

BELARUS – A SUCCESSFUL ALTERNATIVE PATH OF TRANSITION?

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*Abstract*¹

The Belarusian transition model significantly differs from those of the other countries of the region. Having implemented reforms which led to the formation of the market economy only partially, the Belarusian government nevertheless was able to substantially reduce social costs of the transition experienced by the population comparing to the other countries of the region. Recent impressive economic performance allowed officials within the country to speak about the alternative successful transition path. However, a closer look at the Belarusian economic development shows that the Belarusian economy is exposed to the multiple threats and the growth of the Belarusian economy could hardly be considered being sustainable. Hence, there are no grounds to think of the Belarusian transition model as representing an alternative successful path of transition.

Introduction

In the middle of the 90s the Belarusian government substantially slowed down the pace of the economic reforms in the country, and since then the Belarusian economy has been developing in a quite different way compared to the other transitional countries. Nevertheless, having recovered from the consequences of the Russian financial crisis of 1998, the Belarusian economy has been performing very well since 2000. This has allowed the official propaganda within the country to speak about the specific “Belarusian model” of economic development, which represents a successful alternative transition path.

In this essay it will be argued that despite the fact that the economic growth and the dynamics of the main macroeconomic indicators in Belarus in the recent years have been quite impressive, this should be rather explained as the result of the economic policies aimed at the current growth, disregarding the long-run sustainable economic development, with the help of the lucky coincidence of a number of endogenous factors. The Belarusian economy remains structurally rather weak and the existing growth is not sustainable;

¹ List of abbreviations:

GDP – Gross Domestic Product;
EBRD – European Bank for Reconstruction and Development;
CEE – Central and Eastern Europe;
FDI – Foreign Direct Investment;
fSU – former Soviet Union;
CIS – Commonwealth of the Independent States;
SOE – State-Owned Enterprise;
IMF – International Monetary Fund;
WTO – World Trade Organization;
VAT – Value Added Tax.

hence there are no grounds to consider the “Belarusian model” as a successful alternative model of the transition that “have preserved all the best from the socialist economy while adding all the best from the market one”².

The “Belarusian model” of economic development

At independence in 1991, Belarus inherited one of the highest standards of living in the former Soviet Union. Since then, the country has passed through several phases in its political and economic development. During 1991-1995, with the support of international organizations, Belarus initiated preliminary reforms towards a market economy. However, from the end of 1995 onwards, the government sought to insulate its population from the pain of reform by protecting jobs and wages. The state retained control of most productive resources, and a significant share of GDP was allocated to social expenditures and subsidies. This was accompanied by extensive administrative controls over prices, margins and the exchange rate. Market-oriented reforms were very limited. All these allowed the government to partially avoid severe economic and social shocks for the population: the unemployment level remained around 2-3% throughout the 90-s and there was no sharp increase in social inequality³.

The main difference of the contemporary “Belarusian model” from the mainstream transition path is the predominance of the state-owned enterprises⁴ and the strong state role in the economy. According to the data presented in the 2004 EBRD Transition Report⁵, on the minimum/maximum scale among all of the transition countries Belarus “proudly” occupies the “minimum” spot in the large-scale privatization, governance/enterprise restructuring and the price liberalization (See Figure 1 below).

The budget constraints of the state-owned enterprises are still soft enough and the amount of state subsidies is substantial. Another distinctive characteristic of the Belarusian economy is the absence of the large foreign debt – average level of 6% of the GDP in 1996-2004⁶, however accompanied by the low level of the foreign direct investment – in 1996-2004 its average level accounted only for \$23.4 per

² President of the Republic of Belarus, *Speeches* (Official site, 2005), <<http://president.gov.by/eng/president/speech/2004/poslan/>>.

³ Ministry of Statistics and Analysis of the Republic of Belarus, *Labor* (Official site, 2005), <<http://belstat.gov.by/homep/en/indicators/labor.htm>>.

⁴ The share of private sector in GDP is about 25% - the lowest among all transitional economies (EBRD 2004) In addition there exist excessive “golden share” provisions and they are exercised in relation to a number of privatized enterprises.

⁵ EBRD, *Transition Report*, (Official site, 2004), <<http://www.ebrd.com/pubs/econo/6086r.pdf>>.

⁶ Ministry of Statistics and Analysis of the Republic of Belarus, *Economic and financial data for the Republic of Belarus*, (Official site, 2005), <<http://www.belstat.gov.by/homep/en/specst/np.htm>>.

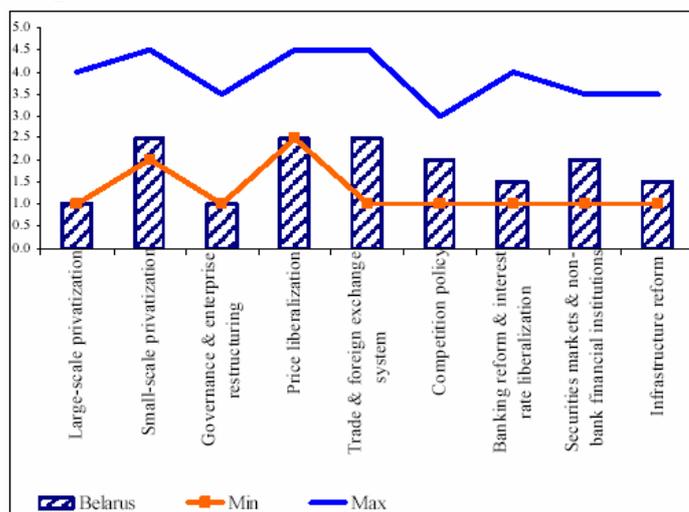
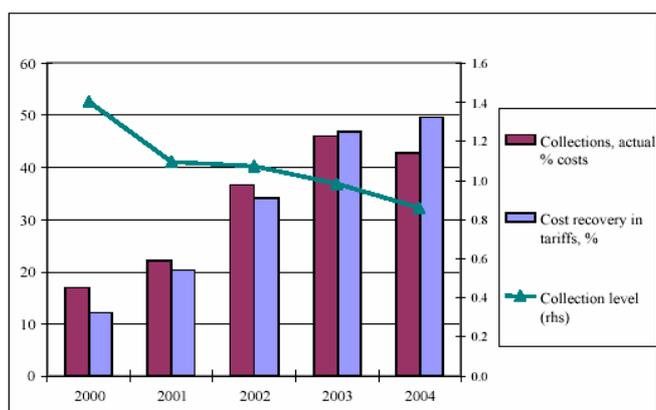


Figure 1. Belarus Transition Indicators, 2004⁷

capita annually (for instance, in CEE and the Baltic countries average FDI level varied between \$500-700 per capita)⁸.

There still exist significant protectionist measures, though their amount shrinks gradually since the government is concerned about joining the World Trade Organization in the near future. The government still maintains a somewhat populist social policy that includes the provision of the mainly free education and healthcare, highly subsidized utilities tariffs and the significant amount of the social transfers, though in the recent years it did recognize the necessity of, and have started, partial market oriented reforms in the social sector (for instance see Figure 2 below for information on the utilities tariffs).

Figure 2. Cost recovery in the utilities tariffs in Belarus⁹



⁷ Source: Ibid.

⁸ World Bank, *A country memorandum for the Republic of Belarus* (Official site, 2005), <http://siteresources.worldbank.org/INTBELARUS/Resources/328178-1120132035392/1365350-1120132328436/cem_by06_full.pdf>, 4.

⁹ Source: Ibid., 7.

Performance of the Belarusian economy in 2000-2005

The results of the recent economic performance in Belarus are quite optimistic. The Belarusian economy seemed to begin its recovery in 1996-1997, but the Russian financial crisis had a great negative impact on the economic performance of the country. What concerns the level of the GDP, following an estimated decline of about 40 percent during the period of 1992-1995, GDP growth resumed in 1996. Since then official statistics¹⁰ show a continuous and substantial growth in GDP as could be seen from the Table 1. The growth began at a time when almost all other fSU countries continued to experience decline, and even continued through the economic crisis of 1998-1999.

Table 1. GDP growth in Belarus (% to the previous year)¹¹

1996	97	98	99	2000	01	02	03	04	05
2.8	11.4	8.4	3.4	5.8	4.7	5.0	7.0	11.4	9.2

It is noteworthy that, as shown in the recent country memorandum by the World Bank¹² in contrast to some other CIS countries where growth and exports remained concentrated in the extracting sectors with limited employment opportunities, the growth structure in Belarus has been much more beneficial for labor. Growth in labor-intensive sectors, backed by government wage and income policies, helped to ensure that the benefits from the recent growth were fairly broadly shared by the population. The poverty rate declined substantially while inequality remained stable and moderate and even decreased after 2001¹³.

The Belarusian government, through the prudent monetary policy, was also able to bring the annual inflation rate from the 251.2% in the post-crisis 1999 down to the 8% in 2005. The reduction in inflation was due to the policy of positive real interest rates, as well as the unification of the exchange rate in 2000 and the related stabilization of the market for foreign exchange. In addition, in 2004 slowdown in inflation was supported by the cessation of the direct financing of the budget deficit by the National Bank of Belarus.

¹⁰ The expression "official statistics" is used here, because a number of analysts tend to consider the real economic results in Belarus to be somewhat lower than the official data show. More on this will be said later in the text.

¹¹ Source: Ministry of Statistics and Analysis of the Republic of Belarus, *Indicators*, (Official site, 2005), <http://belstat.gov.by/homep/en/indicators/svod_2000_2005.htm>.

¹² World Bank, *A country memorandum for the Republic of Belarus* (Official site, 2005), <http://siteresources.worldbank.org/INTBELARUS/Resources/328178-1120132035392/1365350-1120132328436/cem_by06_full.pdf>, 3.

¹³ Ibid., 2.

*Belarusian economy.*Table 2. Inflation rate in Belarus (% to the previous year)¹⁴

1999	2000	2001	2002	2003	2004	2005
251.2	107.5	46.1	34.8	25.4	14.4	8.0

The fiscal deficit in Belarus was rather small: it has been fluctuating between 0.5-1.5 percent in 2000-2003, it was 0.0% in 2004 and in 2005 the fiscal balance was positive¹⁵.

Belarusian exports grew during the whole period of 2000-2005 with a slowdown in 2001 and peak in 2004¹⁶. Even though the trade balance remained negative, the growth of the imports is explained by new governmental wage policy – the real wages grew rapidly in 2000-2004 and it created a kind of a consumption boom. In 2005 the trade balance finally became positive, and this trend seems to remain relatively stable in the near future.

Table 3. Export growth in Belarus (% to the previous year)¹⁷

2000	2001	2002	2003	2004	2005*
24.0	1.7	7.6	24.2	38.2	17.0

* January – October 2005;

Recent economic performance has allowed the Belarusian government (read: president) to speak about the successful model of the “social market economy”, which is in place in Belarus. As the main distinctive characteristics of such a model are named the preservation of the national property (SOEs), “independence” in terms of the absence of the severe foreign indebtedness, and quasi-socialist social policy that helped to keep unemployment rate very low, to avoid increase in the social inequality and allowed the population to feel relatively protected. As the main points of reference usually are named China in terms of the gradual economic reforms and the Scandinavian countries in terms of the social protection¹⁸

The proximity of the Russian Federation and the close ties, both political and economic, with this country seem to be the main “asset” of the Belarusian economy. The Russian economy stimulates the growth of the Belarusian one in numerous ways, but at the same time this situation creates a major threat for Belarusian economic development. Namely, the Belarusian economy greatly depends on Russia and the sustainable economic development of Belarus greatly depends on the economic growth in Russia and the political will of the Russian government to maintain the relations with Belarus as the preferential partner. The main means of this dependence are analyzed below.

First of all, the economic growth in Belarus is “fueled” by the low prices on the Russian fuel resources, namely natural gas and oil. For instance Belarus buys natural gas in Russia for only \$46 for 1 thousand cubic meters, whereas the market price, paid by the majority of the other countries, is around \$230¹⁹; the price for the Russian oil is also significantly below the market clearing price. The trouble here lies not only in the fact that Belarus imports 100% of the natural gas and around 90% of the oil from a single country. Apparently, Belarus is not the only country which is totally dependent on the imports of the Russian energy carriers – the Baltic States and several CEE countries are in the same position²⁰. The problem is that around 75% of the Belarusian fuel balance consists of the natural gas²¹. Given that Russia has set the price, which is close to the market clearing price, on natural gas in 2006 for all the CIS countries except for Belarus, and in a couple of years Russia would probably join the WTO, obviously one should expect that the prices on the energy carriers for Belarus would reach the world levels in the near future. This poses a major threat for the Belarusian economy: according to the data of the Belarusian Ministry of the Economy in case if the price for the natural gas would reach only \$90 for 1 thousand cubic meters, the profitability of the Belarusian industry would be zero percent.

Another side of the problem is that Belarus possesses large oil processing industry and for the time being low prices on the Russian crude oil have allowed the Belarusian companies to receive enormous revenues by selling the processed oil to the West (oil revenues account for around 20% of the Belarusian

¹⁴ Source: Ministry of Statistics and Analysis of the Republic of Belarus, *Indicators*, (Official site, 2005), <http://belstat.gov.by/homep/en/indicators/svod_2000_2005.htm>.

¹⁵ Ministry of Statistics and Analysis of the Republic of Belarus, *Economic and financial data for the Republic of Belarus*, (Official site, 2005), <<http://www.belstat.gov.by/homep/en/specst/np.htm>>.

¹⁶ The relative slow down of the export growth in 2005 is partially explained by the introduction of the “destination principle” of the collection of the commodity taxes in the bilateral trade with Russia – exports to Russia in January-October 2005 constituted only 90% compared to the same period of 2004 (Ministry of the Statistics 2005d). More on this later in the text.

¹⁷ Source: Ministry of Statistics and Analysis of the Republic of Belarus, *Statistical Information*, (Official site, 2005), <<http://belstat.gov.by/homep/en/indicators/main1.htm>>.

¹⁸ Obviously, such comparisons are somewhat populist and have little to do with the economic reality.

¹⁹ Tatjana Manenok, “Absoljutnaja energozavisimost'. Kak ot nee izbavitsya?” (“Full energy-dependence. How to get rid of it?”), *Belorusskij Rynok* (28 Nov. 2004 - 5 Dec. 2005) : <<http://belmarket.by/index.php?article=26178>>.

²⁰ Ibid.

²¹ Ibid.

export revenues²². Evidently, the price on the Russian energy carriers is a Damocles' sword for the Belarusian economy.

One more endogenous factor that has been conducive to the growth of the Belarusian economy is world oil prices. Unprecedented increase of the oil prices in the recent years did not have direct negative impact on the Belarusian economy, since the oil prices for it are set administratively by the Russian government and do not depend on the world prices fluctuations. However, this situation created a major money flow into the Russian economy; hence there was a consumption boom and this created more than favorable situation for the Belarusian exports. The exports to Russia were growing by average 30% in 2001-2004²³. But, there was a fear that with the further growth of the income in the Russian economy, the Russian consumers would gradually begin to switch to the products of the higher quality (and price); hence abandoning the consumption of the Belarusian goods, which are competitive mostly because of their low prices. Such a situation seems to have become true in 2005 – the exports to Russia in January-October 2005 fell to 90%²⁴, compared to the same period of the previous year, and the government insists that it happened not because of the introduction of the “destination principle” in the VAT collection²⁵.

Though the size of the Russian market is a big help for the Belarusian export-oriented economy, the share of the exports to Russia, which accounted for 47.7% in 2004²⁶, could also be considered as a possible threat to the sustainable economic growth, similarly to the any other kind of the economic dependence.

Another weakness of the Belarusian economy is the structural weakness of the Belarusian exports. The Belarusian complex industrial goods simply are not competitive on the markets outside the CIS region. The Belarusian export outside the CIS region mainly consists of fuels, minerals and raw materials: in January-April 2005 97.08% of the potassium fertilizers, 99.51% of the processed oil products, 72.37% of the black metals, 67.8% of raw wood produced in Belarus were sold in the countries, other than CIS²⁷. Whereas in the same period only 6.57% of the fifth-wheel tractors,

13.2% of the trucks, 9.18% of the metal-cutting lathes, 3.12% of the refrigerators and 0.0% of the TV sets produced in Belarus were sold outside the CIS region²⁸.

In general, the Belarusian economic growth appears to be more quantitative than qualitative. This claim is supported by the aforementioned evidence of the low competitiveness of the Belarusian industrial goods. As the additional arguments to support this assumption could serve several other facts, which are discussed below.

In Belarus there exist the yearly “Forecasts of the Socio-Economic Development” adopted by the Parliament, where the expectations on the growth of the main macroeconomic indicators are reflected. Even though this document is called “forecast”, basically it serves as the plan of the annual economic development. And the main indicator here is the level of the GDP growth. That is why the SOEs' managers have strong incentives to produce as much as they can, regardless of the objective possibility of selling those goods. This results in the constantly high level of the stock of the unsold goods in the Belarusian industry – the ratio of the unsold goods and the monthly amount of production fluctuates between 55-70% (65.7% in May, 58% in November 2005)²⁹. Despite the constant economic growth since 1996, the share of the loss-making enterprises is still very high: though it has decreased from almost 60% in 2000, it still accounted for 36% in January 2005³⁰.

An additional weakness of the Belarusian economy is the low inflow of the FDI. The level of FDI is much lower than needed and predicted given Belarus' strategic geographical location, privileged access to the Russian market, educated and skilled labor force, and relatively good infrastructure³¹. Such a situation leads to substantial lack of investment in the economy³². At the same time, the inability to attract a sizable amount of FDI accompanied by the limited access to international financing and the low level of reserves puts additional pressure on the current account.

The preferential external conditions in the recent years have allowed the Belarusian government to pursue activist industrial policy and sustain rather high level of subsidies. According to the World Bank team

²² Ministry of Statistics and Analysis of the Republic of Belarus, *Foreign Trade* (Official site, 2005), <http://belstat.gov.by/homep/en/indicators/fttrade.htm>.

²³ Ibid.

²⁴ Ministry of Statistics and Analysis of the Republic of Belarus, *Statistical Information*, (Official site, 2005), <http://belstat.gov.by/homep/en/indicators/main1.htm>.

²⁵ “Ocherednoe utochnenie” (“One more specification”), *Belorusskij Rynok* (14-21 November 2005) : <http://belmarket.by/index.php?article=26078>.

²⁶ Ministry of Statistics and Analysis of the Republic of Belarus, *Foreign Trade* (Official site, 2005), <http://belstat.gov.by/homep/en/indicators/fttrade.htm>.

²⁷ Aleksandr Alesin, “Dvulikiy Janus” (“Two-faced Janus”), *Belorusskij Rynok* (27 June – 4 July 2005) : <http://belmarket.by/index.php?article=25103> >.

²⁸ Ibid.

²⁹ Marina Kulikova, “Esli by ne nekotorye...” (“If not for some...”), *Belorusskij Rynok* (28 Nov. 2004 - 5 Dec. 2005) : <http://belmarket.by/index.php?article=26145>.

³⁰ Ibid.

³¹ World Bank, *A country memorandum for the Republic of Belarus* (Official site, 2005), http://siteresources.worldbank.org/INTBELARUS/Resources/328178-1120132035392/1365350-1120132328436/cem_by06_full.pdf, 19.

³² Apparently, the government fully recognizes this threat, but the creation of the attractive business environment would mean a U-turn in the governmental policy concerning its role in the economy and there is no political will for that yet.

estimations³³ the level of the net resource transfers³⁴ to the enterprise sector remained around 5-7% of the GDP in 2000-2004. What I see as the main problem with such a system of state support is even not that it is too costly, too segmented and non-transparent, but that it has a great distortional effect on the enterprises' incentives through softening their budget constraints. For instance, the coexistence of a high tax burden and massive tax benefits and subsidies for those enterprises that are less efficient undermines competition and stimulus for productivity improvements.

When we talk about the growth of the Belarusian economy in general, it is worth mentioning that the prudence of the Belarusian economic statistics is often questionable. Though in the recent Country Memorandum by the World Bank (2005) a special chapter is devoted to show the improvements in the quality of the national statistical data, and it is stated that the IMF mission in January 2005 highly appreciated their reliability, significant doubts about it still remain. It seems that the problem here lies not in the way the statistical data are collected and assessed, but in the data that are actually reported by the enterprise managers. In contemporary Belarus there exist strong incentives for the enterprises to overestimate their actual output. The reason for this is quite simple: every manager of the SOE realizes that if the enterprise would not fulfill the "requirements" of "The Forecast of the Socio-Economic Development", then to be simply fired would be the best possible outcome for him. At the moment, there is a discussion in the government whether to introduce the criminal responsibility for the non-fulfillment of the plan indicators. Given that many of the enterprise managers still have the experience of working under the socialist system, all the aforementioned cast serious doubts on the reliance of the GDP growth indicator.

Conclusions

The Belarusian economy has several features that make it quite different from the majority of the transitional countries. These features include: the dominance of traditional firms (state-owned or partially privatized) both in production and exports; the high degree of the government intervention in enterprise operations, including the preservation of some elements of central government planning of output, wages and employment; the high level of the major budget redistribution of funds aimed at supporting traditional firms and employment and the preservation of the high level of the social transfers, comparable to the socialist one. Despite these differences the economic development remains

relatively stable and the growth in the recent years has been significant.

At the same time the Belarusian economy is highly dependant on the trade with Russia and on the price subsidies for the Russian energy carriers. This is accompanied by the slow pace of the geographic diversification of the exports, low level of the investment and the very slow growth of the competitiveness of the Belarusian goods. These factors do not allow considering the Belarusian economic growth to be sustainable. Thus, the "Belarusian model" could hardly be considered as a successful alternative path of the transition. Several lessons on how to avoid some key mistakes in the early transition definitely could be learned from the Belarusian transition records, but it is a topic for a totally different discussion.

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³³ Ibid., 37.

³⁴ The highly concessional directed credits with the high level of repayment are excluded from the estimation.

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