

November 13, 2020

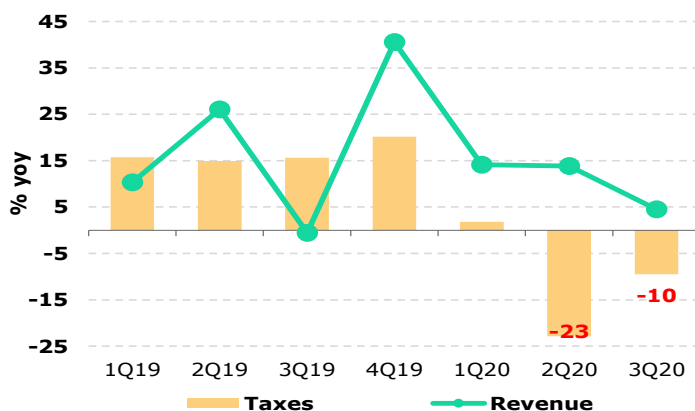
Due to the slower reduction in tax revenues of the state budget in the third quarter to -9.5% yoy against -23% yoy in the second quarter, budget tax revenues decreased by 10% yoy in the first 9 months of this year. Lost tax revenues were compensated by the National Fund transfers, that provided 40% of all revenues in 9M2020. Spending of the state budget increased by 23% yoy in January-September. At the same time, only half of all expenditures were financed from the state budget revenues (62% in 9M2019), the rest was provided by transfers from the National Fund and state loans. As a result of the increased imbalances, the state budget deficit as of the end of the third quarter of 2020 tripled in annual terms to T1.9 tn. The situation with the spread of COVID-19 is still far from resolved, and oil prices remain 30% lower than last year, while the state budget deficit is rapidly increasing and will amount to 3.5% of GDP by the end of the year. Accordingly, the impact of the crisis, together with the need for fiscal stimulation of the economy, will continue to exert pressure on the state budget, which will cause a further increase in the state debt and a reduction in the National Fund's savings.

### Decline in tax revenues slowed in the third quarter of this year

In the third quarter, the contraction in economic activity continued to put pressure on tax revenues of the budget, which decreased by 9.5% in annual terms. Nevertheless, thanks to the transfer from the National Fund, the total state budget revenues in the third quarter were 4.5% higher compared to the third quarter of 2019. Considering that in the second quarter the reduction in tax revenues reached 23% yoy, in the third quarter the situation with tax collections improved slightly.

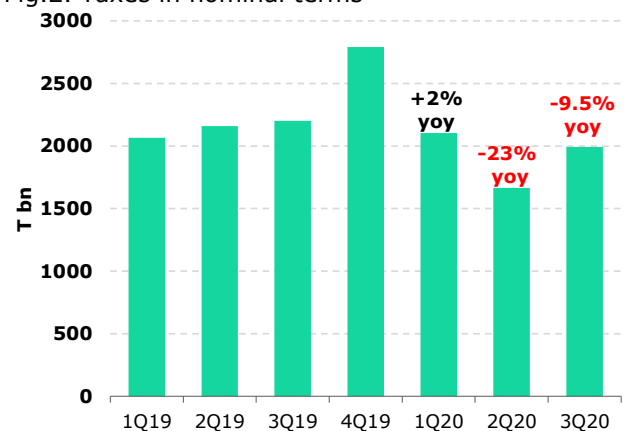
In 9M2020, total budget revenues were up by 11% yoy and exceeded T10.2 trillion. Tax revenues fell by 10.3% yoy, or almost T0.7 trillion to T5.8 trillion, which was close to the 9M2018 figure. In 9M2020, the implementation of the annual plan for state budget revenues amounted to 72.8% (73.4% in 9M2019), and for tax receipts – 64.1% versus 69.8% in 9M2019.

Fig.1. State budget revenue and taxes



Source: MinFin RK, CS MNE

Fig.2. Taxes in nominal terms



Source: MinFin RK, CS MNE

The decline in tax revenues, which exceeded 10% yoy in January-September this year, by 76% was caused by a drop in tax revenues on international trade due to a decrease in revenues from export duties on oil. However, if at the end of the first half of the year the drop in this type of taxes reached -50% yoy, in 9M2020 it "improved" to -45% yoy.

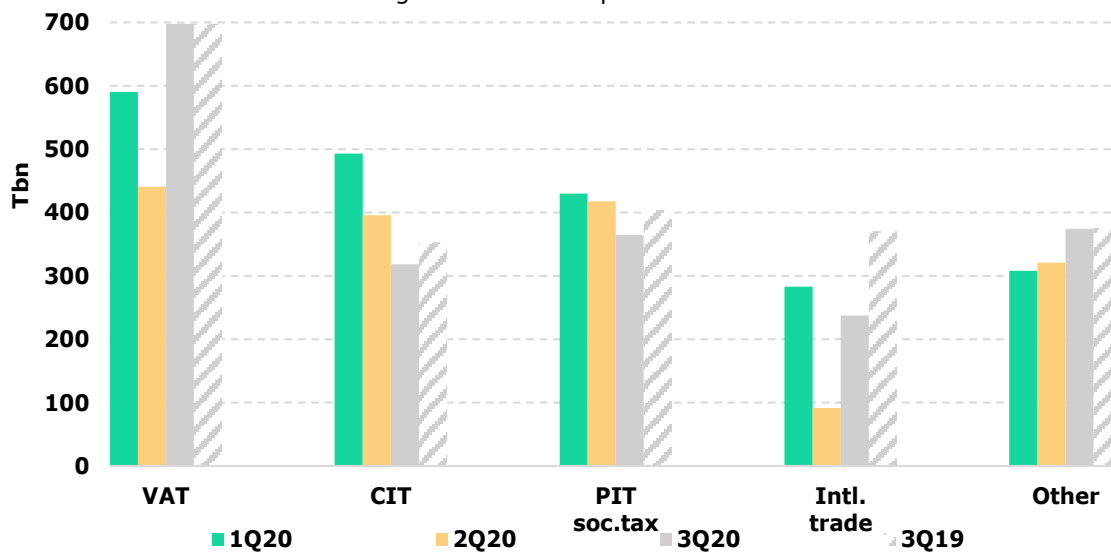
VAT receipts for 9 months decreased by 8% yoy, while in terms of weight, VAT was the second most significant tax by the decline, which is associated with a reduction in both external and internal trade operations. Corporate income tax revenues decreased by 5% yoy. Note that, according to the Ministry of Finance, in the first half of the year compared to the beginning of the year, the number of inactive taxpayers increased by 10.6 thousand, tax receipts from large taxpayers also decreased, receipts from banks fell by almost 37% yoy.

The monthly dynamics of tax revenues is still unstable, one can note the weakening of the fall in the main taxes – CIT, VAT. Personal income tax and social tax receipts, which showed high growth at the beginning of the year, began to decline, which is explained by a decrease in the growth rate of nominal wages to 6.9% yoy in 9M2020 compared to an increase of 13.7% yoy in the first half of the year.

In addition to positive growth in personal income tax and social tax, excise taxes showed a high growth of 27% yoy. However, this fact can hardly be considered unambiguously positive, since their growth is subsequently translated into the prices of goods in the consumer market, causing acceleration of inflation.

Non-tax receipts this year increased by almost 90% yoy, the main growth was associated with the receipt of dividends on the state block of shares in the amount of KZT139bn compared to KZT4bn in 9M2019. At the same time, the overwhelming part of T120 billion was paid to the government by the national holding Samruk-Kazyna.

Figure 3. Tax receipts 9M2020

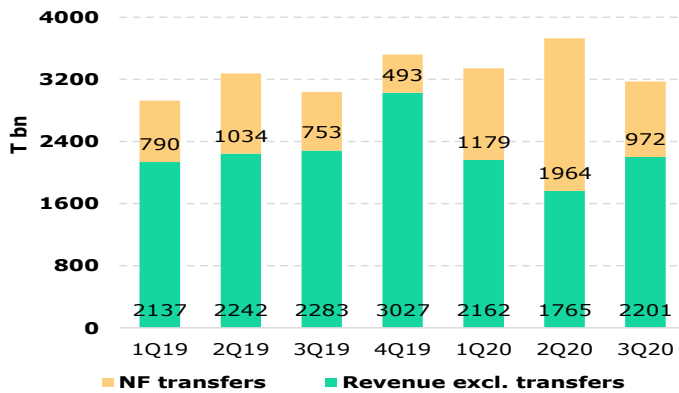


Source: MinFin RK, CS MNE

### The transfer of the National Fund remains the only stable source of state budget revenues

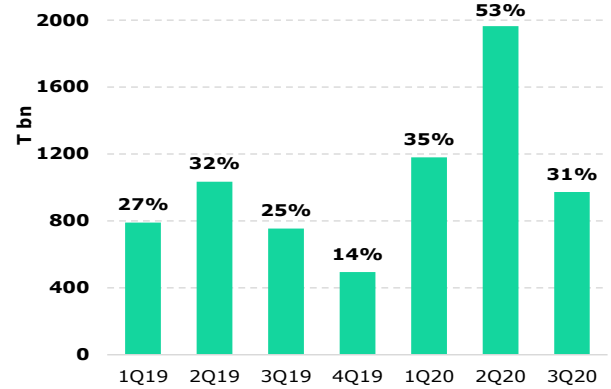
Due to a rather significant reduction in tax revenues this year, the National Fund took the main burden of filling the budget. From January to September, transfers from the National Fund amounted to T4.1 trillion, which corresponded to 40% of the entire budget revenues (28% in 9M2019). In the third quarter of this year, the share of the National Fund transfer decreased to 31% in the state budget revenues from 53% in the second quarter. The decrease in the use of transfers from the National Fund was more than offset by the growth of borrowings of the Ministry of Finance in the domestic and foreign markets: in the third quarter, the Ministry of Finance's liabilities on domestic loans increased by T0.8 trillion or 10% qoq, external liabilities increased by half a trillion or 8% qoq.

Fig. 4. Budget revenue and transfers



Source: MinFin RK, CS MNE

Fig. 5. NF transfers and its share in budget revenue



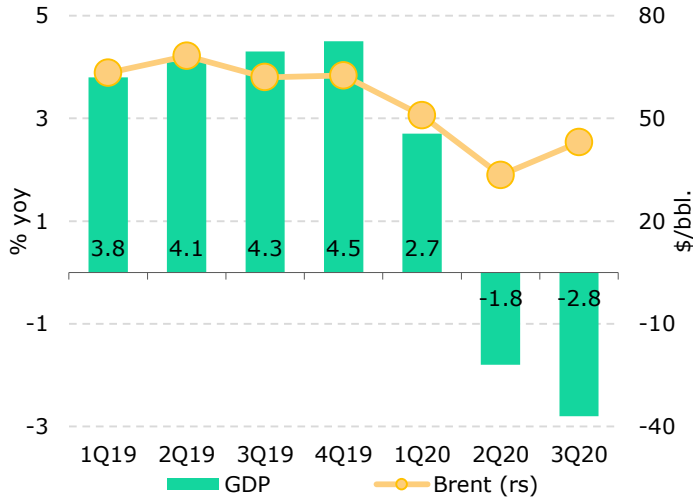
Source: MinFin RK, CS MNE

### State budget expenditures are growing at a faster pace

This year, against the backdrop of an economic downturn that has been going on for two quarters in a row, the state budget expenditures are growing at double-digit rates. In the first quarter, expenditures grew by 11.7% yoy, in the second quarter they increased by more than a third, in the third quarter the state budget expenditures increased by almost 20% yoy. In 9M2020, state budget expenditures increased by T2.3 trillion, or 23% yoy, to T12.1 trillion. In our opinion, sanitary restrictions and lockdowns significantly reduce the effectiveness of increased allocations for the economy, which necessitates a more thoughtful approach to spending. In particular, a larger increase in health spending could improve the effectiveness of the response to the pandemic, which in turn could dampen the downturn and reduce the damage to the economy.

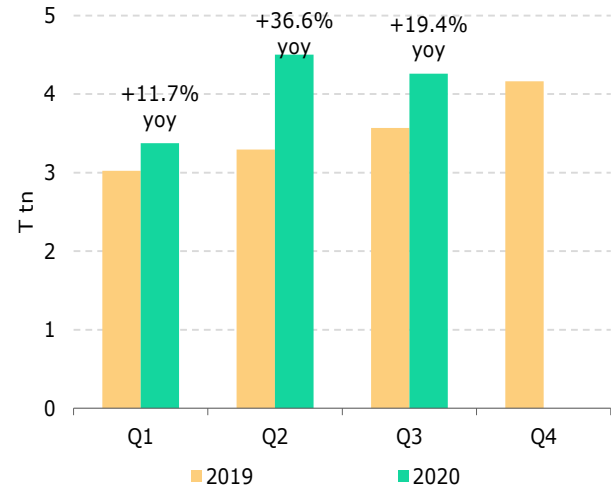
Considering the increase in both transfers from the National Fund and borrowings, in the third quarter of this year, the expenditure part of the state budget was financed by almost 50% not from current income, but from loans (26%) and transfers from the National Fund (23%), which indicates a very difficult situation in which the country's budget system found itself. In general, for 9 months of this year, only half of all expenditures were financed not from the state budget's own revenues, which is significantly higher than the 38% level in 9M2019.

Fig. 6. GDP dynamics and oil prices



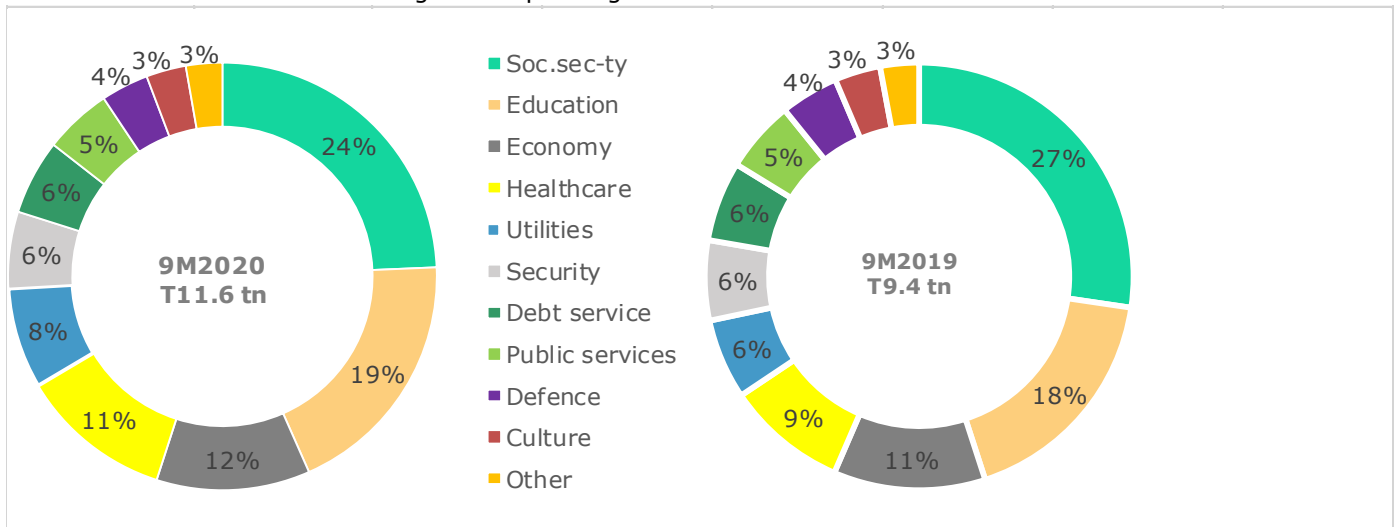
Source: MinFin RK, CS MNE

Fig. 7. Budget expenditures



Source: MinFin RK, CS MNE

Figure 8. Spending structure in 9M 2020 and 2019

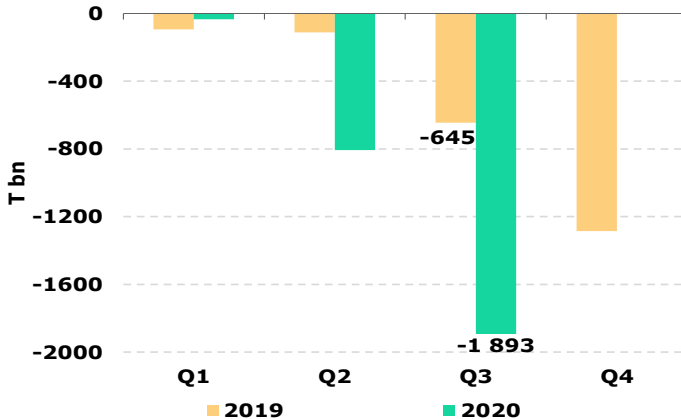


Source: MinFin RK, CS MNE

**State budget deficit widened significantly**

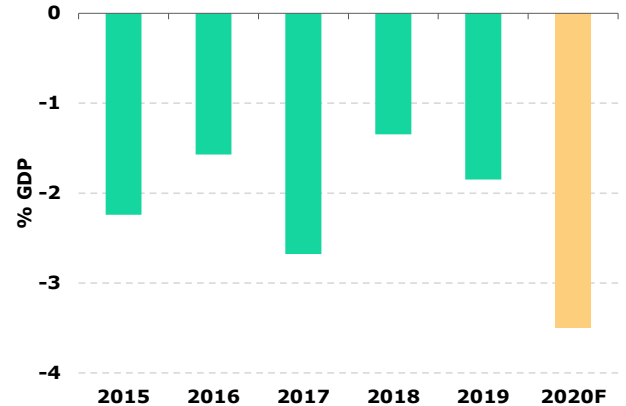
The growth of expenditures in the context of limited funding sources inevitably leads to an increase in the budget deficit. However, if the size of the state budget deficit in the first half of the year increased sevenfold compared to 1H2019, then by the end of 9 months it slightly slowed down its growth, demonstrating a threefold increase compared to the same period last year (-T1.9 trillion versus -T0.6 trillion). According to the government's forecast, the state budget deficit this year will reach T2.5 trillion, which will be higher than the deficit for the previous two years combined. Compared to last year, the deficit will almost double and reach 3.5% of GDP. Due to the presence of a safety cushion in the form of the National Fund reserves, which provide 40% of the state budget revenues, the size of the deficit can still be kept within acceptable limits (without a transfer from the National Fund, all other things being equal, the deficit would easily exceed 10% of GDP). Next year, the situation in the budgetary sphere will not improve significantly, since the government's forecast budget deficit for 2020 is 3.4% of GDP.

Fig. 9. Quarterly change in budget deficit



Source: MinFin RK, CS MNE

Fig. 10. Budget deficit



Source: MinFin RK, CS MNE

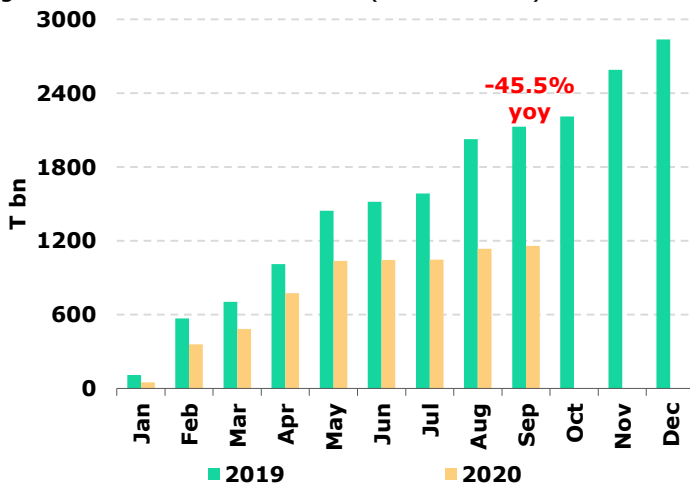
**National Fund assets are dwindling**

Tax revenues to the National Fund for the first nine months of this year amounted to T1.2 trillion, which is 46% or T1 trillion less than in January-September 2019. There was a decrease in all tax revenues, but the main decrease was observed in CIT revenues.

Against the background of the weakening of the national currency, investment income in the period increased by half in annual terms, amounting to T1.2 trillion. In turn, the size of the transfer to the state budget has almost doubled compared to last year and exceeded T4 trillion.

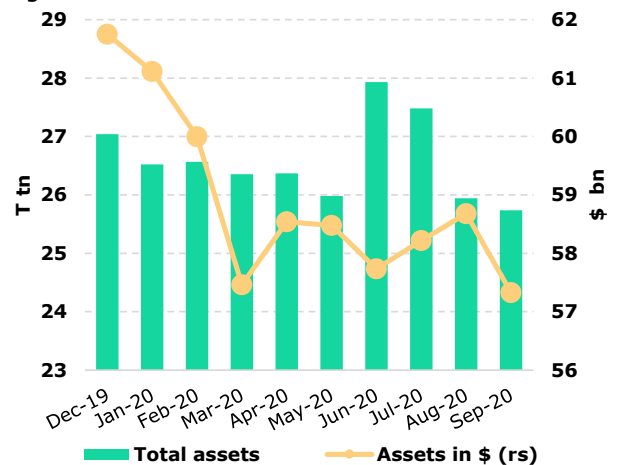
Taking into account investment income, the size of the fund's assets in the third quarter decreased by almost 5% to KZT25.7 trillion. The portfolio of foreign currency assets since the beginning of the year has decreased by \$4.4 billion to \$57.3 billion. Thus, due to the more significant amounts of funds withdrawn from the National Fund compared to receipts, there is a consistent reduction in the National Fund's assets. In particular, in comparison with the maximum level of \$77 billion reached in 2014, the assets of the National Fund decreased by \$20 billion and this trend is likely to continue in the near future.

Fig. 11. National fund revenues (accumulated)



Source: MinFin RK, CS MNE

Fig. 12. National Fund assets



Source: MinFin RK, CS MNE

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