Executive Summary

Twenty-five years after the dissolution of the Soviet Union, Belarus stands out as a special case in transition blending, on the one hand, signs of relative prosperity, socially oriented policies and sprouts of entrepreneurships and, on the other hand, remnants of the communist past. The core of the Belarusian economic model throughout most of this period was a combination of external rents and soft budget constraints on the state-owned part of the economy backed by a strong system of administrative control. In periods of favourable external conditions this mix provided for relatively high rates of economic growth and allowed the authorities to maintain a 'social contract' with the population targeting close to full employment. But this model also led to the persistent accumulation of a quasi-fiscal deficit which time and again came to the surface, and its subsequent monetisation provoked macroeconomic and currency turmoil. At present, Belarus' economic model has run up against its limits and policy changes seem inevitable.

Is Belarus a transition outlier?

The unique experience of Belarus defies many beliefs about the nature and the features of the process of post-communist transition. Belarus embarked on a transition path of its own, different from what was happening in other countries but still delivering a peculiar path of economic transformation.

By the conventional measures of 'progress in market reforms', Belarus is basically 'frozen' in a state of stalled, unfinished market reforms, a point that most other post-communist countries passed by already in the mid-1990s. By this token Belarus lags behind not only the more advanced Central and Eastern European economies but also the countries of the Commonwealth of Independent States and Ukraine.

At the same time, during both of the past two decades, GDP growth in Belarus was higher not only than the average in its closer neighbours, but also than that of the countries of Central and Eastern Europe (CEE) as well as the average rate of GDP growth in Southeast Europe. As a result, Belarus achieved a considerable degree of catching-up: by 2015 Belarus' GDP per capita reached some 70% of the CEE-11 average, up from 48% in 1995. Thanks to its policies of social welfare and internal cohesion, Belarus also achieved a relatively equitable distribution of the growth dividend.

At the same time, Belarus was the country with the highest average inflation rates among all economies in transition; it did not manage to achieve lasting macroeconomic stabilisation and was hit by several subsequent currency crises. Thus in many ways Belarus challenges some of the conventional wisdoms about the transition process: it has been visibly different from other transition economies, following its own transition path, pursuing different political and policy objectives and achieving different outcomes.

How was Belarus different from others?

The mainstream interpretation of Belarus' opaque transition path (also upheld by most international financial institutions) is that Belarus has been buying time to delay inevitable reforms thanks to rents extorted from Russia in exchange of political concessions. The Belarusian authorities did that by negotiating energy subsidies from Russia in exchange for political loyalty and alliance with its big neighbour. Belarus negotiated access to Russian gas and oil at prices significantly below world market prices which resulted in direct subsidies to Belarusian businesses and consumers; plus, it could export processed fuels and other oil- and gas-based chemicals at international prices. All this was equivalent to an implicit cash transfer to Belarus.

Other interpretations drawing on the political economy of transition look at delayed reforms as a rationale choice of local politicians and policy-makers. In most transition economies, the choice of the reform course was not a premeditated policy choice but a self-imposed one, forced by the limited available options. Only countries that had sufficient available or accessible resources to cushion the transition shocks could make deliberate choices on their policy course. Thanks to the long-lasting 'loyalty rent' from Russia, Belarus was among the very few post-communist economies that could make such choices with longer planning horizons.

One original interpretation of Belarus' unique experience draws on the notion of organisational capability and associates its decent growth performance with the preserved organisational capability of the country. Thanks to strong central controls Belarus prevented asset stripping in state-owned enterprises, reduced rent-seeking behaviour, prevented disorganisation and preserved engineering and production capabilities.

Yet another specific in Belarus' transition was the 'social contract' with the population under which the authorities provide stability, order and low levels of income inequality. It has been pointed out that the social values prevailing in Belarus and this 'social contract' played a special role in the way transition evolved in Belarus.

Belarus' unique economic model

It has been suggested by Belarusian economists that the political and economic system that evolved in Belarus can be classified as 'state capitalism'. Such a categorisation differentiates it from the previous system of central planning but also highlights the significant role that the state plays in the economy.

The backbone of the political system is the highly centralised decision-making pyramid, featuring excessive powers concentrated at the top. Belarus adheres to a lopsided presidential system, in which the president de facto has greater power than the legislative branch (a 'super-presidential' political system) while the National Assembly has limited autonomous powers even in its legislative mandate. The members of the Council of Ministers are directly appointed by the president; the Council serves mainly to operationalise the rulings coming from the president's office.

Belarus pursues long- and medium-term policy objectives through 'state programmes' which usually cover a five-year cycle. There is a complex hierarchy of such programmes which is topped by the so-called 'programmes of socio-economic development'. As regards day-to-day policy-making and implementation, there exists an elaborate system of legislative and regulatory arrangements which prescribe specific top-down mechanisms of administrative control over the economy.

However, a deeper and more critical look at the Belarus model of ‘state capitalism’ reveals one key feature that weakens this self-assertion, namely, the absence of hard budget constraints on the operation of state-owned firms. So there is still much more ‘state’ than ‘capitalism’ in the Belarusian economy of today.

In principle, the state has all the levers to impose hard budget constraints on the firms that are under its patrimony. However, the fact is that Belarusian state-owned firms and banks still largely operate under soft budget constraints. State-owned banks have been actively engaged in financial support to state-owned firms, in particular, related to the implementation of different state programmes through the so-called mechanism of ‘directed lending’. Such loans are extended at preferential terms (below market interest rates) for the beneficiaries while the banks were subsidised by the government for the interest rate differential. Directed lending generated market distortions and had serious negative micro- and macroeconomic implications – such as the erosion of incentives of SOEs to restructure, deterioration of the quality bank portfolios and economy-wide misallocation of resources – and, ultimately, led to macroeconomic instability.

No privatisation but growth of a de novo private sector

One of the key differences of post-Soviet Belarus from other transition economies has been the restraint on large-scale privatisation of state-owned firms inherited from Soviet times. Privatisation has been a sensitive and contentious economic policy issue and the authorities have been reluctant to embark on privatisation on a mass scale; only a handful of experimental deals were launched. Some institutional change did take place in the management of state-owned firms mostly in terms of corporatisation – the transformation of Soviet SOEs into corporate business entities.

The reasons behind the repeated privatisation failures are complex. Apart from the lack of political will, there has been a systematic conflict between ask and bid prices as the authorities usually based the ask price on book value while potential investors assess the ‘going concern’ value of the businesses, which is usually much lower. The government also would pose additional post-privatisation requirements and conditions, mostly about preserving employment and output levels, which make the offer unattractive to investors. Plus, potential investors perceive high political risks in Belarus, after several re-nationalisation cases. As a result the few privatisation opportunities in Belarus mostly attracted Russian state-owned corporations. The latter have been able to set prices in closed-doors non-transparent and often politically driven negotiations. Such Russian investors also de facto have sufficient political power of their own to ensure their property rights after the privatisation.

Consequently, the state sector still dominates the economy of Belarus, both in terms of ownership and employment. State ownership prevails especially in the sector of manufacturing; at the other end of the spectrum are the sectors of retail trade and business services. While privatisation has been largely absent in these sectors too, the private sector is already by far the dominant one in most business services, both thanks to the organic growth of de novo private firms and the entrance of foreign firms on the Belarusian market.

Economic governance subordinate to state targets

The governance of SOEs is integrated into the Belarusian administrative system, within the ministries with functional responsibilities in economic policy implementation. The most important governance tool used to be the system of 'state targets' that are communicated from the top to individual state-owned firms and, in some case, to all economic agents. The targets have a hierarchical structure starting from key macroeconomic objectives in the programmes for socio-economic development. These are then translated into annual ones, which are in turn translated into indicative targets by sectors and regions, lower-level indicative economic performance targets as well as main targets for state-owned companies.

This system prevailed during the 1990s and 2000s but it has been weakening in recent years as direct interference into the operations of state-owned companies was diminishing. Nevertheless it has had lasting effect on the performance of firms and banks which are still under state ownership.

There has been a persistent productivity gap between the state sector and the private sector which negatively affected the overall growth in the country. Labour hoarding is key evidence of SOEs' inefficiencies and poor performance. Maintaining or increasing employment levels is usually one of the performance targets of the enterprises, and this in itself is a barrier to restructuring. Directed lending also contributed to inefficient corporate performance as access to cheap loans made SOEs eager to overinvest in physical capital. Moreover, it creates wrong incentives in inefficient companies, as soft budget constraints serve to discourage restructuring.

Energy and agriculture are two sectors that epitomise the opaque system of explicit and implicit subsidies that give rise to soft budget constraints and generate quasi-fiscal deficits.

Distorted financial intermediation leading to misallocation of resources

According to its formal legal status, the National Bank of the Republic of Belarus (NBRB) is 'independent in its decision-making', however, it is subject to informal pressures coming from the top which affect the central bank's decisions. This has implications not only for its relations with commercial banks but also for its wider monetary and exchange rate policy decisions.

The banking sector has a dominant role in the Belarusian financial system as capital markets are practically inexistent. The state still maintains a dominant position in Belarus' commercial banking system: state-owned banks account for some 66% of the total assets of the banking system.

The business model of state-owned banks implies using the capital base as an additional funding source for active operations thanks to their relatively high capitalisation. This translates into greater (compared to private banks) credit exposures including in directed lending by some state-owned banks. On the liability side, state-owned banks enjoy a relatively high share of deposits, largely due to informal instructions to state-owned enterprises to hold their accounts in state-owned banks. In the case of households, state-owned banks are successful in attracting deposits mainly due to their large regional networks.

In the past several years the profitability, capital adequacy, and key indicators of the banking sector have been deteriorating primarily due to an increasing share of non-performing loans in the banks' balance sheets.

Flexible labour contracts and low unemployment protection

The labour market in Belarus has some specific features: on the one hand, it is characterised by flexibility in terms of the duration and conditions of the employment contracts and, on the other hand, by excessive regulation generating rigidities.

The availability of employment opportunities has been an important part of the social contract in Belarus. The principal declared objective of public labour market policies have been the access to jobs for everyone as well as rising personal income, in the first place, through wage growth, in the absence of significant wage differentials. The main policy instrument to target desired wage levels has been the wage scale regulating the salaries for every profession.

There are two types of employment contracts in Belarus: permanent and fixed-term. Most of the employers prefer the fixed-term contract, with the usual duration of one year. This contract does not carry commitments for renewal of the employment after its expiration. It also allows firing an employee with only three-month severance payment if the occupied position is abolished. Thanks to the flexibility of the labour market in terms of contracts, employment has gradually shifted from less productive and low-paid jobs in agriculture and manufacturing to the emerging and rapidly growing services sector.

Economic growth in Belarus during the past two decades was pro-poor, delivering some benefits of growth to everyone, decreasing poverty and preventing high inequalities in the society. The period from 2000 to 2015 saw a 4-fold increase in average real disposable income. As per the 'social contract', the government did not rely on targeted handouts to vulnerable groups but instead sought to provide everyone with opportunities to find a job, offered a wide range of complimentary services and subsidised some prices and tariffs.

At the same time, Belarus is a socially-oriented state without proper unemployment insurance or unemployment benefits. Technically unemployment benefits for the registered unemployed do exist, but they are very low and do not depend on the previous wage level. Moreover, to obtain the benefit the registered unemployed often have to participate in social or public works for free.

Still eastbound trade …

Historically Russia has been the most significant trading partner of Belarus both in terms of exports – over a half of total, and imports – over a third of total. The EU-28 has also been prominent as a destination for exports, as well as a significant origin of imports. Exports to Russia are relatively diverse, comprising, besides commodities and agricultural/food products, also transport equipment and machinery; imports are dominated by petroleum products. By contrast, exports from Belarus to the EU are mostly comprised of mineral fuels, while imports are formed by more advanced goods, including chemical products, machinery and transport equipment.

Mineral fuels traditionally dominated both exports and imports as the key commodity group, constituting over a third of the country's total trade with a wide gap from other products. Belarus inherited large oil refineries from the Soviet Union and processes crude oil coming from Russia into refined fuels, gasoline, etc., to be further exported to the EU. Over time, the share of primary commodities in Belarusian exports has been gradually increasing and squeezing the share of manufacturing exports that could only find a market niche predominantly in the CIS region. The global competitiveness of Belarusian industries is mostly concentrated in agricultural and food products, as well as chemicals.

Both exports and imports of services have been growing steadily in the past 15 years. The positive balance in services trade partly offsets the chronic deficit in the trade in goods. In terms of their composition, services exports are dominated by the transports sector, with transit freight transportation via railway, motor transport and pipelines being the key modes of transport. Also, the ICT and travel sectors increased their shares in the total services exports. The import side is dominated by construction services, transport and travel.

… FDI flows …

FDI inflow in Belarus was marginal before 2007, but since 2008 annual inflows have been fairly stable, amounting to about EUR 1.5 billion per year. After controlling for the size of the country, Belarus has received more FDI than some of its neighbours but less than the new EU Member States.

FDI in Belarus is mainly of Russian origin, amounting to nearly 60% of the stocks. Some Western companies are also finding their way to Belarus also through Russia. In addition, FDI from Cyprus is in all likelihood of Russian origin as well, thus the direct and indirect FDI dependence on Russia is probably greater. The second most important investor by a large distance to Russia is Austria, which accounts for only 3.5% of the FDI stocks.

A significant part of FDI has taken place in the framework of large privatisation transactions; joint ventures with state-owned enterprises and greenfield investments account for smaller stocks. The low number of greenfield investment projects – which are the genuine FDI enterprises – is telling proof of the difficult business conditions in the country. Joint ventures between local state-owned companies and foreign investors are FDI practice favoured by the authorities of Belarus. While the number of such deals is considerable, they do not contribute to larger inflows.

Most of the greenfield FDI projects in Belarus are located in special economic zones. Three such forms exist in Belarus: six free economic zones, a Chinese-Belarus industrial park and the Belarusian High-Technology Park. Special zones can be useful vehicles of FDI policy especially in countries with a risky business environment and vague property rights.

… and integration ties

Traditionally, Belarus' external economic relations have been closely associated with its strong economic linkages with Russia and, more recently, with the Russia-led Eurasian integration project. Eurasian economic integration has been progressing very fast formally, starting from the formation in 2010 of the Eurasian Customs Union by Belarus, Russia and Kazakhstan. Two years later the bloc was replaced by the Eurasian Customs Union–Single Economic Space, and in 2015 by the Eurasian

Economic Union (EAEU). The latter also expanded geographically and now includes, besides the three founding members, also Armenia and Kyrgyzstan.

While the customs union arrangement dealt only with the liberalisation of mutual trade in goods via elimination of tariffs and introduction of a common external tariff, the EAEU will seek to bring integration to a qualitatively new state reaching beyond trade-related matters, and also facilitating the so-called ‘four freedoms’ – a common market for goods, services, capital and labour, as well as the coordination of economic policies and energy markets, which is envisioned to be accomplished by 2025.

Concurrent membership of the EAEU members in the WTO represents a challenge. Belarus remains the only country within the bloc that is not a WTO member and, in general, among the very few countries in the world still not in the WTO. At the same time, it has to indirectly adhere to WTO rules via commitments of its EAEU partners. Belarus itself still appears to be rather far from satisfying the original demands expressed by the WTO related to agricultural subsidies and the high level of government involvement in the economy.

A growth model leading to macroeconomic instability …

During the period 1996-2008 Belarus enjoyed a period of high growth thanks to, on the one hand, a favourable external environment (the re-integration with the Russian economy which opened the way for Belarusian exports and external rents) and, on the other hand, expansionary policies promoting fixed investment and rising incomes.

Things started to change around 2007 when Russia began claiming back part of the Belarusian export oil duties and doubled the gas export prices for Belarus. The Belarusian authorities were faced with a dilemma: to change the policy course more radically (which would eliminate the demand surplus supported by rents) or to keep it while searching to attract additional external resourced compensating for the reduction in rents. The first policy option would have been associated with unpopular austerity measures, so the authorities opted for the second solution.

The combination of a policy focused on demand-driven growth and diminishing external rents resulted in a persistent widening of external imbalances and fast growth of foreign indebtedness: in the second half of the 2000s, Belarus’ current account deficit kept growing, reaching over 15% of GDP in 2010 while gross external debt quadrupled between 2005 and 2010.

One of the main sources of macroeconomic imbalances was the quasi-fiscal deficit resulting from inefficient directed lending and soft budget constraints. Directed credit, one way or another, entailed contingent fiscal liabilities as it was de facto underwritten by the Belarusian state. The bad loans resulting from inefficient directed lending ultimately accumulated as a quasi-fiscal deficit.

The other main source of macroeconomic imbalances was the populist incomes policy which prevailed through most of the period of high growth. Mandated wage increases resulted in significant rises in unit labour costs and competitiveness losses as real wage growth outstripped productivity growth. This was also a source of inflationary pressure as there were no checks on the pro-inflationary effect of wage growth. In effect, monetary policy completely accommodated the upshots of expansionary incomes policies; plus, the quasi-fiscal deficit resulting from directed lending was gradually transformed into an open deficit and was also monetised.

Thus both soft budget constraints and inconsistent incomes policies ultimately generated inflationary pressure and microeconomic instability.

… which has hit its limits

The policy mix prevailing n 2003-2007 was in broad terms a combination of: (i) exchange rate peg; (ii) monetary stimulation; (iii) direct wage stimulation; and (iv) fiscal stimuli (directed at the stimulation of both consumer and investment demand). Trying to mitigate the chronic pressure in the currency market, the authorities resorted to active external borrowings and this happened against the background of a considerable gap between the equilibrium exchange rate and the actual one. As a result, there was a sharp rise in foreign debt after 2008.

Given the built-in inconsistencies of the underlying policies, between 2009 and 2015, Belarus experienced three episodes of currency crises (in 2009, 2011 and 2014-2015) which epitomised the inconsistency of the macroeconomic policy mix. All three cases entailed a massive forced devaluation of the Belarusian rouble reflecting the necessary real exchange rate adjustment.

The policy setup stayed roughly unchanged until end-2014, perpetuating macroeconomic disequilibria. More emphasis on demand stimulation now led not only to a price overhang and a delayed impact on the real exchange rate, but also to direct pressure on prices and the exchange rate through less demand for national currency and more for hard currency. These inconsistencies further reduced the effectiveness of the policy efforts to boost output and incomes.

Is Belarus moving towards a new policy model?

At the turn of 2014, it became evident that the currency peg could no longer be sustained. In several steps, the authorities undertook a complete overhaul in the macroeconomic policy setup. In the first place, the currency peg was abandoned and a floating exchange rate regime was adopted. At par with the change in the exchange rate regime, monetary targeting was announced as the NBRB policy framework with rather restrictive targets for 2015. In turn, the government declared its intention to abolish or curb some of the demand stimulation tools.

The policy setup at present could be summarised as follows: (i) floating exchange rate framework; (ii) monetary targeting with a tight intermediary goal; (iii) fiscal policy tightening; and (iv) less reliance on unconventional demand stimulation tools (directed credit, wage stimulation, etc.).

The introduction of the floating exchange rate regime brought about positive outcomes by helping restore equilibrium and serving as a more effective shock-absorber. A relative tightening of fiscal policy also accompanied the dramatic changes in the monetary sphere. In particular, there were significant cuts in public capital expenditure as well as a reduction in the public procurement of goods and services and budget transfers.

The macro environment in Belarus changed. Before 2015, the stylised macroeconomic picture was a combination of, on the one hand, GDP growth (albeit weakening in recent years) and low unemployment, and, on the other hand, substantial current account deficits, exchange rate overhang and high inflation. After 2015 the picture changed to the reverse: the actual exchange rate roughly corresponds to the equilibrium rate, the current account deficit is close to its estimated mid-term equilibrium and there are signs of disinflation; but this was coupled with output contraction and growing unemployment. In terms of GDP growth, 2015 was the worst year in the past two decades.

Belarus is now facing new challenges and risks to financial stability …

In the current macroeconomic environment, Belarus needs to find new impetus to invigorate growth. The question is whether and how policy can contribute to such impetus, given the challenges that policy-makers are facing at present.

High inflation expectations have become a challenge for the monetary authorities in many respects, effectively reducing its room for manoeuvre. They drive up real interest rates and curb fixed investment. Hence firms may be reluctant to invest, having in mind the poor growth potential and the low expected returns on investments even in the case of an improving external environment.

Suppressing inflation expectations can be regarded as one of the priority goals of monetary policy and macroeconomic policy as a whole. Although the monetary targeting regime reduces the risks of currency crises, it does not help in addressing the problem of high and persistent inflation expectations (the Belarussian rouble was re-denominated in mid-2016).

Breaking the current constellation of ‘dampened capital investments’ requires numerous changes relating both to structural and short-term issues and securing a stable monetary environment. Instability in expectations causes an obvious conflict between the price stability and output smoothing goals for the NBRB. From this viewpoint, prioritisation of price and financial stability leads to a tough stance of monetary policy in terms of output, which dampens business activity.

These policy challenges are amplified by new risks to financial stability, in particular, the growing debt problems which pose risks for future macroeconomic stability. At the micro level, two groups of firms – state-owned enterprises (particularly the beneficiaries of directed lending) and foreign currency borrowers – were the most affected with respect to debt sustainability. The recession of 2015 and the significant depreciation reinforced the debt service problems.

As regards the banking sector, there has been an increase in non-performing loans. The reported share of NPLs, which has already reached an alarming level, may still underestimate the real situation due to irregularities in accounting and reporting practices.

The growing corporate debt burden could be damaging in many respects. The companies facing debt problems are to give up or downsize their investment plans. Banks that are burdened with non-performing loans are forced to provision, which affects their lending capacity and reduces borrowing opportunities which impacts negatively on economic activity. Substandard portfolios affect banks’ operations; further deterioration may be a threat to their solvency, potentially creating risks for the banking system as a whole.

The authorities are aware of these risks. Banks facing deteriorating quality of assets have been advised to seek recapitalisation; however, this may be difficult to implement, especially for state-owned banks. Recapitalising them will generate significant new claims on public resources which may be a threat to public debt sustainability. The government is considering establishing a special agency for managing non-performing loans.

At the macro level, the main risks to public debt sustainability are associated with the currency structure of the debt, where hard currency obligations are dominating. While the level of future forex debt service will be rising, the amounts of future forex revenue of the government is uncertain; the level of international reserves is also low. The government will need to solicit new forex borrowings in order to service its forex obligation or roll over old debt. Public debt sustainability may become questionable in case new borrowings become unavailable, or if the debt burden continues to rise.

… and needs to reinvent its relations with the IFIs

During the 1990s, Belarus concluded two stand-by arrangements with the IMF (in 1993 and 1995); subsequently, however, these were scaled down on the initiative of the Belarusian side, due to contradictions between IMF conditionality and national policy priorities. The global financial crisis of 2008-2009 and the urgent need by Belarus of external finance to support the currency peg pressed Belarus to apply in 2008 for IMF financial assistance through a stand-by arrangement.

In this environment, the Belarusian authorities were more flexible in the negotiations and undertook a number of commitments not only with respect to short-term macroeconomic indicators, but also as regards a number of structural issues, which earlier had been considered as a taboo. The IMF, in turn, took a more flexible stance with respect to structural issues, which in the past had been considered as a starting point for negotiations with Belarus.

Throughout 2009 Belarus abided strictly to the IMF conditionality and most of the stabilisation measures were implemented. However, the situation changed in 2010. The Belarusian authorities were keen to achieve rapid economic recovery and return to the habitual growth rates of output and incomes before the presidential elections.

Aversion of the IMF agenda and availability of other sources of external finance (first of all, the Eurasian Fund for Stabilisation and Development – EFSD) made the Belarusian side reluctant to seek a new IMF-supported programme in 2011-2015. Instead, in 2011, Belarus applied for a stabilisation EFSD loan with the implicit expectation that its conditionality would clash less with their policy objectives and that EFSD monitoring may be subject to political pressure, which indeed turned out to be the case.

At present, Belarus seems to be playing a strategic game between the two possible sources of external financial support, seeking to achieve most favourable lending conditions for itself.

What comes next?

The most intriguing question now is whether Belarus can continue experimenting with an economic strategy and policy agenda which are so different from what other post-communist countries did in the past or whether it will have to accept the mainstream transformation reforms and converge to the common pattern seen elsewhere.

It is important to distinguish between the sustainability of the country's policy course and the sustainability of Belarus' economic model as such. What concerns the first aspect, the answer seems clear: the past policy course has run its course and must be changed. Actually, change is already happening as a new policy model seems to take shape at present.

As regards the sustainability of the country's economic model which is rooted in Belarus' brand of state capitalism, there are no obvious arguments to assert that this type of model is not sustainable. However, to ensure its longevity, the authorities would also need to undertake some reforms in the direction of 'more capitalism – less state'.

The key test of the viability of the Belarusian model of 'state capitalism' would be the willingness of the authorities to impose hard budget constraints on state-owned firms and banks. Capitalism partly based on state ownership is in principle possible; however, it is not consistent with the policy of soft budget constraints. For the Belarusian authorities to be able to justify their claim of 'state capitalism', they would need to move in the direction of imposing hard budget constraints on state-owned firms and banks.

However, such a policy change would have severe social consequences as it would entail restructuring of the state-owned sector of the economy to make it more efficient, including the shedding of redundant labour. Another component of the current economic model that needs reform for making it more efficient is the strictly hierarchical policy decision-making process. It remains to be seen whether the Belarusian authorities would be prepared to take radical steps in these directions.

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