the Government and National Bank of the Republic of Belarus Supported by the EFSD Financial Credit
(prepared based on the Report of the Ministry of Finance of the Republic of Belarus)

The implementation of the Reform Programme of the Government and the National Bank of the Republic of Belarus (hereinafter referred to as the Programme), in the part of the conditions set for the disbursement of the sixth tranche of the EFSD financial credit to the Republic of Belarus, focuses on:

a) reducing the inflation and progressively building up the gross international reserves (GIR) through consistent tight monetary and fiscal policies in the context of the flexible exchange rate regime;

b) reforming the markets of goods and services through further liberalisation of pricing and aligning the state price regulation with the standards of the Eurasian Economic Union; and

c) implementing further structural reforms aimed at strengthening the performance of state-owned enterprises through the introduction of the corporate governance principles, reducing directed lending, as well as at improving the business environment to boost the private sector development.

The conditionality for the disbursement of the sixth tranche includes 25 indicators, of which 15 are control targets. As at the control date for evaluation of compliance with the conditionality for the tranche (1 October 2017), 5 targets[1] were not met, including 3 control ones.

The following control targets were not met:

(1) **Clause 3.5 of the Matrix**: the system of social protection of workers undergoing professional retraining on decision of local governments has not been introduced. The implementation of this measure is aimed at stimulating the process of optimising the number of people employed at state-owned enterprises, while minimizing such negative impacts of this process as unemployment growth and deteriorating living standards of dismissed workers. The condition, in particular, stipulated that local governments would coordinate the process of shedding the excessive labour, the size of which is determined by enterprises based on the methodology of the Ministry of Labour and Social Protection (MoLSP), by arranging retraining courses for workers at risk of dismissal while paying them a scholarship not lower than the subsistence budget.

The Belarusian side believes that the social costs of implementing the reforms aimed at optimising the number of employees can be extremely high. In addition, the authorities believe that they have already implemented the necessary measures, and there

[1] Indicative target 3.1, which covers the transfer of 24 enterprises subordinated to central government bodies to municipal ownership, was met after the control date for evaluation of compliance with the conditionality for the tranche, in November-December 2017.

is no need for additional steps. At present, the financial support to the unemployed is provided not only through the unemployment benefit (which is about 15% of the subsistence budget), but also by offering them and their families financial assistance through the social safety nets; as well as by granting a possibility of temporary employment and participation in paid public works during the period of searching for a permanent job. Unemployed citizens are also entitled to the free career guidance offered by the state employment service and retraining with scholarships paid. With the adoption in October 2016 of Resolution of the MoLSP No. 63, employers are equipped with additional incentives to arrange retraining of their employees at risk of dismissal, since they get a compensation for the costs of retraining.

In view of these facts, the Manager recommends to grant a waiver from this target, being, however, of the opinion that more decisive efforts to optimise the number of people employed at state-owned enterprises and accelerated formation of a flexible and efficient labour market, which ensures reallocation of labour resources to promising sectors of the economy, remain the key factors of strengthening the efficiency and competitiveness of the Belarusian economy.

(2) **Clause 3.7 of the Matrix**: The Resolution of the Government to implement the provisions of the RB Law *On Regulatory Legal Acts* related to the regulatory impact assessment (RIA) of draft regulatory and legal acts affecting business operations has not been adopted. The failure to meet the target is explained by the fact that amendments to the Law *On Regulatory Legal Acts* providing for the establishment of the RIA mechanism have not yet been adopted by the Parliament. However, under a Decree of the RB President, the RIA is already performed to assess legal acts presented for the consideration of the RB President.

The Manager recommends to grant a waiver from this target if the following measures treated as prior actions for the disbursement of the sixth tranche are taken by the Belarusian side: (a) introducing the requirement to perform the regulatory impact assessment of draft regulatory legal acts to the Instruction approved by Resolution of the RB MoF and MoE No. 88/124, dated 30 June 2009, and (b) including again the condition requiring the adoption of the Government Resolution on the regulatory impact assessment of all draft regulatory legal acts affecting business operations into the conditionality for the seventh tranche as a control target.

(3) **Clause 4.2 of the Matrix:** the Manager is of the opinion that the amendments introduced to the Regulations on the Council for Entrepreneurship Development (CED) (the Regulations) by Decree of the RB President No. 730, dated 10 October 2017, which mainly deal with strengthening the role of the CED in law drafting, are insufficient to recognise it as the ombudsman for entrepreneurs' rights in the context of the generally accepted international practice. In accordance with such practice, the institution of the ombudsman for entrepreneurs' right (the business ombudsman) should be seen as a function provided for by the constitution or a legislative act. In addition, this institution should be headed by an independent senior public official, whose powers are sufficient to implement the key goals of the function – supervising the observance of rights and legitimate interests of businesses. The practice of operation of such institutions within the EAEU and in the broader region entails assigning to the business ombudsman a wide range

of powers, enabling it to take measures under the law to remedy violated rights and legitimate interests of businesses.

Under the existing Regulations, the CED is a standing *advisory* body under the RB President, discharging its functions on a voluntary basis and issuing decisions, which are *not binding*. The key objective of the CED is to "issue recommendations on the development and comprehensive support of non-state-owned economic entities to ensure the structural transformation of the economy, develop competitive relations, and coordinate the operation of public associations of businessmen". As to protecting the rights of entrepreneurs, the tasks of the CED are limited to developing recommendations on improving the legislation related to entrepreneurial activity, drafting proposals on protecting the rights and legitimate interests of entrepreneurs, and addressing requests of businesses. However, the Manager finds that the CED has not got enough powers to assist in remedying such rights.

The Manager recommends to grant a waiver from this target if the prior action under clause 3.7, which ensures the implementation of the practice of regulatory impact assessment of regulatory legal acts as a key mechanism to alleviate the pressure on business development, is met.

The following indicative targets are not met:

(4) **Clause 1.4 of the Matrix**: the ceiling for reserve money has been exceeded. As at 1 October 2017, the reserve money was BYN 5.8 billion against BYN 5.2 billion fixed as the ceiling and BYN 4.5 billion as at 1 January 2017. The key reason for failing to meet the target was the increase in reserve requirements for foreign exchange deposits of banks by 4 percentage points introduced from 1 July 2017 that resulted in the base money growth by BYN 0.7 billion. In addition, the easing of the NBRB's monetary policies, which was manifested in lowering the refinancing rate and interest rates for the NBRB's standing facilities, contributed to the base money growth. In contrast, the tight fiscal policies, in their turn, contributed to controlling the base money growth.

Since the increase in reserve requirements for foreign exchange deposits contributed to the containment of money demand and dedollarization of the economy, the Manager recommends to grant a waiver from this target.

(5) **Clause 1.5 of the Matrix**: the maximum broad money growth is exceeded. At the programme exchange rate, the money growth registered from the start of 2017 was 9% (against zero growth fixed in the conditionality and growth by 0.1% in 2016). The contribution of the BYN money supply growth was 5.4 percentage points, while that of the foreign exchange component was 3.6 percentage points. The money supply growth was supported by the growth of cash in circulation (the contribution of that factor is 1.5 percentage points), growth of local currency deposits (3.9 percentage points), and growth of the foreign currency component of money supply (3.6 percentage points). Net of the placement of the funds resulting from the repayment of the gas-related debt, the money supply growth has been 6.8% since the beginning of the year.

As the money growth in the RB occurred in the context of an economic recovery and a relevant increase in the money demand, the Manager recommends to grant a waiver from this target on condition that additional macro-prudential standards agreed with the EFSD are introduced by the NBRB to contain consumer lending growth.

The Manager recommends disbursing the sixth tranche of the EFSD financial credit of US $200 million to the Republic of Belarus based on granting a waiver from compliance with the targets, which are not met, and meeting the prior conditions for the disbursement of the sixth tranche, including the following: (a) introducing provisions on the regulatory impact assessment of draft regulatory legal acts to the Instruction on the Methodology of Preparing Business Cases to Support Draft Regulatory Legal Acts, approved by Resolution of the RB MoF and MoE No. 88/124, dated 30 June 2009, (b) including again the condition requiring the adoption of the Government Resolution on the regulatory impact assessment of all draft regulatory legal acts affecting business operations into the conditionality for the seventh tranche as a control target, and (c) the NBRB introducing macro-prudential standards agreed with the EFSD to contain excessive growth of consumer lending.

I. Current Macroeconomic Situation in the Republic Belarus

The factors contributing to the economic growth in 2017 included improved terms of trade and stronger external demand for Belarusian exports, combined with a recovery of household incomes and declining interest rates of commercial banks. The recovery of the Russian economy and depreciation of the real effective exchange rate of the Belarusian rubel paved the way for the growth of non-energy exports, which became the key driver of the economy in 2017. The second half of the year was characterised by a recovery in exports of energy goods and growth in domestic demand, whose impact on economic growth was partially offset by the accelerated growth of imports of consumer and investment goods. Exports of energy goods grew against the background of the resolution of the gas debt dispute with Russia, while the domestic demand was supported with administrative measures and monetary policy easing. Growing wages in the context of a recovery of household incomes boosted the consumer activity of households[2], while the acceleration of investments was combined with declining interest rates of commercial banks[3] and clearing of the balance sheets of commercial banks and enterprises by means of building up the domestic debt of local governments. The GDP growth amounted to 2.4% in 2017.

The broad general government surplus emerged in 2017 as a result of the consolidation of expenditures, *inter alia* through a conversion of part of direct expenditures of local governments into contingent government liabilities. The broad measure of the fiscal balance, based on the EFSD methodology,[4] showed a surplus of 2.1% against 0.5% of GDP in 2016 due to the reduction of recurrent expenditures (by 1.9 percentage points of GDP) and off-balance sheet ones (by 0.4 percentage points of GDP). Among other things, this was facilitated by reforms implemented under the EFSD financial credit programme. The increase in the cost recovery through utility and transportation tariffs for households observed in the last two years and the reduction in the size and rates of financing the directed lending contributed to lower budget subsidies. There was also a deceleration of growth of expenditure on public sector wages[5], as well as a drop in the size of guarantees executed by the government in relation to debts of state-owned enterprises. Following a three-year period of decline, capital spending showed growth (by 0.5 percentage points of GDP) reaching 4.2% of GDP. In view of the drop of revenues from export customs duties[6] and the property tax, the total budget revenues amounted to 30.1% of GDP against 30.2% of GDP a year earlier. At the same time, some expenditures of local governments related to restructuring the debts of municipal enterprises to commercial banks (in the amount of 1% of GDP)[7] were incurred through issuing securities and building up the debt of local governments[8]. Although local government debts do not make part of the government debt, the recent acceleration of growth of these debts boosts the risks of contingent liabilities of the Government transforming into its direct expenditures. The deficit of the Social Protection Fund (SPF) had a negative impact on the broad measure of the fiscal balance. The worsening of the position of the SPF budget is

[2] In December 2017, wages grew reaching US $494 (US $408 in December 2016), while the gap between real wages and labour productivity widened by 1.3 percentage points in January-November 2017.

[3] The real interest rate for new bank loans in local currency went down from 16.6% in May 2016 to 9.9% as at end-2016 and further to 9% in May 2017.

[4] The broad measure of the fiscal balance is defined as the sum of changes in central and local government deposits with the NBRB and commercial banks adjusted by the net government debt financing. The net government debt financing excludes operations related to government bond issuance to address the problem of bad debts of enterprises under government programmes.

[5] Under the Programme conditionality, the wage bill growth is to be limited to the inflation target. In January-September 2017, the average rate of growth of the wage bill was +5.4%. However, the measures taken to raise wages for certain categories of public sector workers in Q4 2017 resulted in a sharp acceleration of the wage bill growth to 20.1%.

[6] The decline in export customs duties was a result of: 1) lowering the export duty rate for potash fertilisers from EUR 55 per ton to EUR 20 per ton starting from April 2017; 2) the short delivery of oil in early 2017 due to the gas-related dispute and lowering the export duty rate for oil and oil products in the framework of the tax manoeuvre from 42% to 30%.

[7] In addition to the securities issued in 2016 in the equivalent of 1% of GDP.

[8] In 2016 and 9 months of 2017, the debt of local governments increased from 1.3% of GDP to 3.0% of GDP.

associated with fundamental problems, including the low retirement age and population aging. The sources of financing the current deficit of the SPF budget included loans from the republican budget.

The policies followed by the Government to refinance its debt adversely affect the country's medium-term debt sustainability. Against the background of economic growth and nominal appreciation of the exchange rate, the government debt amounted to 39.3% of GDP as at 1 January 2018 against 39.2% of GDP in 2016. The external government debt increased by US $ 3.1 billion due to the issuance of Eurobonds and mobilisation of Russian loans, including the one for the construction of the nuclear power plant, and tranches of the EFSD credit. The authorities explain the growth of foreign borrowing by their policies of debt refinancing in 2017 and the need to create a buffer to repay significant amounts of foreign liabilities in 2018.[9] However, the cost of new borrowing continues to exceed the medium-term rates of projected economic growth. As a result, the fundamental problem of debt sustainability persists in the current period, though the burden on the budget and the exchange rate will increase in the medium term. In addition, the approach of the government debt to the threshold of 45% of GDP and the increase in key interest rates in developed countries limit the opportunities for refinancing[10] without an increased risk of breaking the achieved macro stabilisation.

The key elements contributing to the replenishment of foreign currency reserves included the external government borrowings and the NBRB's interventions. During the period of 12 months, the GIR grew by US $ 2.388 billion reaching US $ 7.315 billion by end-2017[11], which corresponds to 2.4 months of imports. Despite the significant increase in reserves in absolute terms, they declined in months of imports due to the strong growth of imports during the year. The sources of growth of reserves included net inflows of funds to the MoF accounts (+US $1927 million) and interventions of the NBRB (+ US $846 million). External borrowings served as a key source of replenishing the MoF's accounts, and the NBRB's interventions were supported by foreign exchange sales by households. Despite the steady growth of remittances from Russia, amid a high level of dollarization of the economy[12], net sales of foreign exchange by enterprises and households have been declining since the second half of 2017 due to wage growth and a decrease in the interest rate differential in favour of dollar deposits[13]. As a result, the share of debt as a source of replenishment of the international reserves increased in 2017, and the contribution of interventions decreased.

The inflation came down to its record-lows due to the favourable external conditions and measures taken by the authorities under the EFSD Programme, however, the prospects for its further reduction are limited in the context of the increased pressure generated by monetary factors. In December 2017, the annual consumer price growth was 4.6%, which is unprecedentedly low for Belarus – in December 2016, the inflation was 10.6%, and during 2010–2015, it averaged at 28%. The record-low inflation was a result of the favourable external conditions (low inflation in Russia and globally), tight fiscal policy, and tight monetary policy followed until mid-2017.[14] However, the rapid reduction of the refinancing rate in 2017—from 18% to 11%—launched the credit expansion and growth of monetary aggregates. Combined with the renewed growth of wages and the planned increase in utility tariffs, it creates risks of inflation acceleration in the near future.

[9] In 2018, new borrowings are expected to be about US $3 billion, while the needs for repayment of principal amount and interests amount to US $3.55 billion, including the repayment in January 2018 of US $800 million of 7-year Eurobonds issued in 2011.

[10] In 2018-2020, government debt repayments will make US $3.5-3.6 billion.

[11] As at end-December 2016, the GIR were US $4.927 billion or 2.0 months of imports.

[12] About 70% of deposits in the banking system are denominated in US dollars.

[13] In 2017, net sales of foreign exchange by households made US $1.76 billion (US $1.89 billion in 2016). While in the first half of 2017, the average monthly net sales were US $189 million, in the second half of the year they amounted to US $104.2 million.

[14] The broad money growth at the programme exchange rate was 0.1% in 2016, accelerating to 13.7% in 2017.

The monetary policy easing, against the background of economic growth, launched the process of credit expansion, which creates risks of inflation acceleration. The reduction of the policy interest rate and growth of household incomes were accompanied by the growth of credit to the economy, primarily to households – by 25.8%. In 2017, the growth rate of the entire loan portfolio of banks was at 7.3% (about 10.8%, taking into account operations to clear the balance sheets of commercial banks at the expense of the local government budgets and the JSC "Assets Management Agency). The main areas of lending are loans to private individuals, retailers, and the manufacturing sector. Although the increase in reserve requirements for foreign exchange deposits from 11% to 17% constrained the growth of the money supply, the positive money overhang, which emerged at end-2017, created prerequisites for a higher inflationary pressure generated by monetary factors. Taking into account the fact that the inflation expectations of households were approximately two and a half times higher than the actual inflation rate[15], the resulting monetary pressure on inflation can be realised as early as in 2018.

The quality of the loan portfolio of banks remains low, despite the measures taken to transfer bad debts to the balance sheet of the general government. The main problem of banks is the large size of non-performing loans, which, combined with the still weak balance sheets of enterprises, limits the ability to lend to the economy and adversely affects the operating performance of banks. In 2016, the share of bad loans increased from 6.8% to 12.8% and remained at that level in 2017. The increase in the share of bad assets was caused by the discontinued practice of recurrent refinancing of bad debts against the background of directed lending reduction (by 1.1% of GDP in 2016 and by 2.2% of GDP in 2017). The increase in the share of bad loans was restrained partly owing to the clearing of banks' balance sheets. According to the estimates of the EFSD, the measures of bank rehabilitation related to the transfer of bad debts to the balance sheets of the general government contributed to the reduction of their share in the loan portfolio by 2 percentage points by end-2016 and by 1.1 percentage points in 2017. The high level of bad debts remains one of the main sources of risk for the banking system of the RB and requires close monitoring by the authorities.

The persistent significant role of the state in the economic creates an unstable foundation for the economic growth prospects in the medium term. In the second half of 2017, as the domestic demand recovered, *inter alia* due to administrative wage increases at a pace exceeding the pace of productivity growth, the demand of households and enterprises for imported consumer and investment goods contributed to the acceleration of imports. Against the background of the imbalance between wages and labour productivity already accumulated in past years, this unbalanced growth in domestic demand poses risks to macroeconomic stability. The growth of fixed investments also relies on the domestic and external government debt refinancing, which is not accompanied by significant structural reforms at state-owned enterprises. Despite its decline in recent years, the level of directed lending is still very high.[16] The situation is fundamentally aggravated by the presence of significant excess employment at state-owned enterprises—estimated by the EFSD at about 20%—and the policy pursued by the authorities of directed wage increases in the economy and maintaining the employment. If continued, such policies would call for a further increase in debt or additional rent-seeking, which also undermines the conditions for sustainable long-term economic growth.

In the context of the current economic growth and low inflation, it is important to maintain the macroeconomic stability through structural reforms, which will serve as fundamental prerequisites for further sustainable development of the country. The current progress in achieving the macroeconomic stabilisation in the context of a fairly stable external environment creates ideal conditions for continued structural reforms. Since further borrowing is limited by a number of factors, including the effective debt service interest rate in excess of the

[15] In November, the perceived inflation rate was 12.9%, the expected one was 11.9%, while the inflation outturn was 4.9%.

[16] As a result of cutting the net lending under government programmes registered in 2016-2017, its share in the loan portfolio of commercial banks dropped from 38.4% in 2015 to 37.7% in 2016 and to 30.4% in 2017.

real GDP growth rates and approaching the legislative threshold for the government debt, it is important to maintain tight monetary policies, including the adherence to an extremely prudent approach to further reduction of the refinancing rate and using prudential measures to ensure a more adequate assessment of credit risks. In addition, to maintain the continued economic growth and keep inflation rates low, it is necessary to narrow the gap between the real wages and labour productivity, which emerged in previous years. Progress in this area largely depends on the success of state-owned enterprise reforms, since the dominance of state-owned enterprises while maintaining the methods of their management unchanged, the lack of a dynamic labour market, and maintaining significant price controls are the fundamental factors, which significantly reduce the efficiency of resource use and limit the growth potential.

II. Status of Compliance with the Conditionality for the Sixth Tranche of the EFSD Financial Credit

The conditionality for the disbursement of the sixth tranche includes 25 indicators to be met as at the control date (1 October 2017). The review has shown that 5 targets were not met, including 3 control ones. The following control targets were not met: (a) the system of social protection of workers undergoing professional retraining on decision of local governments has not been introduced, (b) the institution of the ombudsman for entrepreneurs' rights based on the Council for Entrepreneurship Development has not been introduced, (c) the Resolution of the Government to implement the mechanism of regulatory impact assessment of draft regulatory and legal acts affecting business operations has not been adopted. As to indicative targets, the ceiling for reserve money growth and the maximum broad money growth were exceeded.

The detailed assessment of compliance with each indicator under the sixth tranche is provided below.

I. Macroeconomic stabilisation

These measures are aimed at reducing the inflation and supporting the gross international reserves through tight and balanced monetary and fiscal policies in the context of a flexible exchange rate regime.

Despite its reduction to the single-digit level in the period under consideration, the inflation in the RB is still higher than in its main trading partners. It reinforces the importance of following tight macroeconomic policies in the country. The continued high inflation expectations against the background of the persistent uncertainty, high real interest rates, and significant dollarization impede the efficient functioning of the economy. The significant accumulated gap between the real wages and labour productivity and the still high level of directed lending, which is generally characterised by low efficiency, generate additional inflationary pressures. The resulting faster growth of the marginal production costs is a fundamental factor contributing to the low competitiveness of Belarus' economy.

Clause 1.1. The level of the gross international reserves (GIR) is equal to at least US $5.3 billion (equivalent to 1.9 months of imports) – a control target.

Status: met.

According to the NBRB's analytical review, as at 1 October 2017, its GIR made US $7.3 billion or 2.6 months of imports (against US $5.2 billion or 2.0 months of imports as at 1 June 2017 (the evaluation date for the fifth tranche) and US $4.2 billion or 1.5 months of imports in early 2016).

The GIR build-up in terms of months of imports is needed to improve Belarus' resilience to external shocks in the context of its persistent CA deficit[17], declining capital inflow, and high burden associated with servicing the external debt.

The flexible foreign exchange policies (based on the continuous two-way auction method to determine the exchange rate), monetary targeting policies, and net sales of foreign exchange by households contributed to the GIR build-up in the analysed period.

Since the start of 2017, the GIR have grown by US $2.3 billion. The sources of such growth include external borrowings by the RB MoF (US $1.4 billion as a result of issuing Eurobonds and US $0.7 billion of the bilateral loan from the RF MoF), the NBRB's foreign exchange interventions (US $1.1 billion), mobilisation of tranches of the EFSD financial credit

[17] Last time, Belarus registered a CA surplus back in 2005.

(US $0.6 billion), and domestic borrowings by the MoF (US $0.4 billion). In addition, the GIR amount increased owing to the asset revaluation (gold price growth) by US $0.2 billion. At the same time, the factors constraining the GIR growth include foreign exchange expenditures of the Government, primarily related to its debt obligations (-US $2.9 billion), and reduction of the NBRB's debt to residents and non-residents (-US $0.5 billion).

The GIR threshold was greatly exceeded owing to the unplanned borrowings of the MoF in external markets, in particular the bilateral loan of the RF MoF and the higher than initially planned Eurobond issue. Based on these factors, the Manager has initiated an upward revision of the GIR control target for the 7th tranche.

Clause 1.3. The ceiling for net domestic assets (NDAs) (at the programme exchange rate) is no more than BYN 4.8 billion (including an adjustment to the threshold volume of SWAP repayments of no more than BYN 4.5 billion) – a control target.

Status: met.

According to the NBRB's analytical review, the NDAs were BYN 2.1 billion as at 1 October 2017 against BYN 4.6 billion as at 1 June 2017 and BYN 6.9 billion as at the beginning of 2016. The NDA ceiling was automatically adjusted downwards due to the adjustment of the NIR threshold by BYN 0.34 billion.

This target is aimed at maintaining tight and concerted fiscal and monetary policies to balance the domestic demand.

In early 2017, the NDA growth accelerated significantly compared to the previous year that was mainly caused by an increase in the NBRB's net foreign assets in a currency with restricted convertibility[18] by BYN 1 billion, as well as a decline in liquidity sterilisation by BYN 0.9 billion. However, due to the significant borrowings in foreign markets and the broad fiscal surplus, the RB MoF replenished its deposits with the NBRB, which brought down the net loan to the government by BYN 4.6 billion. In addition, the NBRB's lending to the economy was reduced by BYN 0.2 billion. Due to this, the NDAs were significantly below the ceiling. Since the growth of the MoF's deposits with the NBRB is primarily explained by additional borrowings in foreign markets, this target will also be revised in the framework of the 7th tranche.

Clause 1.4. The ceiling for reserve money (at the programme exchange rate) is no more than BYN 5.2 billion – an indicative target.

Status: not met.

According to the NBRB's analytical review, its reserve money was BYN 5.8 billion as at 1 October 2017 against BYN 4.5 billion as at 1 January 2017.

Controlling the reserve money level helps consolidate the benefits of the disinflation policies.

The key reason for failing to meet this target was an increase in reserve requirements for foreign exchange deposits mobilised by banks by 4 percentage points from 1 July 2017, which resulted in an increase of the based money by BYN 0.7 billion. In addition, the easing of the NBRB's monetary policies, which was manifested in lowering the refinancing rate and interest rates for the NBRB's standing facilities, contributed to the base money growth. In contrast, the tight fiscal policies, in their turn, contributed to controlling the base money growth.

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[18] Under the Technical Memorandum, this item is treated as part of the NBRB's NDAs.

Since the increase in reserve requirements for foreign exchange deposits contributed to a decrease in the money multiplier and dedollarization of the economy, the Manager recommends to grant a waiver from this target. The Manager also initiated the process of an upward revision of the ceiling for this target for the 7th tranche.

Clause 1.5. The maximum broad money growth at the programme exchange rate is 0% – an indicative target.

Status: not met.

At the programme exchange rate, the money growth from the start of 2017 was 9% against a decline by 2% over the same period of 2016, and the contribution of the BYN money supply growth was 5.4 percentage points, while that of the foreign exchange component was 3,6 percentage points.

The money supply growth was supported by the growth of local currency deposits (the contribution of that factor is 3.9 percentage points), growth of the foreign currency component of money supply (3.6 percentage points), and growth of cash in circulation (1.5 percentage points). The BYN money supply growth was generated through money emission as a result of the NBRB's interventions. The growth of the foreign exchange component was mainly a result of the decision of *Gazprom Transgaz Belarus* OJSC to deposit the funds, which were received from Belarus to cover the debt to Russia for gas supplies, with Belgazprombank (about US $400 million or 2.2 percentage points of the money supply growth), as well as that of commercial banks to issue foreign currency denominated securities (US $169 million or 0.9 percentage points of the money supply growth). The monetary policy loosening reflected in the reduction of the refinancing rate by 8 percentage points from the start of 2017 and by 6 percentage points in 2016 was another factor contributing to the money supply growth in excess of the set ceiling.

The Manager highlights that the money growth in the RB occurred in the context of an economic recovery— the GDP growth from the year start was 1.7%—and a relevant increase in the money demand. Therefore, the Manager recommends to grant a waiver from this target on condition that additional macro-prudential standards are introduced to contain consumer lending. The process of the threshold revision for the 7th tranche has also been initiated.

However, the Manager notes that the money supply growth outpaced the GDP growth rate and, if maintained, this trend would result in inflation acceleration. In view of the persistently high inflation expectations, the Manager recommends the NBRB to take a more conservative approach to expanding the money supply.

Clause 1.6. No multiple exchange rate practices – an indicative target.

Status – met.

There are no multiple exchange rate practices. In 2017, exchange rates did not deviate from the official one by more than 2%. Some small deviations of the over-the-counter and the cash market exchange rates from the official one were last registered only in the periods of sharp depreciation in 2015—in January, when the depreciation reached 30%, and in August, when the BYN exchange rate vis-à-vis the US $ depreciated by 15%.

This measure is aimed at creating a level playing field for all market actors and constitutes an important prerequisite for bringing down depreciation expectations and building up the GIR.

The implementation of this measure became possible thanks to lifting all administrative restrictions on foreign currency conversion. The Manager emphasises the importance of preventing multiple exchange rate practices in future.

Clause 1.7. The exchange trading mechanism in the mode of continuous two-way auction is maintained operational – an indicative target.
Status: met.

The two-way auction mechanism has been operational since 1 June 2015. Resolution of the NBRB Board No. 106, dated 1 March 2016, opened access to trading in the exchange currency market for economic agents operating through RB banks.

This measure aims at improving the operation of the domestic foreign currency market and its liberalisation, which promotes greater flexibility of the BYN exchange rate. Improvement of the foreign exchange policies also facilitates the elimination of foreign trade imbalances by generating adequate price signals in the foreign exchange, money, and commodity markets.
The implementation of the two-way auction mechanism has helped establish a platform for transition to a floating exchange rate regime and mitigated the risks of foreign exchange speculation, which facilitated net purchases of foreign exchange by the NBRB of US $1.5 billion in 2016 and US $1.1 billion for 9 months of 2017. Resolution of the NBRB Board No. 106 lifted the ban introduced in the first half of 2015 on foreign exchange purchases by economic agents in the Belarusian Currency and Stock Exchange and restriction of their participation in trading at the exchange exclusively to surrender of part of their foreign exchange proceeds. At present, the results of analysis show that economic agents continue trading in foreign exchange mainly in the over-the-counter market, and over 90% of the volume of their transactions in the exchange is associated with sales of their own foreign exchange proceeds. Currently, interested government bodies are working on improving the terms of access of non-bank legal entities to the exchange.

Clause 1.8. The operational system of bank liquidity management tools is consistent with the monetary targeting policy – an indicative target.
Status: met.

In January 2015, the NBRB adopted the monetary targeting regime as part of its monetary policy implementation, with money supply control, based on a fixed target for its growth, as its principal tool for achieving the inflation rate target.

This measure improves the effectiveness of the disinflation policies—as inflation remains a key economic challenge for the RB—and maintains the necessary level of liquidity in commercial banks.

Since 13 May 2015, a system of liquidity management tools consistent with the monetary targeting regime has been in place and running. The NBRB regulates the money market by modifying the volume of transactions of regulating the liquidity of the banking system. Both in the money market and the NBRB's auctions, the interest rates are determined on the basis of market factors, with due account of liquidity available to banks.

The implementation of this tool has had a positive effect on inflation deceleration over the EFSD Programme period. Since 2016, this tool has also been successfully used for sterilisation of the excess liquidity, resulting from foreign exchange purchases by the NBRB in the open market. Since mid-2017, liquidity withdrawals have decreased, which is associated with an increase in the National Bank's standard reserve requirement and a decrease in its rates for providing and withdrawing liquidity.

Clause 1.9. Decisions on changing the refinancing rate are made taking into account the need to meet the inflation target, the actual developments of interest rates for the NBRB's auction transactions[19], the interbank interest rates, the status of the current account of the balance

[19] The NBRB's operations of providing liquidity.

of payments, and with the aim of minimising exchange rate support interventions – a control target.

Status: met.

Since the start of 2017, the NBRB has revised the level of the refinancing rate downwards on eight occasions, thus, the refinancing rate was 11.5% as at the control date for evaluation of compliance with the conditionality for the tranche (11% from 18 October 2017) against 18% in early 2017. The decisions on bringing the refinancing rate down were made in the context of the foreign exchange supply significantly exceeding the foreign exchange demand in the domestic market. In view of their lower real incomes, households used their foreign exchange savings to support their consumption, which became the main sources of the foreign exchange supply. The NBRB was purchasing the foreign exchange, generating an inflow of liquidity to the economy, which led to lower interest rates in the NBRB auctions. In July-October 2017, the NBRB targeted the auction and the interbank interest rates at a level of 8.5%-9%.

Since early 2017, the rate of inflation has sharply dropped in the RB from 10.6% in December 2016 to 4.9% at end-September, while the annual target was no more than 9%. The reduction of inflation was ensured through the implementation of tight monetary policies in 2016, the high base of 2015, and the stable BYN exchange rate and low global inflation.

In January-September 2017, the CA deficit to GDP dropped to 0.9% from 3.0% in the same period of 2016 – respectively US $0.35 billion and US $1.0 billion in absolute terms. The trade balance deficit, net of energy and potash fertilisers, went down to 2.2% of GDP (US $0.87 billion), against 3.1% of GDP (US $1.1 billion) a year earlier. Thus, when making its decisions on interest rate reductions, the NBRB followed the Programme requirements.

This measure is aimed at containing the pressure of the money overhang on the inflation and exchange rate and reducing the volume of directed lending. Despite the significant progress in reducing their size achieved in 2016-2017, the high share of directed loans is a factor, which both generates pressure on the balance of payments and makes credit resources more expensive for other market players, while bringing down the effectiveness of the interest rate channel of monetary policies.

The Manager recommends the RB authorities to stick to a conservative approach when making decisions on further interest rate reductions. The rapid interest rate reduction in 2017 was one of the factors contributing to the failure to meet the money supply growth ceiling (clause 1.5). All other things equal, an unbalance growth of money supply weakens the monetary policy transmission to inflation reduction. The Manager has stressed in several discussions with the NBRB the low reliability of the factors, which contributed to the inflation deceleration in 2017 – the sales of foreign exchange by households are dropping as their incomes improve, the growth of consumer imports is accelerating that, in its turn, boosts the demand for foreign exchange. Targeting the interbank interest rate of 8.5%-9% results in a fast growth of lending that, in its turn, leads to import growth. All of the above factors strengthen the risk that the deceleration of inflation registered in 2017 would become unsustainable in the medium term.

Clause 1.10. Liquidity support provided to banks by the NBRB in its capacity of the lender-of-last-resort is based on interest rates not below the level of its refinancing rate – a control target.

Status: met.

According to the information posted on the NBRB's website, the interest rates for operations related to providing liquidity have been maintained above the refinancing rate throughout the EFSD Programme period. At the same time, on the back of the refinancing rate reduction, the spread between the refinancing rate and the interest rate for providing liquidity was narrowed from 5 percentage points in early 2017 to 1.5 percentage points as at the control date for the evaluation of compliance with the conditionality for the tranche.

This measure ensures proper performance by the NBRB of its function of the lender-of-last resort. As many interest rates for long-term loans and deposits are linked to the refinancing rate, maintaining the latter at a level higher than that of the liquidity provision rates may distort price signals in the banking sector. In particular, it may lead to excessive earnings of banks generated by long-term loans or pricing of long-term deposits at levels above the interest rate for liquidity management instruments, while the interest rates of the lender-of-last resort should remain the highest, because its capacity of lending to the economy is limited only by demand.

Implementation of this measure helped the NBRB effectively manage liquidity and avoid distorted price signals in the lending and deposit markets.

Clause 1.16. Unconditional implementation of the Government Debt Management Strategy for 2015-2020, including the annual mobilisation of non-project related loans to the government[20] of no more than 75% of the annual government debt repayment needs. In case of exceeding this level, the amount of borrowings in excess of the 75% threshold is allocated exclusively to replenish the gold and foreign currency reserves – a control target.

Status: met.

In January-September 2017, the ratio of government borrowings to repayments was 165.6%, including the ratio for external debt of 303.7% and that for domestic debt of 38.3%.

The amount of borrowings in excess of the 75% threshold was allocated to replenish budget deposits. For 9 months of 2017, in the context of the broad measure of the consolidated budget surplus, the deposits grew by BYN 4,698.7 million (equivalent to US $2,456.6 million).

This condition is aimed at reducing the level of government debt and improving the external investment position of the RB.

The mobilisation of significant external borrowings since the start of 2017 is explained *inter alia* by the need to create a buffer to meet the obligations coming due in 2018. In particular, US $800 million of 7-year Eurobonds issued in 2011 is coming due in January 2018. In general, the government debt repayments will total US $3.7 billion (6.4% of GDP) in 2018. In the medium-term perspective (2019-2021), the repayments will make US $3.4-3.5 billion annually.

Clause 1.17. Maintaining the government debt to GDP ratio of no more than 45% – a control target.

Status: met.

In view of the new borrowings significantly in excess of repayments, the government debt is growing. From the year start, its ratio to GDP increased by 0.8 percentage points reaching 40.0% of GDP.

This measure is aimed at strengthening the debt sustainability and the external investment position of the RB.

Since the start of 2017, the external government debt has grown by 2.5 percentage points reaching 30.9% of GDP, while the domestic government debt has moved in the opposite direction dropping by 1.7 percentage points to 9.1% of GDP.

[20] In the framework of this document, non-project related loans are defined as loans not related to the implementation of investment projects with a significant import component.

II. Goods and services market reform and reduction of government support

The implementation of this set of reforms is aimed at setting up market-oriented pricing mechanisms, efficient use and allocation of commodity, financial, and human resources and improvement of competitiveness of the Belarusian economy. The specific measures to perform this task include price liberalisation, raising housing and utility, and public transportation tariffs for households to reach the full cost recovery in the medium term, as well as reduction of the share of lending under government programmes in the banking system, since it is a fundamental factor of structural imbalances distorting pricing in the money, foreign exchange, and commodity markets.

Clause 2.1. An independent anti-monopoly authority on the basis of the Ministry of Trade is established and functioning – an indicative target.
Status: met.

The Ministry of Anti-Monopoly Regulation and Trade was established under Decree of the President of the Republic of Belarus No. 188, dated 3 June 2016, *On the Anti-Monopoly Regulation and Trade Authority* and started functioning on 8 September 2016.

The implementation of this measure is aimed at establishing an independent anti-monopoly authority, whose main objectives are the promotion of market relations on the basis of competition and entrepreneurship development, prevention and restriction of monopolistic activities and unfair competition, *inter alia* through price controls exercised on monopolies and state supervision over compliance with the anti-monopoly legislation.

In September 2017, the structure of the Ministry was improved in order to combine anti-monopoly regulation and price control within dedicated directorates. This change facilitated building a unified system for competition assessment and control within a particular industry and improving the communication both with industry representatives and within the Ministry.

Clause 2.2 Liberalisation of prices for goods and services: adoption of regulatory legal acts on setting prices and tariffs by the RB Government and other government institutions is to be limited to the lists of goods and services fixed by Decree of the RB President No. 72, dated 25 February 2011, and Resolution of the RB Council of Ministers No. 35, dated 17 January 2014, as well as other regulatory legal acts consistent with the RB obligations within the framework of the EAEU – a control target.
Status: met.

The regulatory and legal acts adopted by government bodies on issues related to pricing and tariffs during the period since the start of 2017 were limited to the provisions of Decree of the President of the Republic of Belarus No. 72 and Resolution of the Council of Ministers of the Republic of Belarus No. 35, and did not contradict the RB obligations within the framework of the EAEU.

The implementation of this measure is aimed at reducing of administrative price controls and at setting prices on the basis on market signals. Price control practices affect the financial condition of enterprises producing regulated goods and distort price signals for economic agents.

Under Resolutions of the RB Council of Ministers No. 22, dated 12 January 2017, and No. 81, dated 27 January 2017, the socially important goods, which used to be permanently regulated by the MART, as well as fruits and vegetables, which used to be permanently regulated by oblast and Minsk city executive committees, were included in the lists of goods, priced for which can be regulated for no more than 90 days per year. Taking into account the liberalisation of prices for socially important goods performed earlier, the RB provisions on state price regulation are aligned with the provisions of Annex No. 19 to the Treaty on the Eurasian Economic Union[21]. The exception is the continued regulation of pricing for products of enterprises that hold a dominant position in the market (that is to be lifted in the framework of the seventh tranche), while the EAEU provisions limit price controls exclusively to the prices for goods of natural monopolies, as well as cases of state price regulation for goods as defined in clause 85 of Appendix No. 19 to the Treaty on the Eurasian Economic Union of 29.05.2014..

According to the Manager's estimates, as at the control date for evaluation of the compliance with the conditionality for the tranche, the liberalisation measures taken ensured a reduction of the share of administratively regulated prices to 20% of the CPI basket, of which 8,6 percentage points is the share of tariffs for the services not regulated by the EAEU Treaty, while a year earlier the share of regulated prices was 22%.

Clause 2.5. In the first half of 2017, there is a negative net increase of lending under government programmes and activities provided by commercial banks and the RB Development Bank using all sources of financing, while the ceiling for new lending under government programmes is at BYN 1.3 billion (at the programme exchange rate) – a control target.

Status: met.

According to the RB MoF, the net decline of the directed lending by commercial banks and the Development Bank was 3.4% of GDP during the period of 6 months of 2017, while new loans amounted to BYN 921 million.

This measure aims at stabilisation of the macroeconomic situation through reduction of inefficient investment and budget consolidation through cutting interest rate subsidies.

The massive and inefficient directed lending was one of the fundamental factors contributing to both internal and external imbalances of the RB in the past years. The accelerated phasing out of this instrument will have a positive effect on the quality of the loan portfolio of the banking system, the parameters of the government budget, and the rate of growth of the economy owing to the credit being allocated to implement more efficient projects.

The decline in the net lending under government programmes registered in 2016-2017 helped bring down their share in the loan portfolio of commercial banks from 37% in 2015 to 36.3% in 2016 and to 32% for 9 months of 2017, while reducing the government budget expenditures on subsidising the preferential interest rates by BYN 317 million.

Clause 2.6. The established data base on lending under government programmes is updated quarterly – a control target.

Status: met.

The RB MoF has created a data base on government programmes, which includes information on the indicators agreed earlier with the Manager – the amount of loans, dates of their disbursement and repayment, financial terms and conditions (the interest rate, share compensated by the budget, guarantees), volume disbursed and repaid in the reporting period, outstanding stock as at the start and end of the reporting period. All the data are available with a breakdown by

[21] At present, the measures of permanent government control cover only certain types of services, strong alcoholic beverages, medicines, fuel and products of enterprises that hold a dominant position in the market. In addition, the regulator is able to introduce price controls in relation to a certain list of socially important goods for a period of 90 days within a calendar year.

commercial banks and the Development Bank, regulatory acts approving the key parameters of government programmes and loan currency. The data base is maintained by the RB MoF based on the information received from commercial banks and the Development Bank. In the framework of evaluation for the sixth tranche, the Manager received data for 3 quarters of 2017, which show that net repayments under government programmes for 9 months of 2017 were 2.9% of GDP, while their share in the loan portfolio of commercial banks and the Development Bank dropped to 36.4% against 38.8% for the first half of the year and 41.8% as at the start of 2017.

This measure is aimed at strengthening the monitoring and improving the quality of decision-making on government programmes through consolidation of the fragmented information within a single data set.

III. Commercialisation / privatisation of state-owned enterprises and strengthening social safety nets

The measures contained in this section are aimed at optimising the role of the government in economic activities and strengthening the social protection of the population.

Clause 3.1 Independent directors are elected to the supervisory boards of 7 joint stock companies. A decision is adopted by the RB President on transferring at least 25 enterprises to municipal ownership. A decision is adopted by the RB President on the sale of shares of at least 5 joint stock companies through the stock exchange – an indicative target.
Status: met.

As at the control date for evaluation of the compliance with the conditionality for the tranche, 12 independent directors were elected to the supervisory boards of 11 joint stock companies, in respect of which central government bodies perform owner supervision.

In November-December 2017, the President signed a number of regulatory acts providing for the transfer of 24 enterprises subordinated to central government bodies to municipal ownership – Order of the President No. 176rp, dated 22 November 2017, and No. 206rp, dated 22 December 2017, and Decree of the President No. 454, dated 19 December 2017.

On 18 July 2017, the RB President adopted Order No. 116rp *On Sale of Shares*, which defines the end of the year as the deadline for the sale of packages of shares of 5 joint-stock companies in the trading system of the Belarusian Currency and Stock Exchange OJSC. It covers the following joint stock companies: *Minsk Promtransproekt* (480,477 shares or 17.4057% of the total number of shares of the OJSC); *Motex* (50,741 shares or 20.4980%); *SUM-96* (53,209 shares or 11.8333%); *CAUK* (11,723 shares or 8.1232%) and *EKTB* (1,331 shares or 10.0023%). The shares of *EKTB* OJSC were sold at the auction held on November 21. The initial stock price was determined by independent appraisers based on the market value in accordance with the methodology adopted under the EFSD Programme. The auction held on 28 December 2017 was declared invalid. However, the State Property Committee (SPC) finds it appropriate to continue auctioning the shares of the above companies in 2018 in view of the interest in purchasing the shares, therefore it plans to get Order No. 116rp amended to extend the deadline for the sale of shares until 30 June 2018.

The implementation of these measures is aimed at improving the quality of management of state-owned enterprises and their performance through the introduction of corporate governance principles and optimisation of the number of economic agents subordinated to central government bodies. The transfer to municipal ownership of those enterprises, whose operation is of no strategic importance, will help improve their management and align their operation with the needs of the region, *inter alia* through their privatisation on decision of local governments.

Clause 3.2 Building the capacity of the Government for managing state-owned enterprises. Developing a methodology to assess the fiscal risks generated by state-owned enterprises. Developing a training programme for members of supervisory boards of open joint stock companies and launching the training – a control target.

Status: met.

In early 2017, the RB MoF developed the Guidelines on Fiscal Risk Assessment; that methodology was used to prepare a report reflecting the scale of fiscal risks based on the reporting data for 2016 and the first half of 2017.

The State Educational Institution *Centre for Advanced Training of Top Managers and Specialists of the SPC System*, together with the SPC, developed and approved a programme for advanced training of representatives of the state and other members of companies' supervisory boards titled *Practical Issues of Managing a Company with a Share of the State in its Statutory Capital*. As at 1 October, 38 people completed training under that programme.

The implementation of the measure is aimed at improving the quality of management of state-owned enterprises through raising the awareness of government bodies of the scale and causes of fiscal risks generated by state-owned enterprises in order to make appropriate decisions to mitigate those risks, as well as improving the level of training of managers of state-owned enterprises.

The Fiscal Risk Assessment Framework (FRAF) of RB MoF covers 3,750 enterprises with any state-owned share, with about 50-60 indicators analysed for each. Several categories of ratios are calculated for each enterprise: (1) solvency, (2) debt burden, (3) overdue taxes and fees, (4) wage arrears, and (5) a consolidated ratio of fiscal risks. According to the RB MoF estimates, about 50% of fiscal risks are generated by agricultural enterprises, 50% – by industrial enterprises, of which half of the risks are generated by the industry of construction materials.

The fiscal risk assessment reports prepared by the Ministry of Finance for 2016 and for the first half of 2017 will allow the RB Government to more accurately assess the risks arising from the poor performance of state-owned enterprises and will complement the rationale for the ongoing reforms of the state-owned sector. The implementation of measures to develop a training programme for representatives of the state and other members of companies' supervisory boards and its launch will contribute to building the capacity of the Government for managing state-owned enterprises.

Both measures are aimed at improving the efficiency of state-owned enterprises, whose contribution to the GVA reaches 47.2%.

Clause 3.3. Liberalization of the operation of the public sector enterprises. Reducing the requirement for surrender of foreign exchange proceeds by exporters from 20 to 10 percent – a control target.

Status: met.

According to Resolution of the NBRB Board No. 368-1, dated 6 September 2017, the requirement for surrender of foreign exchange proceeds by exporters was reduced from 20 to 10 percent from 1 October 2017.

This measure is aimed at ensuring greater freedom of entrepreneurial activity and reducing the administrative costs for businesses.

The ability of an enterprise to independently manage its foreign exchange earnings implies its greater operational independence, higher rates of its profitability owing to incomes from the exchange rate revaluation, which ultimately improves the investment attractiveness of enterprises in the medium term. In the environment of the floating exchange rate regime, lower foreign exchange supply by enterprises would not lead to the depletion of the National Bank's reserves as it would be compensated by exchange rates adjustments. Thus, the Manager supports this measure, which promotes the liberalisation of the economy of the Republic of Belarus.

In accordance with the Programme conditionality, the requirement for surrender of foreign exchange proceeds is expected to be fully lifted in the second half of 2018.

Clause 3.5 Strengthening the social protection in the context of potential unemployment growth: Introducing a system of social protection of workers undergoing professional retraining on decision of local governments – a control target.

Status: not met.

The condition, in particular, stipulated that local governments would coordinate the process of shedding the excessive labour, the size of which is determined by enterprises based on the methodology of the Ministry of Labour and Social Protection (MoLSP), by arranging retraining courses for workers at risk of dismissal while paying them a scholarship not lower than the subsistence budget.

The implementation of this measure is aimed at stimulating the process of optimizing the number of people employed at state-owned enterprises through the creation of adequate social support for persons subject to dismissal.

Meanwhile, the Belarusian side insists on the adequacy of social protection measures for dismissed and retrained workers in the process of enterprise reorganisation. In accordance with the national legislation[22], unemployed citizens have the right to free consultation and information provided by the state employment services to help choose the occupation, find employment, learn about opportunities for training, retraining and advanced training. Scholarships are paid to citizens for the period of their training by the assignment of the state employment service. Unemployed citizens and members of their families, as well as persons undergoing retraining, may qualify for financial assistance following the prescribed procedure. Resolution of the MoLSP No. 63, issued in October 2016, aims at encouraging employers to organise retraining of their employees by offering a compensation for the incurred costs of retraining. The Resolution approves the instruction on the procedure and conditions for compensation of the costs of vocational training, retraining, and advanced training of certain categories of workers, including those at risk of dismissal and dismissed in the process of enterprise reorganisation, to be paid to employers by labour, employment, and social protection bodies. According to the Instruction, an enterprise (employer) shall get a full or partial compensation for organising retraining if this retraining was organised in full compliance with the requirements of the RB legislation on education, and also provided that the retrained employee was employed at this or another enterprise.

The Manager recommends to grant a waiver from this target, being, however, of the opinion that more decisive efforts to optimise the number of people employed at state-owned enterprises and accelerated formation of a flexible and efficient labour market, which ensures

[22] In particular, Article 7 of the Law "On Employment of the Population of the Republic of Belarus" and Resolution of the RB Council of Ministers No. 1334 "On approval of the Regulations on the organisation of vocational training, retraining, advanced training of the unemployed and other categories of citizens and their completing the training courses by the assignment of labour, employment, and social protection bodies"

reallocation of labour resources to profitable sectors of the economy, remain the key factor of strengthening the efficiency and competitiveness of the Belarusian economy.

Clause 3.7 The Resolution of the Government to implement the provisions of the RB Law *On Regulatory Legal Acts* related to the regulatory impact assessment (RIA) of draft regulatory and legal acts affecting business operations is adopted – a control target.

Status: not met.

As at the date for evaluation of the compliance with the conditionality for the tranche, the resolution was not adopted. The authorities explain the delay in meeting this target by the fact that the discussion of the draft RB Law *On Regulatory Legal Acts* providing for the establishment of the regulatory impact assessment mechanism has been shifted by the House of Representatives of the RB National Assembly to the spring session of 2018.

This measure is aimed at reducing the regulatory burden for businesses by introducing the regulatory impact assessment into the law drafting procedures.

It should be noted that the regulatory impact assessment has already been introduced by Decree of the President of the Republic of Belarus No. 40, dated 13 February 2017, *On Optimisation of the Administration of the President of the Republic of Belarus* as part of procedures of the Administration of the President related to issues of social and economic development presented for the consideration of the RB President. In addition, the issues of assessing the regulatory impact of regulatory legal acts on the business environment have already been incorporated into the programme of advanced training of civil servants at the Academy of Public Administration under the aegis of the RB President.

Due to the delay in the adoption of the Law on Regulatory Legal Acts by the Parliament, the Belarusian side plans to amend the Instruction on the Methodology of Preparing Business Cases to Support Draft Regulatory Legal Acts, approved by a Resolution of the RB MoF and MoE, to require the performance of assessment of the regulatory impact of draft regulatory legal acts on the business environment and the consequences of their adoption for various groups of the population.

The Manager recommends to treat the adoption of these addenda, agreed with the Manager, as a prior action for the tranche disbursement.

Clause 3.8 Promoting privatisation by introducing amendments to the legislation: Submitting to the Parliament the draft Law *On Privatisation, inter alia* providing for a shorter term of limitation for action in case of privatisation deals – an indicative target.

Status: met.

On 17 October 2017, draft amendments to the RB Law *On Privatization of State-Owned Assets and Transformation of State Unitary Enterprises into Open Joint-Stock Companies* were submitted to the House of Representatives of the National Assembly of the Republic of Belarus. The draft amendments provide for a shorter term of limitation for action in case of privatisation deals, which is reduced from 10 to 3 years.

This measure aims at promoting privatisation by strengthening the rights of investors since, according to the existing legislation, the results of privatisation deals closed 10 years ago could be revised in court.

IV. Business climate improvement / private sector development

Measures, provided herein, are aimed at the development of the legislative framework and establishment of institutions enabling the private sector development.

Clause 4.1 Adoption and implementation of the Directive of the President, agreed with business community representatives, on further measures to develop the entrepreneurial initiative and promote business activity in the RB – an indicative target.[23]

Status: met.

As at the date for evaluation of the compliance with the conditionality for the tranche, the RB Government implemented a few measures aimed at improving the business climate and ensuring the private sector development, including the following: (1) reduction of administrative barriers and regulatory burden; (2) simplification of the procedures related to private business entry and exit; and (3) introduction of the legislative framework for tax advisory.

The key aim of this measure under the Matrix is the development of the private sector as a factor of ensuring sustainable economic growth in Belarus.

In the reporting period, the RB President adopted a few decrees aimed at reducing the regulatory impact on businesses, establishing new service industries and improving the ease of doing business for established businesses:

- Decree of the RB President No. 376, dated 16 October 2017, *On Improving Control (Supervision) Activities* promotes a systemic approach to improving the control and supervision activities by shifting the focus of activities of control bodies to prevention; reducing the range of grounds for arranging unscheduled inspections; eliminating the right to issue instructions to hold inspections based on materials dealt with by the law enforcement bodies; establishing the administrative liability of control officers for grave violations in the process of holding inspections; as well as a package of other measures aimed at optimising the control bodies and their functions;
- Decree of the RB President No. 337, dated 19 September 2017, *On Regulation of Activities of Private Individuals* expands the list of activities, for which no registration as an individual entrepreneur is required.
- Decree of the RB President No. 338, dated 19 September 2017, *On Tax Advisory* introduces a new framework for tax advisory in the Republic of Belarus and ensuring the quality of tax advisory services;
- Decree of the RB President No. 345, dated 22 September 2017, *On Developing Trade, Public Catering, and Consumer Services*[24] provides for a possibility of establishing a special tax regime in the area of trade, public catering, and consumer services on certain territories, with the profit tax rate fixed at 6 percent for enterprises and a single tax of one base value unit fixed for individual entrepreneurs, as well as other simplified conditions introduced for these activities. In addition, there is a provision on exempting economic entities from the value added tax, the real estate tax, the land tax, and the rental for land plots owned by the state;

[23] In view of adoption of a range of legislative acts aimed at developing the entrepreneurial initiative, including Decree of the President No. 78 and the Government Programme *Small and Medium Businesses in the Republic of Belarus* for 2016-2020, which cover most of the strategic provisions of the new version of Directive No. 4, it is no longer reasonable to adopt this Directive. Thus, the progress in realising the Plan of Action to implement the current version of Directive No. 4 (Resolution of the RB Council of Ministers No. 251/6, dated 28 February 2011) and the Plan of Action to implement Decree of the President No. 78 (approved by RB First Deputy Prime Minister No. 11/100-59/49, dated 4 March 2016) is monitored under this measure.

[24] This Decree applies only to rural areas and small towns with the average population of up to 10 thousand people.

- Decree of the RB President No. 364, dated 9 October 2017, *On Private Individuals Engaged in Crafts* grants additional rights to craftsmen: the list of crafts is expanded, the right is granted to sell items of crafts through new channels – the Internet, postage etc.; and
- Decree of the RB President No. 365, dated 9 October 2017, *On Agro-Ecotourism Development* expands the prospects for establishing and developing agro-ecotourism facilities: barriers are lifted in the part of construction and land regulations, the list of services offered is expanded.

In January-October 2017, further efforts to reduce the regulatory burden on businesses resulted in repealing 19 and simplifying 9 administrative procedures.[25.]

In addition, on 23 November 2017, the RB President adopted the Ordinance *On Entrepreneurship Development*.

This ordinance establishes:

- a moratorium on raising tax rates and introducing new taxes, fees (duties) during the period through 2020;
- a list of economic activities, on starting which business entities submit notifications to local executive and administrative bodies;
- uniform fire safety requirements, sanitary and epidemiological requirements, requirements in the field of environmental protection, veterinary medicine, maintenance and operation of capital structures, etc.;
- the approval by the RB President of the Unified List of Administrative Procedures performed by state bodies and other organisations with respect to business entities;
- the cancellation of certain administrative procedures in the sphere of trade, consumer services, production of products, advertising, construction, transport activities;
- provisions aimed at attracting qualified foreign specialists; and
- simplification of procedures in the field of trade and public catering, advertising, transportation, holding exhibitions and fairs, in the field of manufacturing, property relations, conformity validation, etc.

In the reporting period, a draft RB Law *On Introducing Amendments and Addenda to the Code of Administrative Offenses of the Republic of Belarus and the Procedural-Executive Code of Administrative Offenses of the Republic of Belarus* was presented for consideration by the House of Representatives of the RB National Assembly. The draft Law provides for the liberalisation of the administrative legislation to eliminate its punitive nature. The implementation of these measures will significantly improve the business environment, reduce the costs and uncertainty of regulatory procedures for businesses, as well as facilitate the foreign economic activity.

Clause 4.2 Assigning the functions of the ombudsman for entrepreneurs' rights to the RB Council for Entrepreneurship Development and introducing relevant addenda to the Regulations on the Council – a control target.

Status: not met.

[25] As a result of the measures taken in 2016 to reduce the administrative barriers, 32 redundant administrative procedures were repealed; 12 procedures were digitalised, thus, the total number of e-procedures reached 107 – see the Progress Report of the Manager for the Fourth Tranche.

The amendments introduced to the Regulations on the CED (the Regulations) by Decree of the RB President No. 730, dated 10 October 2017, which mainly deal with strengthening the role of the CED in law drafting, are insufficient to recognise it as the ombudsman for entrepreneurs' rights in the context of the generally accepted international practice. In accordance with such practice, the institution of the ombudsman for entrepreneurs' right (the business ombudsman) should be seen as a function provided for by the constitution or a legislative act. This institution should be headed by an independent senior public official, whose powers are sufficient to implement the key goals of the function – supervising the observance of rights and legitimate interests of businesses. The practice of operation of such institutions within the EAEU and in the broader region entails assigning to the business ombudsman a wide range of powers, enabling it to take measures under the law to remedy violated rights and legitimate interests of businesses. Under the existing Regulations, the CED is a standing *advisory* body under the RB President, discharging its functions on a voluntary basis and issuing decisions, which are *not binding*.

The key objective of the CED is to "issue recommendations on the development and comprehensive support of non-state-owned economic entities to ensure the structural transformation of the economy, develop competitive relations, and coordinate the operation of public associations of businessmen". In principle, the tasks and powers granted to the CED are limited to the framework of its goal. As to protecting the rights of entrepreneurs, the tasks of the CED are limited to developing recommendations in improving the legislation related to entrepreneurial activity, drafting proposals on protecting the rights and legitimate interests of entrepreneurs, and addressing requests of businesses. If a business files a complaint about a violation of its rights, the CED has not got enough powers to assist in remedying such rights.

The practice of operation of such institutions within the EAEU and in the broader region entails assigning to the business ombudsman a wide range of powers, enabling it to take measures under the law to remedy violated rights and legitimate interests of businesses. These powers include the right to issue to the state bodies (officials), whose actions (inaction) violated the rights and legitimate interests of business entities, recommendations on measures to be taken to remedy the violated rights, *inter alia* calling the persons guilty of violating the rights and legitimate interests of business entities to responsibility; the right—in case of disagreement with the opinion of government bodies—to file petitions with the prosecution authorities in order to further remedy the violated rights of entrepreneurs; the right to request from government bodies (officials) information, documents and materials affecting the rights and obligations of business entities, with the exception of information constituting state, commercial, banking and other secrets protected by law; the right to sue on behalf of the business community.

The Manager recommends to grant a waiver from this target if the authorities implement the practice of the regulatory impact assessment of regulatory legal acts as a key mechanism to alleviate the pressure on business development.

Clause 4.3 Introduction of the international financial reporting standards and mandatory independent audit of such reporting. Consideration of the practicability of expanding the list of companies required to prepare their annual reports based on the IFRS – an indicative target.

Status: met.

Under Resolution of the RB Council of Ministers and the NBRB No. 657/20, dated 19 August 2016, 42 IFRS and 26 IFRS Commentaries became part of the national legislation from 1 January 2017.

Under the Law *On Accounting and Reporting*, starting from 1 January 2017, private individuals holding the position of the chief accountant of an insurance organisation or an open joint-stock company, which is the founder of unitary enterprises and/or the parent company of subsidiary economic entities, must have certificates of professional accountants issued by the RB MoF. In addition, starting from the same date, organisations and individual entrepreneurs providing services in accounting and preparing accounting reports and/or financial statements for insurance organisations or open joint-stock companies must make sure that such services are provided at least by one staff member with a professional certificate issued by the RB MoF.

By the control date for evaluation of compliance with the conditionality for the tranche, 89 specialists had received certificates of professional accountants.