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The Belarusian Currency Market During War in Ukraine: Hidden Problems and New Trends

Belarus has faced unprecedented sanctions during the last year and the new economic conditions have led to a GDP decline and inflation growth. At the same time, the situation on the currency market has been stable since April 2022. The Belarusian Ruble demonstrated a gradual appreciation to the US Dollar and the Euro and a decline to the Russian Ruble. The appreciation of the Belarusian Ruble against the US Dollar has given households the illusion that the economic situation is not that bad. This brief analyses the main factors of the current situation on the currency market as well as describes the challenges which might destabilise the market. The importance of changing selected currencies in the currency basket and the start of a reorientation of the Belarusian economy from Western to Eastern partnerships, are also described.



The National Bank of the Republic of Belarus' Policy on the Currency Market

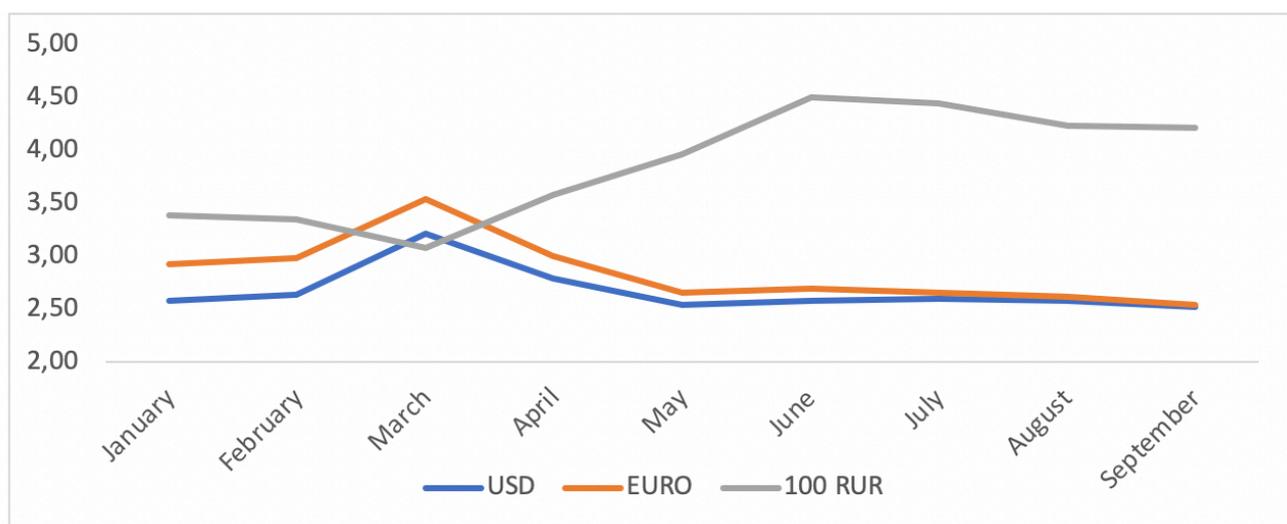
In Belarus, currency has always played an important role as an indicator of economic stability. Household's reactions to sharp fluctuations of the Belarusian Ruble have been expressed in an immediate demand growth for foreign currency (US Dollar and Euro mostly). After the war in Ukraine started and the exchange rate of the Belarusian Ruble began declining, people tried to make currency deposits from banks and buy foreign currency. In contrast to the Central Bank of Russia, the National Bank of the Republic of Belarus (NBRB) introduced no restrictions on the currency market. However, Belarusian financial institutions imposed their own limits on carrying out non-cash exchange operations, cash withdrawals from ATMs and from bank accounts. Financial institutions also limited the availability of currencies in exchange offices and imposed limits on payment

transactions by credit card outside of Belarus. All these processes took place under the condition of a sharp devaluation of the Russian Ruble.

The dynamics in the Russian Ruble have affected the Belarusian Ruble fluctuation (see Figure 1). The correlation between the currencies was strong even before the war, given that the Russian Federation is a dominant economic partner for Belarus, and has since become stronger.

The share of Russian Ruble in the Belarusian currency basket is at 50 percent. Moreover, in Q1-Q3 2022 the Belarusian dependency on the Russian economy increased in the aftermath of losing the Ukrainian market and facing European export shortages. Between January and August 2022, the share of export of goods to CIS countries (where the main share of exports goes to Russia) was 65,7 percent, as compared to 58,4 percent for the corresponding months in 2021. The same tendencies are apparent when considering the import of goods. The share of import from CIS countries reached 64,7 percent between January and August in 2022, as compared to 61,3 percent for January-August in 2021 (BSCBR, 2022).

Figure 1. The weighted average exchange rate of the Belarusian Ruble, in Belarusian Rubles.



Source: Statistical Bulletin #9 (279) 2022.

Sanctions and the Russian Central Bank's policy have led to a stabilisation on the Russian currency market. The Central Bank of Russia has introduced restrictions on capital outflow from the country,

limited cash withdrawals from bank accounts and foreign currency purchases in exchange offices (Tinkoff, 2022). The cancellation of budget rule has further supported the Russian Ruble exchange



rate. But the main reason for the Russian currency exchange rate reversal post March 2022, relates to the situation regarding foreign trade. Due to sanctions, imports had significantly decreased. At the same time, high energy prices allowed for export growth. Between January and June 2022 Russia displayed a high positive trade balance (169,62 billion USD), the largest in the last 7 years (CBR, 2022). As a result of sanctions, the Central Bank of Russia started to prepare the market to work with currencies of friendly countries.

Similar tendencies can be seen in Belarus. NBRB has changed the composition of the foreign currency trade to turn the Belarusian economy from a Western to an Eastern direction regarding economic cooperation. In July 2022 the Chinese Yen was included in the currency basket. At the same time the share of Russian Ruble was at 50 percent, the US Dollar at 30 percent, the Euro at 10 percent and the Chinese Yen at 10 percent. In August 2022, the NBRB began to define daily exchange rates for the Vietnamese Dong, Brazilian Real, Indian Rupee and UAE Dirham. Finally, since October 2022, the exchange rate for the Qatari Riyal has been defined on a monthly basis (The National Bank of Belarus, 2022). These changes are indicators of ongoing and planned structural changes to the economy to accommodate increased cooperation with the Eastern economies.

Currency Market Stabilisation and Current Risks

The Belarusian Ruble has not repeated the fluctuation of the Russian currency. It did however copy its tendency to appreciate to the US Dollar and the Euro, as of April 2022. Besides the appreciation of the Russian Ruble and personal bank's restrictions on national currency markets, the stabilisation of the Belarusian Ruble can be explained by the positive trade balance. In contrast to Russia, the growth of net export in Belarus was due to a faster decline of imports than exports. There are several reasons why this can be a

problem for currency market stabilisation in the future.

First, Belarus' foreign trade has become more and more oriented toward the Russian market. If the main trade partner experiences difficulties (for example, oil price caps) this could lead to a devaluation of the Russian Ruble and, as a result, declining competitiveness of Belarusian goods on the Russian market.

Second, reorientation of Belarusian exports from Western to Eastern countries require time and additional financial resources and exports are not always profitable due to high logistical costs. Any additional sanctions may further limit such opportunities.

Third, main export-oriented services, such as the Transport and ICT sectors, are affected by sanctions and their consequences. In Q3 2022, the transport turnover was equal to 68,3 percent, as compared to the same period 2021. The ICT sector is still having a positive impact on GDP growth. However, in January-September 2021 the positive contribution from this sector to the Belarusian GDP was 0,9 percent, while it between January and September 2022 was only 0,2 percent.

Recent success in foreign trade is mostly due to the continuation of selling potash, nitrogen fertilisers and other products on the global market, a strong Russian Ruble and Russian market openness towards Belarusian companies, low levels of Belarusian imports, and cheap Russian gas (the special price for Belarus is 128 US Dollars for 1000 cubic meters). If the terms of trade with Russia worsen and key export-oriented industries suffer from sanctions and reputational risks, the currency market could however be destabilised.

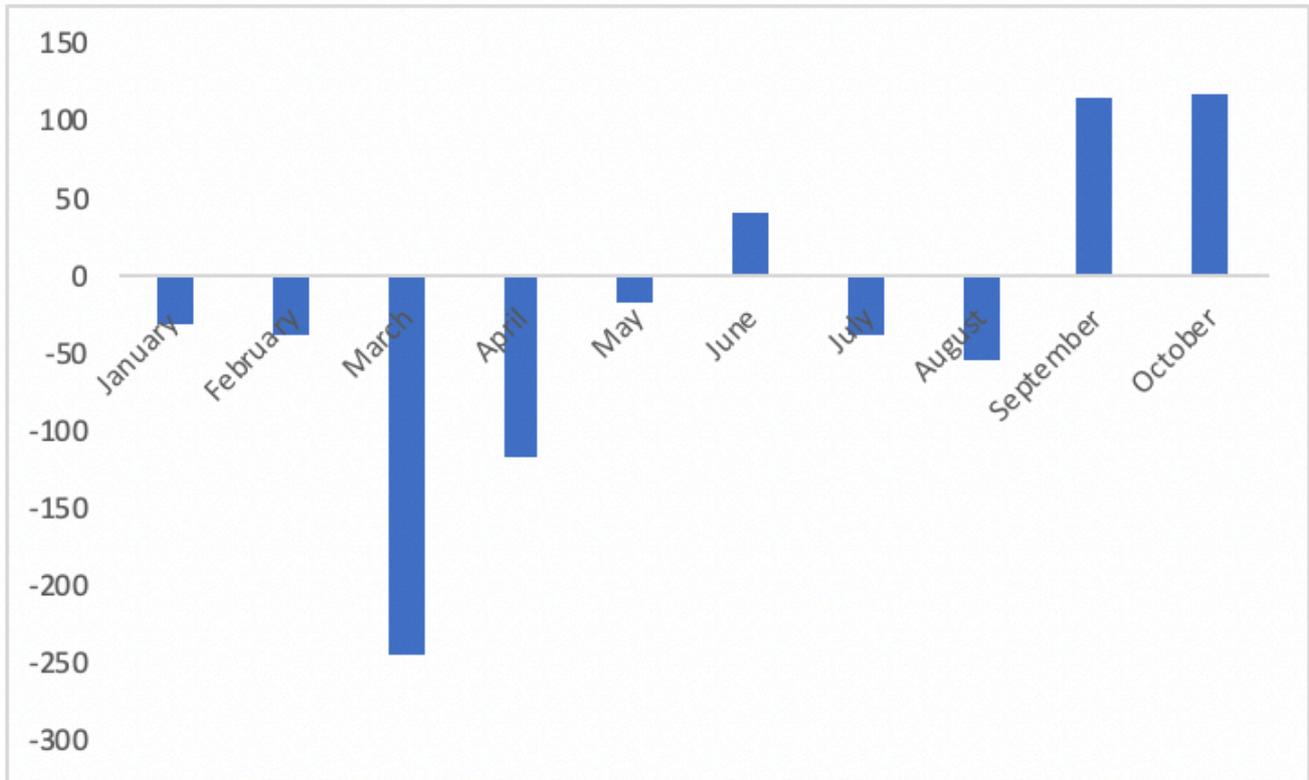
Another problem for the Belarusian Ruble stability in the middle and long term is related to household behaviour. In January-August 2022 Belarusians sold more foreign currency than they bought. Despite the Ruble fluctuation, the high levels of net sales in March was due to bank restrictions. In June, the net purchase was related to seasonal factors (see Figure 2). For the other



months of the period the net selling can be explained by a stable situation on the currency market and real incomes declining. People sold

currency in an attempt to maintain their previous standards of living.

Figure 2. Balance of purchase and sale of foreign currency by households (+ “net purchase”, - “net sale”), mln. USD.



Source: Based on data from the National Bank of Belarus.

In September-October 2022 Belarusian households bought more than (an equivalent of) 300 mln. USD on net basis, primarily in USD or Euro, which is very unusual for the Belarusian market situation. There are several possible explanations for such behaviour:

1. Despite difficulties with obtaining visas Belarusians are going to Poland and other European countries to shop. Because of sanctions, retaliatory sanctions as well as a high price control on the domestic market, the range of goods has shrunk, and prices have risen. In European countries Belarusians can purchase much cheaper goods both for personal use and for resale.
2. Partial mobilisation in Russia has increased the uncertainty of further

political steps in Belarus. Households thus purchase foreign currency to establish an extra safety cushion.

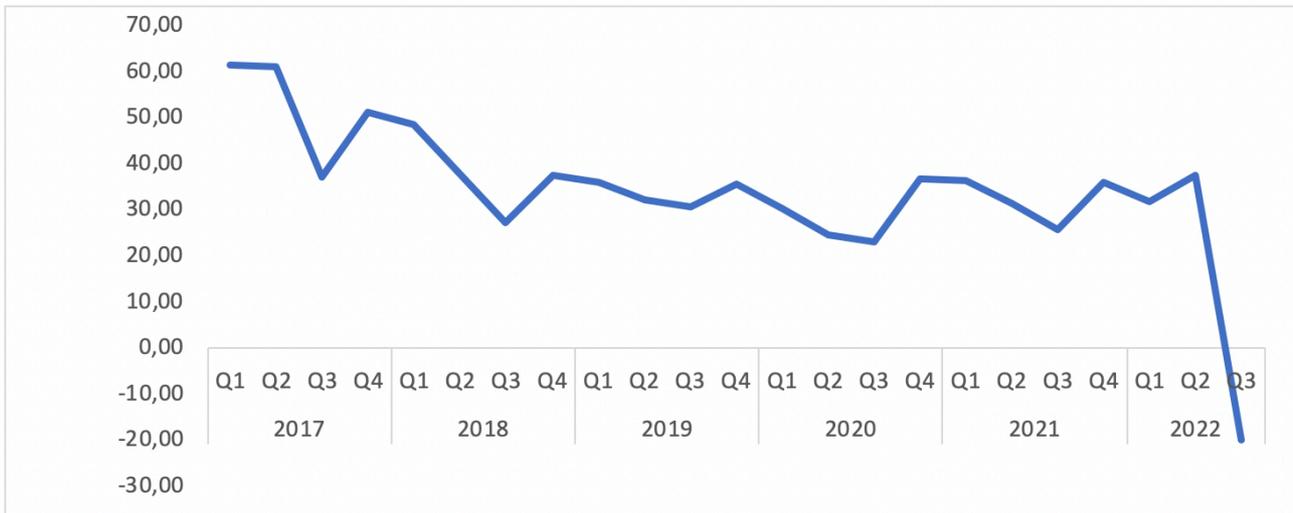
3. In Q3 2022 there was a net cash outflow on international remittances, for the first time since 2017. Traditionally, Belarus has seen a net inflow of foreign remittances. In 2022 Belarusian banks were switched off from the SWIFT system which incurred problems with operations in foreign currencies for banks under sanctions. As a result, cash inflow has declined (see Figure 3). Cash outflows however remained on the same level as in previous years. This can be explained by high-level specialists and people employed within ICT leaving the country. During relocation people have



sold apartments and cars and exchanged accumulated incomes from Belarusian Rubles to US Dollars or Euros and sent to

foreign bank accounts (even under the conditions of facing difficulties with conducting money transfers).

Figure 3. Net cash inflow (+)/ outflow (-) for international remittances, USD mln.



Source: Based on data from the National Bank of Belarus.

Maintaining the trend of net currency purchase together with possible trade balance deterioration may exacerbate the situation on the domestic currency market. Another risk to the currency market stability is posed by the insufficient size of FX reserves (in the amount of less than 3 months of import). Moreover, the 900 mln. US Dollars in reserves, given by the IMF in 2021 as support to fight Covid-19, can't be used as this financial support is given in the form of SDR (Special Drawing Rights), and the exchange of SDR to US Dollars or other currencies is challenging due to sanctions (Congress, 2022).

At the same time, the Government's decision to make external debt payments in Belarusian Rubles supports the FX reserves level. It has also been decided that payments on Eurobonds to the Nordic Investment Bank, the European Bank of Reconstruction and Development and the International Bank of Reconstruction and Development are to be paid in Rubles. These decisions have decreased the country's long-term rating on foreign liabilities to the Restricted Default level. In that sense, short-term gains can lead to significant financial losses in the long term.

In the future it will be necessary not only to pay outstanding debts but also to improve Belarus' reputation on the international financial market. Today, the Russian Federation is the main investor in the Belarusian economy. But since its support is limited, it is likely to be insufficient for the safe functioning of the Belarusian economy.

Conclusion

The stability of the Belarusian currency market is not the result of economic success, but rather a reflection of the tightening of the economy. The appreciation of the Belarusian Ruble to the US Dollar and Euro has taken place during an accelerated reduction in Belarusian imports. At the same time the weakness of the Belarusian currency to the Russian Ruble entails competitiveness of Belarusian products on the Russian market. Foreign exchange reserves, although insufficient, have maintained in size due to the low demand for foreign currency and foreign debt payments in Belarusian Rubles. Disruptions to economic and political relations with Western countries stimulates the Belarusian authorities to reorient the economy towards



Eastern partners, which has led to a modification of the currency basket composition. In the long run, the current stability of the Belarusian currency can quickly disappear in case one or several risks are realized. If the Russian Ruble devaluates or trade balance deteriorates and demand for foreign currency increases, the stability of the Belarusian Ruble exchange rate can be ruined.

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