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NEWSLETTER

German Economic Team
BELARUS

The Belarusian banking sector faces new challenges

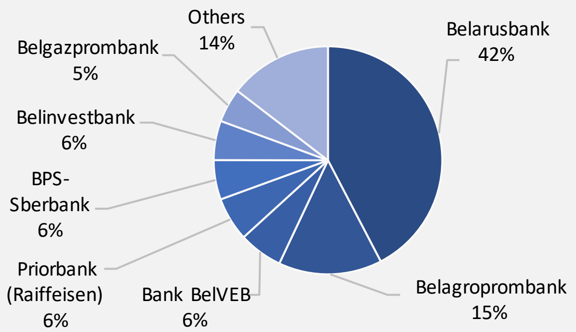
At first glance, not much has changed in the Belarusian banking sector. The number of banks has been constant for years at a total of 24. The size of the sector, measured by the ratio of assets to GDP, has also remained relatively stable. At the same time, about two-thirds of the sector is dominated by state-owned banks, which primarily provide financing to state-owned enterprises. Banks with Russian capital also play an important role, which leaves private (including Western) banks with a correspondingly small market share.

At present, the COVID-19 pandemic and political uncertainty are serious risk factors for the further development of the sector. The strong depreciation of the Belarusian ruble has negative implications for liquidity in the short term, as well as for solvency in the medium term. Banks still have some reserves, but these are limited. Consequently, large efforts should be made to preserve financial stability.

Only minor changes in the structure

There are 24 banks active in the Belarusian banking sector, with the total number remaining unchanged over the last few years. The size of the sector (in terms of assets) has also remained stable, amounting to around 56% of the gross domestic product (GDP) at the end of H1-2020. This makes the sector smaller than in Russia (96% of GDP) and Poland (99%), but slightly larger than in Ukraine (53%). The share of state-owned banks is traditionally very high (65% of assets), and Belarusbank has remained (with over 40% of assets) by far the largest (state-owned) bank for many years. Banks with Russian capital also play an important role, as they hold 22% of the assets. Overall, this leaves little room for private (incl. Western) banks.

Market share (Assets)



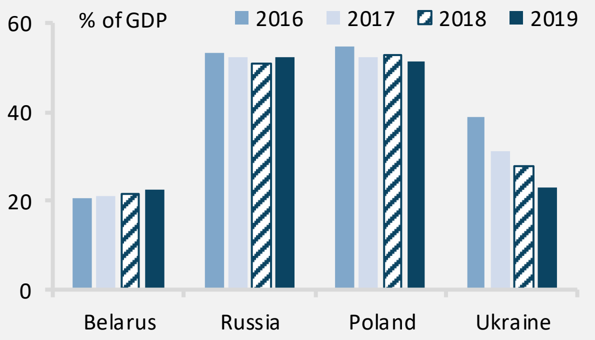
Source: NBRB, own calculations; data as of 01.10.2020

More than half (13 in total) of the Belarusian banks have a market share of less than 1% each. Against the backdrop of the COVID-19 pandemic and the ongoing political turmoil, the question arises as to whether the relatively small banks will be able to master these challenges and survive in the long-term.

Role of the private sector remains limited

There are clear links between the banking sector, which is dominated by state-owned banks, and the real sector, which is largely based on state-owned companies. Against this background, it is not surprising that lending to the private sector is significantly underdeveloped by regional standards.

Loans to the private sector



Source: National banks, own calculations; end of period

Until 2020, positive dynamics have been observed in private lending. Against the backdrop of recent developments, however, this could reverse again. Among other things, the volume of directed lending has been on the rise again – after years of decline – since May 2020. This may support the situation in the real sector in the short term but is accompanied by significant financial risks for the banking sector. Even if no significant increase in nonperforming loans has been observed in the statistics so far, this constitutes a credible risk scenario.

Exposure to new risks

As already mentioned, the banking sector is inherently intertwined with the overall macroeconomic situation. Here, the year 2020 has seen corresponding uncertainty and distortions on a global level due to the COVID-19 pandemic. The Belarusian ruble also saw a sharp depreciation, particularly at the end of Q1, which only eased again toward the middle of the year. In addition, there was another sharp rise in uncertainty after the presidential elections in August 2020, which resulted once again in a depreciation of the ruble. In this regard, it should be emphasized that Belarus has a relatively moderate amount of international reserves (currently USD 7.4 bn). In order to lean against the depreciation, the National Bank had to intervene on the foreign exchange market and significantly tighten

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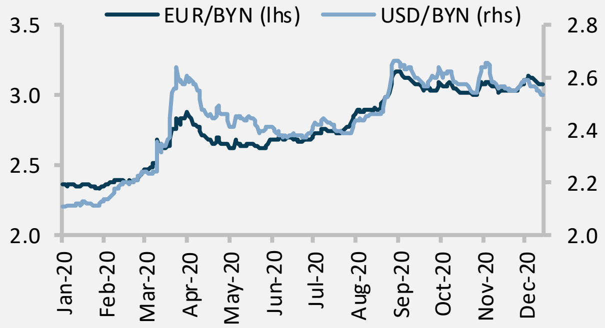
liquidity on the money market. As a result, overnight interest rates rose to as high as 25% in September.

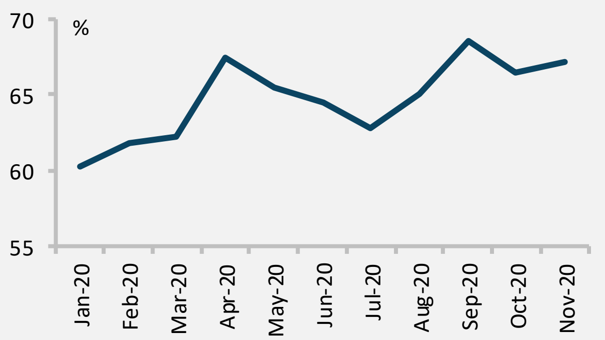
Development of the exchange rate



Source: NBRB

The increase in uncertainty has been followed by a corresponding increase in withdrawals of deposits from commercial banks. Despite interest rate hikes on new deposits in Belarusian rubles, no return of deposits has been observed so far. Moreover, the depreciation has significantly shifted commercial banks' balance sheets back towards foreign currency. This is an unfortunate setback, as the National Bank had been quite successful in the past in increasing the use of the Belarusian ruble in the economy. Meanwhile, almost 70% of corporate and household deposits are again denominated in foreign currency, primarily US dollar. This creates corresponding risks for the banks and reduces the efficiency of monetary policy.

Share of deposits denominated in foreign currency



Source: NBRB; data as of beginning of month; exchange rate effects are not considered

External debt remains quite substantial at around 9% of GDP (end of H1-2020). Refinancing options will in all likelihood deteriorate in the near future and the associated costs will rise. This is also reflected in the recent deterioration of the rating outlook for the larger banks and the state itself, which were changed to negative in November 2020.

Nevertheless, it should be emphasized that the Belarusian banking system remains well capitalized and profitable. For instance, the capital adequacy ratio at the end of the Q3 stood at 16.4% and the return on equity amounted to 8.6%. Even though a deterioration of the indicators has to be assumed due to the current developments, the banking system has a certain buffer in the short term.

Outlook

Since the summer at the latest, the negative economic effects of the COVID-19 pandemic have been overshadowed by the political situation in the country. In this context, the banking sector – as it does in all other countries – reacts very sensitively to corresponding developments, as "future" is being traded here in the truest sense of the word. In the short term, the tensions in the sphere of liquidity are clearly noticeable; in the medium term, a deterioration of key solvency indicators is to be expected – even though the available data is not sufficiently meaningful in this respect.

The tense macro-financial situation implies new risks for the heavily dollarized banking sector. The renewed increase in directed lending is also problematic: it may somewhat ease the financial situation of many state-owned companies in the short term, but comes at the cost of new risks in the financial sector. This kind of short-term stability can turn out to be costly in the medium term.

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