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## Kazakhstan: Strong growth and structural reforms

***In Kazakhstan real GDP will grow by 5% to 6.5% over the period 2013-2015, in particular owing to the increase in oil production with the start of operations in the Kashagan oil field. The country will thus assume the lead in terms of economic growth in the region covered by our analysis. While the banking system continues to struggle with high non-performing loans, the government has decided to reduce significantly its support to the finance sector. At the same time, the government plans to change drastically the landscape of the pension funds sector by nationalising existing private pension funds and merging their assets into one state pension fund, constituting the mandatory pension pillar***

Kazakhstan's GDP growth was close to 5% in the first quarter 2013 year on year. The highest growth rates were achieved in retail and wholesale trade (12.8%), information and communication services (11.5%), and public services (8%). In contrast, construction dropped by 4.9%. Agriculture seems to have started rebounding after an 18% drop in 2012. Industry's value added demonstrated only modest real growth of 1.2% year on year.<sup>1</sup>

Real household income increased by 2.9% year on year during the first quarter of 2013, in March growth accelerated to 3.6% compared with March 2012. Another indicator which has a significant impact on final consumption is the dynamics of bank loans to physical persons. Overall, the stock of bank loans to households has been growing much faster than the stock of loans to corporate clients – in April 2013, year-on-year growth rates were 25.6% and 8.6% respectively. The comparison gets even more striking if one looks at the data on newly issued loans: in January-April 2013, newly issued loans to physical persons increased by 56.4% compared to January-April 2012, while for corporate loans this indicator was at 15.7%. Newly issued loans for final consumption purposes have been growing even faster – by 66.1% year on year; this category of loans accounted for 77.7% of total loans to households issued during that period. Banks have been turning to consumer loans as a relatively safe harbour, while loans to companies, in particular in

<sup>1</sup> According to the industrial output data for January-March 2013, mining sectors were the most dynamic with 2.7% increase of output compared to the same period last year. Manufacturing attained a mere 1.6% real growth in output during that period, while electricity and water distribution saw their output decrease by 1.8% and 7% respectively.

construction and related sectors, are still perceived as too risky given the unresolved consequences of the housing bubble burst in 2008. However, so fast a growth of loans, which significantly outpaces household income dynamics, carries a risk of possible bubble development in this segment of the market.

These trends must inevitably translate into private consumption growth. Retail trade volume dynamics (12.5% real growth in the first quarter of 2013 as compared with the same period in the previous year) also supports this conclusion. By the end of 2013, we expect consumption of households to increase by 6% in real terms year on year. In 2014, the growth rate will be at the same level of 6%, and will slightly go down to 5% in 2015.

Investment into fixed capital has been growing quite fast in January-April 2013 – by 7.9% year on year in real terms. 57% of investment outlays during that period were financed from own funds of companies – this is 2.2 percentage points higher than in the same period of the previous year. The share of loans in the sources of financing increased as well, even more significantly – by 4.7 p.p. In contrast, government and foreign funding decreased their significance as financing sources compared to the same period of the previous year.

We expect that there will be continuing investment into transport infrastructure (in particular railways and oil pipelines) and oil fields development – financed both by the state and companies. China has been quite active in securing oil supplies from Kazakhstan, in particular through ownership of stakes in oil fields (now it controls 25% of oil production in the country) and co-financing the development of oil transport infrastructure, and it is going to continue investing into infrastructure projects. Construction is going to gradually recover, in particular due to government programmes of residential construction, and reach positive growth by the year-end. Overall, gross fixed capital formation is expected to increase by 5% in real terms in 2013. In 2014 and 2015 annual growth will speed up to 7% and 9% respectively.

Balance of payment data show that goods exports experienced a 7% drop in the first quarter of 2013 (in dollar terms), partly due to the decline in the global oil prices. We expect that this is just a temporary slump, and growth will resume soon on the back of higher volume of oil exports and reach 6% by the end of 2013 – only marginally higher than in 2012. Real exports will be growing faster compared with the previous year, about 6% versus 4.1% in 2012. The main underlying reason for that would be an increase in oil sector output, especially owing to the launch of the Kashagan field's operation in the second half of the year, which is expected to yield an up to 4% increase in oil production in

2013 (up to 3 million tons of oil are planned to be produced at this field by the year-end). In 2014-2015, Kashagan is expected to increase oil production up to 300 thousand barrels per day, which translates into about 20% growth of the country's total oil production. Consequently, both real and nominal exports will speed up their growth.

As a result of the trends described above, Kazakhstan's real GDP growth will be gradually accelerating – from 5% in 2013 to 6% in 2014 and 6.5% in 2015. This makes Kazakhstan a leader with respect to economic growth in the region we analyse. The relatively small size of the country (in terms of population) and the envisaged increase in oil production owing to the start of operation of the Kashagan field limit the negative impact of slightly declining oil prices on the economy.

While the banking sector still continues to struggle with a high ratio of non-performing loans (27.3% in April 2013) and the government has not succeeded yet in helping the banks to clean their balance sheets, the President announced that the commercial banks would no longer get financing from the National Oil Fund. Also, the state holding Samruk-Kazyna, which owns majority shares in the three most troubled banks<sup>2</sup>, was ordered to exit the banking sector by the end of the year.

At the same time, the government plans to drastically change the landscape of the pension funds sector – the state plans to nationalise the existing ten private pension funds and merge their assets into one state pension fund responsible for the compulsory pension pillar. The official justification of the reform is the need to increase the sector's efficiency. Possibly, banks' shares in Samruk-Kazyna's ownership will be exchanged for assets of some of the pension funds.

Another part of the pension reform envisages an increase in the retirement age of women from 58 to 63 years – to be on a par with the male retirement age. The law on pension reform (covering both the creation of a single state pension fund and an increase in the retirement age) was adopted by the Parliament on 23 May. However, due to the strong discontent of the citizens, the President did not sign the law and asked the Parliament to introduce some changes – in particular, postpone the retirement age increase to 2018. Given that the average life expectancy in Kazakhstan is 67 years, the reform is criticised for being too coldly efficient. Besides, there are concerns that it will negatively affect employment of young people.

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<sup>2</sup> Samruk-Kazyna owns 98% of BTA bank, which was the biggest bank by the amount of assets before 2008, and then had to undergo two restructurings and currently has 87% of non-performing loans in its portfolio. Besides, Samruk-Kazyna owns 80% of Temir, 67% of Aliance, and 18% of KKB.

Table KZ

**Kazakhstan: Selected Economic Indicators**

	2009	2010	2011	2012 <sup>1)</sup>	2012 1st quarter	2013	2013 Forecast	2014	2015
Population, th pers., average <sup>2)</sup>	16093	16322	16557	16791	16705	16941	16980	17100	17200
Gross domestic product, KZT bn, nom.	17008	21816	27572	30219	5977	6601	33500	37600	42400
annual change in % (real)	1.2	7.3	7.5	5.0	5.6	4.6	5.0	6.0	6.5
GDP/capita (EUR at exchange rate)	5100	6800	8200	9400	.	.	10100	11000	12200
GDP/capita (EUR at PPP)	9000	9700	10400	11000	.	.	.	.	.
Consumption of households, KZT bn, nom.	7913	9721	11569	13587	2544	.	15400	17400	19400
annual change in % (real)	0.6	11.8	10.9	11.1	12.1	.	6.0	6.0	5.0
Gross fixed capital form., KZT bn, nom.	4727	5307	5772	6298	864	.	6900	7800	9000
annual change in % (real)	-0.8	3.8	3.9	3.3	3.3	.	5.0	7.0	9.0
Gross industrial production									
annual change in % (real)	2.7	9.6	3.8	0.5	2.7	0.9	4.0	7.0	10.0
Gross agricultural production									
annual change in % (real)	14.6	-11.7	26.8	-17.8	-5.1	0.4	12.0	5.0	5.0
Construction industry									
annual change in % (real)	-3.3	2.4	2.8	2.9	-0.7	-4.9	5.0	8.0	10.0
Employed persons, LFS, th, average <sup>3)</sup>	7903.4	8114.2	8301.6	8507.1	8462.5	8546.1	8590	8680	8770
annual change in %	0.6	2.7	2.3	1.0	.	1.0	1.0	1.0	1.0
Unemployed persons, LFS, th, average <sup>3)</sup>	554.5	496.5	473.0	474.8	478.5	474.5	.	.	.
Unemployment rate, LFS, in %, average <sup>3)</sup>	6.6	5.8	5.4	5.3	5.4	5.3	5.0	5.0	5.0
Reg. unemployment rate, in %, end of period <sup>3)</sup>	0.6	0.4	0.4	0.4	0.7	0.6	.	.	.
Average gross monthly wages, KZT <sup>4)</sup>	67333	77611	90028	101079	93947	101237	.	.	.
annual change in % (real, gross)	3.2	7.6	7.1	6.9	11.5	0.9	.	.	.
Consumer prices (HICP), % p.a.	7.3	7.1	8.3	5.2	5.1	6.8	7.0	6.5	6.0
Producer prices in industry, % p.a.	-22.0	25.2	27.2	3.5	11.3	2.7	4.0	5.0	6.0
General governm.budget, nat.def., % of GDP									
Revenues	20.6	19.7	19.5	19.3	23.7	22.8	.	.	.
Expenditures	23.5	22.1	21.5	22.3	23.5	21.5	.	.	.
Deficit (-) / surplus (+)	-2.9	-2.4	-2.1	-3.0	0.1	1.3	-2.5	-2.0	-1.5
Public debt, nat.def., % of GDP	12.3	14.4	11.8	12.7	11.3	11.4	14.0	15.0	16.0
Central bank policy rate, % p.a., end of period <sup>5)</sup>	7.0	7.0	7.5	5.5	7.0	5.5	.	.	.
Current account, EUR mn <sup>6)</sup>	-2950	1049	8822	6003	2474	1247	6900	9400	10800
Current account, % of GDP	-3.6	0.9	6.5	3.8	8.0	3.8	4.0	5.0	5.1
Exports of goods, BOP, EUR mn <sup>6)</sup>	31504	46235	62868	71630	16655	15346	75700	82700	91900
annual change in %	-35.6	46.8	36.0	13.9	39.2	-7.9	5.7	9.2	11.1
Imports of goods, BOP, EUR mn <sup>6)</sup>	20769	24794	29266	36876	7276	7758	40400	43800	50000
annual change in %	-20.5	19.4	18.0	26.0	35.9	6.6	9.6	8.4	14.2
Exports of services, BOP, EUR mn <sup>6)</sup>	3038	3203	3213	3856	826	833	4100	4400	4600
annual change in %	1.0	5.4	0.3	20.0	22.3	0.8	6.3	7.3	4.5
Imports of services, BOP, EUR mn <sup>6)</sup>	7200	8536	7856	9894	2015	2217	11000	12100	13100
annual change in %	-4.7	18.6	-8.0	25.9	47.1	10.0	11.2	10.0	8.3
FDI inflow, EUR mn <sup>6)</sup>	9497	8698	9987	10909	4397	2829	11100	11700	12200
FDI outflow, EUR mn <sup>6)</sup>	2266	5938	3326	1231	476	1458	2100	2200	2200
Gross reserves of NB excl. gold, EUR mn	14352	19044	19477	16674	15310	13243	.	.	.
Gross external debt, EUR mn	78674	89259	96853	103250	97064	.	.	.	.
Gross external debt, % of GDP	95.1	80.1	71.7	65.5	61.6	.	.	.	.
Average exchange rate KZT/EUR	205.68	195.67	204.11	191.67	194.12	199.13	196.1	199.1	202.0
Purchasing power parity KZT/EUR <sup>7)</sup>	118.00	137.95	160.26	163.39	.	.	.	.	.

Note: Gross industrial production and producer prices refer to NACE Rev. 2 (including E - Water supply, sewerage, waste management and remediation activities).

1) Preliminary. - 2) According to census March 2009. - 3) From 2012 according to census March 2009. - 4) Excluding small enterprises, engaged in entrepreneurial activity. - 5) Refinancing rate of NB. - 6) Converted from USD with the average exchange rate. - 7) wiiw estimates based on the 2005 International Comparison Project benchmark.

Source: wiiw Database incorporating national statistics. Forecasts by wiiw.