

Summary

- **LAST YEAR'S FOREIGN TRADE MIRACLE ABSORBED THE SANCTIONS SHOCK, BUT THE FUTURE IS UNPREDICTABLE**

At first glance, the foreign trade balance looks good despite large-scale sanctions. At the same time, the ratios of physical volumes of exports and imports have started deteriorating sharply primarily due to the contraction of exports, which, once compared with peak values, have dropped by almost 40%. Now, the main question is how stable this situation is and what to expect in the future. Many factors will predetermine the development of the situation, some of which do not depend on Minsk.

- **RELOCATION OF BUSINESSES STRENGTHENS NEGATIVE TRENDS IN THE ECONOMY**

Among the businesses that have left Belarus, the majority is IT companies and small companies. Their active life position during the events of 2020 led them to make such a step. Large manufacturing businesses are in no hurry to relocate. Instead, they actively prepare to deal with the upcoming difficulties in the country.

Relocation of business people increases the amplitude of negative trends in the economy. However, under certain circumstances, there are prospects for more than half of the relocated active people to return to the country.

- **OUTLOOK FOR THE RUSSIAN ECONOMY, INCLUDING EXPORTS OF ENERGY COMMODITIES, IS NOT THE BEST**

Sanctions against Russia lead to limitations in domestic production. A large-scale contraction of industrial imports is already visible. Relocations of specialists and businesses will hit the government budget. Russia sells 20% less oil and 15% less gas at prices that are 25-30% below the Brent Crude Oil pricing. Europe intends to abandon Russian energy commodities, but the disposition of the counterparts is unlikely to change significantly in the near future. Despite the difficulties, Moscow will continue to support the Belarusian economy, but only at a minimal level, so that the Belarusians would have something to eat.

The Expert Opinion Bulletin (as part of the project titled "Belarus Economy Monitor: Trends, Attitudes, Expectations") presents a subjective expert review of the key short-term trends in the Belarusian economy. Each bulletin issue selects three key trends based on a survey of three experts: the BEROC staff members and third party experts. The summary captures these trends, as well as the expectations of the three experts interviewed for future economic dynamics. The body of the bulletin provides individual expert opinions on one of the challenges, their expectations and situation development scenarios.

Neither BEROC nor its representatives shall be liable for using the information contained in this bulletin. BEROC will not be liable for any losses and/or damages of any kind arising from using the information provided in the bulletin.

Foreign trade is on the track to deterioration

Dmitry Kruk, Senior Researcher, BERO (Kyiv)

Physical exports have sunk by almost 40%

The situation with the ratio of physical volumes of exports and imports has improved significantly during the period of the foreign trade miracle. In early 2022, despite the first round of sanctions imposed last year, it was one of the best in the last 8-10 years. This was facilitated by the physical exports breaking an absolute historical maximum volume due to the increased global demand against the backdrop of disruptions in supply chains. At the same time, as COVID-19 outbreak, import intensity of production has been reducing for the last two years compared to the average statistical values, and imports have been limited accordingly. In addition, foreign trade conditions have been significantly improving since the second half of last year due to the better ratio of export and import prices over the past five years. This factor does not depend on Belarus in any way. However, Minsk can partially improve these trade conditions manually by maneuvering the geographical focus of exports and imports. This trend is still relevant; but the question is for how long this tool can be used.

If one looks at the situation for the last 2-3 months, it becomes clear that the ratio of physical volumes of exports and imports has started to deteriorate primarily due to the contraction of exports. In March, the physical volume of exports compared to its peak values in the second half of 2021 sank by almost 40%. This is a gigantic gap. However, the overall picture is also smoothed out by the large-scale subsidence of imports and by the still good price environment.

It turns out that the safety margin and a good baseline have mitigated the impact of the large-scale shock in recent months.

Exports of oil products and potash fertilizers sag more actively

The decline in physical volumes of exports has occurred primarily due to intermediate goods: oil products and potash fertilizers. Exports of non-food consumer goods, such as cars, furniture, appliances and equipment, are actively sagging, too. These exports are not so much important in the overall volume, but in technological terms.

Investment goods — engineering products, trucks, agricultural machinery, foods — can still be called the “strongholds of stability” since there has not been any significant subsidence in them.

The types of exports correlate with geography. Physical volumes of Belarusian exports to Russia — predominantly investment goods and food — have not been affected practically, but Belarusian exports to the EU countries — predominantly intermediate goods — have sagged. However, the most significant subsidence is because of Ukraine, which was a Mecca for oil products and manufactured goods some six months ago.

In terms of geography and goods, there is a noticeable decrease in imports primarily due to raw materials, as well as due to the favorite damper of the government authorities: consumer non-foods.

The picture does not look bad, but it is hardly worth hoping that it will not change

Despite the sanctions and the massive decline in exports, there was a surprisingly nice foreign trade balance picture in March-April, and the exchange rate of the Belarusian ruble was strengthening contrary to expectations. However, this is a transitive effect. There is no reason to expect that this state of affairs in foreign trade will sustain.

I presume that today no one has a clear understanding of how the situation in foreign trade will develop in the future. And the authorities hardly have any clear plan of how to respond if the foreign trade balance deteriorates. There is a feeling they still hope for the transitive effect in foreign trade to continue and that foreign trade will not cause headaches.

What will determine the state of foreign trade

The first factor that will generally affect foreign trade: how deep exports will sink. In view of the fact that the sanctions imposed on many commodities have just come into force (they will come into full force on June 4), there is still room to slide.

The second factor is to what extent it will be possible to “redirect export flows” by administrative leverages, especially in the face of serious transportation, logistics and payment barriers. Indeed, many goods can be potentially redirected to Asian and African markets, especially if the pricing is below high market prices. However, given the above restrictions, this is not a purely economic objective. This is an equation with many unknowns.

The third factor does not really depend on Belarus. How the situation with transportation, logistics and payment barriers will develop is a question. So far, as business surveys show, many firms have found workarounds and have built new schemes. Most of them admit that these pathways are more expensive and time consuming, but, at least, they allow the business models of the firms working with foreign markets to be preserved. However, as representatives of the business community note, there is no certainty that there will not be another aggravation as far as any of these three components are concerned. This means that the situation can continue getting colder or can start getting warmer. This gigantic uncertainty is one of the most critical components at the moment, which prevent to answer the question about what will happen to exports.

The fourth important factor is exports to Russia. There is practically no subsidence in the physical volumes of exports. It can be expected that this pattern will continue in the food segment. However, what will happen to investment exports — the main market for which is mainly Russia — is another big question. On the one

hand, as many foreign companies leave the Russian market, a market share is freed up, which Belarus can claim by expanding its piece of the pie. On the other hand, the pie itself will deflate due to the contraction of the Russian economy. It will be important for the Belarusian exports which of these two trends outweighs.

There is some uncertainty with imports, too. So far, the contraction has been partly natural, but its significant part has been with a strong flavor of the administrative leverage. Judging by the statements, including those about import substitution, it is most likely that Minsk is going to pursue a restrictive policy on imports. Following a narrow-minded accounting approach, from the arithmetical point of view on the GDP, imports can indeed be considered as some kind of “evil”. In a short run, a GDP contraction seems to help prevent a GDP decline, but many industrial production processes and sectoral interdependencies are tied to imports. So, this will be disastrous for the prospects of industrial outputs. This is the pathway to a deeper fall in GDP. In addition, the situation of dissociation from the outside world is quite likely. Accordingly, the situation with foreign trade will also depend to some extent on whether the government authorities will try to remove barriers to imports and contribute to the elimination of transportation and logistics barriers or, on the contrary, will stimulate them.

All these factors indicate the absence of a predetermined development track, since it is not clear what will happen to exports and imports, each of which has many unknowns. It is highly probable that the volumes of imports and exports will lose stability: there may be jumps in both directions. But it is more likely to see a deterioration track, since there are much more risks for exports, and all of them have a downward effect. This situation will also affect the exchange rate.

If the hope of the government authorities to maintain temporary stability does not materialize, they will face a dilemma. Two scenarios are possible in this case. The first scenario is to accept the new reality, to recognize the deterioration of the external position, and to try to smooth it out. The main tool available for doing this will be the forex rate. This means its depreciation, and most likely, this depreciation will be faster than the depreciation of the Russian ruble. The main disadvantage of this approach is that it will facilitate new rounds of financial stress and almost certainly lead to a full-fledged financial crisis. However, this pathway can slow down and smooth out the decline in GDP for some time.

The second scenario is to continue fighting with imports, i.e., to stabilize the external position by adjusting imports depending on the decline in exports. This is the pathway to an abruptly increasing overly prescriptiveness and an accelerated decline in outputs, dissociation from the developed world and, I would even say, technological regression. In addition, this means limited diversity of consumer goods, decreased quality of

the goods available on the market at disproportionately high prices.

Small businesses relocate from Belarus more often, but this also reinforces negative trends in the economy

Alexander Knyrovich, businessman, author of the KNYROVICH YouTube channel

Small businesses and IT companies relocate from Belarus more actively

When discussing relocations of Belarusian private companies, one should divide real businesses and IT companies. Relatively speaking, about 20-25% of the IT sector employees have relocated. At that, the number of relocated businesses can hardly be measured because IT companies are not directly tied to a registered legal entity. Their intangible structure allows them to open intermediary companies in any jurisdiction, to operate only as an outsourcing company registered in Belarus, and find many other legal arrangements that complicate evaluation of their activities. I can see Belarusian IT businesses actively registering their legal entities in Poland. At that, they either close their legal entities in Belarus or it takes them a very long time. Therefore, this is more like a diversion of business activity rather than closing a legal entity in Belarus and opening it in another country. But this process is underway, and it is very noticeable.

Why? IT guys are the people who are first to react to the changing environment in the country. They are highly paid specialists, educated, involved in the global context, and not living in the Belarusian context of pro-government folk and harvest celebration festivals like “Slavianski Bazaar” and “Dazhynki”. Before 2020, and even more so in 2022, the country was quite comfortable for them despite the authoritarian regime, and now the main problem is the threat to the future of their children. Obviously, they relocate because it is relatively easy for them to leave.

If we talk about assessments in other areas, they are rather not representative, but based on my communications with the colleagues who have stayed in Belarus, and my observations of what I can see in Poland, Lithuania and Ukraine. Thus, about 400 representatives of relocated companies gather at the events of the Belarusian business association called ABBA. And when we hold a small chamber event announcing it by literally two posts on social media, we get 130 applications. Based on this, it is possible to say that a large number of small and medium-sized businesses were forced to leave because of the events in Belarus. These are often companies that employ 5-10 people, or self-employed individual entrepreneurs.

We have figures for the business profiles among these applications. Supporting services (from freight forwarding to marketing) have the largest representation followed by trading companies, and then IT companies and small businesses in the service sector have equal

shares, and manufacturing companies have the smallest share.

This suggests that small businesses, which are in an active position, including an active position about the events of 2020, relocate more often. These businesses find it easy enough to pack up and leave. As stated above, the IT sector drains smoothly to other countries. And large companies stay. This is primarily because they have a different cost of moving and other tasks. This business does not think in terms of “now we are relocating our plant to Poland.” It is very difficult to move this kind of business. First, such companies are not built in one or two days in large markets. Second, they would have a large number of already established direct competitors in foreign countries.

That is, large businesses — especially manufacturing companies — do not show their direct desire to leave yet. So far, they are busy trying to cope with the current difficulties and get ready to cope with what will happen in the country. It can be seen that large businesses are in fear and full of doubts about their future coming in a few months. But it will be possible to talk about the quick relocation mood only if the problems in the Belarusian market worsen or if the economy starts collapsing at a precipitous pace.

Many representatives of this business segment have long had companies in other jurisdictions. In some cases, this is a parent company of the holding; in other cases, this is just an investment company. For some of them, this is a good wallet or a way to legalize themselves to get documents originated in another country. This is not a new trend that would build up after the war broke.

If we leave IT guys aside, typical business persons who have relocated are the people of active entrepreneurial age — i.e., from 30 to 50 years old — and 70% of them are men, and 30% are women. Are there any other particular traits? Moreover, the only common trait among them is that they have come to this point because of their active life position.

Businesses that have relocated twice see prospects in the process of restoring Ukraine

Business people have been moving predominantly to Ukraine, since mentally, in terms of language and conditions, it is the closest to Belarusians. Poland is the second most popular country. I have not seen specific cases of a real business that has relocated to Lithuania. People talk about Georgia as a comfortable country considering its legislation and taxation. However, this is nothing more than lip service.

Some businesses had to relocate twice: first from Belarus to Ukraine, and then from Ukraine to Poland. These entrepreneurs intend to return to Ukraine. They share a common vision that restoring this country will be a big project, and Belarusian entrepreneurs will engage in it, too.

Consequences of business relocation for the economy

Given the general decline in the economy this year, it is difficult to single out the share of this vector that is associated with business relocation. There are general consequences of government pressure on business. In Belarus, these consequences are manifested in the fact that the number of self-employed individual entrepreneurs per capita is four times less than in Poland. That is, due to the attitude of the government to the private sector and because of the business climate, entrepreneurial activity is many times lower in our country. The contribution of small and medium-sized businesses to GDP is 26% versus 67% in the US or 52% in the European Union. This is our untapped potential. If we only leveraged our higher entrepreneurial activity, we could be at a completely different point in the development of the economy and incomes of the population.

I would not say that the relocation of entrepreneurs sets the trend; this rather amplifies and increases the negative trends.

There is another important point. A big enterprise is like a big ship. If the ship is on course and sees an iceberg upfront, then, realizing it is impossible to avoid hitting the iceberg, the crew swings lifeboats out. So, in the economy, small businesses always play the role of those very lifeboats that quickly seal local problems, ensuring prompt response to challenges. The reduction in the number of small and medium-sized businesses in the country puts the economy in a more dangerous situation if such “icebergs” emerge. This means that fewer taxes will be collected, unemployment will be higher, and wages will be lower.

Whether to expect relocated businesses to come back after the situation changes in Belarus

Among those who have relocated, can I see people who love their Motherland, wish it well and would like not to go anywhere, but to live and develop in Belarus. Speaking about all those who have left Belarus after the events of 2020 — irrespective of their engagement in business activities, — I believe that if changes in the country occur during the active period of life of one generation — that is, in about the next 20 years — then more than half of them will come back home. In this case, the new knowledge and competencies acquired by them abroad will be very useful to the Belarusian society.

If we consider a longer period of time, then I would not assume that people whose children grew up in another country would want to return to Belarus.

Prospects of the Russian economy in the context of sanctions and the energy conflict with the EU

Andrey Movchan, financier, expert of the Economic Policy Program at the Carnegie Moscow Center, founder of the Movchan's Group

Impact of sanctions on the Russian economy

Sanctions against Russia can be conditionally divided into several groups. The first one is a ban to supply high-tech goods and technologies. The second one is the financial transaction restrictions. The third one is export restrictions. There are also personal ones that do not affect the economy in any way. However, a non-sanction pressure, where specific companies stop working in Russia voluntarily, has a strong impact.

Russia is fundamentally dependent on imported technologies. This is from the production of cheese by using foreign equipment and with foreign sourdough to the production of missiles with imported microcircuits and alloys. In this sense, the ban to supply high-tech products is a very serious limitation for domestic production. It will partially cope with it by substituting technologies and importing equipment from neutral countries. But there is bad news, too. Neutral China also imports what will be lacking in Russia. Not for nothing Russian companies used to purchase these technologies in Europe and America. In addition, we can already see how China, while maintaining neutrality in politics, in economics, supports the sanctions policy: Russian airplanes have already been banned to fly to China, and Huawei has left the Russian market, and so on.

The most unpleasant thing will be the break in production chains. If you stop getting components, if your equipment is not serviced – even small elements of the value chain, – then this is a huge problem similar to the problems in Russia back in the 1990's. Back then, chains were also torn due to the opening of markets, due to the reorientation of the CMEA countries, due to inept management, as a result of which not only enterprises, but entire industries were collapsing. Now, there is a reverse process: the closure of markets. We can already see how somewhere, literally, they begin to import microchips in suitcases to maintain production. But you won't get much in this way. It will be possible to see the figures of the impact on production in about six months, but we can already see indirect signs of its contraction: there is a 10-15% drop in household incomes while imports have fallen by half. This means a large volume reduction in industrial imports.

The second problem has largely affected exports. Russia has mainstream exports (hydrocarbons), where a 20-25% drop is expected, but there used to be a lot of small exports (computer software, devices, secondary processing products), which used to provide income to hundreds of thousands or even millions of people. Exports are collapsing primarily because Western partners do not know how to pay for supplies and, frankly, they do not want to pay companies from Russia. And all

these exporting companies used to have a small margin. If they are not paid for two or three months, they will simply die.

The third problem is related to the extra-sanction refusal of companies to work in Russia. If you used to, let's say, sell the Nike sneakers, which has left the market, then theoretically you can switch to Chinese sneakers. However, in practice, this does not work this way, because the entire system is focused on certain supply channels, logistics, clientele, and pricing policy. At the same time, people's incomes are declining, which is why you don't even understand what should be the substitution.

There is another important point, not necessarily directly related to the sanctions. What happened has caused an outflow of labor migrants and specialists from Russia itself. It is estimated differently, but the Ministry of Labor of the Russian Federation says 40 thousand IT-specialists have left the country, and this is only the IT sector. Taking into account the fact that various specialists have left and many specialists are still in the process of relocating or are going to leave in summer, when the academic year of their children is over, one can surely multiply the figure referred to by the Ministry of Labor by 10 or even 30. This also greatly affects the economy, because these people have been at the heart of generating added value in the non-commodity sector. At the same time, many of them owned businesses, and they have either hastily relocated or they are relocating their businesses. We can already see that the share of the government budget oil revenues has doubled, which indicates, among other things, a strong drop in non-oil taxes. Such a blow to the government budget will decrease public investment, i.e., it will affect another sector of the economy where many people were fed and generated the GDP.

In addition, inflation will be double-digit this year, likely reaching 15-20% or more. At that, the indexation of social benefits is, let's say, 10%, which indicates a decrease in real incomes by another 5-10%. This will mean a decrease in demand, which will hit Russian production.

The role of the energy conflict and its prospects

The issue of oil and gas exports is highly politicized. And political issues are poorly predictable, because they depend on the wishes, opinions or the combination of interests of politicians. It should be said that the oil and gas side of the conflict in its phases is very similar to the military side of the conflict. It was a critical phase at the time of an acute military conflict, and now, it is followed by a positional phase. Russia insists it is ready to sell energy commodities if they are going to be bought, but if barriers are set for Russia, it may stop deliveries to Europe. European consumption of Russian energy commodities decreased during the period of acute hostilities. But now this process, apparently, has reached a certain limit. As a result, Russia sells

20% less oil and 15% less gas at prices that are 25-30% lower than the Brent Crude Oil pricing.

Europe, apparently, will continue buying this volume in the medium term: and it's not so important whether this volume will be bought from Russia or from other countries, because if Europe (as the sixth package of sanctions suggests) refuses to buy Russian "tanker" oil, then this oil will go to other regions, and Europe will buy the oil that these regions used to buy before. There will be few changes; perhaps, the volumes will slightly reduce. That is, a kind of winter positional campaign has begun, and, in my opinion, over the course of many months, or maybe for one or two years, this disposition is unlikely to change.

Russia is already looking for ways to reorient sales to third buyers, including China and India. Sales to Asia have already exceeded deliveries to Europe. The process is difficult, but possible. It is extremely difficult, expensive and not always possible to forward oil tankers along the Northern Sea Route, and besides, such shipments have no insurance coverage. Oil tankers will not go around Europe: European ports will stop hosting them soon; foreign tanker companies will not serve Russia, and there is a lack of domestic oil tanker companies. At that, oil is sold to Asia at a large discount, which is about 30%. But the Russian government budget and its foreign exchange account are saved by the pricing: at \$120 per barrel of oil, a drop in revenues even by 40-50% is equivalent to full revenues when oil is sold at \$60-70 per barrel, and this price has always been comfortable for Russia.

Of course, there is a long-term trend in European politics towards abandoning Russian oil and gas. It is caused not only by the war, but also by high prices. This process will continue, but the rejection will come in small leaps. At the same time, Russia will reorganize its sales directions, build its own tanker fleet, deploy gas and oil pipelines. At the same time, the extraction of fossil fuels will reduce due to the fall in both domestic and foreign consumption of oil and gas.

Whether Europe will want the same in three years, I cannot say. We can well expect that in two years the European bureaucrats will forget everything and say that Russian oil and gas are OK for them again. There will be Schroeders and Orbans who will selfishly and

disinterestedly promote the continuation of this addiction, and everything will get back on a usual track. However, if Europe has a will and desire, then total abandonment will come in three to five years. Over the same period, Russian oil and gas extraction may fall by 35-40%.

Russia will continue supporting Belarusian economy, but to a minimum extent

Since the Belarusian economy is small compared to the Russian one, there is no big problem for Russia to support it. I am sure that Lukashenko is well aware he is not a price maker. This is done by the Kremlin on the one hand, and on the other hand, it is done by the Belarusian population, the main expectation from which is that it should not rebel.

The Russian army can enter the territory of Belarus at any moment, and the West, against the backdrop of the war with Ukraine, will not even pay attention to this, because everyone already perceives Belarus as a Russian dominion entirely controlled by Russia. No one would be surprised by the Russian troops entering Belarus, by the arrest of Lukashenko, by the trial of Lukashenko, by enthronement of a pro-Russian president obedient to Russia, by the unification of Belarus and Russia: these will be viewed as a "union beef." This is happening not only because Lukashenko is obedient, loyal and does what he is told.

Supporting the other side — the Belarusian people — in a state when they are not willing to overthrow the regime, does not require a lot of money; so, Russia will continue supporting them. In order to avoid a default on Russian debts, it is enough to simply extend repayment deadlines. Moscow needs the Belarusian economy to somehow provide people with salaries, enabling them to survive. Otherwise, there are no guarantees there will be no nation-wide protest against Lukashenko.

Overthrowing him failed some time ago, because the ordinary Belarusian does not really care who is in power: the Belarusian lives his/her own life. S/he has some resources, his/her life is stable. And if ordinary Belarusians have nothing to eat, then they will join such a protest movement. That is why Russia will support exactly at such a level that they have something to eat, but not more than this.