Eurasian Development Bank
Resources Manager of Eurasian Fund for Stabilization and Development

APPRAISAL

of the request

of the Republic of Belarus

for a financial credit from the resources of the Eurasian Fund for Stabilization and Development to support the budget in the context of the COVID-19 pandemic

in the amount of US$ 500 million

September 2020

Republic of Belarus

Fiscal year: 1 January – 31 December

National currency exchange rate as at 18 September 2020

Currency	**BYN**
1 EUR	3.0586
1 US$	2.5781
100 RUB	3.4420

List of Acronyms and Abbreviations

Belstat	National Statistical Committee of the Republic of Belarus
EBRD	European Bank for Reconstruction and Development
EDB	Eurasian Development Bank
EFSD	Eurasian Fund for Stabilization and Development
EIB	European Investment Bank
EU	European Union
GDP	Gross domestic product
IBRD	International Bank for Reconstruction and Development
MoF	Ministry of Finance
NBRB	National Bank of the Republic of Belarus
NIB	Nordic Investment Bank
RB	Republic of Belarus
RF	Russian Federation
S&P	Standard & Poor’s Financial Services LLC
US	United States of America

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Appraisal of the EFSD Resources Manager of the Request of the Republic of Belarus for a financial credit from the EFSD resources to support the budget in the context of the COVID-19 pandemic

Table of Contents

1. TERMS OF FINANCIAL CREDIT RECOMMENDED BY THE RESOURCES MANAGER

1. Borrower	Republic of Belarus
2. Total amount and currency of credit	US$ 500,000,000 (five hundred million)
3. Credit provision procedure and conditionality	The financial credit is granted to the Borrower as a lump sum of US$ 500,000,000 (five hundred million) based on: - the Agreement on a Financial Credit from the EFSD Resources between the Resources Manager and the Republic of Belarus (hereinafter referred to as the Agreement) and - a Request for Disbursement formalised in accordance with the Agreement. To obtain the Financial Credit, the Borrower opens and maintains a dedicated account in the currency of the credit at the National Bank of the Republic of Belarus (hereinafter referred to as the Account). The Borrower ensures proper protection of the funds in the Account against any claims, confiscations, moratoriums, and misuse.
4. Programme supported with the Financial Credit	The Programme of Actions of the Government and the National Bank of the Republic of Belarus to address the impact of the COVID-19 pandemic on the economy, financial and social sectors, as presented in letters of the Minister Finance of the Republic of Belarus No. 11-27/138 dated 4 September 2020 and No. 11-27/148 dated 17 September 2020 addressed to the Chairman of the EFSD Council (hereinafter referred to as the Programme).
5. Eligible costs	Financing expenditures of the budget of the Republic of Belarus approved by the Law of the Republic of Belarus “On Republican Budget of the Republic of Belarus for 2020” by transferring the proceeds of the Financial Credit from the Account to the Treasury Single Account of the Ministry of Finance of the Republic of Belarus. The transfer of funds from the Account must be made before the end date of the credit availability period.
6. Financial terms and conditions:	
6.1. Front-end fee: rate, calculation, payment procedure	None

6.2. Interest: rate, calculation, payment procedure	Floating. It is defined as the average yield of Eurobonds of the Russian Federation in US$ for a period of 7 years, calculated based on the yield curve, the value of which is rounded to two decimal places using the arithmetic rounding rules. The interest rate determination date, for any Interest Period, means the Working Day occurring 2 Working Days before the first day of the respective Interest Period. Order of accrual: In accordance with clause (a), section 3.01 of the Standard Terms and Conditions. Payment dates: 30 April and 30 October of each year, starting from the first of the specified dates following the Date of Issuance of the Financial Credit and ending with the final payment date for the Principal Debt under the Financial Credit.
6.3. Margin: rate, order of accrual, payment procedure	None
6.4. Commitment fee: rate, order of accrual, payment procedure	None
6.5. Payment dates (interest, margin, commitment fee)	Payment dates: 30 April and 30 October of each year, starting from the first of the specified dates following the Date the Resources Manager transfers the Financial Credit to the Borrower and ending with the final payment date for the Principal Debt under the Financial Credit.
6.6. Term of credit, including grace period	Not more than 10 (ten) years from the Date of Entry into Force of the Agreement, including the period, during which the Principal Debt is not repaid (Grace Period) – no more than 5 (five) years from the Date of Entry into Force. The Date of Entry into Force is determined in accordance with clause 7.1 of the Agreement.
6.7. Principal repayment schedule	Equal payments of US$ 50,000,000 (fifty million) on 30 April and 30 October each year, starting from the first of the specified dates following the end of the Grace Period and ending with the closest of the specified dates before the end of the term of the Financial Credit. After the issuance of the Financial Credit, the Resources Manager notifies the Borrower of the established schedule of the Principal Debt repayment under the Financial Credit.
7. Main objectives	Budget support to finance activities to address the impact of the COVID-19 pandemic on the economy and the financial sector, and to prevent a deterioration of the living standards of the population.

8. Main risks and ways to mitigate them	Strengthening uncertainty, against the background of the post-election developments, may have an additional negative impact on the economic activity in the Republic of Belarus. In turn, it could result in further deterioration of the fiscal position and reduce the Government's capacity to service its public debt. At the same time, the potential RB sovereign credit rating downgrade could significantly limit its access to international markets and increase the risks of refinancing its external liabilities. In these circumstances, timely servicing of public debt may lead to a significant depletion of the gross international reserves in the short term, which would increase pressures on the national currency and would pose risks to the financial stability. In this regard, it is critical to implement consistent monetary and fiscal policies during the Programme period in order to prevent a sharp increase in the budget deficit, acceleration of inflation, and distortions in the exchange rate formation. In the medium term, in order to maintain the macroeconomic and financial stability and improve the solvency of the RB, it is necessary to implement structural and institutional reforms required to create conditions for the country to embark on a trajectory of sustainable economic growth.

2. APPRAISAL OF THE RESOURCES MANAGER

This Appraisal has been prepared based on a request of the Republic of Belarus (hereinafter referred to as the RB, the Borrower) for a financial credit from the EFSD resources (hereinafter referred to as the Credit) in the amount of US$ 500 million submitted to the Chairman of the Eurasian Fund for Stabilization and Development (hereinafter referred to as the EFSD) Council by letters No. 11-27/138 dated 4 September 2020 and No. 11-27/148 dated 17 September 2020 (hereinafter referred to as the Request). The main objective of the Credit is to support a Programme of Actions of the Government and the National Bank of the Republic of Belarus to address the impact of the spread of COVID-19 on the economy, financial and social sectors (hereinafter referred to as the Programme).

Having considered the Request, the Eurasian Development Bank, as the EFSD Resources Manager (hereinafter referred to as the Resources Manager), offers the following recommendations and Appraisal for consideration of the EFSD Council:

1. The Request is consistent with the mission of the EFSD, its funding objectives, lending policy and conditionality, as defined by the Treaty on the Establishment of the EFSD, the EFSD Statute, and the Procedure of Provision of Financial Credits from EFSD Resources.

2. The Request conforms to the requirements of the EFSD and is signed by the Minister of Finance of the Republic of Belarus, a member of the EFSD Council representing the Republic of Belarus. The degree of the Request preparation, in terms of the data required for assessment and availability of the supporting documentation and in view of the consultations held with the RB authorities, is satisfactory.

3. The Financial Credit is requested for the implementation of the Programme, which includes Decrees of the President of the Republic of Belarus No. 143 dated 24 April 2020 “On Supporting Economy”; No. 131 dated 16 April 2020 “On Monetary Incentives for Health Workers”; No. 169 dated 18 May 2020 “On Monetary Incentives for Employees of Organisations Providing Social Services”; Resolution of the Council of Ministers of the Republic of Belarus No. 252 dated 23 April 2020 “On Amending Resolution of the Council of Ministers of the Republic of Belarus No. 314 dated 24 April 2018”; Resolutions of the Board of the National Bank of the Republic of Belarus No. 81 dated 18 March 2020 “On Certain Issues of Banking Regulation in 2020”, No. 93 dated 25 March 2020 “On Amending Resolution of the Board of the National Bank of the Republic of Belarus No. 81 dated 18 March 2020”, and No 136 dated 22 April 2020 "On Amending Resolution of the Board of the National Bank of the Republic of Belarus No. 81 dated 18 March 2020". The Programme is consistent with the mission of the EFSD, as defined by the Treaty on the Establishment of the EFSD. The Programme aims to support the economy, the health system, and the population affected by the COVID-19 pandemic with the ultimate goal of bringing the economy back on a trajectory of sustainable growth.

4. The objectives of using the requested resources of the EFSD meet the requirements established by the Statutory Documents of the EFSD. The credit resources have been requested to finance the budget deficit, which is expected to expand as a result

of lower domestic budget revenues and the need to finance additional expenditures to address the impact of the pandemic (including actions under the Programme).

5. The amount of the requested credit of US$ 500 million is seen by the Resources Manager as justified. According to the EFSD Project Unit, the need for additional financing of the budget deficit for the Republic of Belarus as a result of the revenue shortfall and the involuntary increase in certain expenditure items is estimated at about US$ 600 million. As stated by the Belarusian authorities, part of this gap can be financed using local currency budget deposits of the Ministry of Finance of the Republic of Belarus.

6. The limit of access to the EFSD resources for the Republic of Belarus, which amounted to US$ 1,968 million as at 1 September 2020, is completely utilised. The provision of an EFSD financial credit in the amount of US$ 500 million in 2020 will require redistribution of this amount from the limit of the Russian Federation in favour of the Republic of Belarus through the adoption of a relevant decision by the Council.

7. The financial terms for the credit proposed for approval by the EFSD Council are prepared in accordance with the parameters of the Indicative Financial Conditions for the Provision of Financial Credits from EFSD Resources (Annex 1 to the Procedure of Provision of Financial Credits from EFSD Resources approved by Decision No. 24 dated 8 December 2015). The Resources Manager proposes to provide a financial credit for a period of not more than 10 years, of which the grace period is not more than 5 years, at a floating interest rate determined on a semi-annual basis as the average yield of Eurobonds of the Russian Federation in US$ for a period of 7 years, calculated based on the yield curve, the value of which is rounded to two decimal places using the arithmetic rounding rules.

8. The Republic of Belarus has fulfilled all its obligations provided for in the Treaty on the Establishment of the EFSD, the EFSD Statute, and Decisions of the EFSD Council. The obligations to make an initial contribution to the Fund in cash have been fully fulfilled. The RB Government has no unresolved debt to the EFSD Member States and to main international financial institutions, which is confirmed by the EFSD Member States and the RB Ministry of Finance. The analysis performed leads to the conclusion that the Borrower's debt sustainability is sufficient, and the provision of the Credit will ensure more favourable conditions for the public debt service in 2020 through the preservation of internal reserves.

3. JUSTIFICATION OF APPRAISAL OF THE RESOURCES MANAGER

3.1. Assessment of the macroeconomic situation and solvency of the Borrower

3.1.1. Pre-crisis economic situation in the Republic of Belarus

The growth of the Belarusian economy slowed down from 3.1% in 2018 to 1.2% in 2019 due to less favourable external conditions, including the decelerated growth in the Russian Federation, as well as issues in the oil refining sector against the background of substandard oil supplies. Lower external demand for non-energy goods, *inter alia* due to the BYN real exchange rate appreciation, as well as continued high demand for consumer imports resulted in a negative contribution of net exports to the GDP growth (-3.4 p.p.). Despite some slowdown, private consumption remained the key driver of growth amid high rates of growth of real incomes of the population and consumer lending (+2.5 p.p.). Investments also supported growth (+1.5 p.p.), *inter alia* through an increase in inventories, which reached 66.3% of the average monthly industrial output as at end-2019 against 60.9% as at end-2018.

The current account (CA) deficit amounted to 1.8% of GDP in 2019, while in 2018 the balance was almost zero (+0.04% of GDP). The main reason for the deterioration of the CA deficit was an expansion of the deficit of trade in non-energy goods to -0.7% of GDP against +1.5% in the previous year, against the background of lower external demand and persistent demand for consumer imports[1]. At the same time, the deficit of energy trade remained at the level of the previous year (-5.7% of GDP) as the value of both imports and exports of oil and petroleum products declined proportionally. An increase in the surplus of trade in services from 5.7% to 6.0% of GDP and a decrease in the outflow of investment incomes due to the deteriorating profitability of the economy, which resulted in a reduction of the primary income deficit (3.1% and 3.6% of GDP respectively), somewhat offset the worsening trade deficit.

The BYN real effective exchange rate appreciated by 2.1% in 2019, *inter alia* due to the fact that commercial banks and enterprises became net sellers of foreign exchange after a multi-year period of these sectors being net buyers. At the same time, households, which had been net sellers of foreign exchange for the last 4 years, significantly reduced their net sales in 2019 to US$ 597.7 million (-46.4% compared to 2018), which is partially associated with a decrease in the interest rate differential for national and foreign currency deposits. To prevent excessive BYN appreciation, the NBRB was buying foreign exchange, which helped replenish the gross international reserves by US$ 2.2 billion to reach US$ 9.4 billion (2.7 months imports of goods and services).

The domestic demand slowing down and the effect of the pro-inflation factors of previous years wearing off contributed to lower consumer inflation in 2019, which went down to 4.7% compared to 5.6% in December 2018 and the NBRB's target of 5%. In the

[1] With a total increase in the value of imports by 1.3%, the increase in imported non-food goods amounted to 12.3%.

context of the favourable inflation environment, the NBRB reduced the level of the refinancing rate twice—from 10% at the beginning of the year to 9% at end-November 2019. The reduction of the refinancing rate, significant volumes of foreign exchange purchases by the National Bank, as well as fiscal policy easing contributed to faster money supply growth (+11.4% against 8.1% a year earlier), which, however, remained within the monetary target of the authorities (9-12%). The base money growth rate, by contrast, slowed down to 9.4% from 20.2% a year earlier.

Lower exports of oil and petroleum products against the background of lower world prices and the continued tax manoeuvre in the Russian oil sector resulted in a decline of revenues of the general government budget[2] to 41.7% of GDP in 2019 compared to 42.4% of GDP a year earlier, including a decline in customs duties on oil and petroleum products by 0.9 p.p. The budget expenditures to GDP increased by 0.9 p.p. to 39.3% of GDP, solely due to an increase in financing pensions, the average size of which increased by 8.3% in real terms in 2019. Despite the negative revenue dynamics, the budget was still executed with a surplus, although the surplus declined markedly to 2.5% of GDP from 4.1% in 2018.

The rate of lending slowed down from 15.7% to 10.2% in 2019. However, taking into account the currency revaluation, the rate of growth increased from 10.9% to 11.5%, which was a result of high growth of consumer lending. Despite an increase in directed lending relative to the level planned at the beginning of the year—the amount of new loans amounted to BYN 1.1 billion against BYN 0.8 billion planned at the beginning of the year—the stock of directed loans declined further by about 0.9% of GDP due to the rates of repayment exceeding the rates of issuing new loans. The volume of assets exposed to credit risk decreased from 5% to 4.6%. The exchange rate stability and lower inflation expectations contributed to faster deposit growth. Overall, the deposit base growth accelerated from 7.4% to 12.9%, with BYN deposit growth going up from 14.7% to 26.5% and foreign exchange deposits rising by 8.4% in 2019 following a drop by 5.2% in 2018. Nevertheless, the dollarization of deposits decreased from 64.9% to 60.6% in 2019.

3.1.2 Assessment of the impact of the COVID-19 pandemic and the fall in oil prices on the social and economic situation and the budget of the Republic of Belarus in 2020

Despite the fact that the RB did not introduce quarantine measures domestically during the COVID-19 pandemic, the results of January-July 2020 show a decline in the economic activity against the background of the compressed external and domestic demand. During the reporting period, there was also a slight decrease in the supply of labour. According to Belstat data, the hidden unemployment increased significantly: the total non-worked time due to involuntary part-time employment increased to the level, equivalent to 9,000 people not working daily (3,600 people a year earlier)[3]. As a result,

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[2] The State budget and the budget of the Social Protection Fund.

[3] Data for the first half of the year.

according to some preliminary data, the real GDP fell in that period by 1.6%, against growth by 1.3% a year earlier. The industrial output decreased by 2.5%[4] in January-July against the background of a high level of inventories, which reached 86.5% of the average monthly output as at 1 August[5]. At the same time, the most significant contraction—23.2% in January-July—was recorded in the production of petroleum products, which *inter alia* is explained by the lack of agreements with the RF on oil supplies at the beginning of the year. The latter also resulted in lower cargo turnover (-7.3%) and wholesale trade (-7.7%). Despite the continued growth of salaries and wages during 7 months of the year (+8.2% in real terms[6]), the second quarter, the time of the peak of the pandemic, saw a decline in consumer activity—compared to the same period of last year, the retail trade contracted by 2.1%, paid services – by 19.3% (*inter alia* due to border closures and cessation of tourist activities). As a result, the retail trade growth rate was 2.9% for 7 months of the year, which is half the level of the previous year, and paid services dropped by 10%.[7] The positive value added growth rates observed in agriculture (+3.2%), construction (+6.1%), and IT and communications (+8.6%) prevented a deeper GDP contraction. The growth of the construction industry was partly explained by the expansionary policies followed by the authorities based on higher directed lending: the originally approved limit for this type of lending for 2020 was raised by 70%, and the volume of loans actually issued by the end of the first half of the year was 2.2 times higher than their volume in January-June 2019. On a net basis, the directed lending continued to decline.

The fiscal position deteriorated as a result of lower economic activity, weaker financial position of economic entities, and a drop in both world oil prices and volumes of exported petroleum products. The revenues of the consolidated budget for 7 months of the year dropped by 4.5 p.p. compared to the corresponding period of the previous year, down to 27.9% of GDP. The tax revenues decreased by 3 p.p. to 23.9% of GDP, of which revenues from the profit tax – by 1.2 p.p., and those from the customs duties – by 1.3 p.p. in terms of both export duties on petroleum products and import duties on the back of lower imports to the EAEU. As the flow of funds to the RB budget under the so-called “customs re-clearance” arrangement[8] discontinued, the non-tax revenues dropped by additional 1.1 p.p. of GDP. Budget expenditures increased by 2.8 p.p. to 29.7% of GDP mainly due to higher funding of capital expenditures, including a sharp increase in capital transfers, which included government recapitalisation of statutory funds of state-owned enterprises. Despite a 0.8 p.p. increase in the budget sector wage bill, the current expenditures are broadly unchanged at 23.7% of GDP due to a reduction in funding for other items. In terms of the functional classification, there was an increase in spending on

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[4] The deepest recession occurred during the peak of the pandemic in the second quarter: -3.5% against -0.2% in the first quarter.

[5] Manufacturing industry. As at 1 July 2020, the indicator was even higher at 91.8% of the average monthly output.

[6] In January-July 2019, it was +7.8%.

[7] In January-June.

[8] The subsidy for Belarus embedded in the fixed gas price arrangement with the Russian Federation in the form of a transfer to the Belarusian budget of the amount of duties paid on exports of 6 million tons of oil.

the general government activity (+2.9 p.p.) and health (+0.5 p.p.) as a result of increased financing of anti-epidemic measures, wages and salaries, and electoral activities. The consolidated budget deficit stood at 1.8% of GDP (against a surplus of 5.5% of GDP a year earlier). As the Social Protection Fund maintained a small budget surplus, the general government budget deficit was 1.7% of GDP.

For the first half of 2020, the current account (CA) deficit expanded to 3.9% of GDP from 2.7% a year earlier, with the main factor of its deterioration being a significant expansion of the primary income deficit (-7.4% and -5.3% of GDP) due to more intensive outflows of investment income than a year ago. The deficit of trade in goods decreased (-4.1% and -5.2% of GDP) amid a larger decline in physical import volumes (-12.3%) compared to exports (-9.5%) and virtually neutral terms of trade[9]. The CA deficit was partially financed by net direct investment inflows, mainly in the form of reinvested incomes—4.4% of GDP against 3.9% a year earlier—as well as by Government securities issues in international markets totalling about US$ 1.4 billion[10]. However, a significant decrease in financial account inflows as a whole—by 81% against the corresponding period of 2019—imposed a drain on the gross international reserves (GIR), which declined by US$ 600 million in the first half of the year.

The fact that households and business entities turned from net sellers to net buyers of foreign exchange in 2020 generated additional pressure on the foreign exchange market. In January-July, net purchases by households amounted to US$ 874.1 million and those by resident business entities – to US$ 746.1 million. The demand for foreign exchange significantly exceeded its supply that led to the BYN depreciation vis-à-vis the US$ by 26.2% from the beginning of the year, of which that in August was 10.3%. The depreciation of the national currency and the growing devaluation expectations accelerated the outflow of household deposits from the banking system, which amounted to about BYN 975 million for BYN deposits and card accounts and US$ 624.3 million in August 2020. At the same time, the prospects of full withdrawal of deposits are limited by the predominance of non-callable deposits – approximately ¾ of the entire deposit base.

These trends exert significant pressure on the gold and foreign currency reserves of the Republic of Belarus. As a result of the NBRB’s operations to support the BYN, the gross international reserves dropped by US$ 1.4 billion in August alone, down to US$ 7.5 billion (about 2.4 months of imports). To ease the speculative pressure on the foreign exchange market, the NBRB temporarily[11] suspended bank liquidity support through the overnight credit facility. At the same time, as a result of the NBRB's interventions aimed at BYN sterilisation, the RB banking system faced a liquidity deficit after a period of its structural surplus. In addition, the RB financial sector is characterised by a high level of

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[9] In terms of product categories, there were divergent trends observed for the terms of trade with a significant deterioration for energy goods and neutral terms of trade for non-energy goods in general.

[10] Including Eurobonds worth US$ 1.25 billion and government bonds in the Russian market in the amount equivalent to US$ 140 million.

[11] At the time of preparation of the document, the NBRB set the suspension period through 13 October 2020.

dollarization and is highly dependent on foreign exchange support mobilised from non-residents.

In the environment of high uncertainty about the onset of a second wave of the COVID-19 pandemic, as well as the absence at the moment of detailed information on the composition of economic growth for 8 months[12], the EFSD Project Unit forecasts a potential drop in the real GDP in 2020 by 2 to 3%. At the same time, it is assumed that the country's authorities will continue using expansionary measures, including support of state-owned enterprises through increased directed lending and replenishment of their statutory funds, as well as maintaining positive growth rates of real disposable incomes of households.

The main risk associated with such continued expansionary policies is acceleration of inflation, especially in the face of mounting depreciation and inflation expectations recorded in July-August 2020. The inflation increased to 5.6% for January-August from 5.2% a month earlier, which is above the 5% target set by the NBRB. In addition, such policies raise quasi-fiscal risks, especially given the unprecedented level of uncertainty in view of the pandemic and geopolitical tensions.

In addition, amid the worsening financial health of businesses, the expanding directed lending could lead to a deterioration in the financial performance of the banking sector. The number of loss-making organisations in January-July 2020 increased by 27.5% compared to the corresponding period of 2019, and their share in the total number of enterprises grew from 14.9 to 19%. Net profits of organisations amounted to BYN 3,016.1 million as at 1 August 2020, which is 63.9% less than in the same period of 2019; pre-tax profits dropped by more than half (-56.2%). One of the significant factors that affected the decline in profitability was the BYN depreciation, despite the fact that businesses were granted the right to attribute exchange rate differences to incomes and expenses of future periods.[13] Additional factors included the general deterioration of the economic environment and the slow progress of reforms in the area of state-owned enterprise governance.

According to some estimates of the EFSD Project Unit, the consolidated budget deficit is expected to expand to 3.7% of GDP as at end-2020 (about US$ 2 billion at the current exchange rate). Taking into account the budgeted external and domestic financing, the expected fiscal gap will be equivalent to US$ 600 million. In the absence of new borrowings, the accumulated budget deposits are seen by the RB MoF as the main source of financing for this gap.

As at 1 August 2020, the deposits of the central and local governments at the NBRB and commercial banks amounted to BYN 20.6 billion, of which foreign exchange deposits were US$ 5.1 billion and those in the national currency were equivalent to

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[12] According to some official estimates, the rate of the economic contraction slowed down to 1.3% in January-August compared to 1.6% in January-July.

[13] Decree of the President No. 159 dated May 12, 2020 “On Recalculating Value of Assets and Liabilities”. The right to carry exchange rate differences forward to future periods is not granted to banks, “Development Bank of the Republic of Belarus” OJSC, and non-bank credit and financial organisations.

US$ 3.3 billion (at the average exchange rate for August). In principle, these reserves are sufficient to finance the fiscal gap projected for end-2020. At the same time, considering that the country's authorities have to repay the public foreign exchange debt in the amount of about US$ 1.1 billion by the end of the year, this will significantly reduce the gold and foreign currency reserves and boost the risks for the financial stability, especially with the understanding that the government will have to pay US$ 2.8 billion of its foreign exchange obligations in 2021.

Despite the projected reduction of the trade deficit in 2020, the current account deficit will increase to 3.2% of GDP compared to 1.8% in 2019. In the first place, the CA deficit will be negatively affected by the primary and secondary income deficit expansion. Lower inflows under the financial account in the face of the significantly constrained access of the RB to international financial markets and weaker investment activity in the global economy will lead to the balance of payments deficit of US$ 1.4 billion (2.4% of GDP), the financing of which with gold and foreign currency reserves may negatively affect the sufficiency of the reserves to secure the financial stability.

Table 1. Republic of Belarus: Key macroeconomic indicators

	Actual			Forecast	
	2017	2018	2019	2020	2021
National accounts and prices (in %)					
Real GDP growth	2.5	3.1	1.2	-2.4	1.1
CPI (December, yoy)	4.7	5.6	4.6	6.1	5.0
Money and credit (in %)					
Broad money	17.4	8.5	1.5	5.4	6.1
Policy interest rate	14.1	10.0	9.3	7.5	7.4
Public finance (in % of GDP)					
Consolidated budget revenues	30.1	31.0	29.7	27.0	27.5
Consolidated budget expenditures	27.3	27.2	27.3	30.7	28.9
Budget balance	2.8	3.8	2.4	-3.7	-1.9
External sector (in % of GDP)					
Current account	-1.7	-0.4	-1.8	-3.2	-1.3
Net foreign direct investments	2.2	2.3	2.1	2.5	2.3
Gross reserves in months of imports of goods and services	2.1	2.0	3.2	1.9	2.1

Sources: Belstat, NBRB, RB MoF, Resources Manager's estimates

3.1.3 Assessment of debt sustainability and solvency

Despite the relatively low level of the public debt in relation to GDP at 41.5% of GDP at end-2019—including government guarantees and commitments of local budgets—the high foreign economic uncertainty and the downturn in the economy have significantly increased the risks to debt sustainability. External borrowings account for more than 80% of the public debt. Russia remains the key creditor of Belarus (about

US$ 8 billion, or 44% of external debt). China is the second most important source of debt (18%). About 12% of the external debt is attributable to the EFSD and 20% – to bonds issued on foreign financial markets. The remaining 6% of the external debt is provided by the IBRD, the EBRD, NIB, the EIB, and the US.

In view of the unstable macroeconomic situation and lack of financing, Belarus was active in issuing securities in the second quarter of 2020 in foreign financial markets. In May 2020, Belarus mobilised financing in the amount of RUB 10 billion. In June, two Eurobond issues were completed: Belarus-2026 in the amount of US$ 500 million at an interest rate of 5.875%; and Belarus-2031 worth US$ 750 million at an interest rate of 6.378% per annum. The Eurobond issues contributed to the growth of international reserve assets from their lowest level of US$ 7.8 billion as at end-February to US$ 8.9 billion by end-July. In the face of high domestic uncertainty, the yield of the Belarusian debt has increased significantly. The yield of securities denominated in RUB reached about 8-9% as at end-September and those in US$ – 7-8%.

In early September 2020, S&P changed the long-term outlook for the sovereign credit rating of Belarus from stable to negative. The political tensions and the national currency depreciation provoked outflows for bank deposits and their conversion into foreign currencies, which negatively affected the state of the banking sector. In the face of the higher demand for foreign exchange, there was a sharp decline in reserves – by US$ 1.4 billion to US$ 7.5 billion dollars in early September, which corresponded to 2.3 months of imports.

The current situation has significantly weakened the country's debt position. As a result, as at end-2020, the level of the public debt, including government guarantees and obligations of local budgets, may exceed 54% of GDP. The depreciation of the national currency made the most significant contribution to the growth of the debt burden (about 50%) due to a high share of debt denominated in foreign currency (more than 90% of all government liabilities). The next most important factors include the expanding budget deficit and the GDP contraction.

In 2021, on the back of the projected weak economic activity, the debt-to-GDP level will remain around 54%. Combined with the growing debt burden, it will generate additional pressure on Belarus' economy associated with mounting debt service costs. According to the current payment schedule, the peak of payments will occur in 2023, when Belarus will have to spend almost US$ 4 billion on debt amortisation and interest payments.

In addition to the upcoming significant payments, the debt situation of Belarus is further affected by growing quasi-fiscal obligations. The active interference of the state in the economy resulted in a high level of government guarantees, including those issued by local government and self-government bodies, which stood at 5.6% of GDP at end-2019. In addition, the direct local government debt is estimated at 2.2% of GDP. In the event of further crisis developments, these commitments may materialise and adversely affect the fiscal position and the debt sustainability.

If Belarus gets a loan from the Russian Federation in the amount of US$ 1.0 billion (US$ 0.5 billion in 2020 and US$ 0.5 billion in 2021), as well as a financial credit from the EFSD in the amount of US$ 500 million in 2020, it will help improve the country's capacity to pay. In the medium term, as a result of the lower debt service burden, taking into account its concessional nature, the funds provided will reduce the need to mobilise additional financing. As a result, the financing requirements to GDP are estimated by the EFSD to fall from almost 7% to 5% in 2021-2023. Most of the effect will be observed in 2021, however, the debt service burden will also partially decrease in 2023, when payments are expected to peak.

At the same time, “smoother” debt burden distribution, including the lower debt service pressure, will improve the access of the Republic of Belarus to international financial markets and reduce the risks of refinancing. According to S&P, the outlook for the credit rating may be revised from negative to stable, if, in addition to stabilising the economic and financial sectors, Belarus manages to refinance some of its debt to Russia. If the financial position of Belarus is stabilised in the short term, the level of the public debt is likely to go below 52% of GDP at end-2025.

Despite the expected slight improvement in the debt position and solvency of the RB over the medium term, risks to the public debt sustainability remain. In addition to a balanced budget, in order to improve the debt sustainability, policies should focus on reducing quasi-fiscal risks and improving the stability of the banking sector, *inter alia* reducing directed lending and capital transfers to state-owned enterprises.

3.2. Programme of Actions of the Government and the National Bank of the Republic of Belarus to address the impact of the spread of COVID-19 on the economy, financial and social sectors

Given the practice of the IMF and other donors providing emergency support to counter the impact of the COVID-19 pandemic, the key conditionality for providing budget support from the EFSD resources is a programme approved by the country's authorities to address the impact of the pandemic, aimed primarily at supporting the health sector, the key sectors of the economy, small and medium-sized businesses, and vulnerable segments of the population.

The Republic of Belarus has adopted and is implementing a package of priority stabilisation measures to ensure sustainable functioning of the economy and the social sphere in the environment of an adverse epidemiological situation. Decree of the President of the Republic of Belarus No. 143 dated 24 April 2020 “On Supporting Economy” provides for supporting the economy through provision to the sectors most affected by the impact of the pandemic, including individual entrepreneurs, temporary tax preferences of various forms (deferrals, instalments, tax credits), rent reduction and deferrals, incentives for pharmaceutical production and expanded access of the population to antiseptics, as well as other measures aimed at maintaining the financial stability of business entities. To improve the business activity, the NBRB relaxed a number of prudential requirements until 31 December 2020, including those to the regulatory capital of banks and its sufficiency to cover risks, the maximum size of risk per borrower, the liquidity, the classification of assets exposed to credit risk and provisioning for them.

The financing for the health sector has increased in the part of anti-epidemic measures, including strengthening of the physical capacity through the acquisition of personal protection gear, reagents and the establishment of contact centres. In accordance with the Presidential decrees, supplemental payments were introduced to health and social workers for work in areas with a high risk of infection. In the second and third quarters, BYN 283 million were used from the budget for this purpose.

Measures to support the population include the provision of concessions on housing and utilities payments to certain categories of citizens. In addition, the NBRB recommended commercial banks to consider the option of granting citizens loan repayment and interest payment deferrals and easing requirements when restructuring their debt under loan contracts.

In order to stabilise the macroeconomic situation, *inter alia* by reducing the risks to the budget and the balance of payments, the RB authorities intend to continue implementing prudent macroeconomic policies in the short and medium term. To reduce the budget deficit in 2020, the RB MoF is taking steps to consolidate the budget through the reduction of non-priority spending. In the medium term, there are plans to return to a balanced budget by improving the efficiency of budget spending and streamlining tax benefits. The Government intends to continue working on curtailing directed lending, which will improve the sustainability of the banking system and the ability to redistribute resources to finance commercial projects. In terms of the monetary policies, it is planned to return to the inflation target, continue the policies aimed at ensuring market exchange rate and interest rate formation in 2021. When taken as a comprehensive package, these measures should strengthen the debt sustainability of Belarus.

The objectives of the Programme, the measures and intentions to achieve them, and the status of their implementation as of the date of the Request submission are shown in Table 2.

Table 2. Matrix of measures and intentions of the Government and the National Bank of the Republic of Belarus to address the impact of the spread of COVID-19 on the economy, financial and social sectors

No.	Objective	Measure/Intent	Implementation status
1.	Addressing the impact of the COVID-19 pandemic on the economy and the population	1.1. Adopt and implement a package of priority stabilisation measures to ensure sustainable functioning of the economy and the social sector in the context of the COVID-19 pandemic.	**Implemented.** Decree of the President of the Republic of Belarus No. 143 dated 24 April 2020 "On Supporting Economy"; Resolution of the Council of Ministers of the Republic of Belarus No. 252 dated 23 April 2020 "On Amending Resolution of the Council of Ministers of the Republic of Belarus No. 314 dated 24 April 2018" (provision of concessions on housing and utilities payments to able-bodied citizens not employed in the economy)
		1.2 Provide subsidies to employers to make supplemental payments to employees in involuntary part-time employment to bring their salaries and wages up to the level of the minimum wage. Simplify the procedure and extend the period of STSA (state targeted social assistance) availability.	Decree of the President of the Republic of Belarus No. 178 of 28 May 2020 "On Temporary Measures of State Support for Employers and Certain Categories of Citizens"
		1.3 Provide a possibility to finance expenses related to the remuneration of employees and maintenance of property to be financed with funds from income-generating activities of budgetary organisations from the budget (in the absence of own revenues due to the adverse epidemic situation).	Decree of the President of the Republic of Belarus No. 179 dated 28 May 2020 "On Compensation"

2.	Supporting the health and social protection sectors during the pandemic	2.1. Establish monthly supplemental payments for health workers for employment in coronavirus conditions.	**Implemented.** Decree of the President of the Republic of Belarus No. 131 dated 16 April 2020 “On Monetary Incentives for Health Workers”;
		2.2. Establish monthly supplemental payments for employees of institutions providing social services for employment in coronavirus conditions.	Decree of the President of the Republic of Belarus No. 169 dated 18 May 2020 “On Monetary Incentives for Employees of Organisations Providing Social Services”. As at 1 September 2020, the allocations from the consolidated budget to implement a package of measures to ensure stable operation of the economy in view of the global epidemic situation amounted to BYN 288 million, of which BYN 283 million are to be used to make monthly supplemental payments to health and social service workers for employment in coronavirus conditions.
3.	Maintaining the macroeconomic and financial stability during the pandemic	3.1 Implement responsible and balanced fiscal policies, *inter alia* cut non-priority expenditures and expand the budget spending on health and social protection related to the pandemic. Intent to have a balanced state budget in the medium term through improved efficiency of spending, including the elimination of inefficient tax benefits and preferences	**Under implementation.** In order to balance the budget, a number of measures are being undertaken to streamline budget expenditures. According to some preliminary estimates, the spending on non-priority items will have been cut by the end of the year by about BYN 1.0 billion that makes 3.9% of the approved republican budget expenditures. In 2021-2023, an audit will be undertaken, and inefficient tax benefits will be abolished, which, combined with streamlining budget expenditures, will help execute a balanced budget. The directed lending will be reduced annually in 2021-2022 compared to 2020. All obligations to repay and service the public debt are fulfilled

		in a timely fashion and in full. No arrears are allowed
	3.2 Conduct balanced monetary policies aimed at curbing the inflation. The inflation is gradually brought back to the targeted range in 2021. A flexible exchange rate is maintained.	**Under implementation.** The monetary policies remain focused on ensuring the price stability. The targeted rate of annual inflation for 2020 is set at no more than 5%, and for 2021 it is planned to be set close to 5%. The intermediate monetary policy target is the average broad money supply, its annual growth (excluding the exchange rate revaluation) was 3.9% in August 2020. The exchange rate policy is based on the floating exchange rate regime. In order to avoid sharp fluctuations in the exchange rate, the National Bank may conduct foreign exchange interventions. The interest rate policies take into account the current and the projected inflation. Interest rates in the economy are maintained positive in real terms. In general, the monetary conditions are maintained at a level that contributes to keeping the inflation at the targeted level in the medium term.
	3.3 Ensure the sustainability of the banking sector through transparent prudential regulation of the banking sector, provide the banking system with liquidity using market instruments. Support banks in the process of restructuring debts of solvent customers who are stranded by the pandemic.	**Under implementation.** To boost the business activity, the National Bank of the Republic of Belarus temporarily (until 31 December 2020) relaxed a number of prudential requirements. In the event of a decrease in banks' liquidity, the National Bank stands ready to provide loans to banks for a period of three to six months at the refinancing rate. The National Bank also recommended banks to consider providing to citizens (if there are documents confirming deterioration of their financial position and their inability to

properly meet their obligations under loan contracts) deferrals of loan payment (repayment) and interest payments for the use thereof, while extending the term of loan payment (repayment).

When restructuring debts under loan contracts with legal entities and individuals, *inter alia* by granting deferrals (instalments), banks are advised not to raise the size of interest for the use of such loans.