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*This outlook is drawn up in line with ACRA's [General Principles of Socioeconomic Indicators Forecasting](#).*

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## Kazakhstan's accelerating economy will also support inflation

### Kazakhstan economy: 2021 outlook

- **Kazakhstan inflation has stabilized and it is expected to go down to 6.4% by late 2019 and to 6% by 2021.** After the seasonal growth in winter, the Consumer Price Index (CPI) will return to downslide as early as in spring 2018. Inflation growth rate will slip on the inflation import from Russia and the weak dynamics of real incomes. Inflation drivers will include economic revival and increasing monetary obligations of the National Bank of Kazakhstan (the NBK).
- **Economic growth will be supported by higher mining output and relatively high prices for oil and metals.** From 2017 to 2021, the Kazakhstan economy will grow by 3.2% on average per year (the industry and services sectors will contribute 1.3 pps and 1.1 pps, respectively).
- **In its 3-year budget proposal, the Government of Kazakhstan expects budget revenues to grow in 2018–2020.** The guaranteed transfer is planned for cut down to KZT 2 tln a year (in the last three-year period, the planned cut down was KZT 2.9 tln), while target transfers are to be cancelled. However, such cut down is possible only if the taxation base demonstrates a stable growth.
- **FX interventions revived by the NBK alert the market on a potential change in the exchange-rate regime.** The regulator becomes more active in the foreign exchange market, however, there have been no official statements on a change of the exchange-rate regime, which may indicate to the return to the fixed exchange-rate corridor. A prolonged absence of clear signals from the regulator may cause an exchange rate imbalance and stronger dollarization.
- **The balance of payments is prone to substantial payments to investors and growing exports.** In the forecast period, the trade balance will stabilize. Payments to non-residents under direct investments make the balance on investment incomes more volatile. If exchange rate shocks and subsequent tenge dropdown are avoided, the current transactions account will be maintained with a deficit on the entire forecast period (by late 2021, the deficit may reach 6%).

Table 1. Key indicators of Kazakhstan and other economies in 2014–2021

Indicator	UoM	Act.			Est.	Forecast			
		2014	2015	2016	2017	2018	2019	2020	2021
<b>External business environment</b>									
Urals price	USD/bbl	97.9	51.3	42.3	54	53	54.1	55.2	56.3
World GDP growth rate <sup>1</sup>	% yoy	2.8	2.7	2.4	2.5	1.9	1.8	1.8	1.8
US GDP	% yoy	2.4	2.6	1.6	2	1.8	1.9	1.8	1.7
China GDP	% yoy	7.3	6.9	6.3	6.6	5.6	4.5	4	4
EU GDP	% yoy	1.8	2.2	1.9	2.2	1.9	1.6	1.6	1.7
RF GDP	% yoy	0.7	-2.8	-0.2	1.3	1.4	1.4	1.5	1.5
<b>Production and manufacturing</b>									
GDP in market prices	KZT bln	39,676	40,884	46,193	52,670	58,068	63,874	70,201	77,049
Real GDP growth rate	% yoy	4.2	1.2	1.0	4.3	3.0	2.9	2.9	3.0
Capital investments	KZT bln	6,591	7,025	7,762	8,584	9,227	10,053	10,862	11,515
Real capital investments growth rate	% yoy	4.2	3.7	2.0	-1.0	4.6	2.0	1.2	-0.6
Industrial Production Index	% yoy	0.3	-1.6	-1.1	6.8	5.8	5.1	5.0	4.9
Retail sales	KZT bln	6,332	6,556	7,662	8,697	9,535	10,441	11,421	12,465
<b>External sector and exchange rate</b>									
Current account	% of GDP	2.77	-2.79	-6.31	-7.71	-5.21	-2.98	-2.03	-6.40
Exports	USD bln	79.46	45.96	36.74	47.40	48.58	49.69	50.74	51.74
Imports	USD bln	41.30	30.57	25.38	29.93	31.36	31.89	32.64	33.65
Net services exports	USD bln	-6.30	-5.11	-4.75	-4.12	-4.54	-4.69	-4.88	-5.11
KZT/USD rate (annual average)	KZT	179	222	342	334	338	346	355	360
KZT/EUR rate (annual average)	KZT	238	246	379	370	380	392	402	410
KZT/RUB rate (annual average)	KZT	4.76	3.61	5.11	5.7	6.0	6.1	6.2	6.4
<b>Incomes and labor market</b>									
Average payroll	KZT/month	121,021	126,021	142,351	147,512	153,202	156,703	159,511	161,856
Real income index growth	% yoy	3.4	1.4	-0.7	-5	3.05	2.28	2.03	1.96
Population (annual average)	mln people	17.16	17.42	17.67	18.03	18.29	18.56	18.83	19.10
EAP <sup>2</sup> (at end of period)	mln people	9.1	9	8.9	8.9	8.9	8.8	8.8	8.7
Unemployment (at end of period)	%	5.0	5.0	4.9	4.9	4.8	4.7	4.7	4.6
<b>Monetary/budget</b>									
Inflation (CPI)	% Dec./Dec.	7.4	13.6	8.5	7.8	6.0	6.4	6.3	6.0
NBK's base rate	%	-	16.0	12.0	10.0	9.0	8.0	8.0	8.0
Corporate loans issued by Level 2 banks	KZT tln	10.6	9.4	9.8	11.4	12.7	14.1	15.6	17.4
Cash in circulation	KZT bln	1,122.3	1,237	1,749	1,684.6	1,933	2,123.1	2,397.9	2,696
Budget deficit of Kazakhstan	% of GDP	2.7	2.2	1.6	3.2	1.4	1.4	1.3	1.2
Consolidated budget deficit of Kazakhstan	% of GDP	11.0	6.3	5.7	8.3	6.4	5.4	4.6	3.7

Source: SC MNE RK<sup>3</sup>, the National Bank of Kazakhstan, the Ministry of Finance of Kazakhstan, World Bank, ACRA estimates

<sup>1</sup> World Bank methodology, real growth.

<sup>2</sup> Economically active population.

<sup>3</sup> SC MNE RK means the Statistics Committee of the Ministry of the National Economy of the Republic of Kazakhstan.

## Kazakhstan's dependence on world's market trends and neighbor economies will be high

*Better oil market conditions (Brent up to 55 USD/bbl in 2017 and up to 57 USD/bbl in 2021) and a sound growth in oil production will strengthen external balances of the country. However, Kazakhstan's substantial obligations on the income balances does not allow the current transactions account to turn positive.*

In the forecast period, the world GDP will continue to grow moderately (from 2017 to 2021, the average annual growth rate will be 1.8–2.5%). The prices for the main export goods of Kazakhstan will be moderately favorable. The OPEC's decision to extend the oil production cut has balanced the oil market. However, the potential growth in oil shale production will cap the oil price growth in the medium term (within the range of 53–57 USD/bbl). Closure of inefficient production sites in Russia and China will support prices for ferrous and non-ferrous metals. Prices for ferrous metals will remain at the level of 2016, the price for non-ferrous metals will grow against the 2016 level.

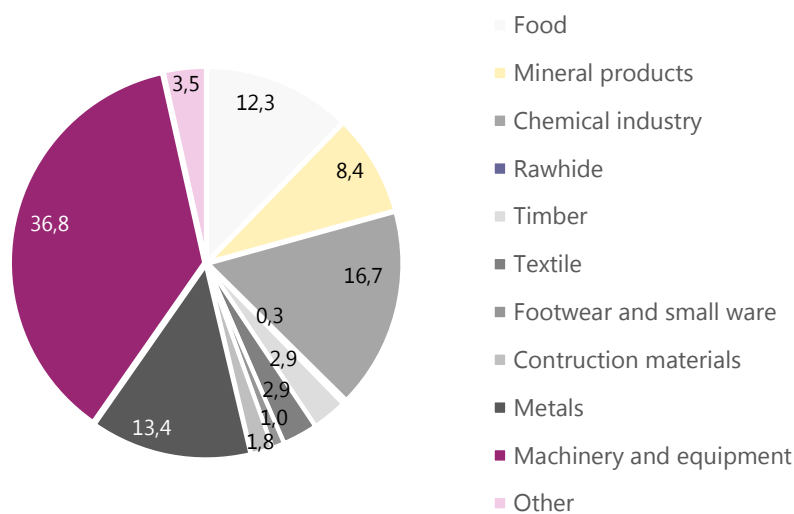
Kazakhstan is a small open economy (0.18% of the world GDP; the ratio of trade turnover to GDP is 61%<sup>4</sup>). As macroeconomic trends in the country reflect the external prices for the key traded commodities that are now in the limited growth zone, the external price impulse for is positive the economy, but restrained.

In January–August 2017, the shares of the three main trade partners of Kazakhstan (the European Union, China and Russia) in the national foreign trade profile have not decreased. Moreover, the share of the European Union in the Kazakhstan's exports (Kazakhstan exports 52% of goods to the European Union) and the share of Russia in the Kazakhstan's import (39% of imported goods) have been growing. In total, three key foreign trade partners account for 73.5% of exports and 74% of imports of Kazakhstan.

ACRA expects that in 2018–2021, the Chinese economy will grow by 4–5.6% a year; the growth rates in the EU and Russia will be in range of 1.6–1.9% and 1.4–1.5%, respectively. Therefore, in 2019–2021, the external demand for Kazakhstan's commodities will slightly decline.

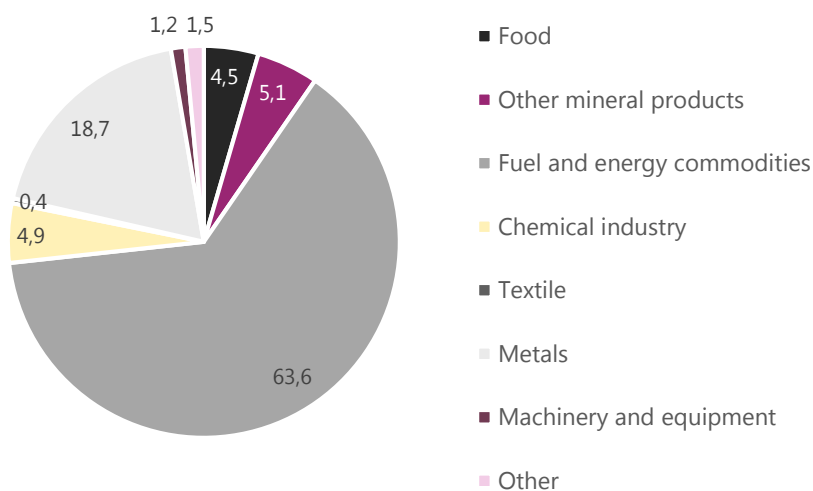
<sup>4</sup> Source: the Statistics Committee of the Ministry of the National Economy of the Republic of Kazakhstan, ACRA estimates (data for January–August 2017).

**Figure 1. Kazakhstan import profile by product group: natural diversification (% , January-August 2017)**



Source: the Statistics Committee of the Ministry of the National Economy of the Republic of Kazakhstan, ACRA estimates

**Figure 2. Kazakhstan export profile by product group: fuel and energy commodities are most important (% , January-August 2017)**



Source: the Statistics Committee of the Ministry of the National Economy of the Republic of Kazakhstan, ACRA estimates

### **Current account will be negative irrespective of stably positive net exports**

The 2017 payment balance will mostly reflect higher net exports (about plus USD 17 bln for products and minus USD 4 bln for services) and stably high balances of primary incomes, which is caused by payments to non-residents under direct investments.

In 3Q2017, a period of substantial growth in direct investments ended; its peak was in 2–3Q2016. The total of direct investments amounted to USD 12.3 bln. This amount resulted in a negative financial account for 2016 (USD 8.6 bln). The balance of services and the balance of secondary incomes have also impacted, but not overwhelmingly, the current transactions account.

In the forecast period, we see the following key trends in the external sector of the economy: stably high payments on the balances of incomes and a positive and relatively stable net export. In 2017–2021, it will vary within USD 17.5–18.1 bln. Being negative, the trade balance in services will grow up to USD 5.1 bln by 2021. The total goods turnover will grow thanks to goods (37% up) and external services (1.5 times up). Unlike the trade balance, which will stabilize on the short-term horizon, the investment income balance is more volatile due to payments to non-residents under direct investments. ACRA expects that, in the forecast period, the current transactions account will be in the negative area, with the negative balance getting stronger by 2021. The external sector of the Kazakhstan's economy will be most impacted by the exchange-rate policy and the volumes of direct investments. In its current estimates, ACRA proceeds from the assumption that the floating exchange rate of tenge will not be subject to a change in the forecast period.

See ACRA outlook

[Russian government to become a net borrower and Kazakhstan government to remain a net creditor in 2018](#)

published July 27, 2017.

**Figure 3. Kazakhstan export-import outlook**



Source: the Statistics Committee of the Ministry of the National Economy of the Republic of Kazakhstan, ACRA estimates

### By late 2018, real personal incomes may finally start to grow in Kazakhstan

Until 2021, the Kazakhstan's macro-economy will not be affected by demographic trends (mere 3% of population is employed in the mining industry, an added value growth driver). In extraction industries, one employee yields 4.7 times more added value than the national average (except extraction industries). Taking into account a heavy dependence of Kazakhstan on the commodities

See ACRA research

[Low inflation in Russia to force the government and businesses to seek new forms of flexibility](#) published October 9, 2017.

sector, in the midterm, the labor force dynamics will not play such a significant role as in more diversified economies.

Unless a threat of major migration flows arises, the Kazakhstan's population will grow annually by 260 thousand people on average in the foreseeable future. In 2021, the annual average population of the country will grow up to 19.1–19.2 mln people.

At the same time, regardless of the step-by-step and stable population growth (2014 was the peak year), the economically active population tends to decline slowly. In the midterm, the unemployment rate is forecasted to be lower than the current level. By end-2021, the rate will go down from 4.9% to 4.6%, as growing mining industries drive services sector (63% employees are employed at the tertiary sector<sup>5</sup>) and real personal incomes, which stabilize under a restrained inflation.

Real money incomes have continued to fall year-on-year. We expect that by the end of 2017, they will drop by 4–5%. The real income index will be able to enter the plus area only next year and only under more restrained inflation. Decreasing inflationary tendencies and inter-sectoral flows of added value will lead to the fact that by the end of 2021, the aggregate real incomes of the population will grow by 1–2%.

It should be noted that the approved draft national budget for 2018–2020, based on a more conservative vision, will restrain growing real incomes. In ACRA's opinion, the monetary factors will contribute approximately 50% to inflation. We believe that the NBK's monetary policy will not result in a decline in the CPI below the official corridor of 5% set for 2018, which will restrain the restoration of real personal incomes.

Since 2016, real salaries, similar to real incomes, have been characterized by a weak negative dynamics. Positive dynamics may arise in 2018, only after the effect of revenues from raw materials is fully embodied. As with the real personal incomes, the near-stagnation dynamics will not exceed 3% yoy.

### Industry sector becomes an economic driver again

After a restrained growth in 2015–2016, the industrial sector of Kazakhstan have entered the stage of consistent development. By late 2017, the national industry will gain momentum. The real growth will be 6.3%, driven by the mining industry (8.2% up) and processing capacities (less impressive, 4.5% up). In 2017, the aggregate contribution of the industry sector to the growing GDP amounted to 1.65 pps (the share of mining industry is 1.1 pps).

The increasing production of oil, gas and metal ore has played the most significant role. From 2H2016 to 2017, those industries have shown more than a strong dynamics. It is explained primarily by the low base at the start of 2016, as well as by a relatively favorable price environment. At the same time, in the forecast period, the impetus for growth in the extractive industries will weaken: it will drop to about 5% in the mining segment and to about 4% in the processing segment. The industry will show a 4.6% growth by the end-2021.

See ACRA research

[Recovering prices for non-ferrous metals to boost import substitution in Russia](#) published September 13, 2017.

<sup>5</sup> According to the three-sector theory of Clark-Fisher (quaternary and quinary sectors are excluded because the economy of Kazakhstan may not be categorized as 'developed post-industrial').

The services sector has been showing signs of recovery. The growth of 1.5–2% is most likely. Until 2021, the positive trend will get stronger. The accelerating dynamics in the volume of services will be driven by the restoring real salaries and a subsequent, albeit slow, decline in the unemployment down to 4.7%.

The agricultural sector of Kazakhstan, which has been in the growth zone since 2013, may also show a slight upswing in the current year. The sector is extremely volatile: standard fluctuations in its yearly dynamics in real terms is almost three times higher than that of real GDP.

In 2017, the construction sector got an additional positive impulse from the projects related to Expo 2017<sup>6</sup>. Like the transport and communications sector, this segment of the economy is not a basic growth driver and, being dependent on the industrial growth and purchasing power of the population, it will show a restrained growth.

**Table 2. Real sector and wholesale and retail sale profile in Kazakhstan, GDP share**

GDP segment	GDP share, %, 2012	GDP share, %, 2016	GDP share, %, 2021 (ACRA estimate)
Agriculture, forestry and fishery	4.3%	4.6%	3.6%
Mining industries	17.1%	12.9%	14.7%
Processing industries	11.1%	11.3%	11.9%
Electric power supply	1.7%	1.7%	1.8%
Water supply	0.3%	0.2%	0.2%
Construction	6.2%	5.9%	5.8%
Wholesale and retail sale	14.9%	16.8%	16.2%
Transportation and warehousing	7.4%	8.3%	7.7%

Source: the Statistics Committee of the Ministry of the National Economy of the Republic of Kazakhstan, ACRA estimates and forecast

### Inflation will decline within the NBK's target corridor

At the end of 2015, Kazakhstan experienced a devaluation shock. By early 2017, the situation had completely stabilized: the inflation rate entered the 6–8% target corridor established by the regulator. The further trajectory of consumer inflation assumes its gradual decrease in 2017 down to an annual average of 7.5%. In subsequent years, the decline will continue — down to 6.9% in 2019 and to 6.5% in 2021.

Slowing down inflation in Russia, which directly affects the food inflation in Kazakhstan, will serve a price stability factor. Inflationary pressure will be stronger with the growing influence of real industrial growth on other sectors of the economy. The most significant slowdown in inflation will occur in 2H2018, after the weaker industrial growth year on year is recognized. The dynamics of many factors (for example, the volume of commodity exports) remains ambiguous from the forecasting viewpoint, as increase in oil exports in excess of the limits set by the OPEC+ agreement largely depends on the political attitude.

See ACRA research

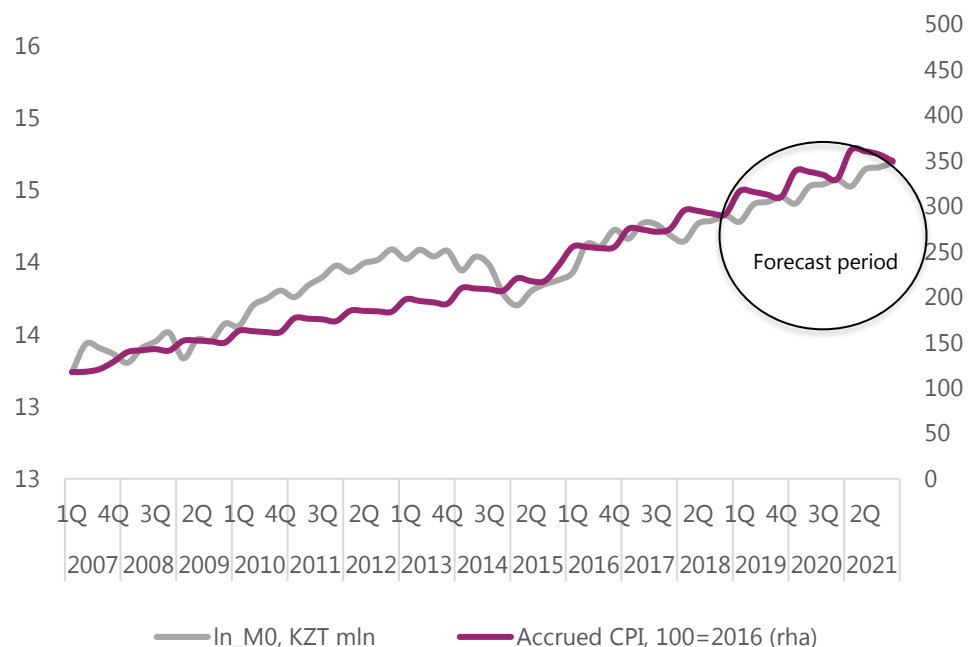
[Although a favorable period in the iron & steel industry is running its course, creditworthiness of Russian producers would improve](#)  
published November 16, 2017.

<sup>6</sup> Expo is an international exposition, a symbol of industrialization and a site open for technological achievements.

Since 2H2016, after the exhaustion of the devaluation shock, the consumer price index in Kazakhstan has been correlating with the dynamics of cash in circulation, lagging behind by two or three calendar quarters. At the same time, the inflation risks are structural and, unless the current structure of consumer inflation change, the CPI will respond sharply to monetary policy: non-food—to a greater degree, food—to a lesser degree. It will react less clearly to changes in the labor costs (first, services, second, food). ACRA is of the opinion that the above is associated with a slow translation of the economic growth into incomes and a potential increase in the exchange rate volatility.

In the forecast period, with a slowing down cooling of inflation, the base rate of the National Bank of Kazakhstan will continue to decline slightly, restraining domestic lending. The regulator will finish the 2017 with the base rate equal to 10–10.25%. By 2018, the rate is projected at 9%.

Figure 4. CPI and Ln\_M0<sup>7</sup>



Source: the Statistics Committee of the Ministry of the National Economy of the Republic of Kazakhstan, the National Bank of Kazakhstan, ACRA estimates

### Forex interventions by the NBK indicate to a potential change in the exchange-rate regime

After almost a year's break, the National Bank of Kazakhstan intensified its forex interventions in June 2017. In June–October, the volume of interventions reached USD 0.62 bln. Given the intensification of this trend month on month (the largest volumes were in October), the regulator's opposition to the free floating KZT exchange rate will mean a return to a forcibly maintained exchange rate and an imputed exchange rate imbalance, with stronger dollarization of banking products and melting currency reserves of the NBK.

In 2016–2017, the regulator also increased significantly its obligations under short-term notes (in September, notes circulation exceeded 150% of tenge in

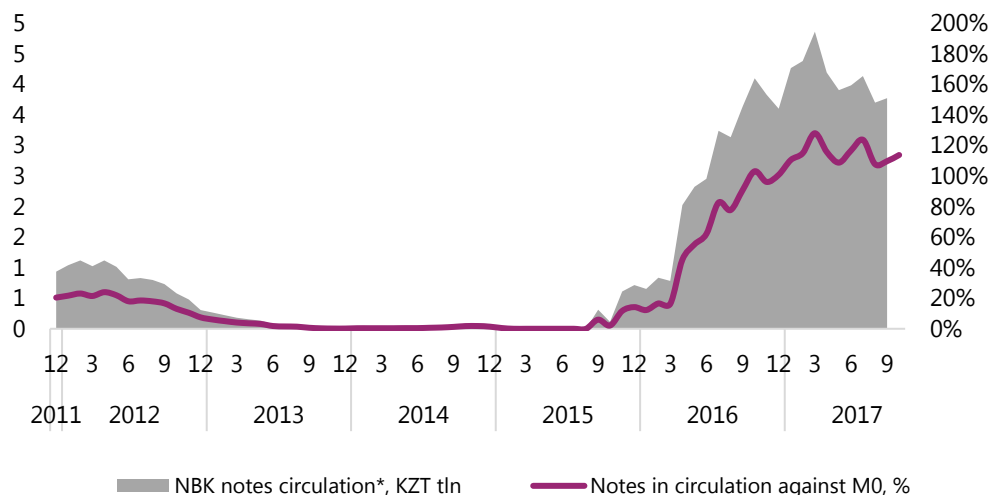
<sup>7</sup> Ln\_M0 is a natural logarithm of monetary aggregate M0, which includes cash in circulation.



circulation). Such policy, in the absence of the government's forex interventions, would fit well into the stated scenario, but, in the current conditions, it increases uncertainty.

The NBK policy is even more unclear, as the real KZT exchange rate is low against either Russian ruble or a basket of currencies. Since the NBK has not made any official statements about any changes in the regime, the regulator sends ambiguous signals to the currency market.

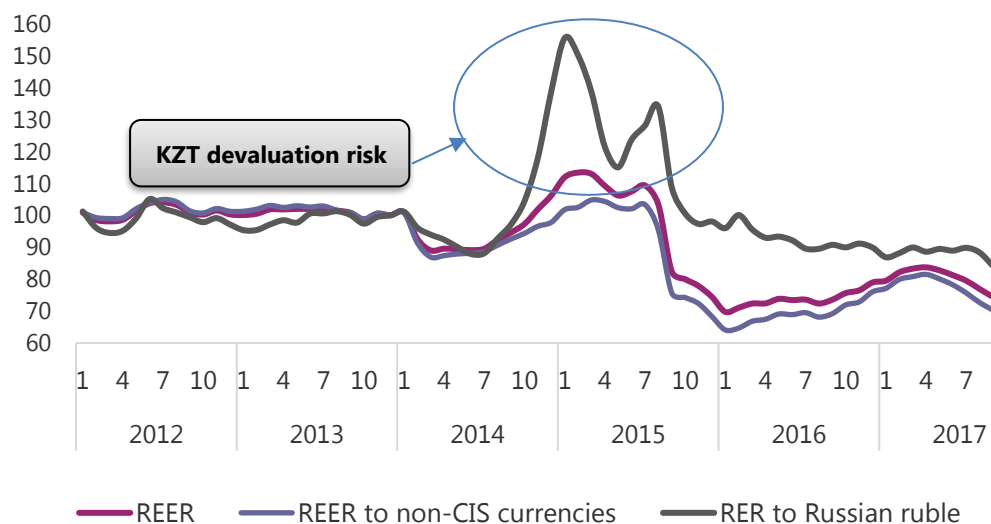
**Figure 5. In 2016–2017, the regulator has increased its obligations under short-term notes**



\* The National Bank of Kazakhstan

Source: the National Bank of Kazakhstan, ACRA estimates

**Figure 6. In 2016–2017, the KZT devaluation risk is insignificant**



Source: the National Bank of Kazakhstan, ACRA estimates

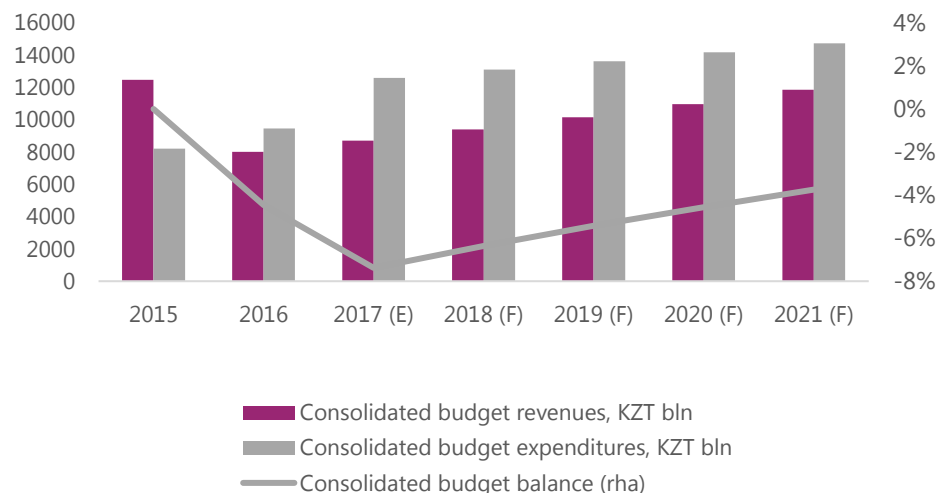
**The Government is hard on budget transfers and expects revenues to grow in 2018–2020**

The 2017 state budget is expected to have a deficit of 3.3%, which implies a 22% growth of revenues (yoy) in nominal terms and a 33% growth of expenditures.

The 2018–2020 state budget is based on the oil price of 45 USD/bbl and the KZT/USD exchange rate of 340. On the one hand, the scenario is quite optimistic: with the oil price of 45 USD/bbl, the above tenge rate can be maintained only under a fixed exchange-rate regime. On the other hand, the scenario is conservative: in ACRA's opinion, the Urals oil price will fluctuate in the range of 53–56 USD/bbl in the budget period. Therefore, since the free exchange-rate regime is expected to be applied, eventually, the budget may be closed with less deficit.

The key purpose of the national budget policy is to decrease the dependence of the budget on fund transfers from the National Fund of the Republic of Kazakhstan. The 2018–2020 consolidated budget that includes transfers from the National Fund contains plans to reduce guaranteed annual transfers down to KZT 2 tln (in the previous three-year period, the transfer amounted to KZT 2.9 tln) and to cancel special-purpose transfers. Such a conservative budget paradigm suggests that, in the forecast period, a stable economic growth is expected, accompanied with a corresponding expansion of the tax base. The budget also includes expenditures for special state support programs (Nurly Zher<sup>8</sup>, Nurly Zhol<sup>9</sup>, 2020 Regional Development Program<sup>10</sup>, Digital Kazakhstan<sup>11</sup>), therefore, the budget revenue component is expected to increase significantly. According to ACRA estimates, the Kazakhstan consolidated budget deficit will shrink from 6.4% of GDP in 2018 to 3.7% of GDP in 2021.

**Figure 7. In the forecast period, the consolidated balance of Kazakhstan's budget will be in deficit area**



Source: the Ministry of Finance of Kazakhstan, ACRA estimates

<sup>8</sup> Nurly Zher is a state housing construction program of Kazakhstan for 2015–2019.

<sup>9</sup> Nurly Zhol is a transport and logistics program of Kazakhstan for 2015–2019.

<sup>10</sup> 2020 Regional Development Program is a plan for territorial and spatial development of the country until 2020, designed by the Ministry of National Economy and implemented in the period from 2015 to 2019.

<sup>11</sup> Digital Kazakhstan is a program aimed at formation of a digital eco-system for sustainable economic growth.

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