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Privatisation in Belarus during the Global Financial Crisis: No Time to Lose

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Executive Summary

Until 2007, state ownership was one of the pillars of the socio-economic model implemented by Belarus. Accordingly, privatisation was not considered as an important policy goal for the country. However, this ideology changed at the start of 2007. Privatisation and foreign direct investment became central goals of economic policy and were set high on the political agenda. A number of steps to improve the business climate and the regulation of foreign investment were taken and several privatisation deals were conducted in 2007 and 2008. While the privatisation receipts very negligible in 2006, they amounted to USD 1.2 bn in 2007 and to roughly USD 0.9 bn in 2008.

However, with the arrival of the global financial crisis to Belarus at the end of 2008, the privatisation process has run into a standstill. So far, practically no new deals were conducted in 2009, and the outlook is cloudy. A major factor for this development is the clear decrease in prices, which can be secured for privatisation deals today, as compared to last year and before. As it looks, policy makers do not want to sell states companies "under" value. While the motivation behind this attitude is comprehensible, we emphasize in this paper that privatisation is not just a fiscal exercise, but a crucial measure for the modernisation and the improvement of the competitive position of the country, which raises the medium-term growth potential of the country. Thus, the current standstill might have some merits from a strict fiscal, but not necessarily from an economic point of view: The economic costs of not going ahead with privatisation are huge. Belarus is losing time in a highly competitive international environment, in which no time is to be lost. Thus, the privatisation process has to continue. But how to do this? By "fire selling" a large number of valuable state assets?

We propose a "dual strategy" to secure the continuation of the privatisation process, without conducting a large scale fire selling. The first part of the strategy consists in the selling of state enterprises in sectors, which were not massively hit by the crisis, such as consumer-related industries (food processing, agro-business) and (partly) energy. There is a realistic chance of fetching decent prices for good assets in these sectors, assuming "decent prices" are not interpreted as the "highest ever recorded prices" just before the global asset price bubble burst in 2008. However, this goal can only be achieved if Belarus continues and significantly speeds up improvements in the business climate. The second part of the strategy consists of the instrument of pre-privatisation. In the context of such deals, the country could sell minority equity stakes of state companies to international financial institutions, so-called IFI's. This instrument is especially appealing for companies, whose potential privatisation prices heavily declined due to the current financial crisis. By conducting pre-privatisation deals, badly needed money for investments can be attracted, without losing the perspective to realize higher prices in the future, when the global economy recovers. But more importantly, the new co-owners, which have vast experience with restructurings in a transition context, would push forward necessary reforms at the company level and thus contribute to the badly needed restructuring of the Belarusian economy at the macro level. Furthermore, a future sale of the remaining stake in state hands could be conducted according to transparent and competitive standards. In short, this dual strategy should be considered as an adequate way to avoid losing time in a highly competitive environment.

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Introduction

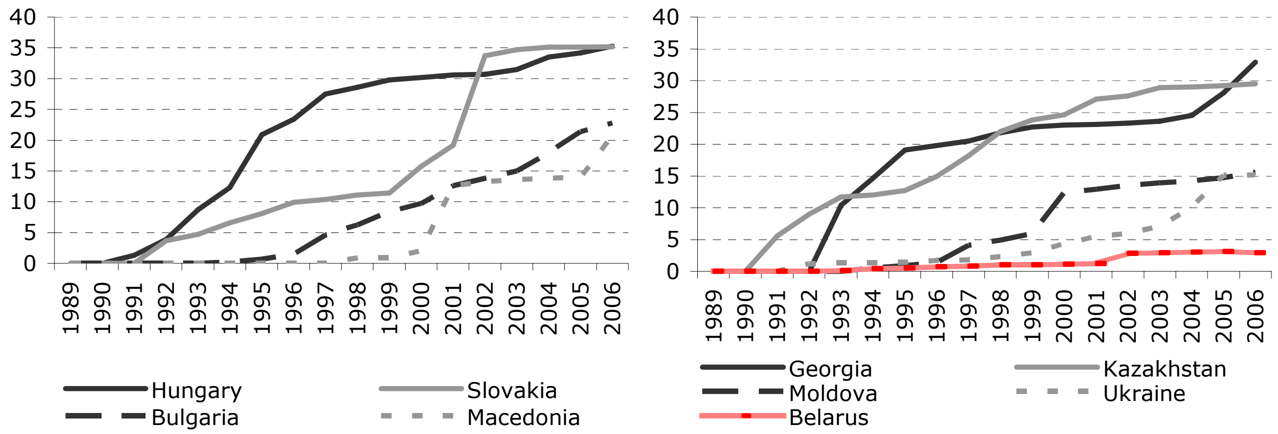
The topic of privatisation remains high on the economic policy agenda of the Belarusian authorities. But whilst in 2007 and 2008 a number of important privatisation deals were conducted, so far no major deals took place in 2009. Clearly, the conditions for privatisation are far from optimal during the current global financial crisis. But does this mean that the privatisation process should be halted in Belarus until the global economy and financial markets recover? Or are the ways to keep the process moving and not to lose valuable time?

In this paper we try to address such questions. In Part 2 we provide an overview of privatisation policy and transactions conducted during the last three years. In Part 3 we describe the current dilemma Belarusian policy makers are facing: An objective need for the privatisation process to go ahead, while in many cases the prices that can be secured for the sale of state enterprises to private investors have decreased. In Part 4 we recommend implementing a "dual strategy" to tackle the described dilemma. Part 5 concludes.

2. Privatisation in Belarus: Overview and latest developments

Until the end of 2006, economic policy making in Belarus was based on the principle of state ownership and on a special relationship with Russia, including a customs union and heavy Russian subsidies through artificially low energy import prices. But also from a fiscal point of view there was no pressure to go ahead with privatisation deals, since public finances were rather solid. Under such background, it is hardly surprising that privatisation activity was extremely limited. The cumulative privatisation revenues as % of GDP was much lower in Belarus than in many other transition economies in Central and Eastern Europe, as shown by Figure 1.

Figure 1: Cumulative privatisation revenues (% of GDP)



Source: EBRD.

The situation changed dramatically when Russia decided to gradually phase-out energy subsidies to Belarus. In 2007, the price of imported gas from Russia more than doubled, putting a strain on the trade balance. Besides, the conditions regarding the oil trade worsened for Belarus, having a significant negative impact on public finances. Following this "energy shock", which is still underway, it became clear to the Belarusian authorities that the old socio-economic model was not feasible anymore. Also, fiscal pressures became evident. Under such circumstances, the authorities decided to fundamentally change the model of economic policy making. Since then, the attraction of foreign direct investment and the privatisation of state assets are seen as key factor for the modernization of the partly out-dated capital stock and as mean to increase efficiency, wages and the international competitive position of the country. Besides, privatisation revenues are highly welcomed, given the possible need to finance some transitory negative consequences of the restructuring of the economy, such as higher unemployment.

This change in economic policy making that took place in response to the "energy shock" can be illustrated in several ways. The following observations sum up the major changes:

First, the rhetoric of public officials changed completely. The goal of opening up the country and of cooperation with foreign and Western investors has been repeatedly declared by high ranking officials, including the President. In the autumn of 2008, Belarus presented a selection of investment opportunities at the London investment forum, which was a new step for the country.

Second, a number of measures to improve the investment climate and to develop the stock market were successfully implemented. Such improvements were immediately reflected in form of a huge upward jump of Belarus in relevant international indices[1], which measure such progress. Below, we highlight the major legislative changes:

– Cancellation of the institute of special right of the state to govern joint stock companies (JSC) ("golden share")[2]. Despite the limited practice in the use of the golden share[3], the existence of such an institute negatively influenced the investment climate;

– A privatisation plan for the period 2008–2010 has been approved[4]. The plan consists of 2 parts. The first part includes of a list of 519 enterprises to be corporatised: 176 enterprises in 2008, 213 in 2009 and 130 in 2010.[5] The second part presents a list of 147 joint stock companies, whose shares are to be sold according to the Decree No. 7. This list consists of enterprises from different industries, including potentially interesting enterprises from the machinery industry and the military complex;

– The Presidential Edict No. 113 allows the purchasing of loss-making state enterprises in form of a contest[6]. This is an important step in privatisation of loss-making enterprises, since the procedure of privatisation through bankruptcy is blocked in Belarus.[7] However, the multiple financial and social conditions[8] attached to such a procedure might discourage potential buyers;

– The Presidential Decrees No. 5[9] and No. 7[10] intend to liberalise and develop the stock market. The Decree No. 5 reduces the tax rate for incomes from shares and bonds from 40% to 24% (starting from April 1 2008). The Decree No. 7 determines the gradual cancellation of the ban to trade shares of privatised enterprises, which were acquired for vouchers[11]. The cancellation of the ban is to be implemented in 3 stages.[12]

Third, and most importantly, the quantitative importance of privatisation deals increased dramatically in 2007 and 2008, as compared to 2006. While the privatisation receipts[13] were negligible in 2006 (a mere USD 0.03 m), they amounted to USD 1203 m in 2007 and to USD 945

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[1] Belarus moved from position 115 in the "Doing Business" report prepared by the World Bank in 2008 to position 85 in 2009, i.e. an improvement by 30 positions within one year. This ranks the country fourth among the top 10 regulatory reformers over this period.
[2] Presidential Edict No. 144 from 04.03.2008.
[3] The "golden share" has only been applied in Belarus in 22 cases.
[4] Presidential Decree No. 7 from 14.04.2008; Resolution of the Council of ministries No. 1021 from 14.07.2008.
[5] See Appendix A.1. for information on the implementation of these corporatisation plans.
[6] Presidential Decree No. 113 from 25.02.2007.
[7] See the "Law on Bankruptcy", No. 423 from 18.07.2000.
[8] The most important conditions are: Paying off all arrears of the enterprise; implementation a wide social program; preserving employment; rent of land – i.e. absence of possibility to privatise the land where the enterprises is located.
[9] Presidential Decree No. 5 from 20.03.2008.
[10] Presidential Decree No. 7 from 14.04.2008.
[11] According to Presidential Decree No. 3 from 20.03.1998, and further changes in the Law "On privatisation" in 1999, the shares bought by Belarusians on preferential conditions (20% less than nominal price) or for privatisation vouchers cannot be sold, presented, inherited during the process of voucher privatization (which is still formally on going). This was made in order to prevent mass sale of shares by individual shareholders ad to control incoming foreign capital and ownership structure.
[12] At the first stage (starting from April 1, 2008), the ban is cancelled for enterprises in which the share of state ownership is either absent or consists of more than 75%. At the second stage (starting from January 1, 2009) the ban also applies for enterprises with state ownership between 50% and 75%. At the third stage (starting from January 1, 2011), all limitations are cancelled. However, according to the Resolution No. 1927 by the Cabinet of Ministers, during the first and second stages the cancellation of the ban does not apply for 162 strategic enterprises, mostly from key sectors such as machinery, chemistry, oil refinery, meat and milk processing industries. See http://gki.gov.by/info-center/state-property-fund/share/forms/d58758c818db 4e79.html. Thus, the full impact of this measure is to be expected from 2011 onwards.
[13] By "privatisation receipts" we refer to the amounts received by the sale of state shares.

m in 2008. A break-down of the major transactions that took place in 2007 and 2008 is provided in Tables 1 and 2 below.

Table 1: Main privatisation deals in 2007

Enterprise	Industry	Buyer	Deal size, USD m
Mobile operator Velcom (31%)	Telecom	SB-Telecom[14], Cyprus	556.00
Beltransgas shares[15] (12.5%)	Gas transit	Gasprom, Russia	625.00
Motovelo (99.7%)	Machinery	ATEC Holding GmbH, Austria	7.20
JSC Berezovski kombinat silikatnyh izdelii (100%)	Construction	Triple Ltd, Belarus	0.15
Belvnesheconombank (47.4%)	Banking sector	Vnesheconombank, (VEB) Russia	24.10
Belschettechnika (30.1%)	Metallurgy	Dainova Ltd., (Ukraine-Russia-Great Britain JV)	2.81
ATEP-5 (1.51%)	Transportation	Norvegijas Riepas, Latvia	0.21
Orbita-Service (26.78%)	Repairing of home radio electronics	FE Elitepartner, Belarus-Ukraine	0.19
BelOMO-Stroi (51%)	Cash registers production	Vanjes Holdings Ltd, Cyprus	0.21

Source: The State property Fund.

Table 2: Main privatisation deals in 2008

Enterprise	Industry	Buyer	Deal size, USD m
Mobile operator BeST (80%)	Telecom	Turkcell, Turkey	500.00[16]
Beltransgas (12.5%)	Gas transit	Gasprom, Russia	625 .00
Experemental plan named after Gastelo (49%)	Machinery	JSC Amkodor, Belarus	1.08
Red October (91.25%)	Textiles/Shoes	Ltd. Marko (Belarus)	0.08

Source: The State Property Fund.

However, this impressive record came to a sudden stop in 2009. Besides the selling of 12.5% of Beltransgas for USD 625 m, a deal already signed in 2007, no major privatisation deals took place in 2009. The topic of privatisation is still high on the political agenda, but this did not translate into concrete transactions. An analysis for the reasons for these latest developments is provided in the next section.

3. The current dilemma regarding privatisation in Belarus

Policy makers in Belarus face currently a dilemma when it comes to the further conduct of privatisation policy. On the one hand, there is an objective need to go ahead with the privatisation process initiated in 2007. From a structural point of view, privatisation is crucial to modernise the capital stock and to introduce modern management skills at the company level. This serves as an important anchor to restore the medium-term economic growth potential, and thus to secure macroeconomic stability over the longer term. A crucial objective should be to improve the quality of Belarusian goods, in order to better compete on international markets and to expand the quite narrow geographic destinations of exports (excluding oil). The fresh push by Russia for a simultaneous joining of the WTO in the near future means that Belarus has no time to lose in this respect. But also from the point of view of the balance of payments there is a major role to play for privatisation. Following the energy shock in 2007, but also due to the "sudden stop" in private capital inflows that started in end-2008, the country needs additional sources of capital inflows to rebalance the foreign exchange market and to support the national currency. Finally, privatisation is also important from a fiscal point of view. Privatisation receipts would be highly welcomed today as the fiscal pressures become evident, not only in Belarus.

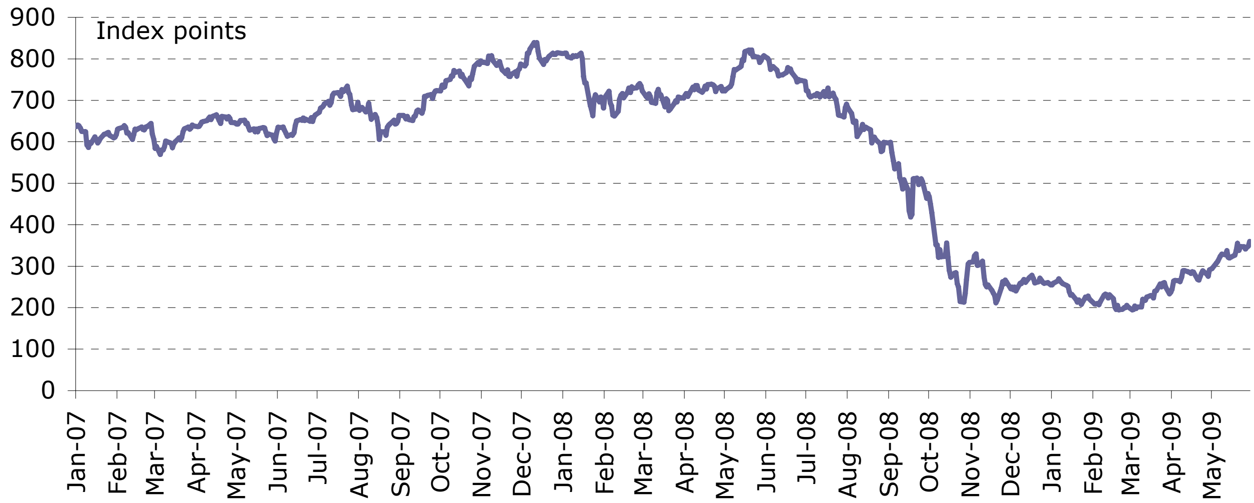
[14] In October 2007, Cyprus-registered SB-Telecom sold the stake in the Belarusian mobile operator further to Telekom Austria for EUR 535 m.

[15] According to the signed contract, Gasprom annually buys 12.5% of Beltransgas shares for USD 625 m till 2011 (it has then acquired 50% of shares for a total sum of USD 2.5 bn).

[16] However, the company had a credit debt outstanding to China that amounted to USD 234 m. Due to the changes in legislation, payment for this credit was included in the final price of the BeST sale. Therefore, the amount actually received for 80% of BeST shares was only USD 266 m.

On the other hand, the global environment is currently not supportive for privatisation deals. Companies around the world are facing their own problems and their appetitive for "risky" investments abroad has strongly diminished. At the same time, the strong recessionary environment in Central and Eastern Europe has clouded the future growth and profit opportunities for companies operating here. On top, it is quite difficult to secure the necessary financing for acquiring new assets, given the poor state of the international banking sector and the strategy of de-leverage by major banks. In the current global economic conditions, investors prefer to wait. As a result of this negative environment, the prices/valuations for companies have plummeted world-wide. This is especially true for Central and Eastern Europe, a region particularly hardly hit during the crisis, as shown in Figure 2. The fall in stock market valuations in the region can be used as a very rough proxy for the probable decline in prices to be fetched for the privatisation of large state companies in Belarus. Thus, in case Belarus decides to go on with its ambitious privatisation plans, it is quite likely to secure very modest prices for its assets.

Figure 2: Stock price developments in Eastern Europe, 2007–2009



Note. This index includes in total 92 shares traded in 5 different countries (Russia, Poland, Turkey, Hungary and Czech Republic.
Source: MSCI, EM EUROPE Standard Core Index (in US-Dollars).

In short, Belarus faces currently a major dilemma regarding the future course of its privatisation policies. On the one hand, a continuation of the privatisation process is of paramount economic importance; on the other hand, nobody really wants to sell a large number of valuable assets at discount prices ("fire selling"). Given this dilemma, an immediate question arises: What to do? Should Belarus sell numerous state companies despite low prices? Or should the country wait for better times to continue with its privatisation process? Or is there a strategy, which ensures a continuation of the privatisation process without major fiscal losses? In the next section, we present such a strategy.

4. Recommendations on how to proceed with the privatisation process

As became clear in the last section, the overall objective for policy makers must be the continuation of the privatisation process, even under the currently challenging international conditions. The country must not loose precious time in the necessary modernisation of the capital stock, which helps to recover from the current crisis and raises its medium-term growth potential. We propose for Belarus to follow a dual strategy, consisting of the following two elements:

4.1 Continuation and acceleration of privatisation efforts

A narrow focus on privatisation from a merely fiscal point of view is not adequate, as the economic benefits of privatisation are much larger. When taking a broader view, which takes other benefits into account, it becomes obvious that the process of liberalising the business environment and increasing the share of private sector activities needs to be continued. Consequently, privatisation as a crucial part of this framework of structural change needs to be stepped up.

The increase in privatisation efforts as envisaged in the revised IMF program, which foresees further institutional and legal changes, are therefore fully supported from our side[17].

Having demonstrated that a very narrow focus only on fiscal arguments is not correct, there are still mechanisms at hand to mitigate remaining fears. While stock markets around the globe, and especially in Central and Eastern Europe, have sharply declined during the crisis, a more differentiated picture emerges from a sectoral analysis of price patterns. While it is still true that stock market valuations (and thus prices to be achieved for selling state-assets) are currently lower than their historic highs in the middle of 2008, some clear distinctions between different industries and sectors can be seen. In certain industries, in which Belarus has interesting assets (e.g. oil and gas, consumer/retail, telecoms), the price declines have not been as steep as in others (see Appendix A.2. and the figure shown there for more details). Furthermore, when judging about the "right" level of prices or valuations, the question is what period can be considered a correct "benchmark" for answering this question. While the "golden years" of mid-2008 in terms of prices are not within reach, it can be also doubted that these valuations will be seen any time soon. Taking a medium term historic perspective and abstracting from this arguably "price bubble", valuations are reaching now a more reasonable level.

While we argue above that even under the currently challenging external conditions, there are still promising opportunities in several sectors, the government has further instruments at hand to increase the fiscal revenue stemming from a sale of its assets. When offering state-owned assets to private investors, the state can influence the successful outcome of such negations by setting the right conditions and incentives. For privatisation efforts to show positive effects, a number of features are of paramount importance, in our view:

– Flexibility in imposing *ex-ante* conditionality: Not to impose too many strict conditions on potential investors (about employment, production and sale policies, obligation to keep social infrastructure etc.) is a key factor. It has to be stressed that private investors evaluate state-owned assets primarily under the aspect of generating future profits.

– Limit possibilities of interference *ex-post*: Likewise, limit the interference of the state with the work of the privatised enterprises from an *ex-post* point of view– from price policy to the necessity to agree with the government investment or employment policies. This is, however, part of a broader framework to liberalise the business environment further, and touches private sector enterprises in general.

– Privatisation of profitable and loss-making assets: The question if an enterprise is profitable or loss-making should not influence the strategic decision to privatise it. In a fair and transparent auction or tender, this question is simply a determinant of the price to be achieved. While loss-making assets are hardly attractive for investors and thus may fetch only a low price, the commitment to sell also stakes in commercially successful and profitable enterprises would contribute to higher state revenues to be achieved.

– Transparency, competition and openness: It is very important that the privatisation framework follows best international practices and is conducted in a transparent and open manner. In opposition to that, some of previous privatisation deals were not in line with these demands. They were conducted mainly by direct sale (in 4 cases by issuing a presidential edict) and the negotiations exhibited a closed character (including no official publishment of the final price). Procedures provided by the respective law such as organizing a tender or contest, as well as the possibility to buy shares of a new emission of shares were not followed.

– Avoid abrupt policy changes: At the beginning of 2007, there were negotiations on privatising cement plants, but later the government decided to develop the cement industry itself. The same situation applied to cases in the brewery and food industry. This sudden reversion of planned privatisation plans was in the eyes of many interested foreign investors a major set-back in terms of a transparent, orderly and reliable privatisation process. This in turn affects negatively the country image, undermines investors' trust in the system and lowers thus the prices that can be achieved. Thus, there are direct negative fiscal consequences from such policy reversals.

[17] Among these changes, the establishment of a new privatisation agency, as well as the enactment of a privatisation law in line with international "best practice" have to be mentioned.

4.2 Pre-privatisation

The objective economic need to continue with privatisation, even under the conditions of the global economic and financial crisis, has been demonstrated above. There is no alternative as to proceed with structural changes in the economy. However, to alleviate the existing fiscal fears of selling at too low prices, this general direction of reform should be complemented by so-called <u>pre-privatisation</u> transactions. Such deals make especially sense for companies, whose potential privatisation prices declined severely due to the current global financial crisis.

A pre-privatisation can be defined as a sale of an equity stake of a state-owned enterprise (e.g. 25% plus one share, even though the concrete stake needs to be negotiated, and can be also combined with a loan) to a <u>public</u> international financial institution (IFI). This might be a multilateral public institution (like the EBRD, or IFC), or a bilateral development bank (like Germany's KfW/DEG)[18]. The ultimate purpose underlying this transaction is a future sale of the remaining stake in state hands, i.e. a full privatisation. In the meantime, the new co-owner uses its experience to help to restructure the enterprise and improve corporate governance and thus increases its future value for private investors. A successful example for the implementation of a pre-privatisation deal can be found in Box 1:

Box 1: Case study of a pre-privatisation transaction: Banca Comerciala Romana (2003)

State-owned Banca Comerciala Romana (BCR) is the largest bank in Romania, with a 35% market share at end-2002. In the context of a wider support to financial sector reform, the EBRD and the International Finance Corporation (IFC) decided to conduct a pre-privatisation equity investment. They purchased a minority stake of 25% (plus two shares) in the bank from the Romanian privatisation agency. The total investment for this stake amounted to USD 222 m.

According to the EBRD, the project had explicitly two main objectives. First, the investment has facilitated the transfer of ownership of the bank from state to private hands. The government committed itself to privatise the bank by the end of 2006 completely, i.e. around 3 years later, a goal that it also achieved (Austria’s Erste Bank being the acquirer). Second, the transaction helped to prepare the bank for privatisation by improving the bank's business and operations, as well as its corporate governance. The EBRD, the IFC and the government entered into a Shareholders' Agreement that included an Institution-Building Plan (IBP), outlining how the bank prepares itself for the future privatisation. In addition, the transaction had an important demonstration effect for the country in general, signalling confidence in its banking sector and in the overall investment climate.

Source: EBRD information, http://www.ebrd.com/projects/psd/psd2003/29327.htm.

There a number of advantages associated with the instrument of pre-privatisation:

– <u>Strong signal of official commitment</u>: First of all, the privatisation process keeps moving. Funds from international public institutions can be utilized on top of existing private sources. Such a strong official commitment is also a positive signal to foreign private investors, which may feed-back into their respective investment decisions.

  However, at the heart of such deals is the need for a clear and transparent timetable regarding the future full privatisation to private owners, including deadlines and penalties when these deadlines are not being met. Without the full commitment to such a scheme, the interest of IFIs will be very low. This implies a very close coordination between the IFI (i.e. the minority shareholder) and the government, including the setting of specified target dates regarding the future privatisation process. In order to protect themselves from a possible delay or failure of the process, IFIs have in the past negotiated so-called "put-options" in their original investment contracts with the government. This mechanism allowed the international financial institution to sell the minority stake previously acquired back to the government when delays or outright failures of the process materialise.

– <u>No “fire-sale”</u>: The IFIs pay normally relatively good prices for a certain stake of the companies involved, i.e. there is no "fire-selling" of state assets involved. While the prices to be achieved will also closely mirror economic realities, they are likely to be less dependent on the short-term volatility currently observed in private capital markets. How-

[18] These names serve for general illustration purposes. At this stage, it is not possible to give the concrete names of the institutions that might be the most likely partners in such transactions, as this depends on general aspects like the country strategy of the bank in question, as well as on transaction-specific details.

ever, the money invested does not go directly to the state, as a pre-privatisation deal is normally done via a capital increase, i.e. the money stays with the company for financing further investment. Only indirectly can the state profit from such a scheme, as possibly less subsidies are needed for the companies involved.

– Balance of payments support: The invested amount supports the balance of payments and thus the exchange rate of the Belarusian Rubel.

– Restructuring: Apart from the financial aspects realised in the short-term, the participation of experienced international financial institutions as strategic co-owners entails additional benefits in the medium to long term. The new co-owner can actively help to restructure the company, thereby increasing its economic potential and thus the value of the company obtained in a future sale to a private strategic investor. This implies also a very close coordination between the IFI (i.e. the minority shareholder) and the government, including the setting of specified target dates regarding the future privatisation process. In order to protect themselves from a possible delay or failure of the process, IFIs have in the past negotiated so-called "put-options" in their original investment contracts with the government. This mechanism allowed the international financial institution to sell the minority stake previously acquired back to the government when such delays or outright failures of the process materialized.

– Support in future sale of remaining state stake: Last but not least, the professional experience of such institutions in preparing an open and transparent future sale process according to best international practices should be noted. Since the IFI and the state will exit the company together in such a sale, the interests of both parties are aligned. This guarantees that conditions for achieving an optimal sale price for the remaining state stake are in place, which further helps to mitigate the fears of selling at "fire-sale" prices at the initial stage.

5. Conclusions

Since 2007, Belarus has undertaken important steps to liberalise its state-dominated economy. A more active privatisation agenda was one of the cornerstones of this major shift in economic policy. But under current tough global economic and financial conditions, the implementation of this strategy has been put on hold. Most likely, the reason for this stop is the currently observed decrease in prices that can be achieved for selling state-owned assets. Public authorities prefer to wait with further transactions until valuations have improved.

We argue strongly in the paper that the privatisation process in Belarus should under no circumstances be stopped. In order to raise the medium term growth potential and to secure macroeconomic stability on a sustainable basis, the process needs to continue, even at a higher speed than before. Waiting is not an option, as loosing time is throwing the country backwards.

We respond to the arguments by suggesting a dual strategy: First, we strongly recommend that the privatisation process targeted at private (foreign) investors needs to continue, even if somewhat lower prices than in 2007/08 can be realised. With the benefit of hindsight, one could say that these "golden years" in terms of valuations are a thing of the past and unlikely to come back soon. In the meantime, urgent investments needs into state-owned enterprises make a speeding up of the privatisation process necessary, as further delays decrease the economic value of the capital stock. Furthermore, as mentioned, the general decrease in stock prices across the region overshadows the fact that on a sectoral basis, there still exist a number of attractive assets in industries which have not seen such a big decline in valuations. The consumer-related industries (agro-business, including food industry) and selected energy companies have still the potential to achieve prices which are not at a "fire-sale" level. The second part of our strategy consists of the more active use of the instrument of "pre-privatisation". Here, minority stakes of state-owned enterprises belonging to sectors hardly hit by the financial crisis are sold to public international financial institutions (IFIs), with the aim to sell the remaining stake later in a second stage. In the meantime, the IFI helps to restructure and modernise the enterprises, which increase their economic value as well as future prices that can be expected from a sale. In order to pursue the idea of pre-privatisation more actively, the state should identify a small number of projects (e.g. ten), which are potential success stories. By implementing these "lighthouse" projects successfully, the signal and commitment effects will be accordingly very strong. Overall, by following the dual strategy proposed, fiscal fears of selling state-assets at too low prices can be considerably alleviated while keeping the speed of reform efforts high.

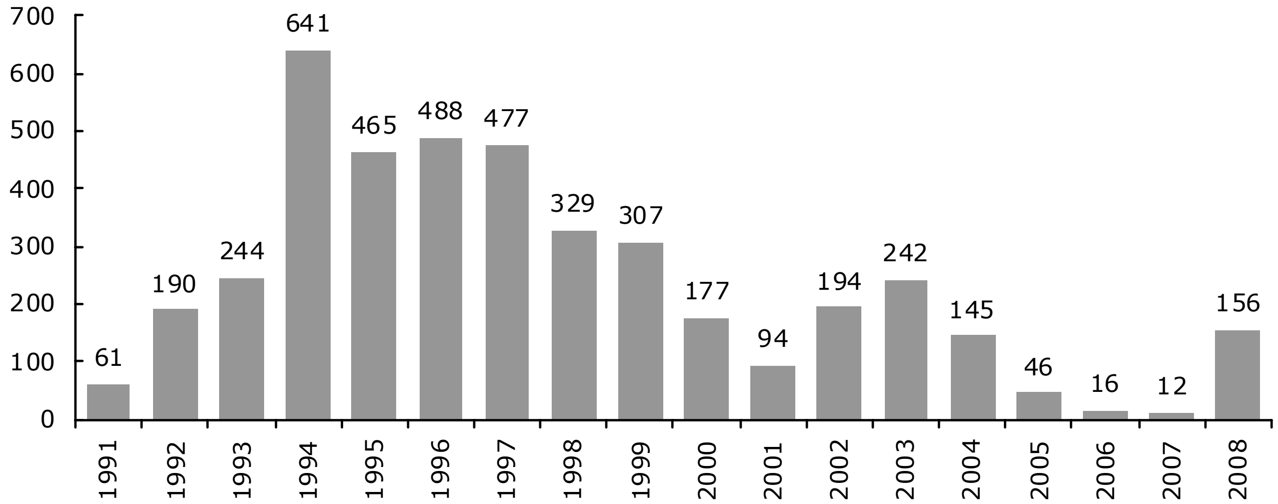
Appendix

A.1. Dynamics of legal ownership change in Belarus in 1991–2008

In Belarus, the corporatisation ("акционирование") of state enterprises is the first step in the privatisation process. During corporatisation, a state company changes its juridical status, and instead of a state unitary enterprise it becomes a joint stock company (JSC, "акционерное общество")[19]. In this process, all assets are valued (in terms of nominal and market prices), registered, and the (joint) capital is formed and divided upon a certain amount of shares. It has to be stressed that all created joint stock companies (JSC) have still 100% state ownership at the end of this process.

In the past, the development of corporatisation has taken place in certain waves, as Figure A1 demonstrates. After a first wave in the mid-1990ies, the number decreased steadily until 2001. In the first half of this decade there was a second, smaller, wave. However, by 2007 the absolute minimum of enterprises going through the procedure of corporatisation was reached, as only a hand full of legal ownership changes took place. But this changed rapidly in 2008, when legal reform accelerated, and a much higher amount of changes in legal ownership took place. If in 2007 only 5 JSC were created (out of a total of 12 cases where a change in the juridical status took place), then in 2008 this number rose to 107 (out of 156 cases). However, in general the process of corporatisation is still extremely slow – by 2009 in industry only about 40% of enterprises are corporatised, in construction – 32%, in services – 70% of enterprises. This implies that there is still a great amount of work ahead in terms of changing the legal ownership of Belarusian companies.

Figure A1: Dynamics of legal ownership change in Belarus in 1991–2008.



Source: The Ministry of Economy/ State Property Fund.

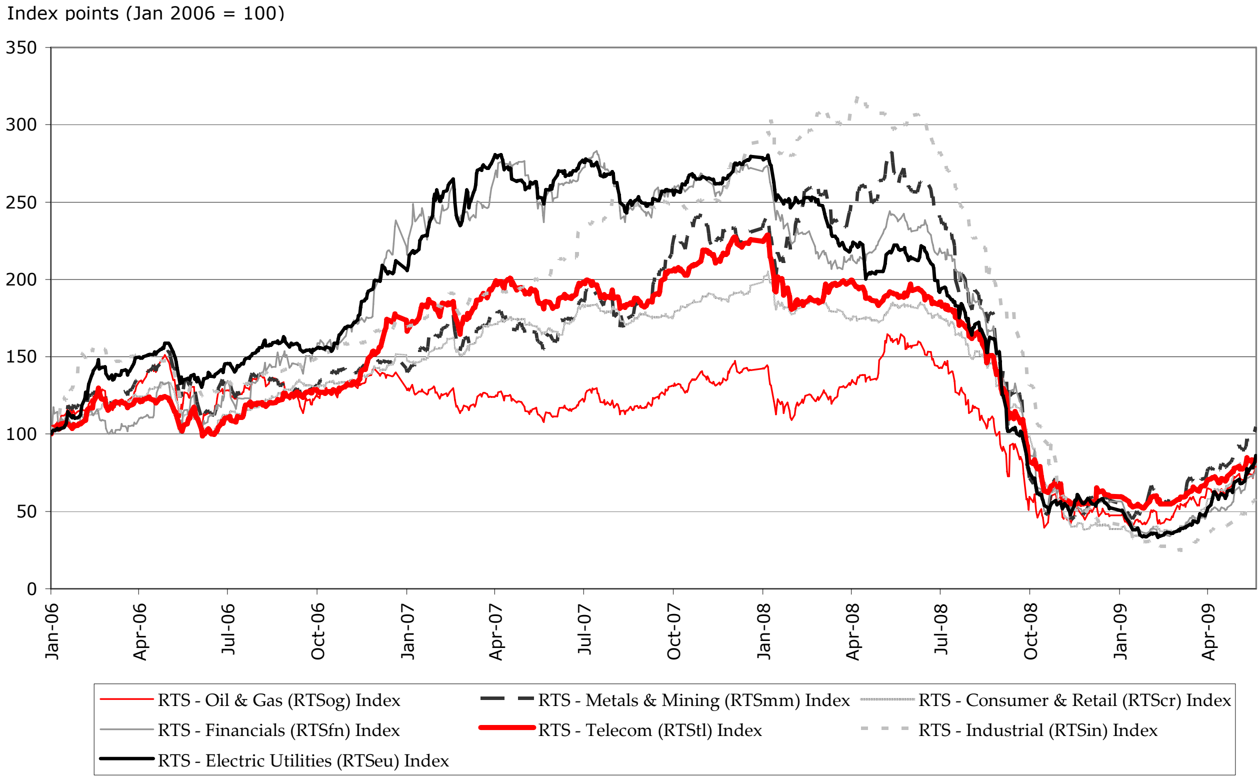
A.2. Stock Price Developments: A Sectoral View

Since no relevant Belarusian stock market data exist, we show in the figure below the development of different sectors of the Russian stock market index, the RTS Index ("Russian Trading System"). Here, we can clearly see that on a sectoral basis, the price dynamics can differ to a large degree, even though the general market trend is mirrored in all series. This in turn implies also that some sectors in the economy have shown a relative resilience to the global crisis and investors are still willing to pay relatively stable prices for these assets.

As can be seen, the "Metals and Mining" sector is currently leading in performance relative to the base date (01.01.2006) and has almost reached its initial value. The sectors of "Utilities", "Consumer/Retail" and "Telecoms" are following, all fields in which also Belarus has potentially interesting assets to offer.

[19] As a result of the changes in its juridical status, also other types of companies can be created in this process. However, the JSC is the main type.

Figure A2: Sectoral Stock Price Dynamics in Russia (2006–2009)



Source: Russian Trading System RTS (http://www.rts.ru/en/index/sectoral.html).