

Macroeconomic Update: How big is the Russian energy subsidy to Belarus

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It's commonplace: Belarusian economic performance depends on oil trade with Russia. But how big is its impact? On the one hand, in Jan-Feb 2018, the increase of output in oil processing ensured about 1 percentage point of GDP growth out of its total increase by 5.6% yoy. On the other, capacity of Belarusian oil refineries is limited, and such a direct impact cannot last long. On the one hand, Russia sells oil and gas to Belarus at below-market prices, and this create competitive advantage for Belarusian companies. On the other hand, this makes energy prices a tool of political pressure: political tensions between the two countries can unmade competitive advantage of cheap energy in a twinkle. Cyclical nature of these tensions create uncertainty and makes oil impact on the Belarusian economy even more ambiguous. This update considers Russian energy subsidy as one of the most important channels of the oil impact on the Belarusian economy.

Russian energy subsidy to Belarus include several components. First, Russia usually sells gas to Belarus cheaper than to the rest of the world. Second, it sells oil and oil products without customs duties (again, cheaper). Third, from 2017, Russian government transfers customs duty from up to 6 mln t of crude oil to the Belarusian budget. Below we consider each component.

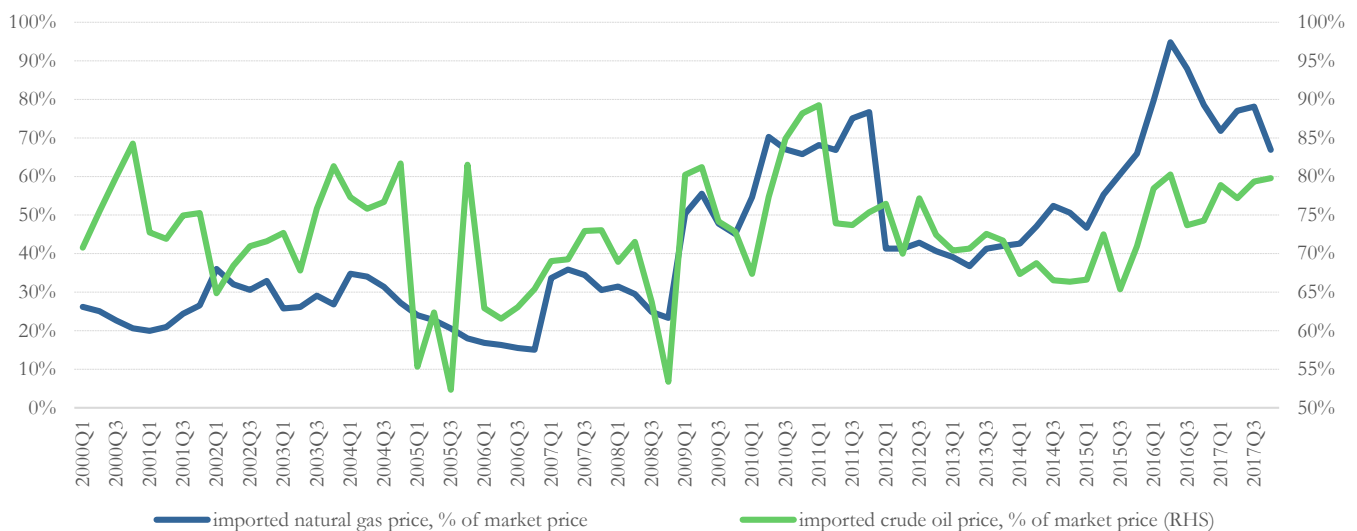
Gas subsidy

Benchmark for a market gas price is not so straightforward. Usually, researchers take Russian gas price for Germany; however, Russia sets different prices for different countries (a sort of price discrimination), and it is more reasonable to say that market price for Belarus would be different from the others. Historically, we have one year when Russia declared that it sells gas to Belarus at market price – in 2010. In the 2010Q4, it was 77% of the price for Germany – the closest value. Thus, as a benchmark of market gas price for Belarus we take 77% of Russian gas price for Germany. Difference between actual price for Belarus and that benchmark (see Figure 1) times volumes of gas imports by Belarus is considered as a gas subsidy, positive or negative.

Oil subsidy

As a benchmark for market price for crude oil, we take *price for Belarusian crude oil exports*; for 2010, when Belarus did not export its own crude oil, we take Urals price as a benchmark (assumed that 1 ton of Urals oil contains 7.28 barrels). Difference between actual Russian oil price for Belarus and the benchmark market price (see Figure 1) multiplied by volumes of crude oil imports by Belarus is considered as an oil subsidy.

Figure 1. Prices for oil and gas for Belarus against market prices



Source: own estimates based on Belstat data.

Oil products

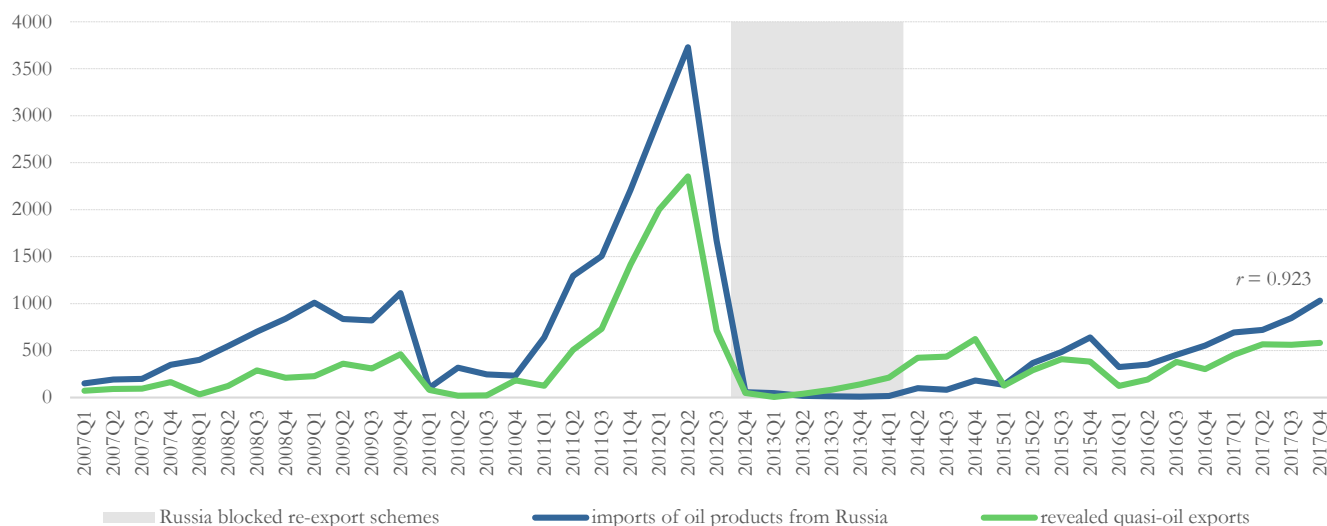
The oil products related subsidy is more complicated. Imports of oil products from Russia closely correlates to exports of Belarusian quasi-oil products (see the Box below). In 2012, Russia blamed Belarus in re-export of Russian oil products and closed the existed scheme¹. Therefore, oil products were imported not (or not only) to substitute Belarusian oil products at domestic

market to leave more of them for exports, but to gain amounts of customs duties not paid to the Russian budget. As we don't know what was earned by each party of the scheme, we just use the following benchmark: when price for imported Russian oil products was lower than *price for Belarusian oil products exports*, we consider the difference (times volumes of oil products imports) as a subsidy; otherwise, we set subsidy equal to zero.

¹ The idea was that Russian oil products were exported to Belarus (no customs duties), and then Belarusian side re-exported them as other

types petrochemicals that does not subject to customs duties, barely re-processed them for this purpose, just re-classified them.

Figure 2. Imports of oil products from Russia and revealed* quasi-oil exports, thousand tons

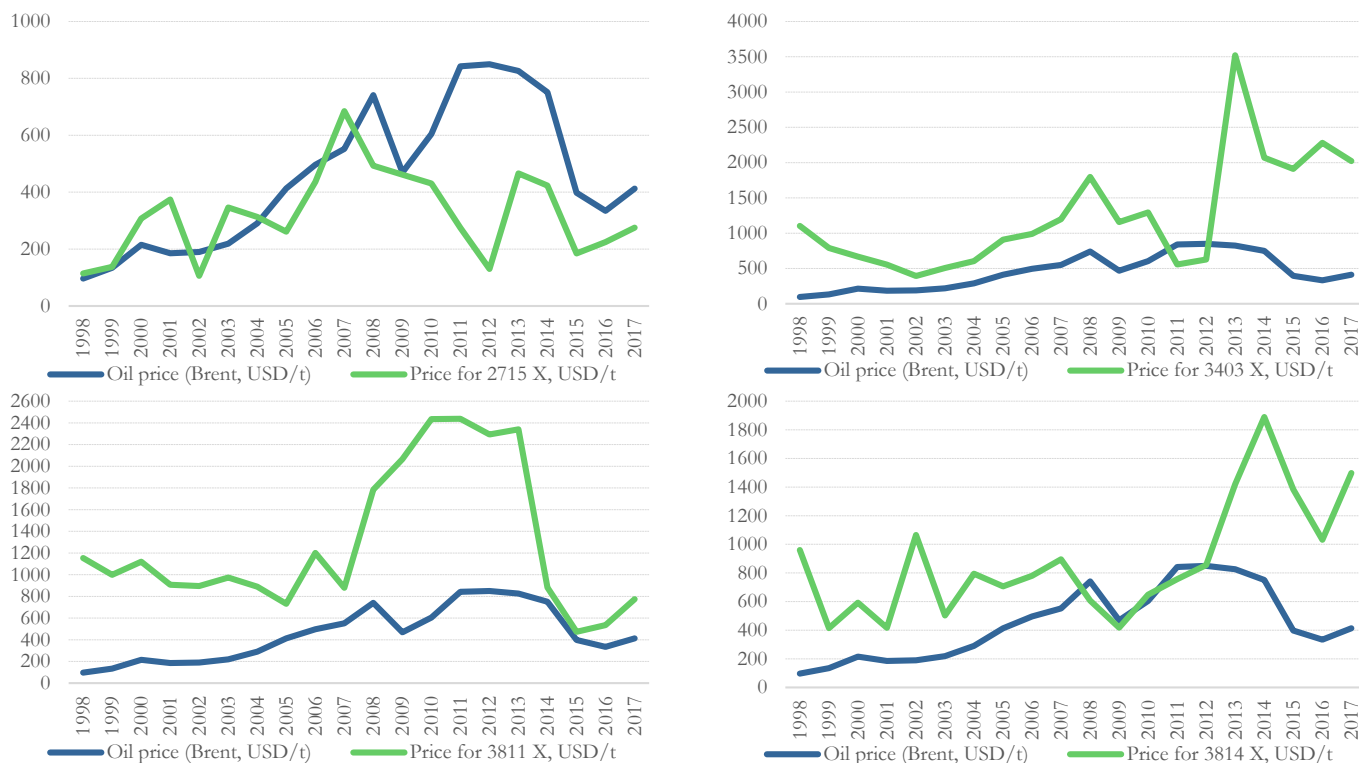


* Sum of the export volumes of the following HS codes: 2713 and 2715 – for the whole period (because they are from the same merchandise group as oil products – 27, “mineral products”); 3814 – for 2008Q1–2012Q3, 3403 – for 2011Q2–2012Q3; 3811 – starting from 2014Q2.
 Source: own estimates based on Belstat.

Box: Quasi-oil products and re-export schemes

Apart from crude oil and oil products exports, Belarus historically exports at least two more items from 27th group (“mineral products”): 2713 (petroleum coke, petroleum bitumen and other residues of petroleum oils) and 2715 (bituminous mixtures based on natural asphalt, natural bitumen, petroleum bitumen, mineral tar or mineral tar pitch). However, only for 2713 group export volumes were sizable enough each year, which allows to consider exports of products of this group as “normal”. For 2715, volumes were up to 10 thousand tons a year until 2012; in 2013, their exports increased to 47 thousand tons, in 2013 – exceeded 100 thousand tons, and then varied around several hundred thousand tons a year to 1 mln t and almost 1.5 mln t a year in 2014 and 2017, respectively. Similar stories were with merchandise groups 3403, 3811, and 3814 (there are several smaller items that could be considered as quasi-oil exports (like biodiesel, HS code 3826), but due to their relatively small size we skip them). After some point, their exports suddenly hiked to thousands or even millions of tons, and then after some time returned almost to zero. Moreover, their normal prices (varied around 1–2 thousand dollars per ton) suddenly fell to the level of price for Belarusian oil products exports (see Figure 3). All these groups altogether are considered as quasi-oil exports of Belarus, including 2713, although it is subject to customs duties.

Figure 3. Prices for quasi-oil exports vs. crude oil market price



Note. “X” stands for “exports”. HS codes: 2715 – bituminous mixtures; 3403 – lubricating preparations; 3811 – antiknock preparations; 3814 – organic composite solvents and thinners.
 Source: own estimates based on Belstat (export prices) and Index Mundi (Brent price; assumed that 1 ton of Brent oil contains 7.59 barrels).

Customs “re-clearance”

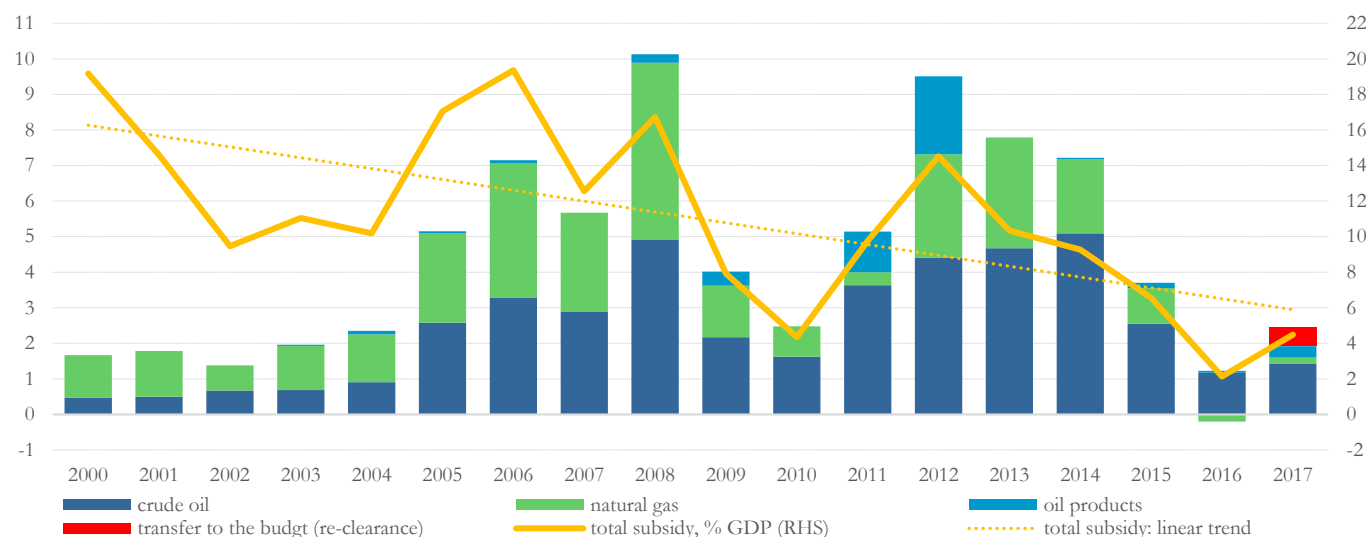
This element of the subsidy appeared in 2017 as a part of the gas deal between Belarus and Russia. In 2016, Belarus stated that it pays too high price for Russian gas², and started to pay less. Russia considered the difference as arrears; as Belarusian side continued not to pay it, Russia started to sell less crude oil to Belarus. This continued till the beginning of 2017, when the presidents of the two countries met and agreed that Belarus (i) will pay back its gas arrears (Russia provided Belarus loan for this purpose), (ii) will keep paying pretty same price for gas, and that (iii) Russia will export 24 mln t of crude oil to Belarus annually, of which at least 18 mln t for processing, and up to 6 mln t for re-export and keeping the related customs duty in the Belarusian budget. Belarusian representatives said that this “extra” oil will pass “customs re-clearance”. As a result, the deal looks as follows: Russian government transfers to the Belarusian government the amount of customs duties for the difference between 24 mln t and actual amount of crude oil imports from Russia, but no more than from 6 mln t.

Size and evolution of the Russian energy subsidy

Size of the subsidy varied over time (see Figure 4), as Belarus and Russia passed through different periods in their political affairs. Until 2008, gas price discount created the largest part of the subsidy, later oil price discount dominated. Since 2008, when re-export schemes arose, oil products from time to time add value to the subsidy. Finally, “re-clearance” part of the subsidy appeared just in 2017, and it is not yet clear how long it will sustain.

Size of the subsidy varied from the equivalent of USD 1–2 bn in early 2000th and 2016 to around USD 10 bn in 2008 and 2012. The subsidy varies over years, but there is a clear trend towards its reduction in relative terms (as a % of GDP): on its peaks (2000 and 2006), the subsidy was close to 20% of GDP; it fell to 4.4% of GDP in 2010 – a year of the probably most severe political tensions between Belarus and Russia, to 2.1% of GDP in 2016, and “recovered” to 4.5% of GDP in 2017, when re-export schemes expanded and “re-clearance” transfer was introduced. These two components constituted more than 1/3 of the subsidy – and they are the most sensitive to political tensions between the countries.

Figure 4. Size of the energy subsidy and its components



Source: own estimates based on Belstat data (nominal GDP, oil and gas trade since 2003), UN Comtrade (oil and gas trade for 2000–2002), NBB (weighted average exchange rate), and IPM RC (black market exchange rate for the periods with multiple exchange rate regime).

Lessons learned

Probably the most important lesson of the history of the Russian energy subsidy to Belarus is that in spite of the really sizable support, Belarusian economy for the same period accumulates significant amount of costly external debt. One of the possible explanations of this fact is that level of technology in the energy-intensive sectors is too low to produce competitive goods in a market environment. Permanent support via low domestic oil and gas prices (“in-kind” part of the subsidy), on the one hand, has not helped them to compete efficiently with Russian companies that were subsidized in a bigger extent; on the other hand, their competitors from the rest of the world (that pay market price for oil) became more efficient. In addition, “monetary” part of the subsidy is distributed between the budget, refineries, participants of re-export schemes, and either helps to service the debt that has already been accumulated, or covers

losses from other activities/sales of oil products at domestic market, or is withdrawn from the country via non-transparent schemes of oil products and quasi-oil exports.

Another important lesson is that it is too risky to rely on the subsidy in the situation of permanent uncertainty in the affairs with Russia – any political conflict between the parties may lead to a painful contraction of the subsidy with repercussions to the real sector, budget, and the sovereign debt.

Finally, there is one issue that goes beyond the scope of this update: mirror statistics shows huge gap between Belarusian oil exports to the world and the world’s oil imports from Belarus, which is an indicator of non-transparency of the oil and quasi-oil exports. Higher transparency is needed in order to be sure that all benefits from the Russian energy discounts are accumulated in the Belarusian budget and as profit of its refineries.

² Indeed, after devaluation of the Russian ruble, Russian gas price for Belarus had become significantly higher than its price in Russia.

Abbreviations used:

bbl	Barrel
Belstat	National Statistical Committee of Belarus
bn	Billions
HS	Harmonised Commodity Description and Coding System
GDP	Gross domestic product
IPM RC	IPM Research Centre
mln	Millions
NBB	National Bank of Belarus
t	Ton
yoy	year-on-year (annual growth rate)
Standard symbols for metric units and ISO currency codes are used.	

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