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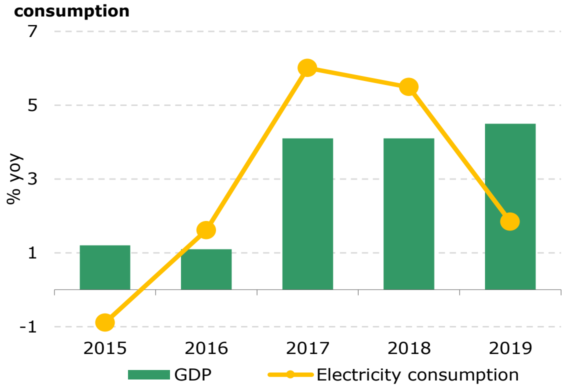
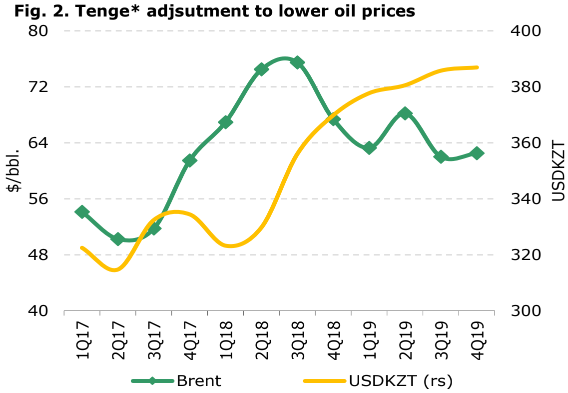
Fig. 1. Acceleration of GDP growth amid decline of electricity consumption



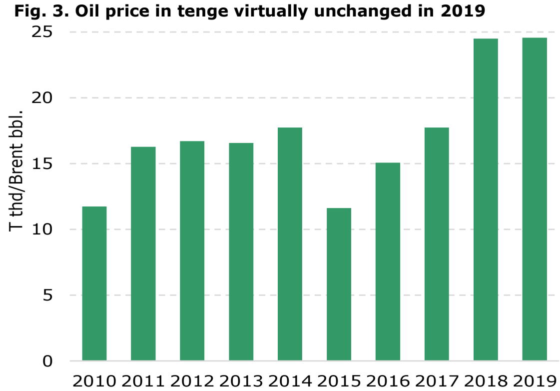
Source: MinFin RK, CS MNE

Fig. 2. Tenge* adjsutment to lower oil prices



Quarter averages Source: NBRK, Bloomberg

Fig. 3. Oil price in tenge virtually unchanged in 2019



Source: MinFin RK, Bloomberg

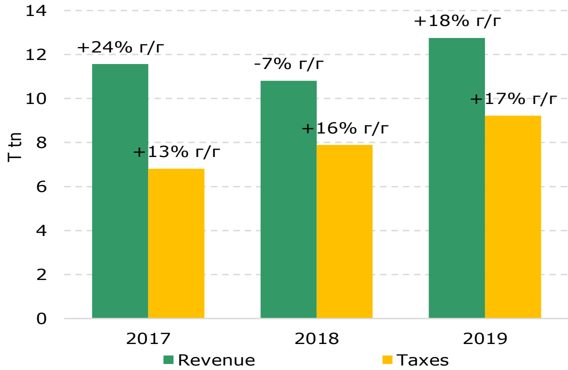
External economic conditions. In 2019, the cost of a barrel of Brent crude oil moved between $54-$75 with an average for the year of $64.2, which was higher than the average of $50 for 2015-2017, but below $71 in 2018 by about 11%. The pressure on oil quotes was exerted by the increase in oil production in the United States, with sluggish global demand amid a slowdown in the global economy.

In 2019, against the backdrop of launched fiscal stimulus, Kazakhstan's GDP growth accelerated to 4.5% from 4.1% in the previous two years (Fig. 1). The share of state budget expenditures relative to gross domestic product increased from 18.8% in 2018 to 20.4%. At the same time, this economic growth was not comprehensive - electricity consumption, an important component of economic development, significantly slowed down its growth from 5.5% in 2018 to 1.8% in 2019, in addition, there was a weaker growth in retail trade turnover – 5.8% versus 6.5%, in some regions there was a drop in business activity, industrial production was at the lowest level since 2017 - 3.8% versus 7.1%, while oil prices, and the national currency have fallen noticeable. As a result, the quality of economic growth remains low, while an increase in the government spending leads to a widening deficit.

In 2019 Tenge closely followed oil prices, showing a 10% weakening over the year. At the same time, the tenge value of a barrel of oil reached another record at T24.6 thousand and was more than twice its minimum at T11.6 thousand in 2015, when the tenge was let to free float (Fig. 3). As a result, the tenge's flexibility allows the budget to receive new recharge depending on the current situation and tends to continuously increase the tenge value of oil.

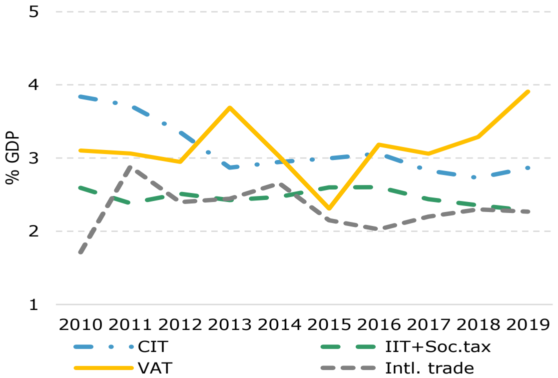
State budget revenues increased by T2 trillion to T12.8 trillion in 2019, where tax revenues increased by T1.3 trillion and transfers of the National Fund increased by almost half a trillion tenge or +18%, played the main role in increasing revenues. Tax revenue showed strong growth of 16.8%. As a result, the share of taxes in state budget revenues amounted to 72%, which was slightly lower than 73% in 2018, but higher than 65% and 59% in 2016-2017. A high growth rate was demonstrated by tax collections on company income + 17%, which is significantly higher than + 9.7% in the previous year and +7.1% in 2017. The increase in CIT payments is explained by the recovery of income from the second-tier banks that sagged in 2018, in addition, the improvement in administration played a role, for example, the taxes on CIT increased several times in Kyzylorda, Kostanay, oblasts and the city of Shymkent, in most other regions there was a double-digit growth rate collectability.

Fig. 4. Revenues and taxes increased



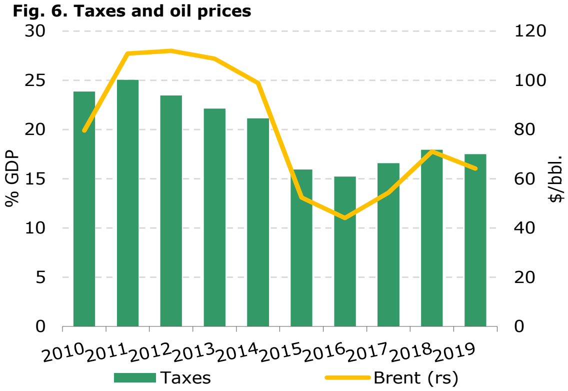
Source: MinFin RK, CS MNE

Fig. 5. Strong growth of VAT revenues



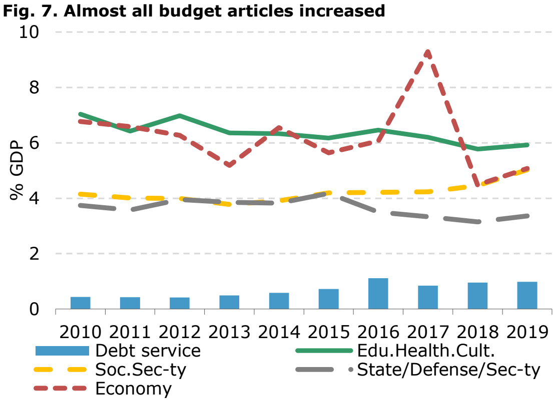
Source: MinFin RK, CS MNE

Fig. 6. Taxes and oil prices



Source: MinFin RK, Bloomberg

Fig. 7. Almost all budget articles increased



Source: MinFin RK, CS MNE

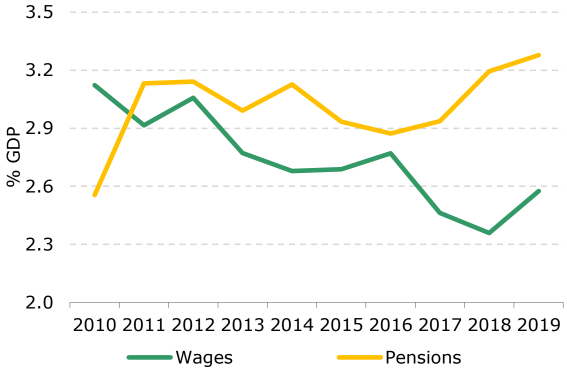
The amount of additionally counted taxes on business exceeded T340 billion. The fall in oil prices offset by the weakening of tenge led to an increase in revenues from the export duty on oil from T1 trillion to T1.1 trillion. Revenues from PIT and social tax increased moderately by 8%, and were at the lowest level since 2010 (+12.2% on average for the same period), which was due to tax breaks for people with low incomes – since 2019 the size of the IIT decreased 10 times for individuals with a salary of less than 25 MCI (T63 thousand) per month, in addition, the minimal wages growth increased the deduction for taxation of salaries. At the same time, the fees for PIT and social tax were 2% higher than planned, while for excise taxes the shortfall was at 5%, for VAT at 4%, for CIT at 2%. In general, we see that VAT collections account for the largest share of the state budget tax revenues at 4% of GDP, whereas previously CIT contributed the same figure, but after weakening of economic growth, CIT taxes have not yet reached 3% of GDP.

The size of the transfer from the National Fund increased significantly by 18.1% to T3.1 trillion in 2019 after it was at the level of T2.6 trillion in 2018. Moreover, earlier in 2018 it was planned to begin the consolidation of budget expenditures, the size of the transfer from the National Fund was supposed to decrease in 2019 to T2.3 trillion, against T3.1 trillion in fact in 2019, in 2020 to T2 trillion, however, due to a sharp transition to budgetary incentives, the transfer of the National Fund was revised upwards to T2.7 trillion in 2020.

Non-tax budget revenues increased by 57% and showed growth due to a four-fold increase in dividends from the state-owned shares in state ownership. Non-tax revenues also increased substantially by 27%, due to increased privatization of state property.

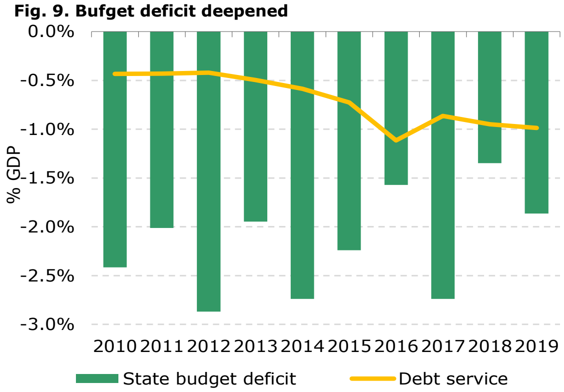
State budget outlays rose sharply by 20.6% to T14 trillion in 2019. The most significant increase was in social security expenses + 26% (25% share in total costs) and economic expenses +26.2% (25% share in total costs), but the increase in economic expenses was due to a strong decline in the previous year and in addition to this it also includes spending on various image projects that are inefficient and costly. All aggregated items of expenditures showed growth, while it is noticeable that total expenditures, with the exception of expenses on social security and debt servicing, are below their previous levels relative to GDP. Thus, expenditures on education, health care, culture previously reached 7% of GDP and only 5.9% in 2019, economic costs corresponded to 6.8% of GDP, but 5.1% last year (6.2% of GDP on average since 2010), public services, defense and security were previously close to 3.7% of GDP, 3.4% of GDP in 2019. Increased attention to the electorate is noticeable in the increased outlays on pensions, the expenditures for which reached 3.3% of GDP, against 2.6% of GDP in 2010.

Fig. 8. Due to increase of the budget workers wages its share in GDP went from decline to growth



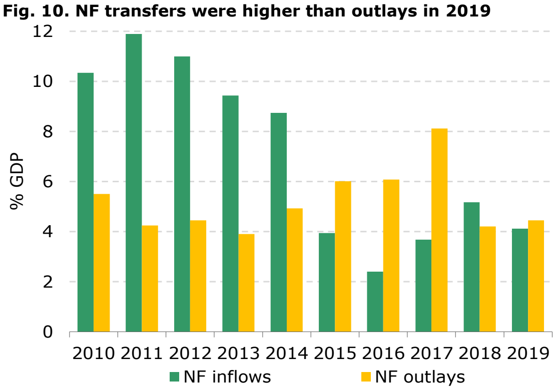
Source: MinFin RK, CS MNE

Fig. 9. Bufget deficit deepened



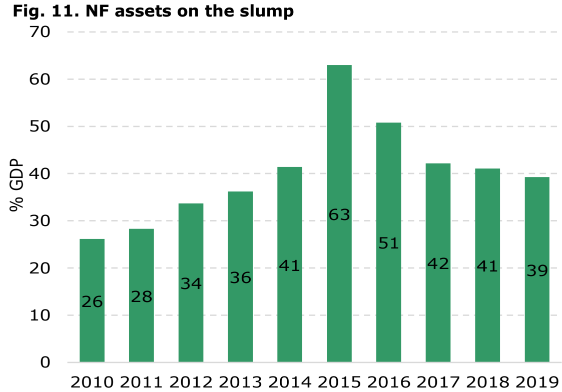
Source: MinFin RK, CS MNE

Fig. 10. NF transfers were higher than outlays in 2019



Source: MinFin RK, CS MNE

Fig. 11. NF assets on the slump



Source: MinFin RK, CS MNE

On the contrary, wage costs from the budget decreased from 3.1% of GDP in 2010 to a minimum of 2.4% in 2018, but thanks to increased funding in 2019, they grew to 2.6% of GDP. Thus, we see a growing orientation of budget expenditures on current consumption, which, among other things, stimulates imports, while the economy receives only a temporary catalyst for growth, which remains in effect while expenses are growing.

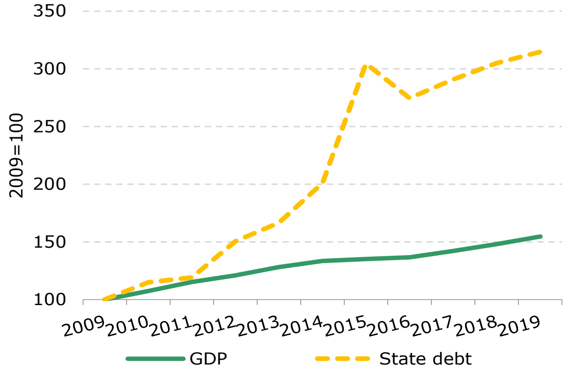
The state budget balance was better than expected and, in our estimation, amounted to -1.9% of GDP, against -2.1% of GDP planned by the government and -1.3% actual figure in 2018. As noted, a year ago, according to plans, the state budget deficit was planned to be reduced to -1% of GDP starting in 2019, but the adopted adjustments in the spring of 2019 significantly changed the budget situation, in addition to the backdrop of falling oil prices, the fiscal stimulus of the economy seems partly justified and timely. Although even without increased budget expenditures, economic growth was at an acceptable level, while the budget deficit could have been within 1% of GDP, which would have reversed the process of accumulation of public debt.

Revenues of the National Fund fell to T2.8 trillion in 2019 (excluding investment income) from T3.2 trillion in 2018. At the same time, an increase in the transfer from the National Fund to the budget from T2.6 trillion to T3.1 trillion led to the fact that the spending of the National Fund exceeded revenues by T0.2 trillion in 2019. The share of transfers in total state budget revenues in 2019 amounted to 24% and did not change over the year. The total assets of the National Fund last year fell to 39% of GDP from 41% a year earlier, which is the lowest reading since 2014.

Oil revenues fell by 6% in 2019 compared with an increase of 41% in 2018 and 61% in 2017. External economic factors provoked a fall in oil prices, which adversely affected oil revenues. Non-oil revenues, in turn, were slightly weaker, showing growth of 13%, which was lower than 14% growth in the previous year. As a result of the outstripping growth in non-oil revenues, the share of oil revenues in the consolidated budget revenue (including the operations of the National Fund) decreased from 35% to 31% in 2019 and is below 38% on average over the past 10 years.

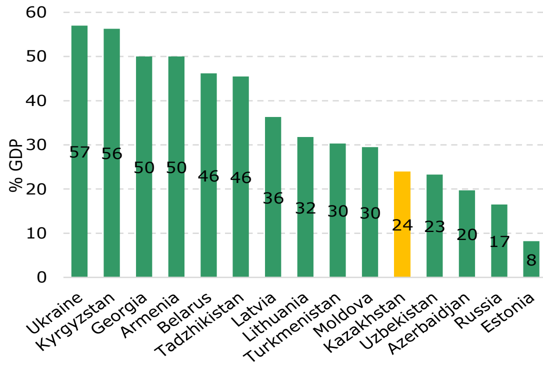
The size of the consolidated budget deficit, according to our estimates, increased to -3.1% in 2019 from -0.2% of GDP in 2018, the main reason for increase was the continuation of measures to clear the balance sheets of the second-tier banks, where more than T900 billion was directed. Size of the non-oil deficit grew to -8.8% according to our estimates from -7.1% of GDP in 2018. Although the non-oil deficit is at a fairly high level, it has been below 9.5% of GDP on average since 2009. Initiatives to reduce it so far remain on paper, while the economy is growing, opportunities to reduce dependence on oil revenues and normalize the budget may be missed.

Fig. 12. State debt outrun GDP growth



Source: MinFin RK, CS MNE

Fig. 13. Government debt



Source: MinFin RK, CS MNE

Government debt continued to grow and increased by 10.1% to T12.9 trillion at the end of 2019. It is noteworthy that the growth of government debt is almost continuously ahead of economic growth, as a result its size doubled from 9.5% of GDP in 2009 to 18.7% at present. Meanwhile, the state debt of Kazakhstan reaches 24% of GDP and is higher than in neighboring Uzbekistan and Russia (Fig. 13).

Our opinion

The economy reached a new level of growth that was facilitated by budget expenditures that increased to 20.4% of GDP and high investment activity. At the same time, the quality of economic growth is without improvement – structural changes are not visible, salaries were temporarily raised due to the budget, expenses mainly financed current needs (75% of total expenses), while the state budget deficit in 2019 widened to -1.9% of GDP from -1.3% a year earlier. The fall in oil prices by more than 10% was accompanied by a decrease in oil revenues by 6% and was partially offset by the depreciation of the national currency. Against the background of growth of tax revenues by almost 17%, the indicators of taxes on CIT, VAT and excise taxes were lower than planned. A positive point is the sharp increase in non-tax revenues of the state due to increased dividend payments by national companies and increased revenues from privatization of state property. In turn, the expenditures of the state budget increased more than the revenue – by 20.6%. State budget spending on the social sector increased by 26% in 2019. Pension costs were 14.4% higher than a year earlier. As part of measures to increase household incomes, wage costs from the budget increased by almost 22%. Considering that three quarters of all state budget expenditures were directed to current expenditures, the budget impulse stimulates the economy only for a short period of time, while the burden on public finances will have a longer-term effect. Due to the outstripping growth of state budget expenditures, increasing its expenditures is counterproductive, while there was accompanying decrease in sovereign fund accumulations due to an increase in the use of its funds. Along the chain, this leads to high values of the non-oil deficit of almost -9% of GDP and cements the dependence of state finances on oil rent.

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