

Russia initiates a new revision of the Belarusian-Russian relations in the oil and gas sector

Anton Boltochko

In early August, it became known that Russia [intends](#) to make changes to the Russian-Belarusian intergovernmental agreement in the oil and gas sector, which regulates the prices, volume and terms of energy products supply to Belarus. At the same time, according to the [explanatory note](#) to the protocol of changes, Russia is ready to use financial levers to apply pressure on the partner. And although the accuracy of the information disseminated has not been officially confirmed, the [events](#) of recent weeks suggest that there is no smoke without fire.

The situation is aggravated by the fact that the Russian State Duma [approved](#) amendments to the Tax Code and the Law on Customs Tariffs, which make it possible to complete the tax maneuver in the oil industry within six years. It implies a gradual [reduction](#) of the oil export duty ([roughly speaking](#), from 30% to 0%) while at the same time [raising](#) the mineral extraction tax by the same amount.

These decisions will potentially have a serious impact on the economy of Belarus. The tax maneuver alone, according to the [estimates](#) of the Belarusian Ministry of Finance, in 2019 will lead to a decrease in budget revenues by \$ 300 million. The total amount of losses for the country as a whole — taking into account the lost revenues of oil refineries and the potential multiplier effect from external shock spillover across other sectors of the economy — can exceed \$ 1 billion. All this will increase the risks of macroeconomic imbalance.

Russia trying to manage the partner's gain

The building up conflict has the same dichotomy at its core. Russia is trying to control the amount of benefits gained by the ally from the preferential conditions of bilateral cooperation in the oil and gas sector. Belarus is trying to maximize this benefit.

In many ways, problems in bilateral relations arise from the complexity and non-transparency of the oil and oil products market in the EAEU. The difficulty is caused by the absence of general principles and rules of trade in this segment of the economy, which leads to discriminatory practices of individual countries participating in the EAEU and an obscure pricing system. The

[creation](#) of a single Eurasian oil and oil products market, designed to solve these problems, is constantly being postponed due to the extreme sensitivity of the economies of Russia and Kazakhstan to the regulation of this industry, as well as the many interests of large business structures. Therefore, currently, relations in the supply of oil and oil products between the EAEU member states are regulated by bilateral intergovernmental agreements.

However, this does not simplify the situation. Bilateral intergovernmental agreements fail to take into account all the nuances of the functioning of the market, especially at the national level. This allows partners to find new ways to secure their own benefits. A case in point is the scheme that Belarus conceived in 2011-2012 for the re-export of petroleum products under the guise of “thinners” in order to circumvent the norms of one of these agreements. Belarus [was obliged](#) to transfer 100% of export duties from the sale of petroleum products produced from Russian oil to the Russian budget. To circumvent this rule, some part of petroleum products was exported as a major chemical product, in particular, by code 3814: “Organic composite solvents and thinners”.

Complexity begets obscurity. This becomes most evident during periods of breach of agreement. When the “solvents-thinners” scheme was used, domestic statistics registered the growth of exports of certain types of chemical products, and the statistics of the main trading partners in the EU contradicted this. Russian authors [noted](#): “Belarus in one year produced over 2 million tons [of solvents and thinners - note], of which 1.5 million was exported to Latvia. For some reason, official statistics in Latvia give completely different figures - there was no explosive growth in imports from Belarus. But the Latvian ports carried out a record transshipment of cargo in 2011 – handling of petroleum products in 2011 alone increased by 2.5 million tons, while liquid chemicals, which are solvents and thinners, accounted for less than 0.2 million tons.”

The rest of the time, the transparency of the oil and oil products market is also questionable. When comparing national [statistics](#) and international trade [data](#) from UN Comtrade, one can spot major discrepancy between the volumes of exports of petroleum products from Belarus to other countries and the volumes of imports from Belarus to these same countries.

In view of the above, Russia constantly initiates reviews of cooperation schemes with Belarus in the oil and gas sector. The launch of a common gas market and the oil and oil products market within the EAEU by 2025, as well as the Russian tax maneuver until 2024, can solve this problem. However, until that time, Moscow is not ready to overpay Belarus for the special status of relations.

Therefore, the most obvious reason for the breakout of the current conflict between countries is as follows. Recently, Belarusian companies have sharply increased imports of Russian oil products, trying to compensate for their own losses from working in the domestic market. According to the [data](#) from Belstat, back in November-December 2017, the average monthly volume of imports of petroleum products from the neighboring country was 1.5 times higher than the value for the previous 10 months. For 6 months of 2018, Belarus [imported](#) 2.1 million tons of petroleum products from Russia, while a year earlier this value did not exceed 1.4 million tons. Thus, import covered the domestic demand by about a third of the annual volume (about 6.3 million tons).

Such a scheme allows Belarusian producers to focus on a direction that is more lucrative for them: the export of petroleum products to other countries. Given that since 2015 up to \$ 1.5 billion of the total amount of duties collected from the export of petroleum products [remain](#) in the Belarusian budget, the benefit of Belarus from using such a scheme is obvious.

The Russian side could also be frustrated by the supply of anti-knock preparation and oxidation inhibitors (code 3811) to individual countries. For example, Belarusian statistics state that since the middle of last year there have been periodic surges in the physical volumes of exports of anti-knock preparations and oxidation inhibitors to Latvia, Lithuania, the Netherlands and Ukraine, at the rate of several times the monthly average. In terms of value, these [volumes](#) are still small: in January-June 2018, total supplies to these four countries amounted to only \$ 68.7 million, but this is three times more than a year earlier.

This does not preclude the probability of Belarus probing into new setups of shipping oil products abroad that still wouldn't tip the scales of the energy supply between the two countries out of indicative balance.

How damaging is this yet another conflict for Belarus?

Technically, all the listed actions of Belarus do not violate the agreements reached with Russia in 2015, which were partially [revised](#) in 2017.

Since the end of 2010, Belarus has been acquiring Russian oil duty-free, but until 2015 the country was obliged to return to the Russian budget the entire amount of export duty on oil products sold abroad (which caused the "solvents and thinners" scheme mentioned above). In 2015, in exchange for Belarus signing the agreement on the creation of the EEU, Russia authorized the allies to transfer the entire volume of export duties on oil products to their budget, provided that it does not exceed \$ 1.5 billion. However, due to the plummeting oil prices oil, the amount of [duties](#) left in the Belarusian budget never exceeded the limit: in 2015 it amounted to about \$ 1.2 billion, in 2016 - \$ 0.5 billion, in 2017 - \$ 0.6 billion. Therefore, in 2017 the Russian side partially offset the loss of Belarus.

The essence of the revised agreements is as follows. Belarus can buy oil from Russia in the amount of 16 million tons (previously - 24 million tons), processing it at its refineries and covering the domestic demand for petroleum products, while exporting the surplus (export duties remain in the Belarusian budget in the amount of up to \$ 1, 5 billion). At the same time, additional 6 million tons of oil will go through Belarus as transit, and duties from the sale of this oil are also credited to the Belarusian budget as compensation for Belarus paying a higher price for natural gas (this arrangement was dubbed "customs re-clearance"). The total of "customs re-clearance" in 2017 [amounted](#) to a little more than \$ 0.5 billion, in 2018 it is expected up to \$ 0.6 billion

Based on these figures, Belarus is unlikely to profit from conflict with Russia, at least for financial reasons. Especially, considering that part of the revenue from the export of petroleum products and "customs re-clearance" is earmarked to repay and service FX sovereign debt, which has significantly increased since the last economic crisis in the country. According to the budget adopted for this year, out of the \$ 3.8 billion that Belarus is to [pay back](#) in 2018, \$0.5 bln will be

[financed](#) precisely through export customs duties. Giving up these funds means challenging the Finance Ministry to search for additional resources to maintain the economic system stability.

It will be especially difficult to find additional financial resources in conditions where further repayment and servicing of foreign debt also largely sourced from the eastern neighbor. Firstly, this pertains to the refinancing of \$ 1 billion foreign debt to Russia via a sovereign loan, which Moscow [promised](#) Belarus.

However, against the backdrop of a possible oil conflict, there are suggestions that Russia may "suspend" its extension. Secondly, Russia can "freeze" the last two tranches of the EFSD loan in the amount of \$ 0.4 billion. And despite the refutation of this information from both the [Russian](#) and the [Belarusian](#) parties, nothing has been credited to the accounts of Belarus yet. Although formally the penultimate tranche of the loan from the EFSD should have been [transferred](#) already at the end of 2017.

Additional losses for Belarus could be Russia's demands to compensate for losses of its own budget as a result of the export of Russian oil products to Belarus. It is rather difficult to estimate the amount of such losses, but it can be assumed that it will be higher than several hundred million dollars. And this is against the background of a tax maneuver, the losses from which Belarusian Finance Ministry has already estimated at \$ 0.3 billion.

How does it look going forward?

Thus, it makes no sense for Belarus to aggravate the conflict - the price is too high. And it is expressed not only in the problem of finding funds to repay and service external debt. But also in the reduction of production volumes in the processing sector of the Belarusian industry in case of restriction of the supply of oil and oil products from Russia. In this scenario, Belarus could lose a few percentage points of GDP, given the multiplier effect on the entire economy. This [happened](#) a year ago, when, within the framework of the gas conflict, Russia restricted the supply of energy resources.

On the other hand, even in the case of a peaceful settlement of the current conflict, the official Minsk will still have to find additional funds to maintain macroeconomic stability. First, the missed revenue of the Belarusian budget due to the tax maneuver requires additional funding. Either through changes in fiscal policy (raising taxes, reducing government spending), or by attracting new credit resources. Secondly, Belarusian refineries [make losses](#) when working for the domestic market due to government regulation of fuel prices. Losses can be partially offset by gradually increasing prices, but this policy has its social fallout. Therefore, Belarus will need additional funds to support its own industry.

Based on the current situation, Belarus is likely to take into account the claims of Moscow, while minimizing its financial losses in the short term. At the same time, the need for a new round of negotiations on the revision of oil and gas agreements between the two states is obvious in order to find a new modality of relations with regard to all the circumstances. The recent change of the main negotiators from both Russia and Belarus also supports this scenario. Since May 2018, the issues of the Russian fuel and energy complex became the responsibility of Deputy

Prime Minister Dmitry Novak. And in August 2018 in the Belarusian government, the head of Belneftekhim Igor Lyashenko replaced Vladimir Semashko as chief negotiator with Russia

Anton Boltochko

Expert, Public Association “Discussion and Analytical Society Liberal Club»

**The publication is supported by the Konrad Adenauer Foundation
(Germany)**

