

DEVELOPING CORPORATE BOND MARKET IN BELARUS

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Abstract. Corporate bonds are fundamental financing instruments that are widely held by institutional investors, fund managers and households all over the world. Corporate bonds play an important role in capital markets. As the economy develops, firms try to borrow first in the form of indirect financing (bank loans). At the same time the bigger firms in good standing seek funding in the form of direct finance from the corporate debt and equity markets. Corporate bond market also offers access to longer-dated, unsecured financing for growth businesses. So the importance of corporate bond market in the framework of direct debt finance can be hardly overemphasized.

The aim of the article is, while investigating the current state of Belarusian corporate bond market and revealing the challenges within this market, to identify more practical and efficient measures to improve it in line with the best practice of developed markets. The research methods used in this article are scientific abstraction, qualitative methods; statistical methods including data evaluation.

The article presents the results of analysis of volumes of corporate and government bonds trading at the platform of the Belarusian Currency and Stock Exchange. The author reveals the problems in Belarusian corporate bond market development as follows: the existing emphasize of household financial savings towards bank deposits; the significant reliance of the corporate sector on bank borrowing; the lack of institutional investors on the demand side; an illiquid secondary market; the lack of information for benchmarking; large borrowing costs for issuers.

The analysis shows that coupon rate is considered as the main factor determining the demand and return on Belarusian corporate bonds. By comparison, the main factors at developed bond markets are loan size and credit rating of the issuer. The coupon rate “corridors” have been examined in the article as well for bonds nominated in national currency (BYN) and for bonds nominated in free-convertible currency (EUR, USD). The article concludes that high-priority measures for developing Belarusian corporate bond market are the simplification of the trading procedure, the enhancement of the competition from demand side and the creation of observable benchmarks for issuers and bond investors. All these measures will encourage issuers and investors, both domestic and international, to participate in the Belarusian corporate bond market.

Key words: *corporate bond market, issuers of bonds, institutional investors, funding*

JEL code: G23, G24

Introduction

Corporate bonds are fundamental financing instruments that are widely held by institutional investors, fund managers and households all over the world (Brealy, 2011; Brigham, 2013; Ross, 2013; Van Horne, 2008). Corporate bonds play an essential role in capital markets; their prevalence-led academic and practitioner communities devote their energies to the analysis of bond evaluations and relevant claim holder’s decisions (Liang-Chih Liu, 2016). More developed bond markets are typically associated with stronger macroeconomic fundamentals, more stable financial systems, sounder and stronger institutional frameworks, more open economies, and the long-lasting presence of institutional investors enhancing the demand for bond securities, especially those holding long maturities (Azimova, Mollaahmetoglu, 2017). Besides, more developed and enlarging sovereign debt market may foster the development and

supply of corporate bond securities in local currency thereby underpinning firms to finance long-term investments (Smaoui, Grandes, Akindele, 2017).

The theme of the article is very topical, because the access to longer-term, unsecured financing is crucially important for growth of businesses in the Republic of Belarus. The volume of government investment support reduced dramatically in recent years. Firms and companies spend significant amount of time and resources to explore alternative sources of funding. These called the Belarusian researchers to explore the phenomena of corporate bond market development further (Belzetskaya A., 2017; Kuznetsov E., 2016). The lack of complex analysis of Belarusian corporate bond market as well as the lack of attention to the experience of developed and developing countries by the Belarusian authors requires an in-depth investigation. At the same time, patterns of behavior in markets for specific goods and services offer lessons about the determinants and effects of supply and demand, market structure, strategic behavior, and government regulation (Bessembinder and Maxwell, 2008).

Therefore, the author proposes and sets forward **the aim** of the research: while investigating the current state of Belarusian corporate bond market and revealing the challenges within this market, to identify more practical and efficient measures to improve it in line with the best practice of developed markets. According to the research aim, the author intends to study the current state of Belarusian corporate bond market to enable him to reveal the key challenges in its development and to find out the directions of improving the situation. In order to achieve above-mentioned aim, **the following objectives** are set out:

- to analyze the current state of Belarusian corporate bond market and the dynamics of its development over the last 6 years;
- to evaluate qualitative data, normative acts and quantitative factors in order to investigate the weaknesses of Belarusian corporate bond market;
- to identify the key challenges of Belarusian corporate bond market' development and to find out their root causes;
- to develop suggestions, required for the successful development of the corporate bond market.

This research is based on a comprehensive review of the literature and utilises the applied methods of scientific abstraction; qualitative methods; statistical methods including data evaluation. Normative acts regulating corporate bond market, data provided by Ministry of Finance of the Republic of Belarus and Belarusian Stock and Currency Exchange, research produced by Belarusian and foreign scientists, and Internet sources form the theoretical and methodological grounding of the paper.

The theoretical and practical significance of the paper lies in researching the problematic issues pertaining to the development of corporate bond market while taking into the account the best practices of developing and developed countries. The structure of the article follows the devised objectives.

Research results and discussion

Sub-Part 1 Analyzing the state of Belarusian corporate bond market

According to the National Classification by Ministry of Finance of the Republic of Belarus, the corporate bonds in Belarus include: bonds issued by banks, bonds of non-banking organizations, and other bonds. In order to evaluate the dynamics of market development it is important to establish, which volumes are there generally and in each group specifically. It is explicitly demonstrated by the information included in Table 1.

Table 1

Volume of cumulative bond issues by categories

Category of issuer	Volume of cumulative bond issues on reporting date, millions BYN					
	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018
Banks	3 157,4	3 219,7	5 292,6	6 530,9	6 569,0	7 196,2
Non-banking organizations	2 731,2	3 245,6	4 586,7	6 182,0	6 503,0	6 010,0
Others	733,2	843,6	1 111,5	1 313,2	2 378,7	3 594,2
All issuers of corporate bonds	6 621,8	7 308,9	10 990,8	14 026,1	15 450,7	16 800,4

Source: Ministry of Finance of the Republic of Belarus

Hereinafter the data for periods earlier than year 2016 led to the comparable view. According to the data in Table 1, the growing tendency within the corporate bond market has been established in recent years. The most important period for the market was between 2014 and 2015. The volume of corporate bonds in Belarus has almost double during these two years.

In order to evaluate the significance of corporate bond market in the Belarusian economy is important to compare volumes of corporate bond issues with GDP as it is shown in Table 2

Table 2

Comparative analysis of corporate bond issues and GDP

	Reporting dates					
	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018
Volume of all corporate bonds, million BYN	6 621,8	7 308,9	10 990,8	14 026,1	15 450,7	16 800,4
GDP for previous year, million BYN	54 761,7	67 068,8	80 579,3	89 909,8	94 949,0	105 199,0
Percentage of GDP, %	12,1	10,9	13,6	15,6	16,3	16,0

Sources: (1) Ministry of Finance of the Republic of Belarus,

(2) Statistics Yearbook of the Republic of Belarus 2018

Figures in table 1 and table 2 show that the years 2014 (before 01/01/2015) and 2015 (before 01/01/2016) have become crucial for the development of Belarusian corporate bond market. The percentage of corporate bond's issues to GDP gained 15.6 % that year and since it has remained at the level about 16 %. However, this is a very low level. In the majority of developed countries, the size of corporate bond market exceeds the GDP.

The other objective is to analyse the proportions of the different categories of bond issuers (see Table 3) in order to find out the trends within the structure of corporate bonds.

Table 3

Structure of different categories of issuers

Category of issuer	Shares of different categories of issuers (%)					
	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018
Banks	47,7	44,1	48,2	46,6	42,5	42,8
Non-banking organizations	41,2	44,4	41,7	44,1	42,1	35,8
Others	11,1	11,5	10,1	9,4	15,4	21,4
All issuers of corporate bonds	100,0	100,0	100,0	100,0	100,0	100,0

Source: Ministry of Finance of the Republic of Belarus

In fact, the main percentage at the market belongs to bonds issued by Belarusian banks. There is only one period (01/01/2013) where the percentage of non-banking organizations' bond exceeded it, but only by 0.3 percentage points. In order to analyze the scale of issuers it is necessary to present the data on the number of issuers (Table 4)

Table 4

Number of corporate bond issuers

Category of issuer	Number of bond issues on reporting date					
	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018
Banks	22	26	26	26	23	23
Non-banking organizations	205	240	276	245	198	158
Others	28	27	49	42	44	66
All issuers of corporate bonds	255	293	351	313	265	247

Source: Ministry of Finance of the Republic of Belarus

As it is shown in Table 4, the busiest category of corporate bonds' issuers are non-banking organisations. However, according to the data in Table 3, the main share of accounts for bond issues is by banks.

In order to address the aim of the article, it is necessary to analyse the volume of corporate bonds per one issuer. It is presented in Table 5.

Table 5

Average volume of corporate bonds per issuer

Category of issuer	Volume of bonds per 1 issuer on reporting date, million BYN					
	01/01/2013	01/01/2014	01/01/2015	01/01/2016	01/01/2017	01/01/2018
Banks	143,5	123,8	203,6	251,2	285,6	312,9
Non-banking organizations	13,3	13,5	16,6	25,2	32,8	38,0
Others	26,2	31,2	22,7	31,3	54,1	54,5
All issuers of corporate bonds	26,0	24,9	31,3	44,8	58,3	68,0

Source: Calculations of the author on the base of tables 3 and 4

The figures in Table 5 clearly show the concentration of bond issues particularly among banks. The ratio of the volume of bonds per one bank to the average volume of bonds per one issuer in general vary from 4.6 (01/01/2018) to 6.5 (01/01/2015) times. It can be explained by three reasons: (1) Banks do not need to use services of Professional Securities Market Participants since they have the licenses for professional securities market activity themselves. (2) The households can easily buy the bonds of banks rather than the bonds of non-banking and other organizations. (3) Banks are active market players not only from supply side but also from demand side.

As for non-banking organizations, the shift in their dynamics is related to the progressive role of amendments of Decree of the President No. 277 (Decree No. 272 of 18 July 2016 "On Amending the Decree of the President of the Republic of Belarus No. 277 of 28th April 2006"). Since 18 July 2016, it became possible to issue unsecured bonds within the limitations of the issuer's net assets.

The structure of corporate bonds by currencies is presented in Table 6.

Table 6

Corporate bonds by currencies

All issues of bonds according to the official exchange rate included	Year 2016		Year 2017	
	million BYN	share, %	million BYN	share, %
	15 450,7	100,0	16 800,4	100,0
nominated in BYN	7 685,6	49,7	8 330,5	49,6
nominated in USD	5 894,8	38,2	5 988,4	35,6
nominated in EUR	1 568,1	10,1	1 968,8	11,7
nominated in RUR	302,2	2,0	512,7	3,1

Source: Ministry of Finance of the Republic of Belarus

This table shows the proportion of corporate bond issues according to the currencies they are nominated in. The national currency (BYN) remains the most popular with the issuers. The table also shows the slowdown of the share of bonds nominated in United States dollars (USD). The unpopularity of bonds nominated in Russian roubles (RUR) can be explained by high instability of this currency recently.

The structure of corporate bond issues according to means of bond's yield is presented in Table 7

Table 7

Structure of different means of bond's yield

	Year 2016		Year 2017	
	million BYN	share, %	million BYN	share, %
All issues of bonds	15 450,7	100,0	16 800,4	100,0
included				
fixed coupon rate	7 919,7	51,3	9 073,2	54,0
variable coupon rate	5 936,8	38,4	7 174,6	42,7
discount yield	1 594,2	10,3	552,6	3,3

Source: Ministry of Finance of the Republic of Belarus

As it is shown in the table, the bonds with fixed coupon rate remain the most preferable among lenders. The bonds with discount tend to slowdown.

The analysis of secondary market is also very important. As noted by A.Belzetskaya (2017), the most preferable bonds for potential investors are collateralized bonds with good secondary market. The volumes of corporate bond turnover in comparison with the average cumulative bond issue are shown in Table 8.

Table 8

Turnover of corporate bonds

Category of bonds	Year 2016			Year 2017		
	Turnover	average cumulative issue	turnover rate	turnover	average cumulative issue	turnover rate
Banks	6 353,0	6 550,0	0,97	4 879,4	6 882,6	0,71
Non-banking organizations	3 274,8	6 342,5	0,52	2 534,9	6 256,5	0,41
Others	386,5	1 846,0	0,21	378,6	2 986,5	0,13
All issuers of corporate bonds	10 014,3	14 738,4	0,68	7 792,9	16 125,6	0,48

Sources: (1) Ministry of Finance of the Republic of Belarus

(2) Calculations of the author on the base of Table 1

The table demonstrates that bonds of banks are more liquid comparing to other bonds. The main cause of this fact is that banks are active market players from both sides of market.

While issuing the bonds, it should be taken into account that the lower limit of their yield is related to the economic interests of the investor and it is limited by the yield of alternative instruments for investing (for example, interest rates on deposits). The upper limit of the yield of corporate bonds relates to the economic interests of the issuer and is determined by the interest rate of alternative instruments for raising funds for bank loans. Therefore, in a functioning market, the yield of corporate bonds should fluctuate within these limits, i.e. it should not be lower than the yield of similar alternative investment options for investors and at the same time, it should not exceed the interest rate on bank loans.

To determine the target group of investors in corporate bonds, the author makes such comparisons according to the latest data of the National Bank of the Republic of Belarus in open access. In September 2018, the average interest rate on newly issued loans for companies in freely convertible currency was 5.22%, while the yield on government long-

term bonds was 4.19% in USD and 3.66% in EUR. The yield of short-term bonds of the National Bank nominated in USD was 3.9%. Such a low "spread" at the presented interest rates largely explains the narrow field for issuing corporate bonds among companies. Moreover, not all companies in non-financial sector within Belarusian economy have enough cash to invest in corporate bonds.

The prospect for the placement of corporate bonds nominated in freely convertible currency among households is more optimistic. According to the same review, the average interest rate on foreign currency deposits in September 2018 was only 1.01%, with a maximum numerical value of 2.19 for deposits of over 3 years. Similar comparisons in national currency are characterized by a completely different situation: the average interest rate on new loans for companies in September 2018 was 11.08%, and the average interest rate on deposits of households during the same period was 9.73%. The yield of short-term bonds of the National Bank in national currency was 9.98%. Hence, the spread for companies as potential investors was only 1.1 percentage points. The spread for households was 1.35 percentage points.

Thus, the current situation at the Belarusian financial market is most desirable for the bonds issues nominated in freely convertible currencies and above all targeted the households.

The author points out that Belarusian corporate bond market is rather weak. Considering the tendency of concentration of bonds issued by banks, it is essential to strengthen a non-banking segment of the market. The author finds out that, when preparing Listing Particulars for their bonds, Belarusian companies should take into consideration the fact that the coupon rate is the most important factor for potential buyers of bonds.

Sub-part 2 Revealing current problems of Belarusian corporate bond market

Taking into account the objectives of the article and the results of the analysis the author determines the most significant problems of Belarusian corporate bonds market as follows:

1) Despite the growing interest of households in the corporate bonds, the volume of such investments is significantly lower than bank deposits of households. According to the Statistics Bulletin of the National Bank of the Republic of Belarus on the 1st of January 2018, the volume of term deposits of the households in Belarus amounted to BYN 16 537.5 millions which almost equals the total amount of all issues of corporate bonds for the period mentioned above (BYN 16 800.4 millions). However, it is important to remind that the most active market players from the demand side are banks. Unfortunately, there is no exact data on the percentage of households' investment into the Belarusian corporate bond market. According to the estimations (Kuznetsov E., 2016) the share of households from the demand side of the market varies from 30 % to 40 %. Therefore, the households in Belarus still prefer to save with the help of deposits.

2) There is a significant reliance of the corporate sector of the Republic of Belarus on bank borrowing. On the other hand, banking loans remain the main financing source for borrowers. Additionally the Belarusian government continues to stimulate this way of raising the funding in spite of potential problems with the other budget expenditure. As an example, the Decree of the President of the Republic of Belarus No. 445 of 16 November 2018 "On financing investment projects" sets out the conditions for lending money to the state enterprises from the large state banks to finance the selected investment projects.

3) The current situation at the corporate bonds market is characterized by the lack of institutional investors on the demand side. Most of Belarusian institutional investors are banks and insurance companies. There are some restrictions concerning their possible investments in security market including bond markets. According to the Ordinance of the Cabinet of Ministers of the Republic of Belarus No. 1750 of 29 December 2006 "On establishing of the Regulation of

investment procedures and placement of insurance reserves”, only 50 % of insurance reserves can be invested in the corporate securities including corporate bonds. This share is divided equally between bonds of banks and non-banking organizations.

As for international investors, their expectations rely to a high extent on the evaluation of country risks. The sovereign credit ratings are shown in Table 9.

Table 9

Sovereign credit ratings of the Republic of Belarus

Rating agency		The worst	The best	The current
Fitch Ratings	Rating	B-	B	B
	The date	26/02/2016	20/07/2018	20/07/2018
Moody's	Rating	Caa1	Ba2	B3
	The date	17/04/2015	22/08/2007	16/03/2018
Standard & Poor's	Rating	B-	B+	B
	The date	18/10/2013	21/08/2007	05/10/2018

Source: Ministry of Finance of the Republic of Belarus

In spite of some improvement in the current situation, the level of sovereign ratings is very low. All that agencies consider government bonds of Belarus as highly speculative. Some banks in Belarus (e.g. Belarusbank, Belinvestbank, and Belagroprombank) have their own credit ratings from S&P or Moody's agencies, with levels comparable to sovereign ratings.

The author suggests that this problem can easily result in related problem – the lack of market information.

4) There is the lack of information for benchmarking both for national and international investors. The problem is that almost all Belarusian issuers are unknown to foreign investors. Moreover, the overall investment image of Belarus is mostly negative.

Even for national investors in many cases the only benchmark within the corporate bond market is Listing Particulars. Some issuers are included into the Belarusian Currency and Stock Exchange Listing. However, they comprise only about 20 % of overall number of issuers.

But as Bessembinder and Maxwell (2008) mentioned, bond issuers hire credit-rating agencies to evaluate their creditworthiness. So the proper and qualified benchmarking is very useful not only for investors but also for issuers of bonds.

5) As it has been mentioned in the previous section, the secondary segment of the corporate bond market in Belarus is very narrow. This causes the difficulty for corporate bond's selling before the fulfillment of the obligations from the side of issuer. Therefore, market players usually invest in the corporate bonds in order to gain the maximum yield generated by coupon rate. Hence, the coupon rate is the main driver at the Belarusian corporate bond market. By comparison, the main factors at developed bond markets are loan size, the bond's credit rating, on-loan percentage and the identity of the borrowing broker (Asquith, 2013).

Both the lack of institutional investors (and consequently, the low level of competition from the demand side) and illiquid secondary market cause another problem – significant borrowing costs for issuers.

6) There are large borrowing costs for issuers of corporate bonds in Belarus. According to Paul Asquith (2013), the borrowing costs for corporate bonds has two major components: rebate rate paid by the lender and the market interest rate. As for Belarusian corporate bond market there is no rebate rate but there are quite large transaction costs. The borrower should pay the commission fee to the Professional Securities Market Participant. The other side of the problem is the high level of coupon rates because of imperfections of current bond market. If market players know that it is very difficult to sell corporate bonds purchased earlier, they would try to maximize their current interest yield.

Therefore, issuers of bonds nominated in national currency (BYN) sometimes offer the extremely high coupon rates up to 16 %. It is much higher even in comparison with the average credit interest rates (see previous section).

Conclusions, Proposals, Recommendations

The conclusions, drawn as a result of the carried out analysis, correspond to the opinions and views of the scientists from the Republic of Belarus and other countries (Altman, 2005; Aquilina and Suntheim, 2017; Azimova and Mollaahmetoglu, 2017; Bektic and Regele, 2018; Belzetskaya A., 2017; Kuznetsov E., 2016, Bessembinder and Maxwell, 2008; Dick-Nielsen, Feldhutter, and Lando, 2012; Kwok and Phelps, 2012; Liang Chih Liu, 2016; Smaoui, Grandes, Akindele, 2017; Paul Asquith, 2013; Tocolovska N., 2017). The development of the corporate bond market in Belarus should take into consideration the best practice worldwide. The research has shown some inequality in the nature of the Belarusian corporate bond market which leads to its imperfect structure. As a result of performed research, the author has identified the following challenges within the Belarusian corporate bond market:

- the existing emphasis of household financial savings on bank deposits;
- the significant reliance of the corporate sector on bank borrowing;
- the lack of institutional investors on the demand side;
- the lack of information for benchmarking;
- an illiquid secondary market;
- large borrowing costs for issuers.

Taking into account the progressive role of amendments of Decree of the President of the Republic of Belarus No. 277 (Decree No. 272 of 18 July 2016 “On Amending the Decree of the President of the Republic of Belarus No. 277 of 28 April 2006”) and reasonably good infrastructure of Belarusian corporate bond market the author proposes the following measure for its prospective development:

1. to simplify the trading procedure in order to make bonds issued by non-banking organizations more accessible for households. This can increase not only the possibilities of potential issuers but also would encourage households to develop secondary market.
2. to enhance the competition from the demand side. The priority should be given to enhancing the financial literacy of households through popularizing the expansion of their investment opportunities using corporate bonds, as well as establishing the effective mechanisms for interactions between lenders and borrowers. This would allow optimizing the borrowing costs of issuers, creating a certain level of competition among potential investors and could help bringing the coupon rates on corporate bonds closer to the economically reasonable range of values.
3. to create observable benchmarks for issuers and bond investors as far as for national and foreign investors. For domestic investors it is worthwhile to make a National system of credit rating suitable for all issuers of corporate bonds. For foreign investors it is vital to meet all the conditions to feel them in familiar environment.
4. to spread the issues of Eurobonds more widely. There are some positive examples already – the collaboration of Belarusian Eurotorg LLC with Irish Bonitron Designative Activity Company enabled Eurotorg LLC to issue bonds at amount 350 million USD.
5. it is vital to address these measures as a complex, what will enable a positive synergetic effect. This complex of measures should enable Belarusian companies to reduce their financing costs, to enhance the transparency and disclosure of companies through the access provided by capital markets and to provide both domestic and international investors for a more efficient allocation of savings.

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