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FOREIGN INVESTMENT: ICT SECTOR AS AN EXAMPLE TO FOLLOW¹

Maryia Akulava, 2019

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Summary

In 2018, only the ICT sector was stably attractive to investors, unlike public sector assets. Belarus' overall investment prospects remained bleak. The government continues looking for solutions. A number of legal acts were issued last year to improve the investment climate and stimulate private sector growth.

Trends

- Stable investment interest in IT projects;
- Positive dynamics in the markets of domestic and external portfolio investment;
- A number of bills issued to improve the investment climate and develop small and medium businesses.

In 2018, the government planned to raise USD 1.4 billion in foreign direct investment.² FDI inflow amounted to USD 1,457 billion³, an increase by 16% from USD 1.276 billion reported for the year 2017. One of the key economy performance indicators was achieved for the first time over the past few years. Actual FDI inflow exceeded the target once, in 2013.

The amount of cumulative foreign investments in 2018 was much smaller than in 2017 (USD 2.551 billion), standing at USD 1.485 billion. FDI constituted a much larger proportion than

¹ This policy paper was published in Б «Belarus Yearbook -2019», that *which is presented under the aegis of the Agency for Social and Political Expert Appraisal and expert community of Belarus Nashe Mnenie ("Our Opinion")*. <https://nmnby.eu/yearbook/2019/en/index.html>

² <http://www.government.by/upload/docs/file5e628caeafe0000b.PDF>

³ <http://www.nbrb.by/Publications/BalPay/BalPay2018.pdf>

portfolio and other investments. This happened because in 2018, Belarus fully redeemed its Eurobond (USD 800 million plus USD 35.8 million in coupon) originally placed in 2011.

The external public debt increased by around 1% to USD 16.9 billion as of January 1, 2019 (28.4% of GDP). A year before it was at USD 16.7 billion (30.7% of GDP). The aggregate external debt decreased 1.1 % to USD 39.5 billion as of January 1, 2019 from USD 39.9 billion in 2017.

Foreign direct investment

In 2018, Belarus managed to raise USD 1.475 billion in FDI. As in previous years, FDI was made by means of reinvestment of incomes (USD 0.8 billion), rather than appearance of new players or technologies in the market (USD 572.6 million). FDI in new projects increased 44% since 2017 (USD 398.3 million).

Investors continue showing reluctance when it comes to the industrial sector. According to *Belstat*, only 16.3% of FDI was channeled⁴ into production, whereas high technologies and innovation are needed to make its development effective and competitive.

There has been no qualitative change in privatization. In early 2018, the State Property Committee presented a new list of enterprises whose state-owned equity stakes were fully or partially put up for sale. This time, the list numbered 43 companies. All of them had been repeatedly named in previous years, but, apparently, were rejected by prospective investors. Low demand still stems from the inefficiency of the enterprises, exorbitant prices, collateral terms of sale, investors' uncertainty about the legal protection of their interests, instability of legislation and the business climate in the country.

Only one privatization deal closed in coordination with the president without an auction. In the autumn of 2018, the Brest Regional Executive Committee sold its 67.7% stake in Beryoza Cheese-Making Plant for BYN 86.33 million to *Savushkin Product* OJSC of the Santa Group, which by this means increased its stake in the company to 81%.

Unlike state-owned companies, the private sector is well aware of the benefits of investment cooperation. Last year's mergers and acquisitions (M&A) were a result of more active efforts of private businesses put forth to attract foreign investments.

The *Alutech Group*, one of the world's leading manufacturers of roller shutter systems and sectional doors, sold 75% of its shares to German *Hörmann*. *Servolux* agricultural holding

⁴ http://www.belstat.gov.by/ofitsialnaya-statistika/makroekonomika-i-okruzhayushchaya-sreda/finansy/operativnaya-informatsiya_14/ob-inostrannyh-investitsiyah2

acquired Belatmeat meat processing plant and bought the staterun Slutsk pig-breeding plant. *Servolux* also sold a minority stake to the EBRD for USD 10 million. The money will be used to build a meat processing plant in Smolevichi.

In 2018, a number of deals were closed in the food retail market. In March, the owner of the Hippo retail chain bought the *Belmarket* chain from Russian A1 Investment Company. In August, the *Santa Group* bought the *Rublevsky* chain of supermarkets. In November, the *Sosedi* chain bought *Preston stores*. The amounts involved in the transactions were not made public. In December, Polish CDRL bought a 90% stake in the *Buslik* children's clothing chain from the Belarusian West Ost Union Commercial Industrial Group. The amount was estimated at USD 6.4 million.

The Orsha Aircraft Repair Plant was re-nationalized in 2018. In 2012, Ukrainian *Motor Sich* JSC and Belarusian Innovations and Investment Systems bought the state-owned stake in the Orsha plant and planned its reconstruction and modernization. The Russian-Ukrainian conflict frustrated these plans. The financial standing of the plant deteriorated significantly, and, in summer 2018, the president of BelarUSDecided to put it back under control of the state. Since November, the state owns 99.08% of the company.

Stadler's decision to build production facilities in Fanipol to manufacture converters for trams and trains (USD 35 million) is worth noting in the *Greenfield* investment segment. *Cipla Limited*, Indian multinational pharmaceutical and biotechnology company, allocated USD 1 million for the construction of a research and technology center for production of pharmaceuticals. Belarusian Unison and Chinese *Zotye* signed an agreement on the construction of a plant to assembly *Zotye* electric vehicles for a total of USD 560 million.

Information technologies remain one of the few sectors capable of attracting potential buyers. Presidential decree No.8 'On Development of the Digital Economy' signed in late 2017 provided considerable privileges to High-Tech Park (HTP) residents, which boosted quantitative and qualitative growth of the sector. According to preliminary estimates, in 2018, the HTP registered 267 new resident companies. Its revenues increased 60%, and exports went up 38% year-on-year to over USD 1.4 billion.

In March, the Russian-Belarusian Venture Capital Fund – *RBF Ventures* – invested USD 430,000 in the AgroDrone Group, which designs systems for monitoring cultivated areas and plant health. In April, *WorkFusion*, the robotic automation systems developer, raised USD 50 million for research on the application of artificial intelligence for the automation of the labor market. Also in April, *Targetprocess* IT company sold minority stakes to *Zubr Capital* and the EBRD for USD 5 million. *VP Capital*, *Larnabel Enterprises* and *FaceMetrics* startup (developer

of the AI assistant that counts the time a child spends with a tablet) closed a USD 2 million deal in June.

In July, *Baring Vostok* Private Equity Fund bought a minority stake in ITransition, one of the software development leaders. *Storyline* startup (voice assistant developer) raised USD 770,000 from the *Boost VC* accelerator. In October, Estonian *Helmes* bought a controlling stake in *SolbegSoft*. The amounts were not disclosed.

In the autumn, Belarusian *Flo* application received another USD 12 million from the anchor investors *Mangrove Capital Partners*, *Flint Capital* and *Haxus* Venture Fund. In December, the Belarusian *RocketData.io* startup (online presence and business reputation managing) raised USD 500,000 from *RBF Ventures*.

Bulba Ventures investment company (established in March 2018), which supports technological startups in the field of machine learning, invested in several Belarusian projects last year.

In May, jointly with Haxus, the company invested USD 2 million in Wannaby, the e-commerce and computer vision project. In summer, *Bulba Ventures* supported the RocketBody startup, which develops a tracker for measuring metabolism and supercompensation. In autumn, the company invested in the *FriendlyData* startup (a search interface for working with corporate databases). In October, FriendlyData was bought by American *ServiceNow*.

Portfolio investment

In 2018, the government was quite successful in raising funds through the placement of bonds on world markets. An additional placement of the next tranche of Eurobonds in the amount of USD 600 million at 6.2% per annum until 2030 took place in February.

The timely and full tranche payments in 2018, as well as the slow, yet positive dynamics of country credit risk assessments⁵ enabled Belarus to achieve an acceptable coupon rate. As a result, the yield was lower than in 2017: Belarus-2023 (USD 800 million) at 7.125% and Belarus-2027 (USD 600 million) at 7.625%.

The placement of government bonds on the domestic market continued. The amount of domestic government bonds denominated in foreign exchange totaled EUR 280 million and USD 261.5 million.

The corporate and banking sectors were also active in placing foreign exchange and ruble bonds. Private companies floated foreign exchange denominated bonds worth USD 691.1 million.

⁵ <http://www.oecd.org/trade/xcred/cre-crc-current-english.pdf>

Belarusian Railway was among the leaders with a 28.9% proportion. It was followed by *Savushkin Product* (21.5%) and *Conte-Spa* (11.6%). Banks and leasing companies placed foreign exchange bonds worth USD 1.34 billion in total. AS B Belarusbank (37.4%), BelVEB Bank (11.5%) and the Development Bank of the Republic of Belarus (10.4%) topped the list of issuers.

In 2019, the government will try to float bonds on the Russian market. In summer 2018, the Ministry of Finance of Belarus reached an agreement with the Eurasian Development Bank and several Russian banks on assistance in the organization of bond issues in 2018–2020.

Other foreign liabilities

In 2018, the net amount of other external liabilities increased by USD 520 million. Belarus borrowed USD 1.75 billion mostly from Russia (50%) and China (34%). Around USD 1.2 billion were allocated to pay off the foreign debt, including to the Eurasian Fund for Stabilization and Development (EFSD), the Russian Federation, the International Bank for Reconstruction and Development (IBRD) and China.⁶

The public sector remained the main borrower. In 2018, the net increase in the foreign debt reached USD 200 million. In October, Belarus received USD 200 million in the 6th tranche from the Eurasian Fund for Stabilization and Development under the loan program signed in 2016. The 7th and last tranche is expected in 2019. Belarus suspended talks with the IMF on a new credit program. Their resumption depends on how flexible Belarus will be in meeting the IMF's basic requirements to the national economy and the public sector in particular.

Measures to attract external financing and improve the investment climate

1. *Decree No.286 on Taxation of Some Kinds of Incomes.*⁷

This decree is aimed at fostering investment activities of Belarusian enterprises. It provides for the exemption from taxes on incomes in the form of interest on loans granted by foreign investors to Belarusian companies, and incomes received from the provision of services for the placement of debt securities outside Belarus.

2. *Council of Ministers resolution No.743 of October 17, 2018.*⁸

⁶ http://www.minfin.gov.by/ru/public_debt/pressreleases/cb3b85607ab64d88.html

⁷ <http://president.gov.by/uploads/documents/2018/286uk.pdf>

⁸ <http://www.government.by/ru/solutions/3355>.

The strategy for development of small and medium enterprises for the period to 2030 is aimed at increasing the role of SMEs in the economy, ensuring equal conditions for doing business, and the gradual separation of functions of the state as a regulator and owner. Also, measures were taken to decriminalize business activities and mitigate criminal legislation by making prosecution adequate to the damage done. This program shows that the government recognizes the importance of SMEs in economic development and is willing to take real measures to support them.

3. Decree # 506 on Development of the Orsha District (Vitebsk Region).⁹

This decree establishes a special tax regime for companies operating in the district, imposes a moratorium on inspections, decriminalizes economic risks, and provides for other measures to attract investors.

Conclusion

Plans for 2019 involve borrowing at least USD 1.6 million in FDI¹⁰. Efforts to develop the IT sector started in late 2017 have produced positive results and show genuine interest of foreign investors in Belarusian IT companies. The results of 2018 are qualitatively different from those of previous years, and there is every reason to believe that the positive dynamics showed by the industry will continue in 2019.

Judging by the decrees and resolutions issued in 2018 and the country's leadership commitment to increase the role of the private sector, it is likely that the efforts made to create a favorable business environment will cover other sectors of the economy as well. The plan to ensure equal rights for businesses regardless of the form of ownership and to decriminalize business activities will enhance the country's appeal, since many of the significant barriers to the fast-paced inflow of foreign investment can be removed.

There is a next-to-zero chance for privatization. The government is still inflexible when trying to sell state-owned assets, which repels potential buyers, and the attractiveness of most saleable assets is poor in comparison with the Greenfield projects.

Placement of government bonds denominated in foreign exchange on external markets will continue in 2019. In the next few years, the government plans to borrow around USD 2 billion by placing bonds in Russia and China.

⁹ <http://www.pravo.by/document/?guid=12551&p0=P31800506&p1=1&p5=0>

¹⁰ <http://www.government.by/upload/docs/filea54ccabfba63a99a.PDF>