

Investment Environment in Belarus

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Since independence, Belarus has faced challenges similar to those faced by other CIS countries: the transition from plan to market, the opening of the political process, and the continued delivery of the basic services in an environment of enormous change. Belarus undertook limited, yet sufficient reforms, in an increasingly benign external environment, to deliver significant economic growth and avoid the sharp drop in per capita incomes experienced by many of its neighbours. Rapid economic growth since 2002 reduced poverty in Belarus to one of the lowest levels in the region. Belarus maintains a strong, centralized state capable of mobilizing resources and allocating them to centrally-determined priority uses in the context of generally prudent budget management. Belarus has access to Europe, and has a skilled and highly capable labour force.

FDI Inflows into the Belarusian economy

Since 2007, Belarus has taken a significant step forward in liberalizing the economy and improving the investment climate. Increasing FDI attractiveness was set as a priority by the President.

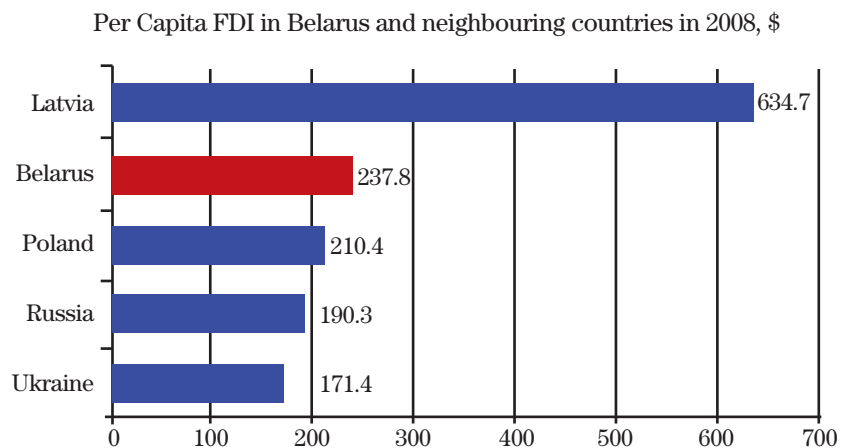
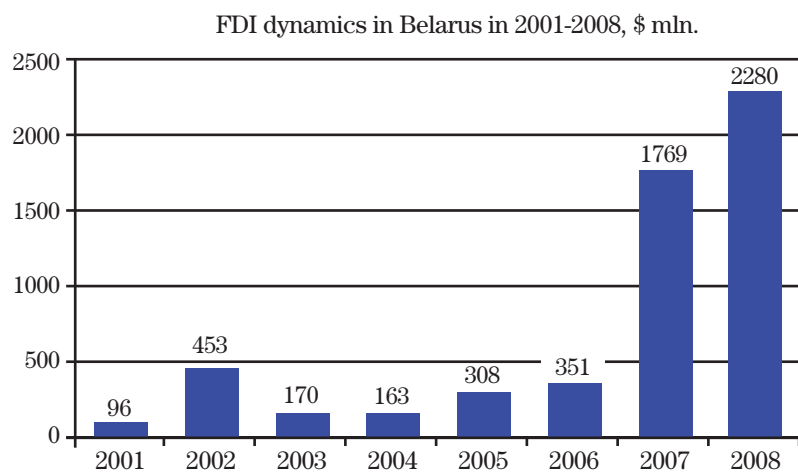
According to President Lukashenka, Belarus is to become one of the top-30 FDI recipients by 2010. Several important presidential decrees and government resolutions have been adopted concerning improvement of the investment and business climate. These include abolition of the “golden share” right; gradual abolition of the ban imposed on trading securities acquired during preferential privatization; announcement of the first list of enterprises to be privatized.

Governmental efforts have resulted in outstanding growth of FDI inflow (a fivefold increase). Within the past few years many foreign strategic investors have entered the Belarusian market:

- Russian: VTB, GazProm, Alfa-Group
- Western: Mobilkom Austria Group, TurkCell, Heineken NV, Generali & PPF, Baltic Beverages Holding

Firm steps have been taken by the Government and the National Bank towards creating and developing a national stock market. As a result, according to the World Bank “Doing Business 2009” report, Belarus is in the TOP-10 world reformers.

FDI inflows into Belarus have been steady growing over the last 5 years. 2008 FDI net inflow reached \$ 2.3 bln,



demonstrating 29% yoy growth rate. By 2008 FDI stocks in Belarus reached \$6.7 bln (3.5 - 3.7 times less compared to Lithuania and Estonia and 1.2 less than in Georgia). In 2008 Belarus ranked second among neighbouring countries by FDI inflow per capita. Last year FDI inflow into Belarus amounted to \$237.8 per capita, while in Poland it was equal to \$210.4 per capita, in Russia and the Ukraine -

\$ 90.3 and \$ 171.4 respectively. At the same time, FDI per capita in Lithuania reached \$634.7.

However, the situation with FDI attraction is not so evident. Nowadays, major part of FDI falls on credits and loans of parent companies to their subsidiaries (about 67% of the total FDI volume), and, therefore, new investments from strategic investors

are considerably lower. 1H 2009 results showed that 82.3% of FDI inflow for the period constituted different types of financial relations, like payables and receivables, between holding companies and their subsidiaries.

In spite of recent growth in FDI inflow, Belarus stands far behind the majority of countries in the region. According to UNCTAD, Belarus has the lowest index of FDI attraction effectiveness among its peer countries.

M&A activity in Belarus

The total estimated value of M&A deals in 2008 exceeded USD 1.5 billion showing a significant increase compared to 2006-2007. The number of M&A cross-border deals amounted to 21, with a total declared value of USD 831 mln.

These figures do not take into account the acquisition of Beltransgaz shares by Gazprom (the Belarusian budget to be paid USD 625 mln annually from 2007 till 2010). They also do not count for real estate industry transactions. The majority of deals were completed

- Food retail;
- Food & Beverages;
- Pharmaceuticals production;
- Telecommunications;
- Petrochemicals.

Investment sectors with prime appeal and potential

At present, the investment activity in Belarus is determined by the following key factors:

- 70% of GDP is still produced by state-controlled enterprises, including petrochemicals, oil-refining, raw materials, automotive and machinery, agriculture and food industries
- Government is taking clear steps towards liberalization of the stock market and privatization: abolition of the "golden share", issuing lists of hundreds of enterprises to be reorganized into open joint stock companies or sold to investors
- Deterioration of Belarusian terms of trade (growth in energy prices and tension of competition in traditional industries and markets in Russia) leading to a search for external sources of financing for the

liberalization. Assuming that it will, Uniter Investment Company considers the following sectors as the most attractive for investing (in some sectors privatization has been declared):

1. Financial Sector (Banking and Insurance):

Most developed in terms of corporate governance; Huge potential for development (during 2002-2008 Banks' equity grew 7 times, Total Assets soared more than 7 times but the penetration level remains low compared to peer countries); The Belarusian banks are still profitable and demonstrate high operational results despite of the crisis; Insurance sector has a very low level of penetration compared to peer countries. Privatization declared.

2. Telecommunications:

Less affected by the world crisis; Room for privatization (Beltelecom, MTIS – the leading national cable TV operator); Low penetration of telecom services compared to peer countries (Cable Networks, Internet).

3. Pharmaceuticals:

Good generic production base; Strong position at the local market (Pharma market is estimated at \$500 mio); Local producers still covers about 21.5% of the market, the rest is imported. Privatization declared.

4. Food and Beverages:

Sizeable domestic market (population of 10 m, significantly bigger than in Baltic States); High-quality local resource base (agricultural sector is heavily supported by the State); Low level of industry consolidation in some sub-sectors (milk and cheese production, meat processing);

Open niches with a high share of imports (juices).

5. Retail:

Low level of modern trade formats penetration (compared to the same on Russia or Ukraine) accompanied by the comparable income level and purchasing power.

6. Wood processing:

Rich local resources base (woods) compared

Sectors	Number of M&A transactions		Cost of M&A transactions, \$ bln.	
	2007	2008	2007	2008
Banking	7	6	87	175
Insurance	2	4	N/A	N/A
Leasing	0	2	N/A	N/A
Retail	3	1	N/A	11
Machinery	1	1	7	6
Transportation	0	1	0	6
Food production and processing	1	3	N/A	133
Telecommunications	1	2	350	500
TOTAL	15	20	444	831

in the financial sector (13 deals in 2008, and 9 – in 2007). The value of M&A deals in the banking sector reached USD 175 mln.

In 2009 we expect growth in M&A activity in:

Insurance sector and, probably, in banking (privatization)

Belarusian economy (issue of the first sovereign Eurodollar debt in 2009 expected).

However, future development of the situation will be determined by the steps, taken by the Government towards privatization and further

to EU countries; Excellent exports potential (EU markets).

7. Logistics: Excellent transit opportunities; Underdeveloped logistics infrastructure (no “A” class logistic centers until now).

8. Basic construction materials (cement, gravel, gypsum): 100% state domination in the sector; Strong domestic demand, strong exports potential due to closeness to potentially booming Russian market; Privatization declared.

9. Petrochemical complex: Solid industrial base created in the Soviet times (yarns and fibers, PET, basic petrochemical products, oil refining); Close oil and oil products transporting facilities links with the Russian Federation (main supplier of petroleum).

10. Energy sector: Underdeveloped sector, a serious restructuring is needed; Supported by the state due to reasons of the national energy security.

Belarusian capital market: development prospects

Recent developments

The Belarusian capital market played an insignificant role in the economic life of Belarus until 2008. The key reasons lay mainly in the legislative environment and taxation policy of the Government.

Market development was bound by the following negative factors:

1. 70% of Belarusian industrial enterprises are state-owned or state controlled.
2. In 1997 moratorium was imposed on selling shares acquired during preferential privatization.
3. Tax at a rate of 40% on profits received from securities trading was extremely high.

However in 2007- 2008, a large step forward was made by the Belarusian President and Government in creating a full-blooded capital market.

January	Passing of the National program for corporate securities market development
March	Presidential decree on “Golden share” right abolition
March	Presidential decree lowering taxation of security trading to the level of income tax: from 40% to 24%.
April	Presidential decree allowing unsecured bond issuance
April	Presidential decree on gradual abolition of ban imposed on securities trading acquired during preferential privatization
April	Important decision declared on control stake of the largest Belarusian Banks sale
May	A mortgage law was adopted
May	Announcement of the first list of enterprises to be privatized
June	Creation of a list of strategic enterprises and enterprises led out of the ban on trading their shares
July	Governmental resolution on OTC market trading limitations
July	On 17 July 2008, the resolution on share trading took effect. OTC market is almost closed for JSCs’ share trading
July	A list contained 140 enterprises to be privatized released by the Government
July	A list contained more than 500 enterprises to be transformed into public companies released by the Government
December	A list comprising 162 strategic enterprises released by the Government, unofficially launching a large scale privatization.

Infrastructure

The national system of security trading is organized on the basis of JSC “BCSE” (the Belarusian currency stock exchange).

The Belarusian stock market is represented by two segments: the organized market and the OTC market. Until July 2008, the organized market was not liquid. The largest volume of trading was provided through OTC. The share of organized trading did not exceed 0.1% of the total.

The Republic has a two-level depository system, which is one of the most advanced among CIS countries. As of 1 January 2009, the number of listed issuers reached 1749, while the

number of shareholders amounted to more than 1.5 million, consisting both of individuals and legal entities. As of 1 July 2009 the number of professional market players reached 71.

The major market instruments are the following:

- Shares;
- Bonds;
- Bills;
- Derivatives.