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# Kazakhstan

Growth slowed to 5.0% from 7.5% in 2011, as industry largely stagnated and severe drought cut agricultural output by nearly 18%. Inflation also slowed. Rapid import growth, linked partly to public investment programs, narrowed the current account surplus to 4.3% of GDP from 7.2% in 2011, but assets in the country's sovereign wealth fund again increased. Growth is expected to recover slowly, to 5.2% in 2013 and 5.6% in 2014, as continued government investment spending boosts domestic demand.

## Economic performance

After 2 years of strong recovery, economic growth slowed to 5.0% from 7.3% in 2010 and 7.5% in 2011 (Figure 3.4.1). The service sector was again the main source of growth, while the contributions of agriculture and industry fell to their lowest levels in 15 years.

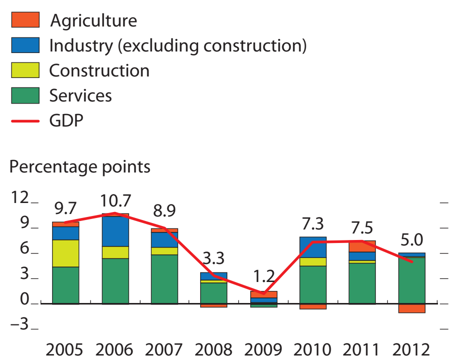
Services, which generate more than half of GDP, rose by 9.8%, reflecting more than 14% growth in retail and wholesale trade and smaller gains in communications, transport, and hotels and restaurants. Professional services rose by 16.2% and public services by 12.2%.

Agriculture contracted by 17.8%, mostly from poor harvests. Severe drought almost halved grain output from the record high harvest in 2011, despite major investments and producer subsidies. Industrial production grew only marginally, by 0.5%, compared with 3.7% in 2011, reflecting weak growth in mining (0.2% versus 1.3% in 2011) and manufacturing (0.7% versus 6.2% in 2011), the latter reflecting a decline in metallurgical production. In the broad mining sector, crude oil output declined by 1.4%, while coal extraction grew by only 1.7% and natural gas by 3.1%. Construction expanded by 2.9% (about the same as in 2010 and 2011), again benefiting from state-led projects under a program to accelerate industrial and innovative development and incentives for residential construction.

On the demand side, consumption expanded by 11.4%, with public consumption growing more quickly than private consumption (Figure 3.4.2). Growth in net exports slowed to 10.0%, as imports grew much more rapidly than exports. Fixed capital investment grew by 3.8%, up from 2.8% in 2011, reflecting faster growth in investments by small and medium-sized enterprises.

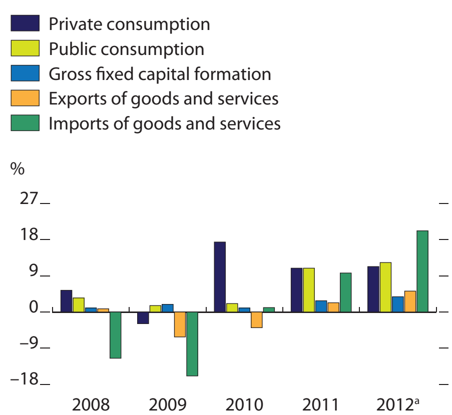
Inflation slowed from 8.3% in 2011 to a post-independence low of 5.1%, reflecting a dramatic slowdown in food prices, mainly for grain products, to 4.5% from 11.9% in 2011, and a smaller decline in inflation for nonfood goods, to 4.3% from 5.4% in 2011. Prices for services rose by 6.8%, as in 2011, including double-digit increases for transport, telecommunications,

**3.4.1 Supply-side contributions to growth**




*Source:* Agency of Statistics of the Republic of Kazakhstan.
*Click here for figure data*

**3.4.2 Growth of GDP demand components**




[a] Data for 2012 are for 9 months only.
*Source:* Agency of Statistics of the Republic of Kazakhstan.
*Click here for figure data*

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and postal services. Inflation accelerated somewhat beginning in August but remained moderate over the full year. The 12-month (December over December) rate decelerated to 6.0% from 7.4% in December 2011 (Figure 3.4.3).

Fiscal policy was more expansionary in 2012, as the deficit in the republican budget expanded to 3.0% of GDP from 2.1% in 2011. Receipts reached 15.5% of GDP, including 4.6% ($9.2 billion) in transfers from the National Fund of the Republic of Kazakhstan (NFRK, the sovereign wealth fund), down somewhat from total receipts of 16.1% of GDP in 2011. Expenditure amounted 18.5% of GDP, up from the 18.2% recorded in 2011. The adoption of several new social programs, including measures to develop small towns and build affordable housing, helped boost expenditures.

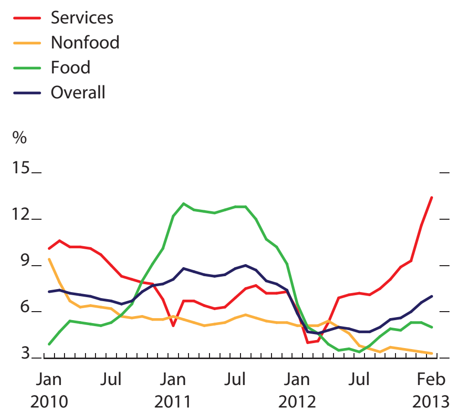
At the end of September 2012, public external debt stood at $30 billion, or 15% of GDP, 3 percentage points of which was government and government-guaranteed debt, the other 12 points being the debts of state-owned enterprises. Including the domestic debt of state-owned enterprises, estimated at 10%–12% of GDP, and that of the government and central bank, estimated at 12.2% of GDP, total public sector debt approached 37%–39% of GDP.

Monetary policy was eased in 2012, reflecting slower inflation. The central bank gradually reduced the policy interest rate from 7.5% in February to a post-independence low of 5.5% in August of 2012. Broad money growth slowed to 7.9% from the 15.0% in 2011, reflecting slower currency expansion and a decline in corporate deposits. The increased need for budget financing raised interest rates on short-term government notes to 2.14% from 1.63% in 2011. The tenge exchange rate fluctuated within the range of T147.8–T150.5 per $1, with an average rate of T149.1 for the year, depreciating from T146.6 in 2011 as the central bank avoided major interventions in the market (Figure 3.4.4). However, the real effective exchange rate against a basket of 34 currencies appreciated by 5.2%.

The banking sector is still beset by problems, despite efforts by the government and the central bank to improve the situation. The percentage of nonperforming loans has been growing since 2009, climbing to 37% by the end of 2012 from 35% a year earlier. A fifth of banks are losing money, with the largest losses at BTA Bank, which was nationalized in 2009 and underwent a second restructuring of its external debt in 2012. Several banks applied for assistance from the central bank's distressed assets fund established in April 2012. Some of the largest created subsidiaries to deal with nonperforming loans, which have made many banks risk averse, prompting them to invest excess liquidity in short-term government securities and central bank notes. This has suppressed rates on these assets.

The current account surplus diminished to 4.3% of estimated GDP from 7.2% in 2011, as faster growth in imports shrank the trade surplus (Figure 3.4.5). The services deficit expanded by $1.3 billion, or 20%, while outward transfers tripled to $1 billion from $0.3 billion in 2011. The deficit in the capital and financial account, including errors and omissions, narrowed to about $11.5 billion from $13.3 billion in 2011, largely reflecting a better position for short-term capital. Net foreign direct investment

**3.4.3 Inflation**




*Source:* Agency of Statistics of the Republic of Kazakhstan.
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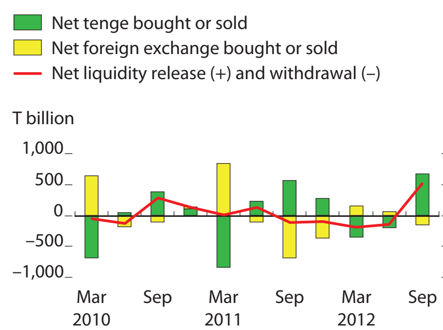
**3.4.4 Central bank currency interventions**




*Source:* National Bank of Kazakhstan. 2012. *Financial Stability Report.*
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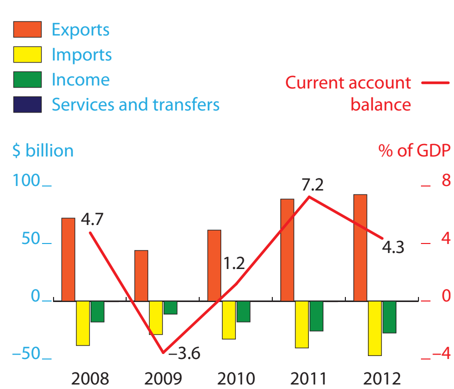
**3.4.5 Current account indicators**



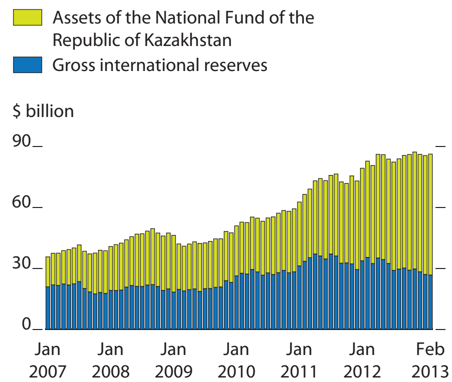

*Source:* National Bank of Kazakhstan.
Click here for figure data

grew by 40% to $12.7 billion from $9.1 billion in 2011, as investments abroad contracted from $4.6 billion to $1.4 billion and inward foreign direct investment rose modestly, from $13.7 billion to $14.2 billion. A net $16.7 billion outflow on portfolio investments was largely explained by the $14 billion rise in the NFRK's foreign assets and the almost $1 billion decline in Kazakh banks debt liabilities—and possibly a significantly greater decline with BTA Bank debt amortization.

The central bank's gross international reserves rose during the first half of the year but fell from August, as the central bank used part of its reserves to replenish the NFRK, ending the year at $28.3 billion, or $1.1 billion less than a year earlier. NFRK assets grew steadily, totaling $57.8 billion at the end of 2012 (Figure 3.4.6).

Total external debt—more than half owed by local subsidiaries to their parent multinational firms—was estimated at 67.3% of GDP at the end of September 2012, marginally down from 70% a year earlier. The country's net foreign position, including balances in the NFRK, contracted by $1.7 billion and stood on 1 January 2013 at $11.9 billion.

**3.4.6 Foreign exchange reserves and fund assets**




*Source:* National Bank of Kazakhstan.
*Click here for figure data*

## Economic prospects

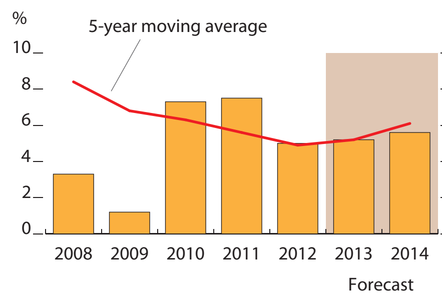
GDP is forecast to grow by 5.2% in 2013 and 5.6% in 2014, largely reflecting higher domestic demand, including investment spending under the industrialization program and the more active investment of NFRK assets (Figure 3.4.7). Some $1.5 billion of NFRK assets will be lent to the national oil company KazMunaiGas in 2013, and $2.5 billion more in 2014. Economic performance will also depend on demand from Kazakhstan's major trading partners: the European Union, Russian Federation, and People's Republic of China. Production from the Kashagan project, postponed again in 2012, is now expected to begin in the second half of 2013 with limited scope before expanding in 2014 to boost oil exports.

Construction and development for Kazakhstan's Expo 2017 will expand government investment but may also raise public debt unless the private sector participates. The adoption in February 2013 of a program to develop agribusiness will require a substantial $20 billion of public support during 2013–2020, potentially attracting three times as much in private investment. The government is initiating a new law on public–private partnership to finance and implement large social and infrastructure programs.

Inflation is expected to remain moderate but toward the middle of the central bank's 6%–8% target range, reflecting the continued administration of prices, the use of special food stabilization funds in the regions, and a conservative monetary policy. Tariffs for services, including transport and communal utilities, will continue to rise in 2013, affecting the cost of all goods.

Fiscal policy is expected to remain somewhat expansionary, with a bias towards spending for industrialization, social modernization programs, and social safety nets. However, the republican budget deficit is forecast to narrow to 2.1% of GDP in 2013 and 1.8% in 2014 (Figure 3.4.8). The budget deficit will be covered through internal and external borrowing, including about $1 billion in sovereign Eurobonds in 2013—$500 million in the first half of the year.

**3.4.7 GDP growth**




*Source: Asian Development Outlook* database.
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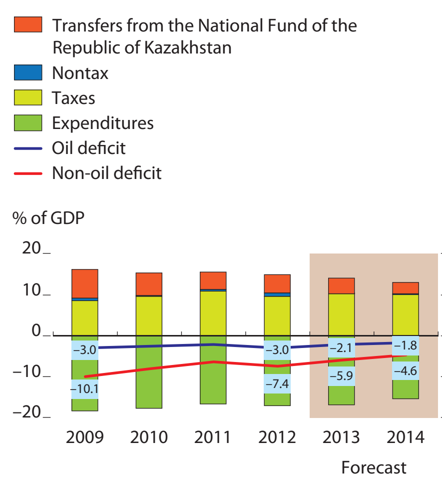
**3.4.8 Fiscal indicators**




*Source:* The Ministry of Finance of the Republic of Kazakhstan.
*Click here for figure data*

Republican budget revenues, including transfers from the NFRK, are forecast to slide from 15.5% of GDP in 2012 to 14.8% in 2013 and 13.5% in 2014 (Figure 3.4.9). Tax receipts should gradually rise from 62% of revenue in 2012 to 74% in 2014, while transfers from the NFRK should remain unchanged in 2013 and decline in 2014. Revenue could be higher if the Kashagan and Karachaganak projects start operations in 2013. In addition, a new feature called "conditional financing," limited to 4% of republican budget expenditure, will be introduced in 2013, to fund more regional programs if current revenue improves.

Total expenditure is forecast to fall to 16.9% of GDP in 2013 and 15.3% in 2014. The planned reform of the pension system will merge 11 funds into one asset management fund and gradually align pension ages for women and men, which may help reduce outlays beginning in 2014.

Monetary policy is expected to remain conservative, with the central bank adjusting its policy rate as needed to contain inflation. Moderate inflation is anticipated, along with a low policy interest rate to encourage commercial banks to cut their interest rates. The central bank is expected to regulate the financial sector in a strong but low-profile manner, focusing in 2013 on cleaning the balances of commercial banks and improving access to finance for priority sectors of economy. As part of this policy the national holding company SamrukKazyna must dispose of its shares in three nationalized banks by the end of 2013. The central bank has enough capacity to keep the exchange rate relatively stable but is not expected to intervene against major trends in the exchange market, having lost over $6 billion in reserves during 2007–2008.

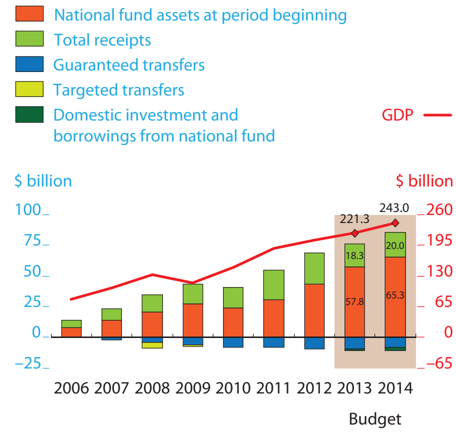
The current account balance could achieve surpluses of 2.5% of GDP in 2013 and 4.0% in 2014, if oil prices are stable (Figure 3.4.10). However, current forecasts anticipate some oil price declines in 2013 and no improvement in metals prices, so surpluses may be smaller. Exports in 2013 and 2014 are forecast to increase by 1%–2% of GDP, reflecting higher oil production. Imports are expected to grow much more quickly to maintain outlays for the program to accelerate industrial and innovative development. This will narrow the current account balance.

Ongoing projects to resolve transport bottlenecks, expand oil fields, and improve infrastructure will not take full effect in 2013 or 2014, possibly meaning further outflows in services and remittances. Reserves are expected to remain largely unchanged from the end 2012, while higher oil prices further build NFRK assets, now projected to reach $75 billion, or 30% of GDP, in 2014.

## Policy challenge—energy efficiency

Although its primary energy reserves are among the largest in the world, Kazakhstan does not meet its domestic energy needs. In 2011 Kazakhstan had the world's third most energy-intensive economy, in terms of energy consumption per unit of GDP. Its emissions of greenhouse gases per unit of GDP are also very high. In addition, the energy system and its regional distribution companies face major risks from limited network capacity, outdated equipment, high losses, and inadequate or absent control systems, while tariffs set too low for cost recovery preclude network reconstruction or modernization. The current electricity market

### 3.4.9 GDP and national fund cash flows



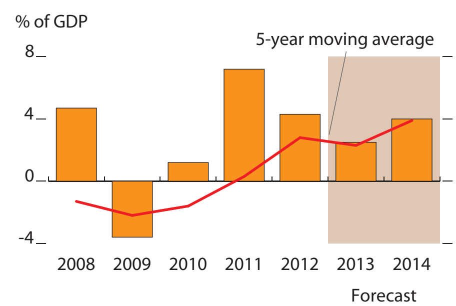

*Source:* The Ministry of Finance of the Republic of Kazakhstan.
*Click here for figure data*

### 3.4.1 Selected economic indicators (%)

| | 2013 | 2014 |
|---|---|---|
| GDP growth | 5.2 | 5.6 |
| Inflation | 6.7 | 6.5 |
| Current account balance (share of GDP) | 2.5 | 4.0 |

*Source:* ADB estimates.

### 3.4.10 Current account balance




*Source: Asian Development Outlook* database.
*Click here for figure data*

and legislative and regulatory frameworks make constructing new power plants unattractive. The government has pursued several programs in recent years to involve the private sector in developing and operating energy facilities, but with mixed results.

High energy intensity reflects the predominance of energy-intensive industries and outdated energy infrastructure. Some 30 industrial enterprises consume over 70% of electricity, and comparisons with the European Union show that more than two-thirds of them could reduce their energy intensity. Moreover, almost 90% of electricity is generated by coal-fired plants with barely one-third of the efficiency of similar plants in advanced economies. Over 70% of the population gets district heating from 40 solid-fuel combined heat and power plants operating in 29 cities. These plants date from the 1960s to the 1980s, and almost all are past their service lives, as evidenced by network distribution losses and frequent failures. High energy intensity defeats coping with demand surges. Additional generation capacity could reduce the supply deficit, which would require new investment.

The government considers energy efficiency a critical pillar of its energy policy. A law on energy saving and energy efficiency came into effect in July 2012, to be followed by supporting legislation. The goal is to reduce energy intensity by 10% in 2015 from the 2008 level and by 25% in 2020. In addition, the government has launched its Green Economy Initiative, to reduce greenhouse gas emissions by 15% in 2020 from the 1992 level and by 25% in 2050.

Kazakhstan could benefit from revived energy trading within Central Asia, which would enable it to draw on its neighbors' hydropower through the regional electrical system that connects Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan. Drawing from pooled transnational assets would reduce the need for reserve power and allow the export of seasonal excess energy supplies to the People's Republic of China, India, Iran, and Pakistan. While transnational energy and water resources would need coordinated management, a study conducted under the Central Asia Regional Economic Cooperation estimates the potential regional economic benefits of energy trading in 2013–2015 could be $2 billion without major infrastructure or system investments.