

The Belarusian crisis is an opportunity for Russia

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On 4 June, the Russian-controlled Eurasian Economic Community (EurAsEC) decided to grant Belarus a US\$3 billion stabilisation loan from its Crisis Fund. The loan is to be made in several tranches over the next three years. As Belarus's sole possible creditor at this time, Moscow has presented its action as economic support for the crisis-ridden Belarusian economy. However, in return for the loan, it demands that Minsk not only carry out partial reforms to stabilise the macroeconomic situation, but above all that it should start privatisation. Under the present circumstances, the only real buyers of the vast majority of key enterprises in Belarus could be Russian investors. As a result of the collapse of dialogue with the West after the breakup of post-election opposition demonstrations on 19 December last year, President Alyaksandr Lukashenka has lost room for manoeuvre in the international arena, and at the moment – under pressure from increasing economic problems – he has accepted the terms of the Russian credit support. The purchase of Belarus's key industrial assets by Russian investors may be a breakthrough in Russia's long-time efforts to take control of the Belarusian economy. The consequence of this will be significant reduction in the sovereignty of Belarus and the power of Alyaksandr Lukashenka.

Belarus's economic problems

This February the Belarusian government applied to the Crisis Fund of the Eurasian Economic Community for a loan. Following months of negotiations, Belarus accepted the conditions put forward by Russia, which is the dominant member of this organisation. This means that a loan of US\$3 billion will be paid in six tranches spread out over the next three years; the first, of US\$800 million, will be paid out in the next few weeks. The payment of the next part will depend on the implementation of macroeconomic reforms and the fulfilment of a three-year privatisation plan, which is expected to generate US\$7.5 billion in revenue; this sum will be an additional fund for Belarus's financial needs, and a guarantee of solvency to the creditor.

Minsk has been forced to adopt the Russian support programme by the drastically deteriorating economic situation in the country. In May, the Belarusian rouble underwent the largest devaluation in the history of the independent state (of up to 56%). However, although the rouble was devalued so strongly, its real value on the black market still remains significantly lower, and so a new program to reduce fluctuations to 2% was adopted; this has made it impossible to determine the Belarusian currency's real exchange rate. At the same time the central bank, thanks to its modest foreign exchange reserves (on 1 June the level stood at US\$3.59 billion, a fall of US\$1.43 billion since the beginning of the year),

cannot intervene in the market. As a result, different exchange rates continue to operate, and exchange offices are lacking foreign currency. Transactions on the interbank market are also very limited.

Because there is so little foreign currency available, many companies have been forced to suspend or restrict their activities, thereby increasing unemployment significantly (the official statistics do not as yet reflect this problem). The largest losses have been borne by the importers, most of which are private companies. Only the main state exporters (machine and petrochemical plants, food producers) can rely on access to foreign currency, distributed by the individual ministries, which allows them to finance the imports of essential components and materials. This maintains the relatively good condition of those establishments; thanks to the fall in value of the Belarusian rouble they may increase their sales, including to the Russian market.

Rising inflation is a major problem. In the period from January to May this year it ran at about 20%, and according to official government estimates its level over the year may reach 39% (although this figure seems to be an underestimate). In response to drastic price increases in recent weeks, the Belarusian public has bought up a great deal of goods in bulk, which has caused temporary shortages in stores and raised social tension. So far, the Belarusian authorities have limited themselves to administrative regulations (such as price fixing) or *ad hoc* solutions such as allowing the possibility of making partial payments (such as for petrol) in foreign currencies. These activities are not enough to solve the crisis, though, and only a far-reaching reduction in budget expenditure and a restructuring of the country's inefficient command-and-distribution business model can lead Belarus out of the crisis.

The Belarusian crisis is an opportunity for Russia

The deepening economic crisis in Belarus has opened up an opportunity for Russia to increase its influence in the country significantly. Moscow realises that after the violent aftermath of the presidential election in Belarus, Minsk lost any opportunity to obtain financial aid from the West (the EIB, the EBRD, the IMF). It can only be helped by Russia, which, however, has set out specific conditions for doing so. Firstly, the Belarusian government is expected to carry out economic reforms (including the further devaluation of the rouble and reducing the budget deficit), resulting from Moscow's fears of the negative consequences of Belarus's possible economic collapse. Secondly, Moscow demands that Minsk start full privatisation, in the expectation that Russian companies will be the main beneficiary of this move. In this way, Russia is seeking to achieve one of its long-time key objectives regarding Belarus, namely buying up strategic companies in that country (see Appendix).

Russia's actions towards Belarus are deliberate tactics. Russia could make a unilateral loan to Belarus, but has in fact chosen to do so under the banner of the EurAsEC to create the impression that this is a collective decision, part of a rescue plan for a member state (as happens within the International Monetary Fund). Moreover, the current loan is in no way sufficient to rescue Belarus's financial system (according to calculations by independent Belarusian economists, approximately US\$10 billion would be needed to fully stabilise the situation by the end of 2011). Russia has thus sent a signal that Belarus can only obtain the

necessary funds to overcome its crisis by undertaking privatisation. In addition, on 31 May, the Russian foreign minister Sergei Lavrov suggested that Russia does not intend to coordinate its policy towards Belarus with the EU, and likewise would not join the EU's current sanction programme. The Kremlin has thus clearly stated that it intends to pursue its own policy towards Minsk.

Forecast

In the next few months, Moscow will take advantage of the difficult situation in Belarus in order to achieve its own interests. As of this moment, the sale has been announced of a 50% stake in the Belarusian firm Beltransgaz (which owns Belarus's gas pipelines) to Russia's Gazprom, which already owns half the shares. However, Minsk has made this transaction conditional on price discounts for supplies of Russian gas, which may postpone the signing of the contract. Later this year, Russia expects to sign an agreement to merge the Belarusian motor vehicle plant MAZ with the Russian KAMAZ. Furthermore, it is important for Russia to obtain guarantees from Minsk which will protect the rights of Russian investors in Belarus. In the longer term, the sale of further strategic companies may lead to Belarus *de facto* losing its economic sovereignty, thereby increasing the political control of Russia. In the case of Belarus, this factor is critical because its economy is largely based on a group of several large companies which provide most of the country's revenue, and are one of the main instruments of Lukashenka's rule.

If Lukashenka does not present a comprehensive reform program or relax his internal policy, he will continue to depend on expensive support from Russia. Although the Belarusian government did make a request to the IMF on 31 May for yet another stabilisation loan to the tune of US\$8 billion, for now this support seems unlikely. Regardless of where the credit comes from, the Belarusian government will no longer be able to avoid the market reforms which it set aside in the early 1990s. Continuing the current policy of *ad hoc* actions and administrative restrictions may lead to economic collapse and/or an outbreak of social discontent which would be dangerous for the authorities. On the other hand, the reforms and the privatisation will lead to the undermining of the system which has so far guaranteed Alyaksandr Lukashenka his power.

Appendix 1

Key Belarusian assets already belonging to Russian investors:

- Beltransgaz, 50% of the shares (to Gazprom)
- MTS-Belarus, 49% (to MTS Russia)
- The refinery in Mazyr, 42.5% (to Slavnieft)
- VTB Bank, 71.4% (to VTB Bank)
- Belgazprombank, 98% (to Gazprom)
- Belpromstroybank, 97.9% (to Sberbank)
- Belvnieshekonombank, 97.4% (to VEB Bank)
- Alfa Bank of Belarus, 88% (to Alfa Group)

LUKoil-Belarus, which controls the petrol station network, 100% (to LUKoil)
Yamal-Europe, Russia's main transit pipeline (to Gazprom)
A group of Belarusian defence contractors, which are concentrated within the Russian
Oboronitelnyye Sistemy consortium

Appendix 2

Belarusian assets which Russian companies are targeting:

Beltransgaz (the owner of Belarus's non-Yamal pipeline network), 50% of shares
The refinery in Novopolotsk, and the remaining stake in the Mozyr refinery
MAZ (truck factory)
BielAz (factory for large construction vehicles)
The Hrodna nitrite chemical plant
Beltopgaz (distributor of gas to Belarus)
The Belarus section of the Druzhba pipeline
Beltelekom (the largest telephone network operator)
The Belarusian Metallurgical Plant (BMZ)
The Belarusian Potash Company Belkaliy (potassium salt extraction and fertiliser
production)
Integral (manufacturer of electronic components)