A comparison of performances on social indicators might also be useful, and it might also be interesting for the Fund's strategy on poverty reduction, where I think Belarus would come out as a world champion.

On the major issues today, the authorities are mindful of the staff's arguments on the consequences of directed lending, quasi-fiscal activities, and mandated wage increases, competitiveness, and the potentially adverse impact of the golden share. Clearly, the authorities are implementing Fund advice, even though, in the eyes of many, not fast enough. As recognized in the Selected Issues Paper, quasi-fiscal operations are being reduced, albeit from very high levels. And on wage policy, taking into account staff's point about competitiveness, a shift has been made towards indicative targets. And here, Mr. Misra and Mr. Srinivas have asked about what this actually means, and I can explain that wage movements are no longer reported to the Council of Ministers, which in a well-organized society like Belarus means that enterprises are freer to decide on the basis of profitability and the needs of the firms.

The Belarusian economy has also been in transition in terms of less government ownership of the economy, making it de facto a more mixed economy than its defenders or detractors want to see it. Nevertheless, the positive results in terms of growth and social indicators confirm the authorities' gradual approach to implementing certain recommended changes. And given the movement towards reform, the authorities would therefore disagree with the statement that the macroeconomic policy mix is ultimately unsustainable. In the same vein, the two scenarios presented by the staff, mainly current policies versus reform scenario, are perhaps in reality not as clear-cut and simple.

I also take note of Mr. Raczko's and Mr. Piatkowski's note of caution on privatization, and I also sense an implicit note of caution even in the staff's call for transparent privatization.

And finally, I would like to emphasize that the authorities are very much interested in continuing the very good technical cooperation with the Fund. I should add that this view is shared not only by the government and the central bank, but also by circles outside the government. Our office has been in contact with these outside circles as part of our long and continuous relationship with Belarus. All elements of the Belarus society recognize the value of the Fund's involvement, be it in the form of Article IV consultations, technical assistance, or the resident representative office.

On the latter point, I have, of course, to express our disappointment that, after Lithuania's succession to the European Union, the Resident Representative was not moved to Minsk as requested. Of course, we do appreciate the Fund has slightly upgraded the existing local staff in the Resident Representative's office. But we hope that soon the Fund will appoint a Resident Representative to Belarus because the technical assistance is well used and all technical missions of the Fund have been enthusiastic about their discussions and the implementation of technical advice by the Belarus counterparts. I am grateful for the support for technical cooperation today in the Board, and I hope that management and the Board will find it in their hearts and minds to support more technical cooperation with Belarus and eventually re-establish a resident representative to Belarus.

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IMF Executive Board Concludes 2005 Article IV Consultation with the Republic of Belarus

On June 17, 2005 the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Republic of Belarus.[1]

Belarus experienced strong economic growth in 2004, supported by policies aimed at raising incomes and credit, and a favorable external environment. Inflation was halved during 2004, and slowed down further to 11 percent in April 2005, aided by a balanced budget, exchange rate stability, and continued remonetization on the back of rising trust in banks and the national currency. Inflationary financing of the general government budget from the National Bank was discontinued, and budgetary consolidation progressed further. International reserves have increased, and the government's debt is at a low level. A surge in the current account deficit in late 2004 was largely reversed in early 2005.

However, market-oriented structural reforms have stalled. Privatization has largely ground to a halt and the private sector's share of GDP remains low at around 25 percent. Further, the "golden share" rule has been expanded in 2004, giving government a unique power to intervene in any company which used to have state ownership. The business environment is not conducive to private—including foreign—investment.

While the economy's current momentum is likely to result in significant growth in 2005, its long-term prospects are uncertain in the absence of wide-ranging structural reforms and a phasing out of massive quasi-fiscal activities. Under current policies, growth is expected at 7.1 percent in 2005 and 4 percent in 2006, gradually grinding even lower.

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

Executive Board Assessment

Executive Directors recognized Belarus's improved macroeconomic performance in recent years and welcomed, in particular, the strong economic growth and reduced inflation realized in 2004. In this regard, they took note of the role played by the balancing of the general government budget, the discontinuation of inflationary financing of the budget, and the exchange rate anchor, as well as demand-inducing policies and advantageous external factors. Directors commended the authorities on the marked improvement in poverty indicators in recent years.

Directors cautioned, however, that Belarus's economy remains vulnerable and that there is a risk that its current strategy would not produce sustainable growth, and observed that continued rapid growth and disinflation would require a tightening of macroeconomic policies and wide-ranging structural reforms to reduce the government's role in the economy and facilitate private sector-led growth. Given the favorable external environment and the economy's current momentum, Directors urged the authorities to take advantage of this window of opportunity to launch reforms and create an environment conducive to private sector growth.

Directors expressed concern about the limited progress made in enterprise and financial sector restructuring. In this regard, they pointed to Belarus's extensive quasi-fiscal operations including, in particular, directed credits and subsidized lending for housing through large state banks. The continued rise in directed credits and subsidized housing loans contributed to escalating liquidity problems in systemically important banks and necessitated another round of government recapitalizations which, as set out in the Financial System Stability Assessment, remain the prerequisite for the continued solvency of Belarus' banking system. In addition, Directors noted with concern the rapid pace of wage increases, which over the past decade outpaced productivity growth and stressed that the enforcement of highly ambitious U.S. dollar wage targets could lead to inflation pressures, enterprise decapitalization, and waning external competitiveness.

Against this background, Directors underscored the need for accelerating the consolidation of quasi-fiscal activities into the budget and at the same time reducing their magnitude in order to safeguard the budget balance. In line with this, while supporting the government's goal of lowering the high tax burden, Directors noted that this would require expenditure cuts. They viewed that given the strong momentum in the economy and the need to keep inflation under control, it would not be appropriate for fiscal policy to provide additional stimulus at this time, despite the easing of the budgetary financing constraint.

Directors agreed that the central bank needed to make low inflation its primary objective and noted that, to this end, the National Bank of Belarus (NBRB) would need to be granted full operational autonomy. They emphasized that while the nominal exchange rate has played a useful anchoring role, further disinflation will require containing credit growth. Directors also saw a need for retaining a measure of exchange rate flexibility to safeguard against excessive real appreciation, to help deal with exogenous shocks, and to allow the NBRB to raise its level of foreign reserves, which remain precariously low, despite a marked increase in the past eight months.

Directors stressed that structural reforms would be key for ensuring growth sustainability by boosting productivity and allocational efficiency. They urged further enterprise reforms and transparent privatization to help harden budget constraints, noting that, together with reduced government intervention in economic activity and a pickup in FDI, this could raise the level of competition and the efficiency of product and labor markets. Directors observed that the resulting increase in productivity growth would provide a sustainable basis for raising income.

Directors warned that the growth contribution of many of the favorable external factors—notably the benefit reaped from Russian energy import pricing—is likely to wane. With rapid growth in neighboring countries, rising incomes and demand for rubels and low external debt, current conditions are conducive to an early transition toward a market economy with minimized costs of policy adjustment. In this regard, Directors stressed that the looming costs of population aging also argued for an early start of reform measures to ensure continued fiscal sustainability.

Directors noted that while Belarus' overall debt ratio remained low, the increasing dependence on short-term liabilities and limited foreign exchange reserves raised roll-over risk.
They stressed that Belarus would need to substantially improve the environment for foreign direct investment, not only to help secure a non debt-creating source of financing, but more importantly to facilitate the knowledge and technology transfer that has proven to be a critical contributing factor for rapid productivity growth in most other transition economies. In this regard, they noted that the golden share rule as applied in Belarus was counterproductive and urged its elimination or the limitation of its application—as in other countries—to a handful of preannounced cases that are of central strategic importance.

Directors noted that for the currency union with Russia to prove beneficial for Belarus, a number of key issues needed to be appropriately addressed. While significant further work remains to be done in this regard, prudent macroeconomic policies and an early start on wide-ranging market-oriented structural reforms would increase the likelihood of such an outcome.

Directors welcomed the constructive tenor of the discussions between the staff and the authorities. They commended the authorities for their good track record in implementing technical assistance recommendations and the significant progress made in the past year in this area, marked by the completion of the Financial Sector Assessment Program, the subscription to the Special Data Dissemination Standard, and the publication of fiscal and data Reports on the Observance of Standards and Codes. Directors supported the continuation of technical cooperation with the authorities.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board.