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Kazakhstan: Fast growth is back, but sustainability problems remain

The Kazakh economy experienced a remarkable rebound in 2010: real GDP growth is estimated to exceed 7%. The driving force behind that fast growth was a revival of external demand for the country's key commodities – oil and metals (together they account for about 80% of Kazakhstan's exports). Growth of industrial production in these sectors accounted for almost two thirds of total industrial growth in 2010. wiiw forecasts that Kazakhstan's GDP growth will slow down in 2011, to 5.5%, due to the higher base for comparison in 2010; in 2012-2013 the economy will grow by 5% per annum.

The oil and metals sectors will continue to play a dominant role in the Kazakh economy during 2011-2013, as increasing global demand for these commodities will allow for fast growth of their exports. According to the recent forecast by the US Energy Information Administration, in 2011, the price of West Texas Intermediate crude oil will average about USD 93 per barrel, USD 14 more than in 2010. In 2012-2013, the oil price will remain above USD 90 per barrel, but is not likely to exceed USD 100 per barrel. China will further gain importance as an export destination for Kazakhstan – in particular, for exports of oil, non-ferrous metals, and uranium. China has been trying to ensure supplies of these commodities by signing long-term agreements on supply (recently a ten-year deal to supply uranium was signed), providing loans to the Kazakh government and investing into the country's oil extraction and energy transit infrastructure.

Private consumption also picked up in 2010, showing about 7% real growth after a 3% decline in 2009 on the back of an increase in household incomes and employment. Real wages are estimated to have increased by 7.4% in 2010, and employment by 4.4%. This also gave a boost to retail trade which expanded by about 12%, after a 2% decline in 2009. In 2011-2013, private consumption is expected to grow by 5% per annum owing to further increases in household incomes – in particular, due to wage increases in public administration, education and healthcare envisaged in the state budget. The share of household consumption in Kazakhstan's GDP remains quite low – around 40% – and will not increase significantly in the short run, when the economy will rely relatively more on net exports and investment as sources of growth.

Investment experienced a significant decline in 2010; according to our estimates, gross fixed capital formation fell by 9% last year. The sluggish construction sector, the lack of access to loans as sources of financing by many enterprises, and the postponing of investment by oil extracting companies contributed to those dynamics. During the forecasting period, however, we expect a revival of investment which will grow faster than private consumption. The major factors behind the expected investment pick-up are the following:

- Budget spending in 2011-2013 within the 'Programme of accelerated industrialization and modernization 2010-2014'. The programme envisages investment of about EUR 9 billion into infrastructure projects, in particular the building of the Western Europe-Western China corridor, upgrading railroads and agriculture infrastructure.
- Increase in investment into oil transit infrastructure. Shareholders in the Caspian Pipeline Consortium agreed to invest USD 5.4 billion to double capacity of the pipeline linking Kazakhstan with the Russian Black Sea.

The reviving economy allowed for rallying general budget revenues: in 2010, tax revenues rose by 32% year-on-year (y-o-y). Budget expenditures grew fast as well, but at a slower rate than revenues. We forecast that the government will continue to increase both current and capital expenditures. However, booming revenues would allow for fiscal consolidation, and the budget deficit will gradually decrease to 1% in 2013.

The consequences of the housing bubble and the banking crisis still remain visible in the economy and pose an impediment to growth. According to our estimates, value-added in financial services decreased by about 5% in 2010. Though there are no problems with liquidity in the banking sector now, the high share of non-performing loans (NPL), the still heavily leveraged non-oil sector and the lack of low-risk borrowers limit the possibilities of banks to issue loans and makes them invest in low-return money market instruments. In 2010, the loans stock decreased by 5.3% as compared with 2009; the decline in newly issued loans was even more profound, 7.2% y-o-y. Monthly dynamics showed some recovery at the end of 2010: in December, the decline in the loans stock slowed down to 0.6% y-o-y along with an increase in primarily short-term loans to the corporate sector. Yet growth in the banking sector is going to remain quite anaemic during the forecasting period, as resolving the problems with NPLs and deleveraging of the non-oil sector will require some time.

The construction and real estate sectors, which together accounted for 24% of Kazakhstan's GDP in 2009, also continued to suffer from the housing bubble consequences and remained stagnant in 2010. Closer to the end of 2010, a slight revival in construction and the real estate market started, partially due to state support to the construction sector; no new construction projects were started though. We expect that poor access to mortgage loans of households and ongoing deleveraging of the construction sector will make the sector's recovery slow.

High oil revenues allowed for an increase in forex reserves and national oil fund assets by about one third in 2010 as compared to 2009. The achieved financial stability and the good prospects for retaining it in the future caused the National Bank of Kazakhstan to announce the plan to switch from the exchange rate corridor to a managed float in 2011. It is expected that a small revaluation of the tenge will be allowed, in particular to deal with inflationary pressures. However, big changes in the exchange rate are not likely as the National Bank will watch attentively KZT/USD developments and will intervene if there is increasing pressure on the tenge in any direction. Therefore we envisage a slight revaluation of the tenge during the forecasting period, from an average rate of 147 KZT/USD in 2010 to 140 KZT/USD in 2013.

Inflation remains a concern for the National Bank, with food prices contributing the most to CPI growth. In 2011-2013, monetary sources of inflation will remain weak, but the expansionary fiscal policy and growing incomes of households, as well as high global food prices will continue to create an upward pressure on prices. We expect that inflation will remain in the 6-7% range during the forecasting period.

The 2011 survey 'Freedom in the World', released by Freedom House, shows that Kazakhstan, similar to Russia, remains a not free country in terms of both political rights and civil liberties, and the situation has been worsening. President Nursultan Nazarbayev and his Nur Otan party continue to maintain almost complete control over the political sphere, using tactics including arbitrary arrests, censorship of opposition media, and politically motivated prosecutions of opposition and human rights activists. Kazakhstan chaired the OSCE last year, which brought the country into the spotlight and attracted more attention of the West to the problems with human rights there. The initiative of the authorities in December 2010 to conduct a referendum which would extend the presidency of Nazarbayev by ten years until 2020 was finally cancelled by the President, who apparently decided not to further worsen the country's external image and called for early presidential elections. It is unlikely though that the opposition will have any chances of fair competition and winning the elections.

At the same time conditions for doing business in Kazakhstan have been improving as measured in the World Bank report: in 2010, the country's rank improved by 15 points to 59, with the biggest improvement recorded in the sphere of starting a business. The only deterioration concerned the possibility of obtaining credits. However, in the long run the authoritarian regime in the country, which creates vast incentives for corruption and thus poor governance, and also inhibits entrepreneurship, is likely to hurt Kazakhstan's economic competitiveness.

d in January 2010 has been still in the transitory phase, thus the effects of it on the Kazakh economy are yet to be seen. Among the issues that have not been solved so far are unharmonized standardization and certification standards, the division of customs revenues among the three states and the incorporation of energy-related sectors into the customs union framework. Besides, Kazakhstan was granted a transition period until 2015 for the harmonization of more than 400 tariff lines. The first effects can be seen only in those sectors which experienced a significant increase in import tariffs (mostly consumer goods such as furniture, footwear, pharmaceuticals etc.).

Table KZ

Kazakhstan: Selected Economic Indicators

| | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 ¹⁾ | 2011 | 2012 | 2013 |
|--------------------------------------------------------------|--------|--------|--------|--------|--------|--------------------|-------|----------|-------|
| | | | | | | | | Forecast | |
| Population, th pers., average | 15147 | 15308 | 15484 | 15674 | 15910 | 16230 | 16500 | 16600 | 16600 |
| Gross domestic product, KZT bn, nom. | 7591 | 10214 | 12763 | 16053 | 16100 | 19800 | 23000 | 25600 | 28500 |
| annual change in % (real) | 9.7 | 10.7 | 8.7 | 3.3 | 1.2 | 7.1 | 5.5 | 5 | 5 |
| GDP/capita (EUR at exchange rate) | 3000 | 4200 | 4900 | 5800 | 4900 | 6200 | 7400 | 8300 | 9400 |
| GDP/capita (EUR at PPP - wiiw) | 7300 | 8000 | 8800 | 8800 | 8600 | 9200 | . | . | . |
| Consumption of households, KZT bn, nom. | 3686 | 4547 | 5468 | 6871 | 7200 | 8200 | 9200 | 10300 | 11500 |
| annual change in % (real) | 10.9 | 12.7 | 11.0 | 6.3 | -3 | 7 | 5 | 5 | 5 |
| Gross fixed capital form., KZT bn, nom. | 2123 | 3084 | 3857 | 4309 | 4541 | 4800 | 5900 | 6600 | 7500 |
| annual change in % (real) | 28.1 | 29.7 | 17.3 | 1.0 | 1.9 | -9 | 10 | 7 | 7 |
| Gross industrial production | | | | | | | | | |
| annual change in % (real) | 4.8 | 7.2 | 5.0 | 2.1 | 2.7 | 10 | 5 | 6 | 6 |
| Gross agricultural production | | | | | | | | | |
| annual change in % (real) | 7.3 | 7.0 | 8.4 | -5.6 | 13.8 | -11.7 | 12 | 5 | 5 |
| Construction industry | | | | | | | | | |
| annual change in % (real) | 47.4 | 28.6 | 5.7 | 1.8 | -4.9 | 1 | 5 | 8 | 10 |
| Employed persons - LFS, th, average | 7261.0 | 7403.5 | 7631.8 | 7857.2 | 7903.4 | 8250 | 8420 | 8500 | 8590 |
| annual change in % | 1.1 | 2.0 | 3.1 | 3.0 | 0.6 | 4.4 | 2 | 1 | 1 |
| Unemployed persons - LFS, th, average | 640.7 | 625.4 | 578.8 | 557.8 | 554.5 | 460 | . | . | . |
| Unemployment rate - LFS, in %, average | 8.1 | 7.8 | 7.3 | 6.6 | 6.6 | 5.8 | 5.7 | 5.5 | 5.5 |
| Reg. unemployment rate, in %, end of period | . | . | . | . | . | . | . | . | . |
| Average gross monthly wages, KZT | 34060 | 40790 | 53238 | 60734 | 67639 | 76000 | . | . | . |
| annual change in % (real, gross) | 11.7 | 10.3 | 17.8 | -2.5 | 3.8 | 7.4 | . | . | . |
| Consumer prices, % p.a. | 7.6 | 8.6 | 10.8 | 17.1 | 7.3 | 7.4 | 7 | 6.5 | 6.5 |
| Producer prices in industry, % p.a. | 23.7 | 18.4 | 12.4 | 36.9 | -22.2 | 15 | 12 | 5 | 6 |
| General government budget, nat. def., % GDP | | | | | | | | | |
| Revenues and grants | 28.1 | 27.9 | 22.6 | 25.1 | 21.8 | 21.7 | . | . | . |
| Expenditures and net lending | 22.3 | 20.4 | 24.3 | 27.2 | 24.8 | 24.4 | . | . | . |
| Deficit (-) / surplus (+), % GDP | 5.8 | 7.5 | -1.7 | -2.1 | -3.1 | -2.7 | -2.5 | -2.0 | -1.0 |
| Public debt, nat. def., in % of GDP | 9.3 | 11.3 | 7.2 | 8.3 | 12.9 | 16.2 | 14 | 12 | 12 |
| Central bank policy rate % p.a., end of period ²⁾ | 8.0 | 9.0 | 9.0 | 10.5 | 7.0 | 7.0 | . | . | . |
| Current account, EUR mn ³⁾ | -848 | -1525 | -5355 | 4742 | -2400 | 3100 | 3900 | 3200 | 2800 |
| Current account in % of GDP | -1.8 | -2.4 | -7.0 | 5.2 | -3.1 | 3.1 | 3.2 | 2.3 | 1.8 |
| Exports of goods, BOP, EUR mn ³⁾ | 22734 | 30881 | 35309 | 48905 | 31500 | 45000 | 51000 | 56200 | 60600 |
| annual growth rate in % | 37.1 | 35.8 | 14.3 | 38.5 | -35.6 | 42.9 | 13 | 10 | 8 |
| Imports of goods, BOP, EUR mn ³⁾ | 14442 | 19216 | 24288 | 26128 | 20636 | 23402 | 28400 | 32700 | 36000 |
| annual growth rate in % | 29.9 | 33.1 | 26.4 | 7.6 | -21.0 | 13.4 | 21 | 15 | 10 |
| Exports of services, BOP, EUR mn ³⁾ | 1790 | 2237 | 2596 | 2978 | 3100 | 3200 | 3400 | 3600 | 3900 |
| annual growth rate in % | 10.7 | 25.0 | 16.1 | 14.7 | 4.1 | 3.2 | 6 | 6 | 8 |
| Imports of services, BOP, EUR mn ³⁾ | 6021 | 6947 | 8491 | 7474 | 7219 | 7808 | 9200 | 10300 | 11500 |
| annual growth rate in % | 46.5 | 15.4 | 22.2 | -12.0 | -3.4 | 8.2 | 18 | 12 | 12 |
| FDI inflow, EUR mn ³⁾ | 1583 | 4958 | 7440 | 9882 | 9000 | 7200 | 8800 | 9500 | 10400 |
| FDI outflow, EUR mn ³⁾ | -117 | -309 | 2369 | 2590 | 2200 | 2400 | 2300 | 2500 | 2700 |
| Gross reserves of NB excl. gold, EUR mn | 5965 | 14525 | 11970 | 13711 | 16184 | 21360 | . | . | . |
| Gross external debt, EUR mn | 36643 | 56252 | 65436 | 76417 | 77881 | 83428 | . | . | . |
| Gross external debt in % of GDP | 79.9 | 87.2 | 86.0 | 84.3 | 99.5 | 82.4 | . | . | . |
| Average exchange rate KZT/EUR | 165.42 | 158.27 | 167.75 | 177.04 | 205.67 | 195.67 | 189 | 186 | 182 |
| Purchasing power parity KZT/EUR, wiiw ⁴⁾ | 68.78 | 83.19 | 93.40 | 116.41 | 118.11 | 132.16 | . | . | . |

1) Preliminary and wiiw estimates . - 2) Refinancing rate of NB. - 3) Converted from USD with the average exchange rate. - 4) wiiw estimates based on the 2005 International Comparison Project benchmark.

Source: National statistics (National Bank, Agency of Statistics etc). Forecasts by wiiw.