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Foreign Investments: Focusing on Debt[1]

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[1] This analytical report is translation from Russian and was published in "Belarusian Yearbook – 2013". The book is presented under the aegis of the Agency for Social and Political Expert Appraisal and the website of the expert community of Belarus Nashe Mnenie ('Our opinion'). http://nmnby.eu/yearbook/2013/en/index.html

Foreign Investments: Focusing on Debt

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Summary

In 2013 inflows of foreign investments in Belarus remained almost negligible. The official attitude to privatization remained unchanged, which is why there were almost no privatization deals in Belarus in 2013. This makes foreign loans the main source of inflow of foreign capital to the country. Because of the tough economic situation the placement of Eurobonds in foreign markets became a real challenge and forced the authorities to explore the domestic debt market. Some legislative moves were made to improve the business and investment climate of the country. Focus was placed on the protection of investors' rights and guaranteed right of dispute settlement.

Trends:

- Raising external financing turns out to be a serious problem;
- Lack of progress in the privatization process;
- A new instrument to raise funding is explored – the authorities start selling foreign currency bonds in the domestic market due to problems in external markets.

In 2013 the authorities planned to attract around USD 2 billion in a form of foreign direct investments (FDI) excluding foreign borrowing, and sell state assets at amount of USD 2.5 billion. According to official statistics, FDI equaled to USD 2.233 billion in 2013[2], meaning that the country succeeded in meeting the target. Moreover, FDI inflows grew compared with 2012, when they reached USD 1.442 billion[3].

On the other hand, in 2013 the balance of financial account closed with a deficit of USD 8.135 billion, compared with deficit of USD 961.2 million in 2012. Therefore, in 2013, inflow of foreign capital was mostly due to an increase in liabilities to foreign creditors. External liabilities grew by USD 7 billion in 2013 to USD 48.29 billion. Besides, the growth rates of external public debt are also quite alarming: as of 1 January 2014, external debt reached the level of 58.5% of GDP or USD 39.124 billion. Given that on

[2] http://nbrb.by/statistics/BalPay/Comment/2013.pdf
[3] http://nbrb.by/statistics/BalPay/Comment/2012.pdf

1 January 2013 external debt amounted to USD 33.766 billion or 54.6% of GDP, we observe an obvious negative dynamics.

One should remember that Belarus will have to make most of the payments to service its external debt in 2013–2014. In 2014 the country will have to pay USD 1.4 billion. Therefore, the significant growth of the country's external debt raises the question about sources to service the debt.

Foreign direct investments and privatization

There was no FDI breakthrough for the Belarusian economy in 2013. As it was mentioned above, the country raised USD 2.233 billion in a form of FDI in 2013. Reinvested earnings of Belarusian companies amounted to USD 1.2 billion (accounting for 54%), joint-stock capital accounted for 26%, and debt instruments formed the remaining 20%.

There is no difference between 2013 and the previous periods when it comes to foreign investments. The macroeconomic imbalances, high devaluation expectations and high inflation rate discouraged both foreign and domestic investors. Besides, the increased state stakes in two major confectioneries – Kommunarka and Spartak – which essentially resulted in nationalization of both producers, stopped some investors from operating in Belarus. As a result, the country failed in meeting its privatization targets, and there were virtually no transactions of selling state assets. Nevertheless, there were some M&A transactions with a foreign capital involved. However, in most cases both parties were privately-owned businesses rather than state-owned enterprises.

In the beginning of 2013 RTL-Holding, which owns the Rublyovski retail chain, purchased 78.5% in CJSC Nevel, paying a total of USD 3.3 million. In autumn 2013 the chain expanded its presence in Belarus by buying a controlling share in the Volgograd supermarket store for USD 6.7 million. Further, a financial holding Getin Holding purchased 95.5% of Belarusian Bank for Small Business for approximately EUR 4.87 million. At the end of the year it was announced that the authorities had reached an agreement with a Russian investor to sell a stake in OJSC Minsk Wheeled Tractor Plant (the producer will have an additional share issuance). Finally, a 99.5% of OJSC Belgips was sold to Russian Volma corporation for USD 5.27 million.

One of the peculiarities of 2013 was the growth of deals with Belarusian investors acquiring both local and foreign companies. Belarusian agricultural holding CJSC Servolux acquired 49.93% of shares in OJSC Smaliavicy broiler plant for Br430.2 billion. Furthermore, in spring, joint Belarusian-German venture Santa Bremor purchased CJSC Russkoe more for USD million.

Evrotorg LLC expanded its presence in Russia and increased the number of its stores to eleven. In the summer 2013, the company acquired company Prevar that is based in Fanipol in order to build its meat-processing facilities there. Finally, in September 2013 the Alutech group bought German Gunther-Tore that is a producer of sectional and rolling gates. The deal enabled the Belarusian Company to access the markets of Western Europe, Asia and Africa and become one of the leading producers of gate components in Europe.

Portfolio investments

The difficult economic situation affected the market of portfolio investments. In 2013 Belarus continued advertising of its debt instruments and negotiated opportunities for placing sovereign bonds in Europe, Singapore and China. The country held a series of road-shows in Germany, Switzerland, the United Kingdom and Asian countries. However, the presentations of Belarus' investment opportunities did not have the desired effect and the question remained open and unfinished.

The situation with the debt instruments placed previously remains vague. The first half of the year turned out to be quite favorable for Belarusian Eurobonds with maturity in 2015 and 2018. In May 2013 the yields to maturity (YTM) of Belarusian sovereign bonds hit the bottom of the annual level. The YTM of the five-year Eurobonds with maturity in 2015 amounted to 5.83% (compared with a yield of 8.7% set during placement) and YTM of seven-year Eurobonds with maturity in 2018 equaled to 6.19% (the original yield was set at 8.95%). However, the conflict with Uralkali produced a devastating impact on the Belarusian debt securities, and yields hiked to 11.9% (five-year bonds maturing in 2015) and 11.46% (seven-year bonds with maturity in 2018). Once the conflict was resolved, the situation improved, and at the end of the year yields settled at 7.55% and 8.5% respectively, while prices stood at USD 101.2 and USD 101.4.

The difficulties that Belarus faced while trying to enter foreign markets encouraged the authorities to issue and place foreign currency-denominated debt instruments in the domestic market. Back in December 2012 the first two issuances were placed, totaling to USD 50 million. In January and May 2013 further issuances occurred with a total sum of USD 100 million. In September another attempt of selling state bonds at amount of USD 100 million was made. However, bonds at amounts of just USD 22.51 million were sold to the households. The government is seriously planning to use this debt instrument in the future. In 2014 the Ministry of Finance of Belarus plans to borrow up to USD 900 million in the domestic market, where USD 100 million will be formed by the funds of households and USD 800 million will be sources of the companies.

Other external liabilities

Other external liabilities increased significantly in 2013 (by USD 4,829.1 billion), while in 2012 they dropped by USD 578.5 million. Therefore, the share of other foreign liabilities in the total amount of foreign investments attracted in 2013 formed 69%. Most of the funds were raised through external borrowing of the authorities and commercial loans.

In January and April 2013 Belarus received the fourth and fifth installments of the EurAsEC Anti-Crisis Fund (ACF) loan at a total sum of USD 880 million. The country expected to receive the sixth and final installment of the loan in November-December 2013. However, the Council of ACF decided to postpone the allocation of the loan for six months due to disappointment with the way Belarus meets its obligations. As of today, ten out of 14 conditions have not met yet. Five of them (including the annual privatization of the state assets at amount of at least USD 2.5 billion) are the so-called 'check' parameters. Other important loans include the USD 377.8 million export loan issued by Russia for the construction of the Belarusian nuclear power plant. Besides, Chinese banks provided loans totaling USD 333.8 million, and the International Bank for Reconstruction and Development (IBRD) gave a USD 105.5 million loan to Belarus.

Privately-owned businesses faced difficulties in attraction of internal capital and due to that had to look for external lenders. The A-100 group received a seven-year loan from the European Bank for Reconstruction and Development (EBRD) worth USD 10 million. It is planned that the money will be invested in the group's network of filling stations. The EBRD also provided an eight-year loan to private company Kronospan for the construction of a woodworking facility, which will specialize in production of oriented strand boards. OJSC Belarusian Metal Plant (BMZ) reached an agreement with the Eurasian Development Bank (EDB) and OJSC ASB Belarusbank about a USD 280 million loan for the construction of a small-section and wire mill. In autumn 2013, an agreement between Evrotorg LLC and Sberbank of Russia was reached. As a result the Belarusian company will receive a USD 150 million credit facility, which will be used to build several shopping centers in Minsk. In December 2013 OJSC ASB Belarusbank attracted another USD 110 million syndicated loan from a group of Russian commercial banks.

Arrangements to raise external financing and improve investment climate

In summer 2013 two legislative acts were passed of investors and the expert community, and so did some other legislative initiatives of the authorities.

1. Law No.53-3 'On investments' dated 12 July 2013

The law came into force on 24 January 2014[4]. The document expands the notion of 'investments', which now covers movable assets and real estate, rights and claims with appraised value and other entities of civil law rights having appraised value. The law spells out the main principles of investing, inadmissibility of interfering into investors' private business and equality of investors' rights, along with the protection of their rights in case of violations. Further, the law makes it possible for an investor to claim for compensation for nationalized business in any foreign currency. In addition, according to the law, efforts to resolve investment disputes will be meet the regulations of international agreements, and disputes will be settled not only in Belarus, but also in an arbitration court or the International Center for Settlement of Investment Disputes.

2. Law No.63-3 'On concessions' dated 12 July 2013

The law came into force on 26 January 2014[5]. Concession contracts were available to investors even before the new law became effective. However, it was this new document that allowed concession agreements not only at the national, but also at the local level. Furthermore, the law guarantees that the state will not interfere with investors' business and protects investors' rights, specifically in case of legislative changes. In addition, the document allows settling disputes in international courts of arbitration. Finally, if an investor successfully implements a concession contract, it will have a chance to make a new concession agreement on special terms and without any tendering procedures.

Therefore, these legislative acts make adjustments to the investment environment of the country and essentially offer foreign and domestic investors equal rights. It should be noted that over the last few years, the inequality between foreign and Belarusian investors was considered to be one of the most serious barriers to businesses entering the Belarusian market.

3. Resolution of the Council of Ministers No.241 'On some arrangements to facilitate the development of small and medium-sized entrepreneurship in the Republic of Belarus' dated 30 March 2013

The document aims to increase the role of small and medium-sized business in the Belarusian

[4] http://www.pravo.by/main.aspx?guid=3871&p0=H11300053&p1=1
[5] http://www.pravo.by/main.aspx?guid=3871&p0=H11300063&p1=1

economy[6]. The resolution comprises some of the approved development targets for 2013–2015 and a set of measures to reach these targets. One of the measures is the preparation of a bill to amend the law on privatization of state property and transformation of state unitary enterprises into open joint-stock companies. The bill envisages some arrangements to support private business; specifically, it bans any revisions of privatization results upon its completion.

As is known, the state annually sets itself ambitious privatization targets. However, the nationalization of the leading companies of the confectionery sector OJSC Kommunarka and OJSC Spartak, non-repayable transfer of a 21% stake in OJSC Luch to the state and probable transfer of a controlling stake in OJSC Krasny Pishchevik and OJSC Keramin to the state alarm investors, who seem increasingly concerned about the way Belarus protects investors' rights. Therefore, the resolution is designed to give foreign investors a clear signal that the situation has improved and the Belarusian economy remains an appealing investment destination.

Conclusions

The privatization plan for 2014 assumes sales of state assets at amount of at least USD 4 billion. It is quite likely that in 2014, Belarus will have to get rid of some major state-controlled assets, as privatization remains virtually the only source of attraction of external financing, which is crucial for the national economy. The decision of authorities to reduce the selling price of its share in JLLC MTS at the end of 2013 is an indirect proof of changes in official approach to privatization. The 51% stake in the mobile operator is currently available at a price of USD 863 million (the original price was set at USD 1 billion). Another signal indicating that the authorities are ready for privatization is the decision of the government to allow state companies to get rid of non-core assets. This move may increase the effectiveness of state assets and attract investors, who have repeatedly pointed to the lack of objectivity in price formation.

In 2014, Belarus will continue issuing and placing foreign currency bonds in the domestic market. When it comes to Eurobonds, Belarus will attempt to raise up to USD 700–800 million by placement of its debt securities via VTB Capital and Sberbank CIB. However, the final decision about new issuances will depend on the economic situation in Belarus and the world.

The problems accumulated in the national economy suggest that the pattern of raising foreign resources will change in 2014. The need for economic reforms remains in place and encourages the authorities to revise their attitude to the privatization process and use it as an instrument that can

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[6] http://pravo.by/main.aspx?guid=3871&p0=C21300241&p1=1

facilitate the renewal of production assets and introduction of innovation, which are important prerequisites for enhancing the competitiveness of the Belarusian economy.