

KAZAKHSTAN

Growth slowed in 2022 mainly because of temporarily interrupted oil production and delivery. Inflation accelerated on currency depreciation, supply chain disruption, and fiscal stimulus, while high global energy prices turned a persistent current account deficit into a surplus. Growth will accelerate in 2023 and 2024, driven by recovering industry, services, and domestic demand. Inflation will subside with tight monetary policy and price controls, assuming a stable exchange rate. As regional disparities widen, addressing them requires place-sensitive policies and improved fiscal decentralization and redistribution.

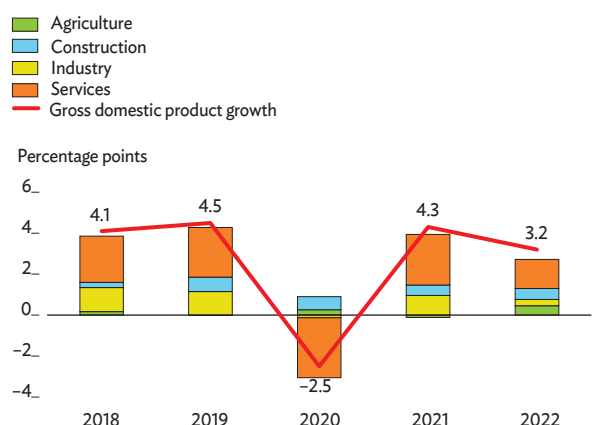
Economic Performance

Disruption to oil production slowed economic activity in 2022, despite high petroleum prices and robust growth in agriculture and construction.

Growth decelerated from 4.3% in 2021 to 3.2% as the economy coped with supply chain disruption, exchange rate volatility, and higher interest rates from tight monetary policy (Figure 2.4.1). On the supply side, mining reversed 1.9% growth in 2021 to decline by 1.0% as production fell for iron ore by 20.6% because of disrupted exports to a sanctioned enterprise in Russia, for oil by 1.9% because of interrupted flows through the Caspian Pipeline Consortium and breakdowns in the Kashagan oil field, and for gas by 1.0%. Growth in industry slowed from 3.6% in 2021 to 1.0% as manufacturing expansion decelerated from 4.7% in 2021 to 3.4% despite support from investment and import substitution measures. Expansion in services also slowed, from 4.4% to 2.6%, despite gains of 8.0% in communications, 5.0% in trade, and 3.9% in transport and warehousing. Growth in construction accelerated from 8.3% in 2021 to 9.4% as subsidized state mortgage programs and pension funds boosted finance for housing. Agriculture reversed drought-induced 2.2% contraction in 2021 to expand by 9.1% as crops rebounded by 15.0% and livestock edged up by 0.9%.

Figure 2.4.1 Supply-Side Contributions to Growth

Growth slowed in 2022 with smaller increases in industry and services.



Source: Bureau of National Statistics of the Agency for Strategic Planning and Reforms of the Republic of Kazakhstan.

Rising exports offset declining consumption.

Data on the demand side, available for only the first 9 months of 2022, show consumption reversing 4.1% growth during the same period in 2021 to decline by 1.5%. Private consumption fell by 1.0% as rising inflation cut real incomes. Growth in investment roused from

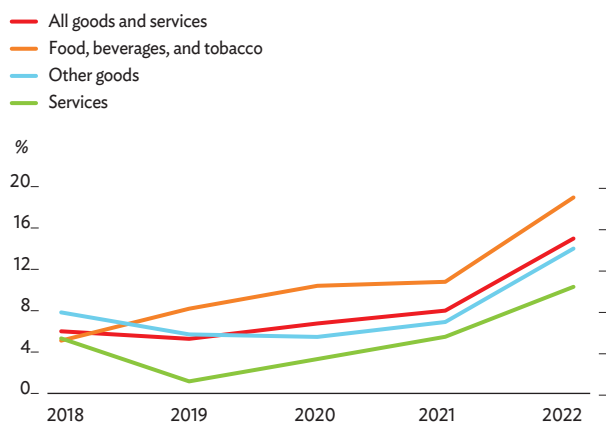
zero in 2021 to 1.0% on a 3.0% expansion in gross fixed capital formation. The key growth driver was an 18.0% rise in exports of goods and services that outpaced an 11.2% increase in imports.

Inflation accelerated sharply to double digits.

Average annual inflation accelerated from 8.0% in 2021 to 15.0% in 2022, reflecting supply chain disruption, shortages, currency depreciation, and rising transportation costs (Figure 2.4.2). Food price inflation rose from 10.8% in 2021 to 19.0%, with prices soaring by 62.8% for sugar, 31.5% for wheat, and double digits for many other staple foods. Inflation for other goods doubled from 6.9% in 2021 to 14.0% on rising inflationary expectations and depreciation of the tenge, by 8.1% against the US dollar and by 20.2% against the Russian ruble. In addition, an influx of migrants from Russia pushed up rents by 30.1% and nearly doubled the rate of price increases for services from 5.5% to 10.3%.

Figure 2.4.2 Average Inflation

Inflation accelerated in 2022, with increases in all major categories.



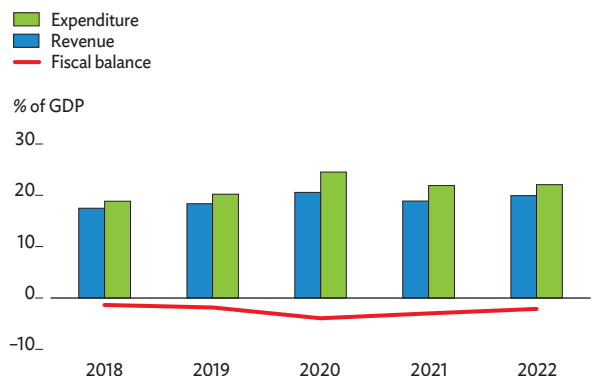
Source: Bureau of National Statistics of the Agency for Strategic Planning and Reforms of the Republic of Kazakhstan.

Expansionary fiscal policy accommodated economic support measures.

Expenditure edged up from the equivalent of 21.9% of GDP in 2021 to 22.1% in 2022 as state defense expenditure climbed by 49.4% from a relatively low base and outlays for education rose by 22.8% and for social spending by 11.6% (Figure 2.4.3). In April 2022, the government raised state expenditure by the equivalent of 2.8% of GDP, financed by transfers from the National Fund of the Republic of Kazakhstan, the sovereign wealth fund. The transfers

Figure 2.4.3 Fiscal Indicators

The fiscal deficit narrowed in 2022 as revenue rose more than expenditure.



GDP = gross domestic product.

Source: Bureau of National Statistics of the Agency for Strategic Planning and Reforms of the Republic of Kazakhstan.

marginally exceeded those in 2021 and constituted 22.6% of budget revenue. Total budget revenue increased from 18.9% of GDP in 2021 to 19.9% in 2022 as tax revenue jumped by an unexpectedly robust 38.4%, partly reflecting 58.5% higher oil export duty. The state budget deficit shrank from the equivalent of 3.0% of GDP in 2021 to 2.1%. Not counting large oil industry revenue, the deficit subsided from 9.6% of GDP to 8.2%.

Public debt remained low.

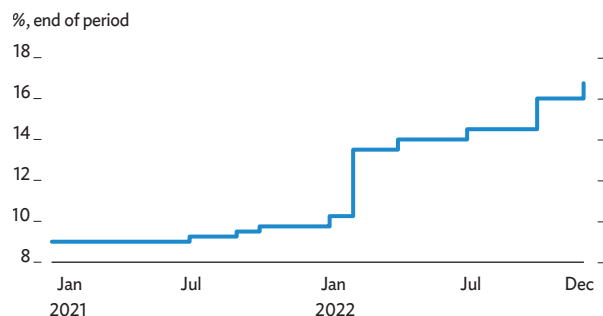
Government and government-guaranteed debt declined from 27.6% of GDP at the end of 2021 to 26.2% a year later. An estimated 63% of the debt was internal, denominated in local currency, and 87% of it had long-term maturity. Government debt service payments as a share of tax revenue declined from 9.1% in 2021 to 8.7% in 2022.

Monetary policy tightened in response to inflation.

In February, the National Bank of Kazakhstan, the central bank, sharply raised its key policy rate by 325 basis points to 13.5% following the Russian invasion of Ukraine (Figure 2.4.4). As inflation accelerated, the central bank raised the rate a further 50 basis points in both April and July, 150 basis points in October, and 75 basis points in December, reaching 16.75% by the end of the year. Growth in broad money (M3) slowed from 20.8% in 2021 to 13.9%, with bank lending rising by 20.1% and deposits by 18.9% (Figure 2.4.5). Mortgage lending expanded by 42.6% as the government extended a subsidized

Figure 2.4.4 Policy Interest Rate

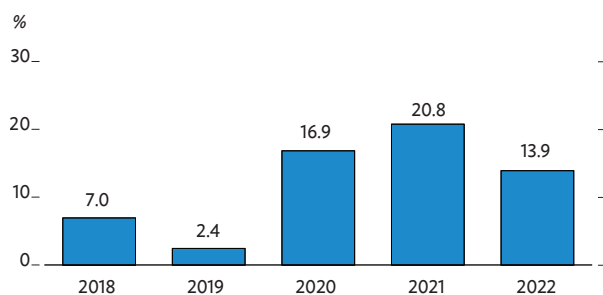
The policy interest rate was raised sharply in 2022 to restrain inflation.



Source: Haver Analytics.

Figure 2.4.5 Broad Money Growth

Broad money growth slowed noticeably in 2022.



Note: Broad money growth is the percentage change from December to December.

Source: National Bank of the Republic of Kazakhstan.

lending program. Total consumer lending grew by 25.1%. Lending to firms rebounded by 17.4% in 2022 after years of contraction, with loans to small and medium-sized enterprises rising by 16.3%. The share of nonperforming loans increased marginally from a historic low of 3.3% at the end of 2021 to 3.4% a year later. The central bank sold 6.4% more of its own short-term securities than in 2021, and government-issued domestic securities rose by 24.0% to finance the budget deficit. The share of foreign currency deposits declined from 37.2% of all deposits at the end of 2021 to 36.7%, and foreign currency loans decreased from 10.3% in 2021 of all loans to 8.1% in 2022.

High oil prices drove export earnings to a decade high that lifted the current account into surplus.

Preliminary estimates show a current account surplus equal to 2.8% of GDP in 2022, reversing a 4.0% deficit in 2021. The merchandise trade surplus almost

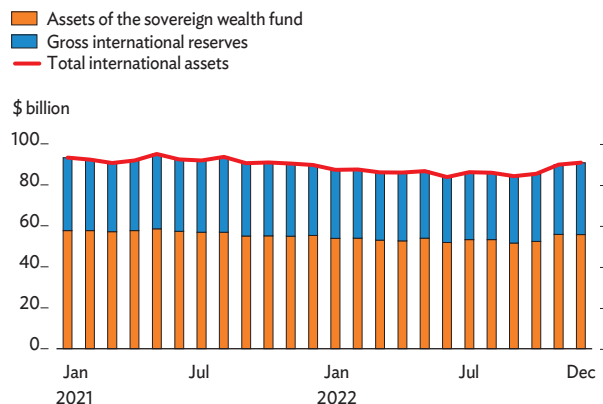
doubled for a second year in a row, benefiting from higher oil and gas prices. Merchandise exports rose by 40.7% to their highest amount in a decade, while merchandise imports grew by 19.6%. The deficit in services fell by a quarter as export growth, reflecting increased transit and personal travel, outpaced 18.0% increase in service imports. Profit repatriation rose modestly by 12.8%, widening the deficit in primary income, while higher outward money transfers pushed the secondary income account into deficit. Net inflow of foreign direct investment quadrupled, while portfolio investment outflow was the highest in a decade.

Strong external earnings boosted foreign exchange reserves.

Despite the central bank selling \$1.4 billion in reserves to support the currency, gross international reserves increased by 2.0% to \$35.1 billion at the end of 2022, providing cover for 7.2 months of imports. However, the share of reserves held in gold dropped from 68.5% at the end of 2021 to 58.4% a year later. Sovereign wealth fund assets fluctuated significantly and grew marginally, by 0.7%, to \$55.7 billion as windfall petroleum profits exceeded budget transfers and market value declines for fund assets (Figure 2.4.6). The sovereign wealth fund sold \$4.3 billion in foreign exchange on the market to finance budget transfers, and state-owned enterprises sold an additional \$5.1 billion. By the third quarter of 2022, external debt, 58.2% of it private intercompany debt, had declined sharply to equal an estimated 74.7% of GDP, reflecting debt repayment by foreign subsidiaries.

Figure 2.4.6 Foreign Currency Reserves and Sovereign Wealth Fund Assets

Gross international reserves and sovereign wealth fund assets fluctuated but finally grew in 2022.



Source: National Bank of the Republic of Kazakhstan.

Economic Prospects

Recovering oil production will accelerate

expansion. Growth is projected to increase to 3.7% in 2023 and 4.1% in 2024 as mining rebounds on higher oil production at the Kashagan and Tengiz oil fields (Table 2.4.1 and Figure 2.4.7). Projected price increases for the main export commodities will stimulate investment and support business sentiment. Spillover from sanctions on Russia poses the greatest risk to the outlook.

Table 2.4.1 Selected Economic Indicators, %

Growth will accelerate, and inflation slow, in 2023 and 2024.

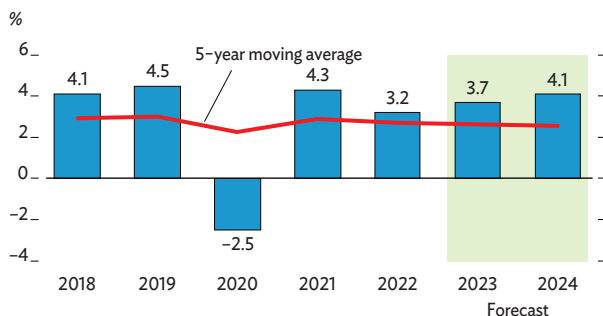
	2021	2022	2023	2024
GDP growth	4.3	3.2	3.7	4.1
Inflation	8.0	15.0	11.8	6.4

GDP = gross domestic product.

Sources: Bureau of National Statistics; National Bank of Kazakhstan; Asian Development Bank estimates.

Figure 2.4.7 GDP Growth

Growth is expected to recover in 2023 and 2024.



GDP = gross domestic product.

Source: Asian Development Outlook database.

Services and industry will become the main growth engines.

On the supply side, growth in services is forecast to accelerate from 3.4% in 2023 to 3.9% in 2024, supported by transport, trade, and hospitality and benefiting from greater trade facilitation between Europe and Asia. Growth in industry is forecast to jump to 4.7% in 2023 on strong external demand for commodities, with mining rising by 5.2%

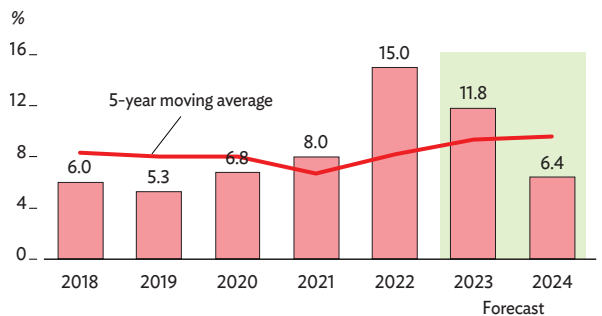
in that year, then slow to 4.3% in 2024, with mining increasing by 4.1%. Firms relocating from Russia and continued government support programs will expand manufacturing by 4.0% each year. Growth in construction will moderate to 5.5% in 2023 and 4.2% in 2024 as large infrastructure projects reach completion. Growth in agriculture will average only 3.5% in 2023 and 2024, reflecting a high base and limited investment inflow.

Consumer spending will support expansion. On the demand side, growth in consumption is projected to rebound to 1.6% in 2023 and 2.2% in 2024 as reduced inflation boosts real incomes and state social support allocations increase. Investment will increase by 3.2% and then 3.7% as companies relocate production facilities from Russia and state infrastructure development programs continue. Net exports are forecast to increase gradually in both years as rising commodity export volume outpaces import growth.

Inflation should gradually subside. Inflation is projected to slow to 11.8% in 2023 and 6.4% in 2024, reflecting tight monetary policy and presuming a stable currency (Figure 2.4.8). Price controls and export restrictions on food staples are projected to slow food price increases to 14.0% in 2023 and 8.6% in 2024. The government extended its ceiling price for gasoline, and market regulation will hold inflation for other goods to 10.0% in 2023 and 5.0% in 2024. Inflation in services is projected to accelerate to 10.6% in 2023 before subsiding to 4.8% in 2024, with the government allowing utility price increases in exchange

Figure 2.4.8 Inflation

Inflation is projected to slow in 2023 and 2024.



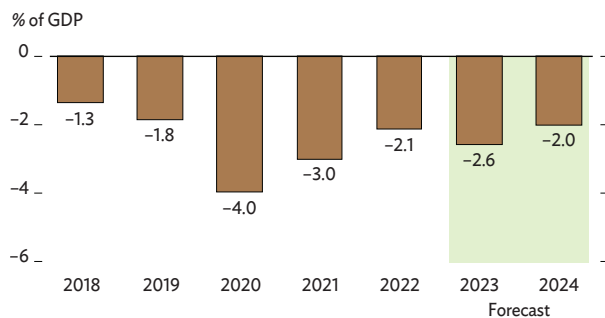
Source: Asian Development Outlook database.

for investment. Focused on bringing inflation down toward the target range of 4%–5%, the central bank will maintain an elevated policy rate in 2023 to manage inflationary expectations until inflation subsides in 2024. Broad money growth is projected to slow to 8.4% in 2023 and 6.4% in 2024 as the central bank drains excess liquidity from the market by issuing securities. The central bank will intervene to contain exchange rate volatility following any exogenous currency shock.

The fiscal deficit will expand as sovereign wealth fund transfers decline. Despite rising tax revenue, total revenue is projected to slide to the equivalent of 18.7% of GDP in 2023 as transfers from the sovereign wealth fund are curtailed, and then increase marginally to 18.9% in 2024 (Figure 2.4.9). Expenditure is forecast to drop to 21.3% of GDP in 2023 and 20.9% in 2024 as economic support programs are phased out. With lower sovereign wealth fund transfers, the budget deficit is projected to widen to 2.6% of GDP in 2023 before narrowing to 2.0% in 2024, with the non-oil deficit narrowing to 7.2% of GDP in 2023 and 6.8% in 2024.

Figure 2.4.9 Fiscal Balance

The fiscal deficit will widen in 2023 before narrowing in 2024.



GDP = gross domestic product.

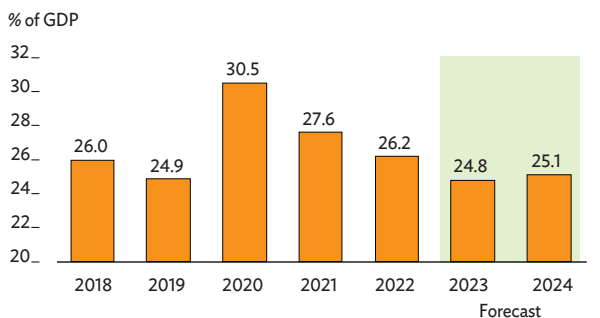
Source: Asian Development Outlook database.

Public debt is forecast to remain stable.

Government and government-guaranteed debt is projected to decline as a share of GDP to 24.8% by the end of 2023, rising marginally to 25.1% a year later (Figure 2.4.10). New fiscal rules, including limits on sovereign wealth fund transfers and expenditure

Figure 2.4.10 Public Debt

Public debt is projected to stay near the equivalent of 25% of GDP in 2023 and 2024.



GDP = gross domestic product.

Source: Asian Development Outlook database.

growth, should support long-term debt sustainability. External debt is expected to decline to about 74% of GDP at the end of 2023 and 72% a year later as state-owned enterprises repay foreign debt and foreign-owned subsidiaries repay intercompany debt.

The current account surplus is expected to narrow over the forecast period.

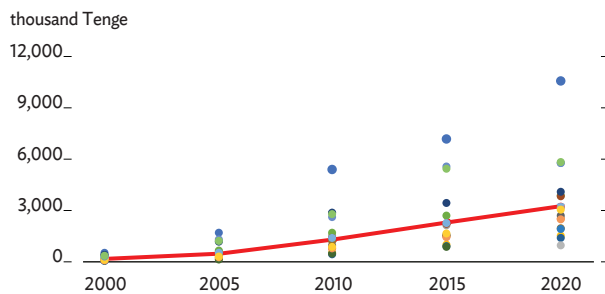
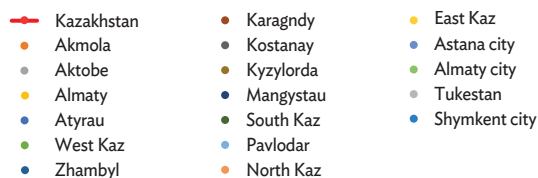
Increasing oil production and relatively high commodity prices will support a modest 0.8% expansion of export earnings in 2023, while imports are projected to grow by 10.3%. The service deficit will gradually narrow as revenue from transit services increase. As commodity investors continue to enjoy and repatriate windfall profits, the primary income deficit will continue. However, outward transfers are expected to decline in 2023, closing the secondary income deficit. Gross international reserves are projected to increase to \$37.2 billion in 2023, providing cover for 7 months of imports, and reach \$40.5 billion in 2024, assuming little intervention in the foreign exchange market. Sovereign wealth fund assets are forecast to expand to \$58 billion in 2023 and exceed \$60 billion in 2024 as budget transfers fall below inflows and earnings.

Policy Challenge—Address Worsening Regional Disparity

Widening regional disparity spurred protests in January 2022. Over the past two decades, Kazakhstan’s economy has performed well, with GDP increasing tenfold, but wealth has become concentrated regionally (Figure 2.4.11). An ADB consultant’s report in 2021 found economic polarization widening among Kazakhstan’s regions, with some stuck in a development trap. The Regional Competitiveness and Cohesion Index, which examines growth, employment, and productivity, revealed considerable regional gaps in opportunity and competitiveness. Large urban areas and resource-rich regions enjoyed exceptionally high wealth, while agrarian and more populous southern regions lagged far behind and struggled to benefit from growth.

Figure 2.4.11 Gross Regional Product per Capita

Gross product per capita varies significantly across regions.



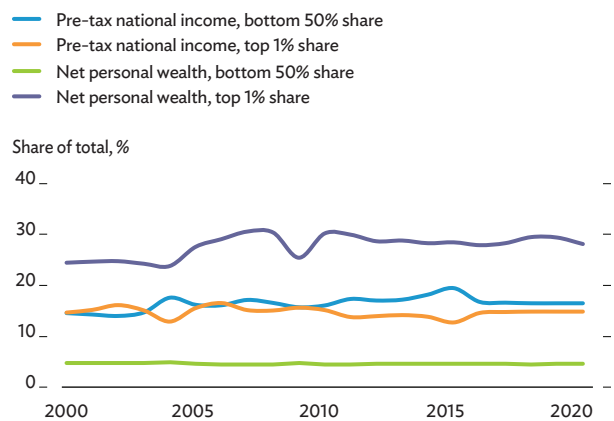
Note: Gross regional product per capita in current prices. Kazakhstan country values are calculated as the arithmetic average of regional values. Source: Kazakhstan Statistical Department.

Standard indexes that show relative income equality do not reflect the high share of informal employment and disparity across regions. The main traditional inequality measure, the Gini index, ranks Kazakhstan as a relatively equal country. However, the index does not capture the shadow economy and hides underreporting among high earners. The World Inequality Database estimates that the top 1% of

Kazakh adults received 15.0% of all income in 2021 and owned 29.2% of all wealth, while the bottom half of the population earned 16.4% of all income and owned only 4.6% of wealth (Figure 2.4.12). Stark inequality also shows in variation in the quality of social services and infrastructure across regions and in people’s access to them. A 2021 report on the education systems nationally estimated a 50% gap between the regions performing best and worst in education effectiveness.

Figure 2.4.12 Income and Wealth Inequality in Kazakhstan

Kazakhstan’s top 1% had 6 times the wealth of the bottom 50% from 2010 to 2020.



Source: World Inequality Database.

Government increasingly devotes more attention to regional development issues. The government has implemented since 2019 its Auyel-Besigi program to improve the quality of life in rural areas by modernizing infrastructure in settlements determined by the government to have potential. In 2022, the government approved the main guidelines for regional development by adopting its Plan for Territorial Development until 2025. More recently the President promulgated a law delegating greater autonomy and decision-making authority to selected metropolitan areas. These programs could better address regional development issues if design and implementation stages include more active public engagement.

Unlocking the potential of all regions and ensuring inclusive growth requires more nuanced and supportive national policies. The government needs to provide guidelines that are flexible enough

to adapt programs to local needs and strengthened implementation capacity in regional government. Suitably flexible regional development programs would be able to adapt to differing regional needs and challenges and promote place-sensitive policies that reflect differences in regional development. This approach would require better coordination between the central and regional governments. Because place-sensitive policies delegate decision-making and empower local authorities, their success depends on adequate regional capacity and institutional development. Corruption and lack of transparency can easily thwart well-intended policies. Introducing local performance audits conducted by independent third parties would instill accountability and improve value for money.

Fiscal decentralization and redistribution policies require development and fine tuning. Since 2018, seven types of tax and nontax revenue have been transferred to subnational governments. However, taxes account for a small share of subnational budgets, as nearly 60% of their revenue comes as transfers from the central government budget. The fiscal redistribution system needs improvement to take into account residents' quality of life and to motivate regional and local authorities to raise living standards. Regularly scheduled surveys that assess perceptions of well-being can be valuable for monitoring and guiding resource allocation to address the most pressing regional and local issues.