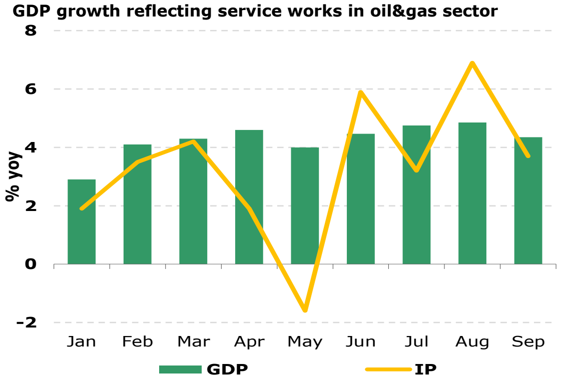
Assan Kurmanbekov
a.kurmanbekov@halykfinance.kz

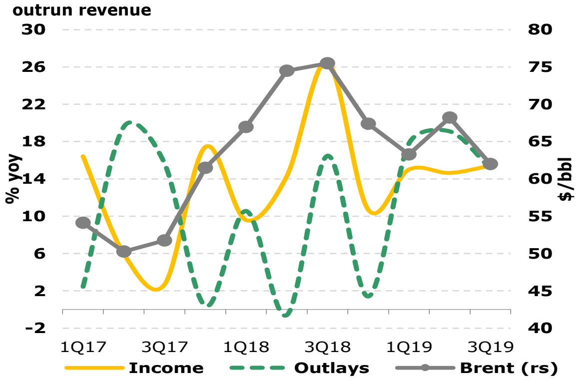
November 2019

Figure 1. Industrial output had put a brake on acceleration of GDP growth reflecting service works in oil&gas sector



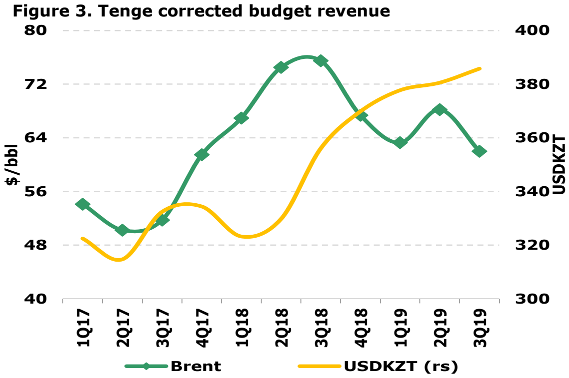
Source: CS MNE

Figure 2. On a backdrop of weaker oil prices, budget outlays outrun revenue



Source: MinFin RK, Bloomberg

Figure 3. Tenge corrected budget revenue



Source: NBK, Bloomberg

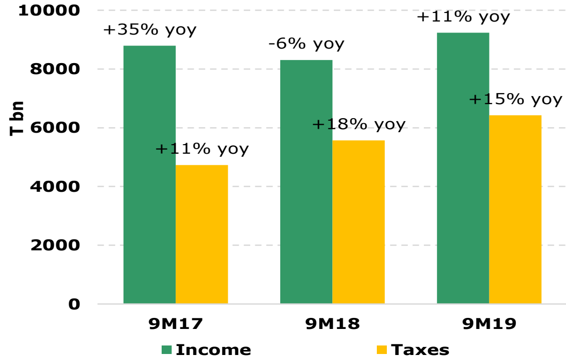
External economic conditions. Oil prices this year were significantly weaker and almost $10 lower than the last year. The reason for the negative dynamics of oil prices was the increase in US oil production while global demand experienced a pullback amid an escalation of trade disputes

Over the first nine months, GDP growth was higher than 4% yoy (excluding only January +2.9% yoy). At the same time, it accelerated to 4.6% yoy in April, and was at 4.8% in July-August (Fig. 1), but the service works conducted in the spring and autumn initially at Kashagan, then on Tengiz and Karachaganak had put a brake on the economic growth. Nevertheless, over the first 9 months GDP growth amounted to 4.3% yoy, which is the result of a strong expansion of fiscal stimulus this year amid a slight decrease in oil production by 0.4% yoy and a drop in oil prices by 11% yoy. In October, major works on the fields were supposedly ended and, accordingly, in the remaining two months of the year, industry would stop to limit the economic growth.

This year, as a result of the adopted decision to increase incomes of the population, the state budget expenditures were immediately increased by T2.4 trillion or approximately 3.5% of GDP and, importantly, to stimulate business activity, they were aimed at general economic issues, rather than saving banks as it was before. Due to the expansion, budget expenditures growth for the first three quarters of this year were approximately two times higher than in the same period last year, exceeding 17% yoy (Fig. 2).

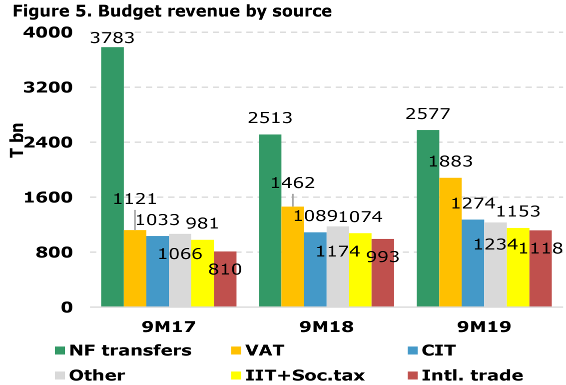
Tenge automatically adjusted to the situation in the oil market and demonstrated a fairly high co-movement. So, a decrease in oil prices by 10.8% yoy for 9 months of 2019 was accompanied by an equivalent weakening of tenge by 11.8% yoy. Thus, weak tenge compensated not only for the fall in oil prices, but also for declining oil production, helping to alleviate pressure on state finances.

Figure 4. Budget revenue growth



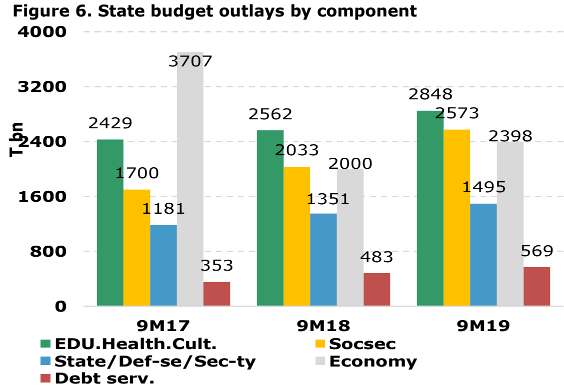
Source: MinFin RK

Figure 5. Budget revenue by source



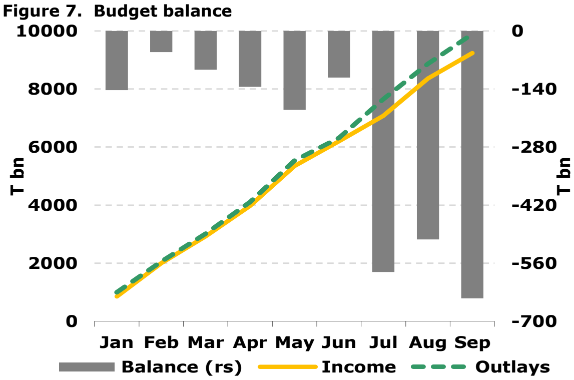
Source: MinFin RK

Figure 6. State budget outlays by component



Source: MinFin RK

Figure 7. Budget balance



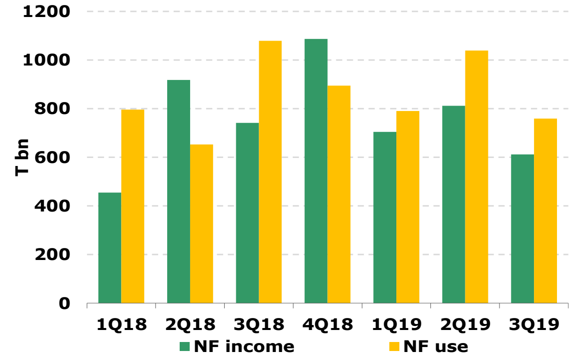
Source: MinFin RK

State budget revenues were largely determined by tax revenues, which increased by 15% yoy for the 9M2019. Meanwhile transfers from the National Fund increased only slightly (+2.6% yoy), which led to an increase in the share of taxes in the state budget revenues up to 70% (67% in 9M2018). In terms of the growth rate of the collection – value added taxes came in at first place showing an increase of 29% yoy (30% yoy on 9M2018). High growth was demonstrated by corporate income taxes +17% yoy, after 5.5% yoy in the same period of 2018. As a result of the fall in oil prices, taxes on international trade increased by 12.6% yoy, against 22.6% yoy in 9M2018. Weak growth rates of less than 4% yoy showed PIT, which is not consistent with the growth of nominal salaries by 14.6% yoy and positive growth of employed population by 1.3% yoy. In general, tax revenues in the first half of this year show slightly worse dynamics, or are the result of a more optimistic expectations of fiscal authorities – tax collection execution amounted to 69.8% of the plan, against 70.6% and 72% in the corresponding period of 2017 and 2018. At the same time, the tax collection lag was also noticeable in the first half of this year, the weaker oil sector revenues, can be attributed to the main reason which are not yet compensated by the improving tax administration.

Outlays of the state budget in the third quarter went ahead of the revenue part, showing growth above 17% yoy. In terms of expense items, the sphere of social security traditionally stands out with an increase of 27% yoy and expenses on the economy with an increase of almost 20% yoy, debt service costs increased by about 18% yoy. In turn, the cost of public services, defense and security increased more modestly by 12% yoy. It is important to note that out of approximately T1.5 trillion of additional budgetary expenditures (for 9M2019), the expenses on the economy corresponded to only 27%, but at the same time included significant amounts for the AIFC and Astana EXPO 2017, which suggests a low expected return from fiscal stimulus, which will mainly go to the current consumption and will have only a short-term effect on economic growth, which for the third year in a row has been hovering around the 4% mark, but wages had to be raised from the budget.

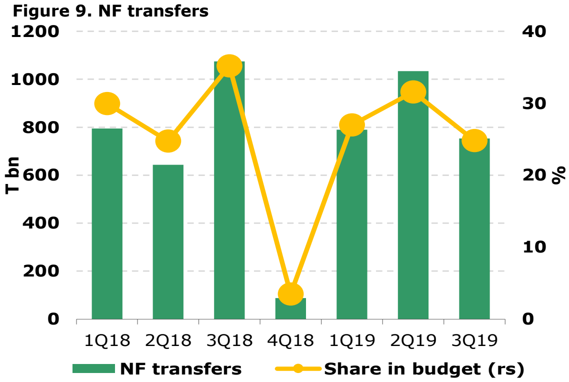
Budget balance after a modest sum in the range of -T120 billion in 1H2019, sharply increased to a deficit of -T645 billion in September 2019 (Fig. 7). The budget deficit in accordance with the plan for the current year is determined at -T1.4 trillion, or about 2% of GDP. It significantly increases in size, from 1.3% of GDP in 2018, but by historical standards and taking into account the fiscal stimulus, is at a fairly moderate level compared to a deficit of -2.9% of GDP at its peak in 2012 and -2.2% of GDP on average since 2010.

Figure 8. National Fund inflows/ouflows



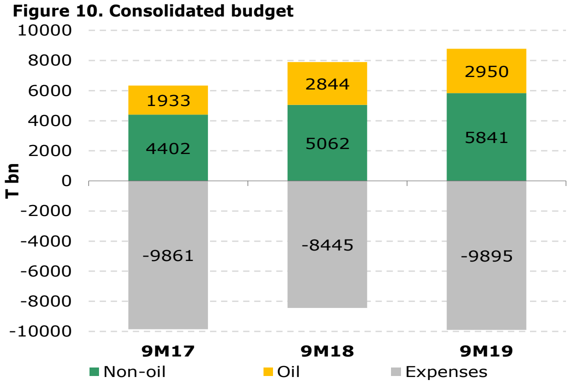
Source: MinFin RK

Figure 9. NF transfers



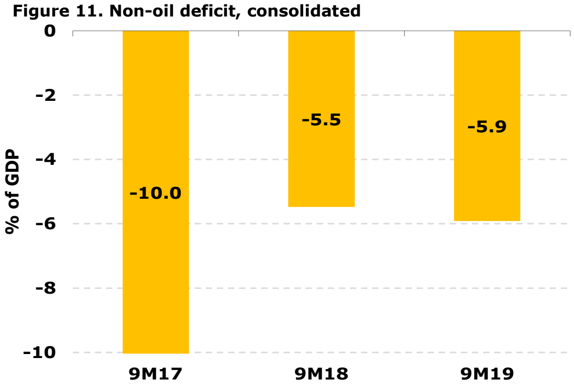
Source: MinFin RK

Figure 10. Consolidated budget



Source: MinFin RK

Figure 11. Non-oil deficit, consolidated



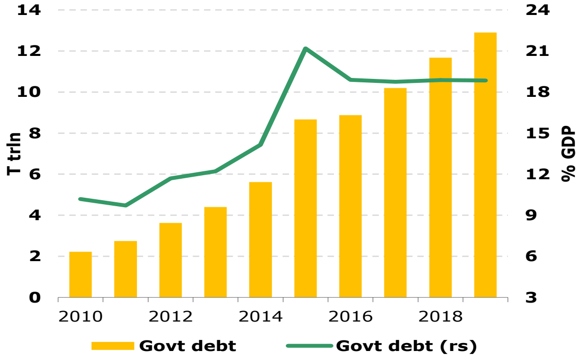
Source: MinFin RK

Revenues of the National Fund for 9M2019 almost unchanged compared to the same period in 2018 and were equal to T2.1 trillion, although in the third quarter they were the weakest at the level of T0.6 trillion, compared with T0.7 trillion and T0.8 trillion in the first and second quarters of 2019. Over the same period, the size of the transfer to the budget amounted to T2.6 trillion, that is, so far, without taking into account investment income, the use of the National Fund's funds exceeded income by T0.5 trillion. At the same time, the share of transfers in the state budget revenues was at 28% on average for January-September. The total assets of the National Fund since the beginning of the year increased by T1 trillion to T26.4 trillion mainly due to foreign exchange revaluation, but relative to GDP, they fell to 39% from 41%, respectively, and have been at its lowest since 2014.

Oil revenues for 9M2019 increased by a modest 4% yoy compared with an increase of 47% yoy in the same period last year. As noted above, the terms of trade this year due to a fall in Kazakhstan's basic export commodity - oil is unfavorable, accordingly, cheaper tenge makes it possible to achieve an acceptable positive effect even under such stressful budget conditions. Non-oil revenues, on the contrary, increased more significantly by 15.4% yoy, slightly improving from 15% yoy in 9M2018. As a result of the outstripping growth in non-oil revenues, the share of oil revenues in the consolidated budget revenues (including operations of the National Fund) fell to 34% in 9M2019 compared to 36% in the same period a year earlier.

Non-oil deficit moderately increased in 9M2019 to -5.9% of GDP from -5.5% in 9M2018 (Fig. 10). The growth of the non-oil deficit is entirely due to the strong expansion of budget expenditures aimed to stimulate the economy and increase incomes of the population.

Figure 12. Government debt



Source: MinFin RK, CS MNE

Government debt since the beginning of this year increased by 10.5% to T12.9 trillion, 80% of this increase was attracted from the local market, the remainder from external sources – mainly through the issuance of Eurobonds. At the end of September, the Ministry of Finance placed Eurobonds, consisted of two tranches in the amount of EUR500 million with a maturity of 7 years and a coupon of 0.6%, and in the amount of EUR650 million with a maturity of 15 years and a coupon of 1.5%. Such a low borrowing cost for the republic was formed against the background of established low interest rates in the Eurozone.

Our opinion

The growth of Kazakhstan's economy in the third quarter accelerated to 4.6% yoy from 4.4% yoy in the second quarter, which was achieved due to a smaller reduction in oil production during technical works than previously expected, a high level of budget expenditures and investment. The deterioration in the external environment, expressed in a fall in oil prices by more than 10%, was automatically compensated by a corresponding depreciation of tenge, which had a positive effect on the revenue side of the budget. Amid increased economic growth, tax revenues are also showing a high growth rate – above + 15% yoy. In turn, the expenditure side of the state budget increased more than the revenue side – by 17% yoy. At the same time, less than 30% of the state budget expenditures for 9 months of this year was invested in the economic development of the country, while the lion's share of the expenditures was directed for financing the current consumption of the state and the private sector in the form of defense, public services, salaries, and social security expenses. Significant budget allocations of funds toward non-productive sectors will ultimately have only a short-term impact on the economic growth, while a longer-term negative effect will be reflected in the increase in the cost of servicing an increased public debt. For example, if in 2010-2013 debt servicing expenses were at a level of less than 0.5% of GDP annually, then since 2016 they stand at 1% of GDP on average, i.e. the urgent issue is the need to increase economic returns from expanding state budget expenditures, which takes place against the background of a gradual reduction in the National Fund reserves to less than 40% of GDP from 63% of GDP in 2015.

Research Department		**E-mail**
Stanislav Chuyev	Head	s.chuyev@halykfinance.kz
Assan Kurmanbekov	Macroeconomics	a.kurmanbekov@halykfinance.kz
Dmitriy Sheikin	Macroeconomics	d.sheikin@halykfinance.kz
Zhansaya Kantayeva	Fixed income	zh.kantayeva@halykfinance.kz
Tair Baigunov	Equity	t.baigunov@halykfinance.kz
Madina Meterkulova	Equity	m.meterkulova@halykfinance.kz

Sales Department		**E-mail**
Mariya Pan	Head	m.pan@halykfinance.kz
Moldakhmetova Aizhana	Institutional	a.moldakhmetova@halykfinance.kz
Asel Baizhanova	Institutional	a.baizhanova@halykfinance.kz
Zhanna Nuralina	Retail	zh.nuralina@halykfinance.kz
Shynar Zhakanova	Retail	sh.zhakanova@halykfinance.kz
Alya Abdumazhitova	Retail	a.abdumazhitova@halykfinance.kz
Alya Mukhametzhanova	Retail	a.mukhametzhanova@halykfinance.kz

Address:
Halyk Finance
Avay av., 109 «B», 5th fl
A05A1B4, Almaty, Kazakhstan
Contact: +7 727 357 31 77
www.halykfinance.kz

Bloomberg
HLFN
Thomson Reuters
Halyk Finance
Factset
Halyk Finance
Capital IQ
Halyk Finance