



KAZAKHSTAN

Highlights

- **Real GDP growth remains above 4 per cent.** The economy grew by 4.3 per cent year-on-year in the first three quarters of 2019, enabled by expansion in construction, trade and transportation. Annual inflation remains within the central bank's target band.
- **The blue-chip phase of the government's privatisation programme commenced with Kazatomprom's initial public offering (IPO).** In November 2018, Kazatomprom, the world's largest uranium producer, sold 15 per cent of its shares. The IPO was conducted on the London Stock Exchange and on the new Astana International Exchange.
- **An asset quality review (AQR) of the banking sector has been initiated.** The AQR will assess loan quality and bank capital needs of the 14 largest banks. The results are expected in December 2019.

Key priorities for 2020

- **The authorities need to further accelerate the implementation of structural reforms.** Key short-term priorities include measures to facilitate public-private partnerships, implement tariff reform in regulated sectors and improve the fiscal framework, all of which are critical for increasing the competitiveness of the economy.
- **Commercialisation and privatisation of large SOEs should advance.** The state- and quasi-state-owned enterprises should make further progress in improving operational efficiency and corporate governance practices to maximise value for the government.
- **The banking sector needs to be strengthened.** Despite a significant clean-up of the banking sector, asset quality remains a key risk in the system caused by weaknesses in governance and lending to related parties.

Main macroeconomic indicators %

	2015	2016	2017	2018	2019 proj.
GDP growth	1.2	1.1	4.1	4.1	3.9
Inflation (average)	6.7	14.6	7.4	6.0	5.2
Government balance/GDP	-6.3	-4.5	-4.4	2.7	0.5
Current account balance/GDP	-3.3	-5.9	-3.1	0.0	-1.5
Net FDI/GDP [neg. sign = inflows]	-3.6	-12.6	-2.9	-0.1	-2.5
External debt/GDP	83.0	118.9	100.3	88.5	89.0
Gross reserves/GDP	15.1	21.6	19.3	18.1	n.a.
Credit to private sector/GDP	37.7	33.0	29.9	27.3	n.a.

Macroeconomic performance

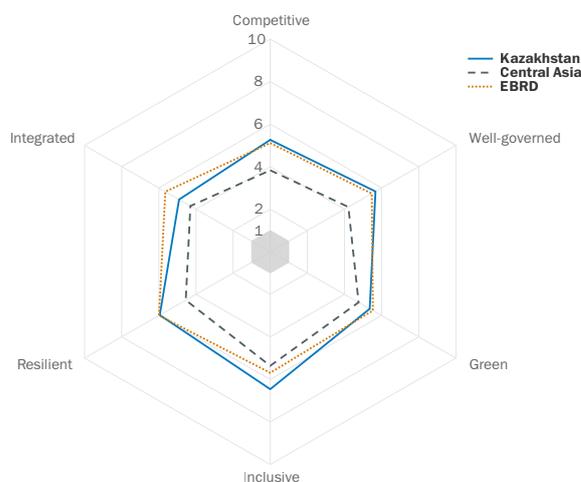
The economy is growing steadily. Real GDP growth continued at 4.3 per cent year-on-year in the first three quarters of 2019. It was supported by expansions in construction, trade and transportation. Oil production slowed down in the first nine months of 2019 due to planned repair works in the three main oilfields. As a result, exports declined by 4.5 per cent year-on-year in US dollar terms in the first eight months of 2019. At the same time, imports rose by 13.2 per cent. The growth in real wages, fuelled by increases in minimum wages and public sector salaries, continues to support private consumption. Fixed investment increased by 9.7 per cent in the first nine months of 2019, partly related to the construction of the Saryarka gas pipeline.

The exchange rate has been broadly stable. Capital outflows and rouble depreciation weakened the tenge against the US dollar by 14 per cent over the course of 2018, but depreciation of the exchange rate in the first half of 2019 has been limited despite market pressures. Annual inflation reached 5.5 per cent in October 2019. Rising inflationary pressures prompted the central bank to increase the base rate by 25 basis points to 9.25 per cent in September 2019. Credit growth has slightly accelerated (6 per cent year-on-year in September 2019), with loans growing only in the retail sector. The non-performing loan (NPL) ratio stood at 9.3 per cent in September 2019.

Fiscal and external accounts improved in 2018. The fiscal balance turned to a surplus of 2.6 per cent of GDP in 2018 from a deficit of 4.4 per cent in 2017, on account of higher tax revenues and a moderation of government spending. The non-oil fiscal deficit narrowed to 5.0 per cent of GDP in 2018 from 10.5 per cent in 2017. Growth on the revenue side was driven by increased corporate income tax and value added tax receipts as well as improved tax administration. Lower spending in 2018 was due mainly to a reduction in banking sector support outlays. However, in 2019 the guaranteed transfer from the National Oil Fund has been increased to KZT 2.70 trillion (US\$ 7 billion) to finance various social support programmes. The current account came almost to balance in 2018, supported by rising net exports, after a deficit of 3.1 per cent of GDP in 2017, but the deficit widened again in the first half of 2019.

Moderate growth is expected to continue. The economy is expected to expand more slowly, by 3.9 per cent in 2019 and 3.6 per cent in 2020, as the contribution of mining is expected to moderate. With minimum wages increasing in January 2019, growth in real incomes, along with higher consumer lending, will continue to drive private consumption. Downside risks include a possible deterioration in the external environment and an escalation of internal banking sector weaknesses.

Assessment of transition qualities (1-10)



Major structural reform developments

The government is enhancing its efforts to attract investment. The Coordination Council for Attracting Foreign Investment, chaired by the prime minister, was created in April 2019. Combined with concrete benefits for investors, including special legal and tax regimes and simplified procedures for obtaining work permits for expatriates, the new approach represents a concerted effort to promote investment opportunities in Kazakhstan to foreign investors.

Renewable energy is gaining traction, while legislative reforms on the green economy are under way. The share of renewable energy in the energy mix increased to 1.2 per cent in total production volume in 2018, up from 1.0 per cent in 2017, with the government aiming to achieve a target of 3.0 per cent by 2020. The ecological code is currently being updated to bring the current legislation in line with Organisation for Economic Co-operation and Development standards and introduce best available technologies. Adoption of the code is expected in 2020. At the same time, in other areas progress on the green economy transition has been limited. Despite the re-launching of the emissions trading system in January 2018, trading of quotas has not commenced. Energy efficiency measures in buildings and industry are lagging behind the declared targets due to weak regulation and lack of economic incentives.

The government has frozen utilities tariff reform. The current system of tariff regulation does not motivate utility companies to improve their performance and minimise operating costs. Most of these firms are therefore loss-making. The first steps have been taken to change long-term tariff regulation to stimulate the economic involvement of utility firms in reducing their operating costs. A new performance-based tariff methodology was developed for water, wastewater, district heating and electricity distribution sectors, and approved by the tariff regulator. The new methodology was referenced in a new law “On Natural Monopolies” that came into force in December 2018. However, the work on methodology has experienced a temporary set-back, with its detailed promulgation delayed due to the government’s decision to reduce or freeze tariffs for all utilities across the country in 2019 in order to reduce the social burden.

Privatisation is proceeding but at a slow pace. As of the end of July 2019, 734 out of 922 state-owned enterprises earmarked for privatisation had been sold for Tenge 453 billion (US\$ 1.2 billion). In November 2018, Kazatomprom, the world’s largest uranium producer, sold only 15 per cent of its shares for US\$ 451 million out of the 25 per cent planned to be privatised. The IPO was conducted on the London Stock Exchange and on the new Astana International Exchange. Partial privatisations of two other blue-chip assets – Air Astana, the national carrier, and Kazakhtelecom, the national telecommunications operator – have been postponed to late 2019. The government is falling behind its target of cutting the share of the state in the economy to 15 per cent by 2020, with the latest data showing that the share remains at 48 per cent. Preparation for privatisation of sizeable blue chip companies is taking longer than expected due to complexities in restructuring and commercialising large operations and a lack of momentum in regulatory reform in key sectors.

Banking sector restructuring has continued and the supervisory framework of the central bank has improved. In April 2019 Moody’s credit ratings agency upgraded its forecast for the banking sector from “stable” to “positive”, enabled by improved capitalisation and asset quality and an overall better liquidity situation. Following the merger of two large banks in July 2018 and revocation of the licences of three smaller banks, sector consolidation has continued in 2019. The fourth largest bank, Tsesnabank, had its distressed assets acquired by the state-owned Problem Loan Fund and was bought out by First Heartland Bank in February 2019. The National Bank of Kazakhstan has strengthened its supervisory functions by shifting to risk-oriented supervision in January 2019. The new approach is forward-looking and focuses on pre-empting risks by identifying problems early on. Another key development is the launch of the independent AQR of 14 (out of 28) banks in August 2019, which will be key to understanding the real situation with problem loans and identifying additional provisioning needs.