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**May 16, 2022**

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*In 1Q2022 high oil prices and other export commodities of Kazakhstan against the backdrop of significant expansion of government spending contributed to the acceleration of Kazakhstan's GDP growth to 4.4% yoy. However, the factors above against the backdrop of the Ukrainian conflict also led to a sharp acceleration of inflation to 12% yoy in March and to 13.2% yoy in April. Rising inflation rates as well as an external pro-inflationary background, contributed to increase in the base rate of the NBK from 9.75% to 14% in April. At the same time, the favorable dynamics of commodity prices led to 2.7 times increase in commodity export earnings and the formation of a current account surplus of \$2.2 billion. Reflecting the growth of geopolitical tensions in the region, the movement of the Russian ruble and the exit of nonresidents from the securities of Kazakhstani issuers, in the 1<sup>st</sup> quarter, there was a high volatility of tenge exchange rate. By the end of March, the national currency weakened by 6.1% since the beginning of the year to 458.2 tenge per US dollar.*

*In the coming month of this year, the main impact on the economy of Kazakhstan will continue to be exerted by geopolitical tensions, the global acceleration of inflation and the tightening of monetary conditions. We forecast Kazakhstan's GDP growth this year at 3.3%, inflation at the level of 12-14%, the exchange rate of 460 tenge per US dollar.*

**High commodity prices and an increase in oil production, while maintaining the fiscal stimulus, will ensure Kazakhstan's GDP growth by 3.3% in 2022.** The negative impact of economic sanctions against Russian Federation, transmitted to the economy of Kazakhstan through close trade ties between the countries, will be offset by favorable trade price conditions in external commodity markets. The global hydrocarbon market is experiencing a shortage of supply, thanks to which oil quotes are kept at high level. The current situation in the global energy market with oil prices at \$100 per barrel will stimulate an increase in oil production in Kazakhstan from 85.7 million tons in 2021 to over 87 million tons in 2022, and this, in turn, will support the growth of Kazakhstani economy at the level 3.3% yoy. High external demand for Kazakhstani exports, support for the economy through a significant increase in state budget spending (+18% yoy), wage and pension increases, and the removal of most covid restrictions will have a positive effect on aggregate domestic demand.

**The acceleration of inflation continues.** At the end of 1Q2022, inflation reached 12% yoy, almost doubling from the previous year. The acceleration of consumer inflation was facilitated by an increase in prices for food products by more than 15% yoy, and for nonfood products – by almost 11% yoy. The main triggers for the acceleration of global and regional inflation were the consequences of global quantitative easing programs, the protracted transition to tightening of the monetary policy of the US Federal Reserve, the consequences of sanctions against the Russian Federation, adverse environmental conditions, as well as the volatility of regional currencies and supply chain disruptions. This has already resulted in an acceleration of inflation in April, which reached 13.2% yoy. Further dynamics of consumer inflation in Kazakhstan will directly depend on the degree of external geopolitical tension, the dynamics of inflation in the world and the successful implementation of government measures to curb price growth in the country. We believe that the peak of annual inflation will be passed in the second quarter of this year and we expect that consumer inflation at the end of 2022 will be in the range of 12-14%.

**Monetary policy – course for tightening.** During 1Q2022, the NBK progressively tightened monetary conditions, raising the rate from 9.75% to 10.25% in January and to 13.50% in February, keeping it at 13.50% in March. Such dynamics of the main rates reflects the strengthening of support within the country, as well as the growing external pro-inflationary pressure due to the conflict in Ukraine. The acceleration is provided in the precedent for further tightening of the monetary policy, when the NBK raised the rate to 14%. Taking into account the continued significant inflationary pressure in the economy, geopolitical uncertainty and food shortages in the global market, as well as based on the rhetoric of the NBK itself, we expect that the base rate will be in the range of 13-15% by the end of current year

**Tenge in search of balance.** During 1Q2022 against the backdrop of growing geopolitical tensions, increased country risks, nonresidents' exit from government securities, the tenge depreciated by 6.1% since the beginning of the year to 458.2 tenge per US dollar. The weakening of the Russian ruble was accompanied by a depreciation of the tenge against the ruble from 5.33 tenge per ruble to 3.98. The national currency of Kazakhstan, which is not under international sanctions, at the moment reached 512.2 tenge per dollar, while trying to find new equilibrium parity against the ruble (average value of 5.33 tenge per ruble in 1Q2022 vs 5.89 tenge in 4Q2021). In April, the tenge exchange rate approached the average equilibrium value of 5.79 tenge per ruble.

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Taking into account close ties between Kazakhstan economy with the Russian economy and our expectations for the weakening of the Russian ruble, as well as our forecasts for the growth of imports of consumer and industrial goods, we expect the tenge to depreciate to 460 tenge per US dollar by the end of current year.

Main macroeconomic indicators	2020	2021	2022		
			Base	Pessimistic	Optimistic
Oil Brent, average, USD/bbl.	42.3	70.4	90.0	65.0	115.0
Real GDP, % yoy	-2.5	4.1	3.3	1.5	4.4
Exchange rate USDKZT, eop	420.7	431.7	460.0	490.0	420.0
Exchange rate USDKZT, average	413.0	426.0	451.0	465.0	439.0
CPI, % change yoy	7.5	8.4	12-14	15-16	10-11
Base rate, %	9.0	9.8	13-15	16-17	11-12
Budget balance consolidated, % GDP	-4.0	-3.1	-3.1	-3.8	-2.8
Current account, % of GDP	-3.7	-3.0	2.3	0.2	3.1

**Despite strong external and internal shocks, economic growth accelerated in 1Q2022**

GDP growth in Kazakhstan in 1Q2021 accelerated to 4.4% from 4.1% yoy in 2021, keeping almost precrisis growth rates (4.2% on average in 2017-2019). At the same time, the January events significantly affected the growth rates of the Kazakhstani economy. Thus, according to the Ministry of National Economy, growth in January amounted to only 1.5% yoy, even despite the low base of January last year, when GDP shrank by 4.5% yoy. In January-February, the situation in the economy has improved – growth has already amounted to 3.5% yoy.

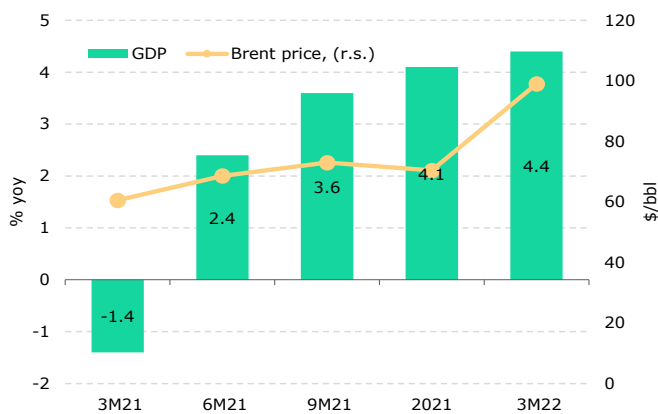
For the country's economy, the first quarter of 2022 turned out to be full of social and economic shocks. Not having fully recovered from the coronavirus crisis, the country's economy was faced with the January unrest that swept the country's major cities. In the third decade of February, the start of the Russian military operation in Ukraine marked the realization of yet another external shock, coinciding with an accident on the CPC pipeline infrastructure, through which approximately 80% of the oil exported by Kazakhstan is transported. The result of the growth of geopolitical tensions and sanctions pressure on the Russian Federation was a sharp depreciation of the national currency and the acceleration of inflation to double digits.

Despite internal and external shocks, rising external demand for Kazakh commodities supported economic growth in the 1<sup>st</sup> quarter. In 1Q2022, world oil prices increased by 24% qoq and 63% yoy to almost \$100 per barrel (on average per quarter), reaching 2014 levels. In addition, an important role in improving the business climate was played by the virtually complete phasing out of quarantine measures, which removed restrictions on doing business by the small and medium business sector, which was hit hard by severe sanitary restrictions in the previous 2 years.

A certain contribution to economic growth in 1Q2022 continued to be provided by the withdrawals of pension savings by the population, which accelerated under the influence of the hype due to the increase in the withdrawal threshold from April 1 of this year. So, in January-March, the population withdrew record KZT0.7 trillion (KZT0.9 billion in 1Q2021). In 2021, population withdrawals amounted to almost KZT2.3 trillion, some impact from the use of which on the economy will continue to be felt in the current year. Taking into account the new threshold, the savings of citizens available for withdrawal for 2022 amounted to KZT0.9 trillion and were available to almost 600 thousand people. Taking into account already withdrawn KZT0.7 trillion for 3M2022, the expected inflow of funds into the economy by the end of the year will be insignificant.

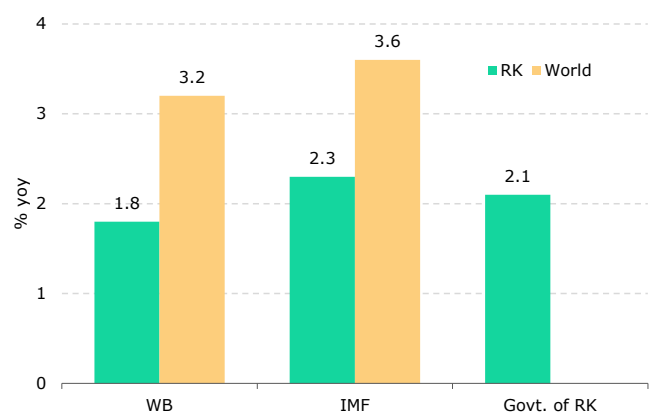
One of the government's measures to reduce social tension in society was the increase in wages and pensions. Note that this measure will affect not only employees of the public sector, but also the private sector of the economy. This will primarily be facilitated by an increase in the minimum wage in 2022 from KZT42.5 thousand to KZT60 thousand (+41%). The increase in the minimum wage this year, according to government agencies, will cover more than 1 million public sector employees and those employed in the quasi-public sector. About 2.8 million employees of large businesses will also see increase in their income.

Fig. 1. GDP RK and oil prices



\* GDP accumulated Source: BNS

Fig. 2. GDP growth forecasts RK and World for 2022



Source: BNS

Military operations in Ukraine, due to the significant economic weight of the Russian Federation on a regional scale, have already begun to negatively affect the global growth dynamics. According to the IMF, global GDP growth in 2022 will slow down to 3.6% from 6.1% in 2021 – 0.8pp below the January forecast. The economy of Kazakhstan, which is closely linked by trade and economic ties with the Russian Federation, will also come under pressure, which, according to the Fund's estimates, will lead to a slowdown in GDP growth to 2.3% in current year after 4% growth last year. The World Bank predicts the growth of the economy of the Republic of Kazakhstan at the level of 1.5% – 2% in 2022, and the Ministry of National Economy of the Republic of Kazakhstan – at the level of 2.1%. In the

framework of the forecast model of the Government of the Republic of Kazakhstan, the cost of oil will be \$90 per barrel, while the IMF proceeds from the assumption that oil will cost \$106.8 per barrel.

**Rise in sectors predominantly oriented on external demand**

The first quarter of 2022 was marked by fairly dynamic growth in the main sectors of the Kazakh economy. Expanding external demand and rising commodity prices supported the economy in the wake of the January unrest, followed by external economic and geopolitical shocks stemming from the military conflict in Ukraine. Thus, the growth of industrial production in the 1st quarter of this year reached a peak from the 2nd quarter of 2020, amounting to 5.8%. High growth rates were noted both in the extractive (+6.5% yoy) and manufacturing industries (+6.1% yoy), however, in comparison, the volumes of production and transmission of electricity increased by only 0.6% yoy.

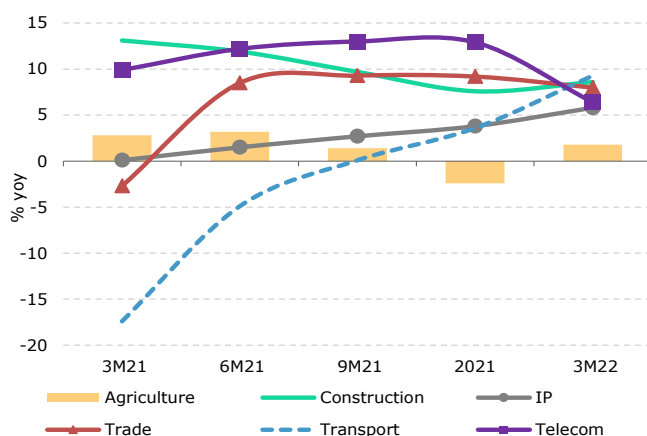
The January events and the shocks of February were broadcast on the sphere of domestic trade. Wholesale trade in January-March increased immediately by 13.5% yoy (-0.5% yoy in 3M2021), reflecting the increased volumes of trade in petroleum products. Retail, by contrast, experienced a 3.3% yoy contraction (-1.2% yoy in 3M2021).

The construction industry, although it showed a significant increase in the volume of construction work at the level of 8.6% yoy in 3M2022, however, this was already below the double-digit growth rates observed in previous years. At the same time, the construction of non-residential buildings increased by 28.6% yoy, while housing construction, on the contrary, decreased by 2.7% yoy. The housing boom seems to be on the slump after all, and last year's infusions of retirement savings only delayed the inevitable. A significant obstacle to the further increase in housing construction was high prices for new housing, which increased by 33% from the end of 2020 to March of this year, while wages added only 13% in the same period. Add to this an increase in the base rate and, as a result, rise in the interest rates for loans, as well as growth in the cost of building materials, which had a negative impact on the housing construction sector.

The gradual lifting of all coronavirus restrictions, the restoration of population mobility in the 1st quarter of 2022 and the low base of last year contributed to the growth of transport services by 9.3% yoy against a decline of 17% yoy last year. The output of agricultural products and services in January-March 2022 amounted to 1.8% yoy and was below the average of 2.4% in the previous three years. The weaker output volumes were affected by the unfavorable epidemiological situation in animal husbandry, the growth in the cost of feed and the rise in prices for agricultural products of intermediate use.

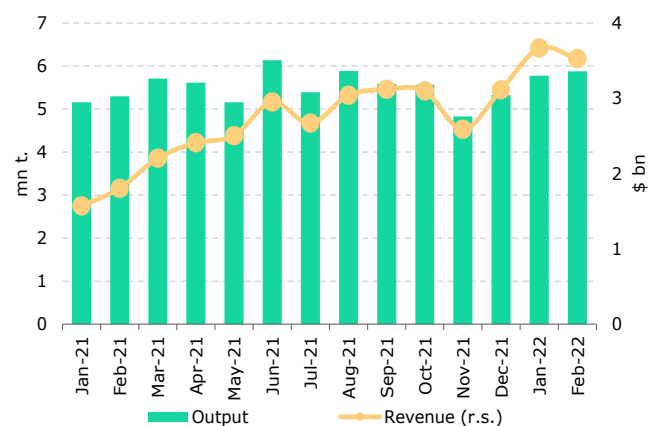
High external demand and commodity prices created favorable conditions for Kazakhstan's foreign trade in the 1st quarter of this year. Thus, the volume of export of goods in January-February increased by 71.4% yoy to \$12.1 billion. The determining influence on the growth of commodity export was primarily due to hydrocarbon trade, the volume of which for 2 months of the current year increased by 2.1 times compared to the same period a year earlier to \$7.2 billion. Thus, the trade in hydrocarbons provided a total increase in Kazakhstan's exports by 76% (\$3.8 billion out of \$5 billion). At the same time, the physical volumes of exports increased only by 11.5% yoy to 11.7 million tons.

Fig. 3. Dynamics of economic sectors



Source: BNS

Fig. 4. Oil output and export



Source: BNS

Growth in trade in liquid hydrocarbons was spurred by an increase in external consumption and oil quotations as a result of an increased risk of a protracted conflict in Ukraine, a reduction in hydrocarbon shipments by the Russian Federation and the fulfillment by OPEC+ countries of their obligations to not increase oil production.

Despite the damage to the CPC pipeline infrastructure at the end of February, through which approximately 80% of oil exported by Kazakhstan is transported, oil production in the republic continued to grow, which amounted to 8.6% yoy in the 1<sup>st</sup> quarter. According to the updated forecast of the Ministry of Energy of the Republic of Kazakhstan, oil production in the country in 2022 will not change and will amount to almost 86 million tons. The previous forecast of the department assumed an increase in oil production to almost 88 million tons. A possible return to the original production forecast of 87.5 million tons (+2% yoy) this year isn't ruled out by the Ministry of Energy.

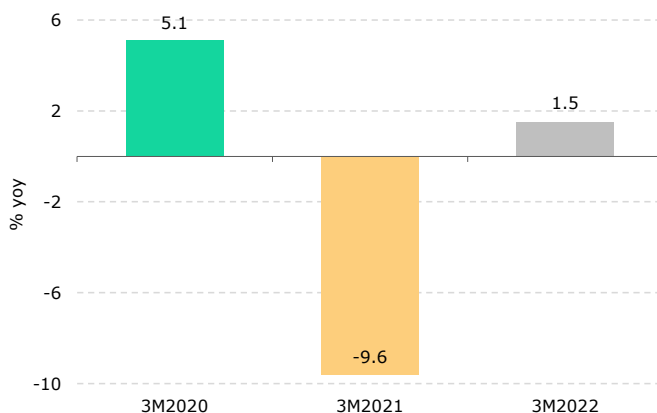
**Weak investment growth of 1.5% yoy**

At the end of 2021, investments in fixed assets returned to a positive growth zone after the decline observed since the second quarter of 2020. However, so far, growth rates are far from precrisis levels, as in the 1<sup>st</sup> quarter of this year, investment growth was at the level of only 1.5% yoy, and their volume amounted to KZT2.3 trillion (KZT2.1 trillion in 1Q2021).

The growth of investments is still driven by the own funds of small enterprises, which in 1Q2021 increased investments in fixed assets by 14.3% yoy to KZT1.1 trillion. Investments of large enterprises amounted to KZT1 trillion (-1% yoy), and medium enterprises decreased by 43.4% yoy to KZT124 billion. The January events had a negative effect on investment growth, the NBK's increase of the base rate from 10.25% in January to 13.50% in March, as well as the weak dynamics of bank lending of the economy due to high geopolitical tensions and the growth of devaluation expectations of the population and businesses. However, the 1<sup>st</sup> quarter of the year is not indicative, and the situation may improve down the road, especially given high prices for raw materials and stimulatory budget policy.

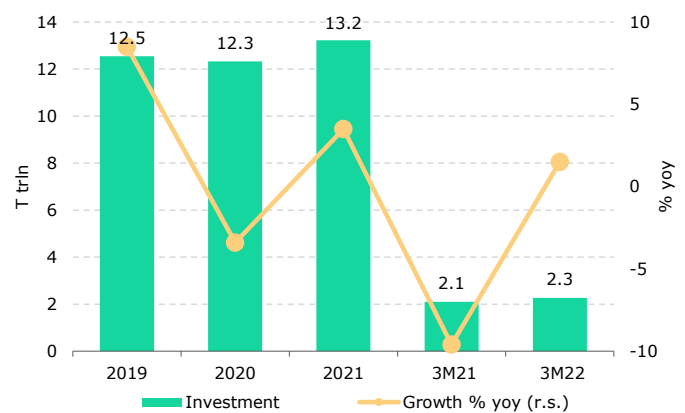
The growth rate of investment in fixed assets in the extractive industry in 1Q2022 increased by 3% yoy to KZT0.8 trillion. Investments in the manufacturing industry showed a decline of 36.2% yoy after a high growth of 135.6% yoy a year earlier. Along with this, there is a significant reduction in investment in the telecommunications sector (-57.5% yoy) and in agriculture (-7.3% yoy). Positive dynamics of investment growth was noted in construction (+120.2% yoy), trade (+31.9% yoy) and transport (+27.2% yoy).

Fig. 5. Volatile investment in 1<sup>st</sup> quarter



Source: BNS

Fig. 6. Investment – from slump to growth



Source: BNS

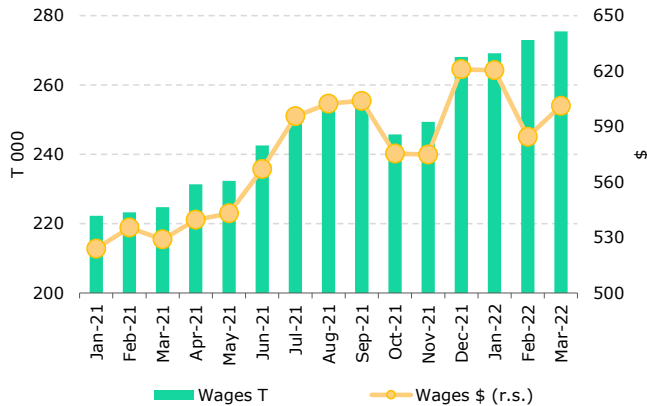
**Despite rising wages, retail trade is declining**

Against the backdrop of accelerating consumer price growth over the past three years, the minimum wage since January this year has increased by 41% from KZT42.5 thousand to KZT60 thousand. This measure, according to government agencies, will directly affect more than 1 million people and will have positive effect on household income. Meanwhile, the average salary in 1Q2022 increased by 3.6% since the beginning of the year and by 23.7% yoy to KZT285k (\$627). The increase in wages this year is under pressure, both from the side of the workers themselves and the calls of the state to increase it for large companies, and by increasing budget expenditures. Thus, in January-March of the current year, the wages from the budget increased by 25% yoy.

January unrest, tenge depreciation and accelerated price growth had a negative impact on retail trade turnover, which decreased by 3.3% yoy in January-March despite monthly growth in domestic trade turnover for the second month in a row in March. At the same time, positive dynamics of retail trade turnover is observed in almost all regions, with the exception of Almaty (-16.4% yoy) and Aktobe region (-10% yoy). In 6 regions of the country, trade growth is still below 1% yoy. The decline in domestic household consumption is primarily due to the turnover of food products, the sales volume of which decreased by 10.3% yoy, while for non-food products, the increase was recorded at only 0.5% yoy.

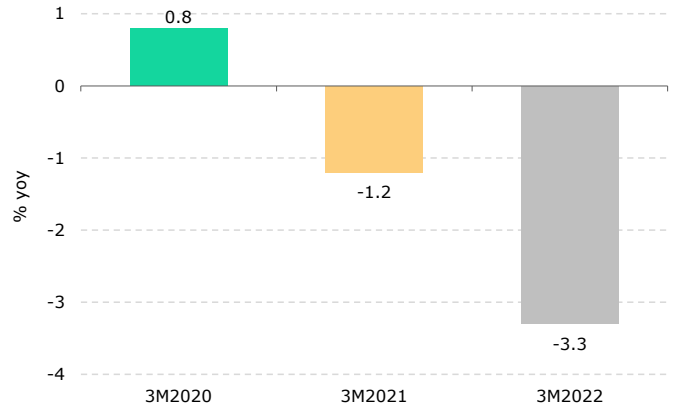
The steady increase in retail sales in February and March compared to January of the current year indicates the temporary nature of the decline in domestic trade at the beginning of the year. At the end of last year, retail trade overcame the recession of the “pandemic” 2020 and has the potential for further growth in consumer activity against the backdrop of rising wages and economic growth. However, an increase in the base rate and, as a result, an increase in the attractiveness of deposits will deter households from completely moving away from the savings model of behavior.

Fig. 7. Wages dynamics



Source: BNS

Fig. 8. Retail trade turnover



Source: BNS

### Inflation hits double digits

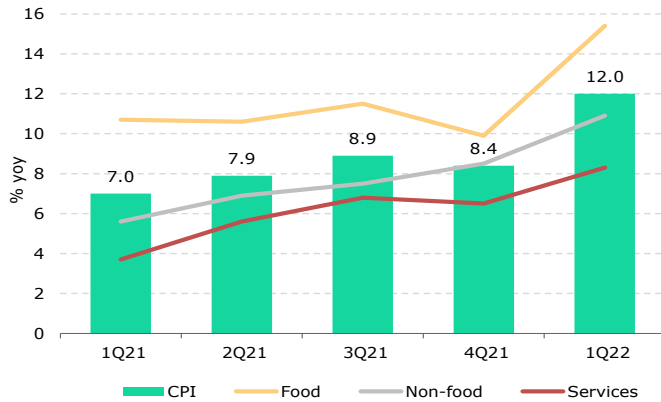
In March, consumer inflation accelerated sharply to 3.7% MoM – the highest since November 2015 (+0.8% MoM in February). In annual terms, in March, the growth of consumer inflation amounted to 12.0% yoy (+8.7% yoy in February). The consumer price index in annual terms shows an upward trend for the third month in a row.

The dynamics of annual price growth accelerated across all components of consumer inflation – food products rose in price by 15.4% yoy (+10.0% yoy in February), nonfood products – by 10.9% yoy (+8.6% yoy in February), and paid services – by 8.3% yoy (+7.1% yoy in February).

Both external and internal factors contributed to the acceleration of price growth in 1Q2022. Among them were an increase in oil prices by 63% yoy to an average quarterly price of almost \$100 per barrel and an increase in the cost of food on the world market by 33.6% yoy to a maximum value since 1990. At the same time, only in March, the FAO food price index increased relative to February by 17.1% for cereals, by 23.2% for vegetable oil, by 6.7% for sugar, by 4.8% for meat and by 2.8% for dairy products. Thus, the conflict in Ukraine has become a powerful new trigger for rising food prices around the world. In addition, agricultural producing countries everywhere impose export restrictions or suspend the export of food, fearing a possible shortage in the domestic market.

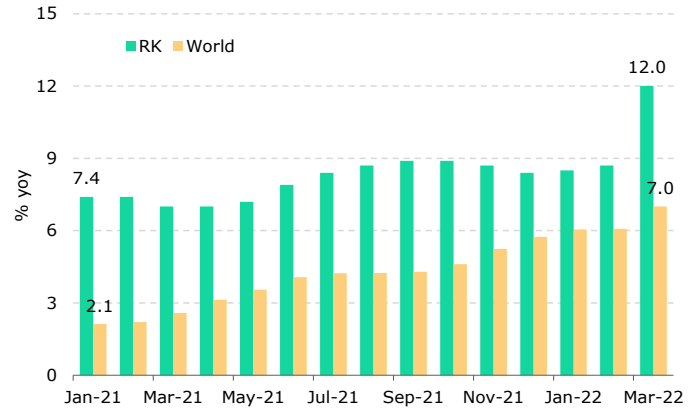
The dynamics of global inflation continues to show an upward trend and, according to the Bloomberg news agency, accelerated from 5.7% yoy in December 2021 to 7% yoy in March. In the Russian Federation, inflation in March reached 16.7% yoy, accelerating from 8.4% in December 2021. Recall that the share of imports from the Russian Federation to Kazakhstan is 40% of the country's total commodity imports, which contributes to the import of inflation from the Russian Federation into Kazakhstan.

Fig. 9. Inflation in RK



Source: BNS

Fig. 10. Inflation in RK and World



Source: BNS, Bloomberg

The budget impulse in Kazakhstan will continue this year due to the growth of budget expenditures by 18%. At the same time, given the expected slowdown in economic growth to 2.1% this year, the impact of growth in government spending on the economy will be more supportive than stimulating, and given the increase in the base rate of the NBK, the effect of the impulse itself on consumer prices will be limited.

However, we believe that the observed inflation is structural inflation (cost of production inflation) and not monetary inflation (demand pull inflation). Therefore, an increase in the base rate will not have a significant impact on its dynamics, but will only lead to a disruption in the investment cycle, which, after the crisis of 2020-2021, only now is slowly starting to recover. An increase in the base rate in the context of the Government's forecast of a slowdown in GDP growth to 2.1% will further reduce lending to the economy by commercial banks. Thus, the ratio of bank loans to GDP decreased from 34.8% in 2010 to 22.5% in 2021. The money multiplier over the same period decreased from 3.3% in 2010 to 2.7% in 2021. Based on this, we expect the expansion of lending to the economy through budget emission. This in turn will be financed by issuing external and internal obligations, but at higher rates, which in turn will lead to an increase in the cost of servicing public debt, which has already grown to 5.7% (KZT1 trillion) in the structure of budget expenditures. The inconsistency between the policies of the Ministry of Finance of the Republic of Kazakhstan and the NBK not only distorts the market mechanisms for lending to the economy and leads to a reduction in the role of the banking sector of the republic, but also reduces the sustainability of the budget structure through an increase in debt and an increase in dependence on NF funds.

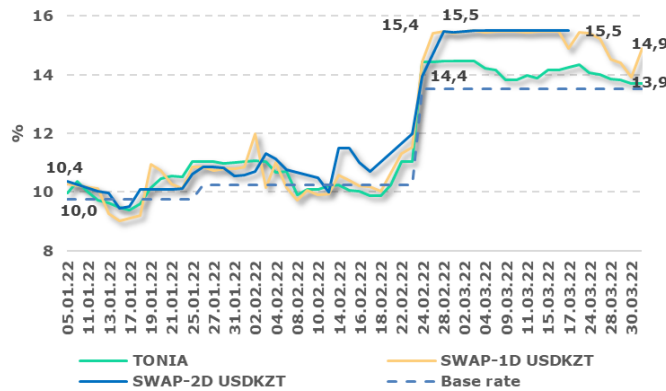
### Interest rate policy – NBK aims to tighten

During 1Q2022, the NBK pursued a tight monetary policy. Against the backdrop of accelerating external and domestic inflation, the monetary policy committee raised the base rate from 9.75% to 10.25% in January and to 13.50% in February, keeping it unchanged in March. At the end of April this year, the NBK decided to raise the base rate by another 50bp to 14%, while the liquidity management corridor remained symmetrical and amounted to +/-1%. The tightening of the monetary policy was facilitated by inflation growth from 8.5% in January to 12.0% in March, as well as unanchored inflation expectations, which amounted to 11.4% over a 12-month horizon, with an inflation forecast of 8-10%<sup>1</sup>. The increase in the rate was supported by GDP growth of 4.4% in 1Q2022, accompanied by an increase in prices for the entire range of Kazakhstani exports. In addition, there was an expansion in household consumption due to consumer lending and growth in real incomes of the population. Significant pro-inflationary pressure, according to the NBK, will be provided by fiscal policy due to the expansion of budget expenditures by 23.6% y/y in 2022 and maintaining the size of the guaranteed transfer at the level of 4.6 trillion. The influence of the indicated pro-inflationary factors will continue throughout the current year, which will serve as a pretext for further tightening of monetary conditions.

Tightening monetary conditions by global central banks against the backdrop of high inflation rates (especially food), geopolitical uncertainty regarding the Russian Federation, as well as maintaining high volatility of exchange rates due to sanctions in connection with the armed conflict, monetary conditions in Kazakhstan will gradually tighten, but the tightening will be short-term.

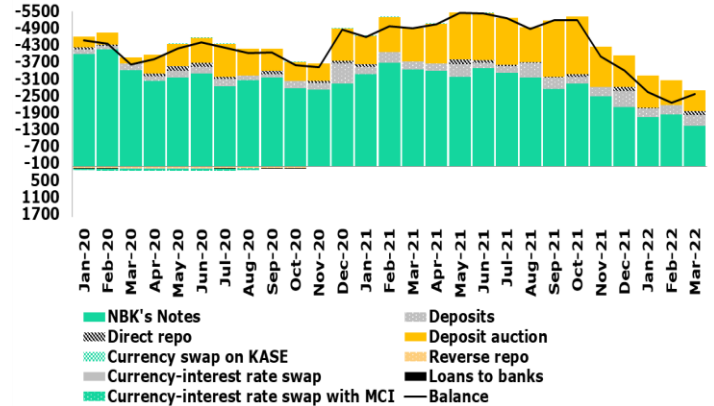
<sup>1</sup> Согласно прогнозам правительства на 2022 г.

Fig. 11. Money market rates at the end of the period



Source: NBK, Halyk Finance

Fig. 12. Withdrawal of excess liquidity



Source: NBK, Halyk Finance

The rate on automatic REPO (TONIA) operations at the end of March 2022 was at the level of 13.7% (10.56% at the end of December 2021) with an average value of 11.8% (9.6% in 4Q2021). The volume of transactions on automatic REPO in 1Q2022 decreased by 3.1% QOQ (+86.8% YOY) and amounted to KZT37,896 billion, while the average value of daily transactions for the period amounted to KZT676.7 billion (KZT620.7 billion in 4Q2021). The maximum daily volume of transactions on automatic REPO operations occurred at the end of January 2022 and amounted to KZT1,026 billion (KZT1,357 billion at the end of December 2021). The contraction in money market transactions was accompanied in 1Q2022 by a contraction in the money supply (MS) of 1.9% since the beginning of the year. Recall that in 2020 and 2021, the money supply in the republic increased by 16.9% YOY and 20.8% YOY, respectively. The correlation between the market rate and the volume of transactions in the money market decreased from 85% in 4Q2021 to 17.5% in 1Q2022 (24.5% in 1Q2021).

The volume of transactions on overnight swaps on the USDKZT pair in 1Q2022 increased by 31.8% QOQ to KZT4,043.5 billion. At the end of 1Q2022, the overnight swap rate for the pair stood at 14.9% (9.5% at the end of 4Q2021) with an average rate of 12.4% (9.4% in 4Q2021). The volume of transactions on two-day swaps on the USDKZT pair in 1Q2022 decreased by 58.8% QOQ to KZT347.9 billion. At the end of 1Q2022, the USDKZT two-day swap rate stood at 15.5% (10.24% at the end of 4Q2021) with a quarterly average of 11.9% (9.5% in 4Q2021). Demand for shorter swaps reflected the strong volatility of the USDKZT pair in late February and March 2022.

In 1Q2022, the money market rate was formed closer to the middle of the corridor (10.35% average) for liquidity management almost until the end of February 2022. After the February increase in the base rate to 13.50%, the money market rate was formed at the upper border of the corridor (14.1% average). A significant reduction in the correlation coefficient between the rate and the volume of transactions in the money market indicates a certain time lag in the adaptation of the money market to changes in monetary conditions and to the monetary shock in the country. The currency swap market showed an increase in the volume and value of money both as a reaction to an increase in the base rate and to a sharp depreciation of the national currency.

### Exchange rate – forced weakening

As of the end of March, the national currency exchange rate depreciated by 6.1% since the beginning of the year to 458.2 tenge per US dollar (depreciated by 8.0% YOY), while the average value of the exchange rate was 455.11 tenge per US dollar in 1Q2022. reached 512.2 tenge per US dollar. The volatility of the exchange rate was largely due to both internal and external geopolitical factors. Economic factors, on the contrary, favored the strengthening of the tenge. Thus, the quotation of Brent oil increased by 38.7% since the beginning of the year and amounted to \$107.9 per barrel. At the moment, quotes reached \$128 per barrel, and the average value for 1Q2022 was \$97.6 per barrel (\$78.5 per barrel in 4Q2021). The volume of NBK foreign exchange transactions for the NF in 1Q2022 decreased by 14.2% QOQ to \$2.1 billion. However, the total supply of foreign currency in the foreign exchange market, taking into account foreign exchange interventions, in 1Q2022 increased by 22.7% QOQ and amounted to \$3.6 billion. In the foreign exchange market, in the segment of exchange trading for the USDKZT pair in 1Q2022, there was a decrease in foreign exchange operations by 18.4% QOQ to \$8.7 billion (+23.5% YOY). The volume of purchases of US dollars in exchange offices in 1Q2022 decreased by 48.8% QOQ to KZT441.5 billion (\$970 million). The largest depreciation was observed in March by 67.2% MoM to KZT64.9 billion (\$149 million).

The weakening of the exchange rate of the Kazakhstani tenge in 1Q2022 was facilitated by the withdrawal of nonresidents from the government securities of the Republic of Kazakhstan. Thus, the volume of government



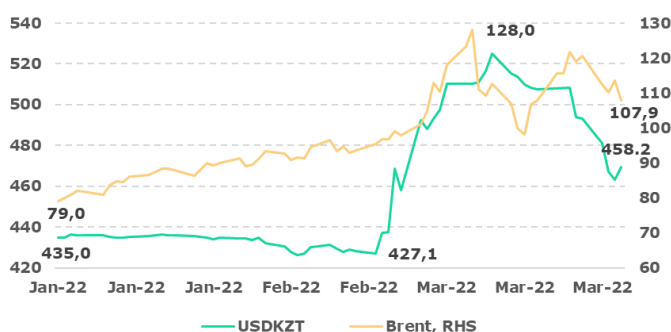
securities held in nominal possession by nonresidents decreased by 28.7% to a 16-month low of KZT424 billion, comparable to KZT430 billion in January 2021.

Against the backdrop of growing geopolitical tensions and the outflow of capital from the Russian Federation and Europe, the US dollar strengthened against the currency basket of the world's leading currencies. The DXY index at the beginning of this year was in the range of 95.7-96.2pp and remained at this level until February 24th. Since the beginning of the military operation of the Russian Federation, the index began to grow dynamically, reaching values of 99.3pp and as of the end of March amounted to 98.3pp. In the last days of April, the index confidently overcame the mark of 100pp and amounted to 103.8pp. In the context of rising tensions due to the confrontation in Ukraine, the growth of the DXY index is due to the growth of transactional demand for US dollars as a relatively stable means of payment, as well as growing interest in US assets.

The volatility of the tenge exchange rate at the end of April and March of this year was fully due to the imbalance in the exchange rate of the Russian ruble against the dollar and the euro due to an extensive package of sanctions. As of the end of March, the Russian ruble has weakened by 13.2% since the beginning of the year and amounted to 84.1 rubles per US dollar. At the moment, the value of the Russian currency on the currency exchange of the Moscow Exchange (MOEX) reached 120.4 rubles per dollar, however, as the mirror sanctions against unfriendly countries of the Russian Federation expanded, the exchange rate began to grow and, as of the end of April, the currency strengthened by 2.7% since the beginning of the year to 72.3 rubles per US dollar.

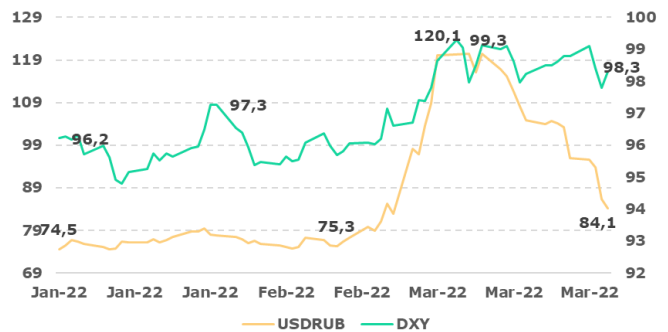
At the same time, the parity between the Kazakhstani tenge and the Russian ruble, as the ruble weakened against the US dollar, decreased from 5.8 tenge per ruble at the beginning of the year to 3.98 tenge per ruble, and as of the end of March, when the ruble strengthened, it amounted to 5.49 tenge per ruble. As of the end of April, the parity shifted to 6.1 tenge.

Fig. 13. Change of quotes USDKZT vs Brent



Source: Bloomberg, NBK, Halyk Finance

Fig. 14. Change in USDRUB and USD index



Source: Bloomberg, CBR, Halyk Finance

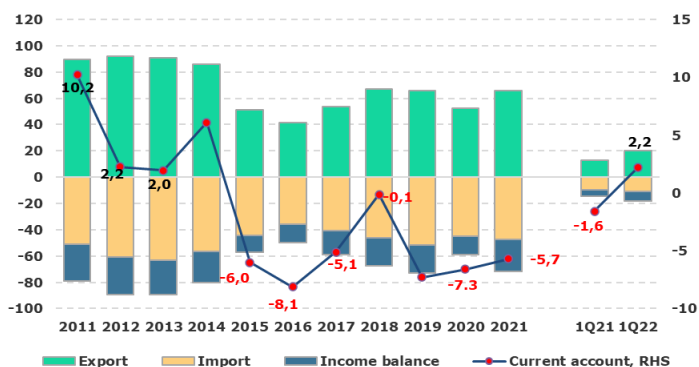
The exchange rate for the USDKZT pair in 2022 will be formed based on the exchange rate of the National Bank for the Russian ruble (the parity will be maintained at the level of 5.5-6.5 tenge per ruble). The DXY index will be formed at the level of 98-101pp, which will have a weakening effect on the tenge rate. Oil prices at \$98 per barrel on average for the year (Bloomberg consensus forecast for 2022) will contribute to the inflow of foreign currency and support the tenge from weakening. The risks of a complete embargo of Russian energy carriers remain, but seem implausible to us this year. Thus, based on the predicted macroeconomic and geopolitical picture of the development of events, we believe that the national currency rate will be at the level of 460 tenge per US dollar by the end of this year.

**The balance of payments has developed with a surplus**

The current account of the Republic of Kazakhstan in 1Q2022 developed with a surplus of \$2.2 billion (deficit of \$1.6 billion in 1Q2021). The trade surplus in the Republic of Kazakhstan in 1Q2021 was at \$9.9 billion due to outpacing growth of exports by 66.4% YOY to \$19.1 billion over imports, which grew by 17% YOY to \$9.1 billion.

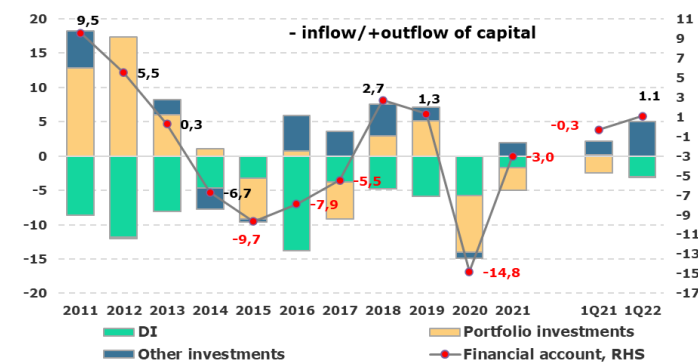
The growth in the cost of energy resources in 2021 (an increase in exports by \$9 billion due to price changes) and industrial metals (an increase in exports by about \$3.7 billion) on international markets (83.5% of the export structure in 2021) led to an outstripping growth in exports (26.9% YOY to \$60.3 billion) over imports (5.8% YOY to \$41.2 billion). This contributed to the expansion of the trading account surplus in 2021 by 2 times to \$20.7 billion. This trend continued in 1Q2022, when the average Brent oil price reached \$97.9 per barrel, and the trading account surplus increased by 2.7 times.

Fig. 15. Current account surplus, \$bn



Source: NBK, Halyk Finance

Fig. 16. Financial account outflow, \$bn



Source: NBK, Halyk Finance

The expansion of private equity income from \$4.5 billion to \$7.0 billion in 1Q2022 widened the primary income account deficit from \$4.9 billion in 1Q2021 to \$7.4 billion in 1Q2022. Deficit in the balance of services in 1Q2022 formed at the level of \$369 million, which is slightly more than the deficit of \$321 million in the 1<sup>st</sup> quarter of last year. The deficit in the balance of secondary income in 1Q2022 was at \$28.4 million and coincided with the size of the deficit in 1Q2021.

Thus, the increase in prices for the main nomenclature of Kazakhstani exports in 2021, which continued in 1Q2022, had a beneficial effect on the nominal value of the country's commodity exports. The gradual recovery of the world economy contributed to the growth of investment activity and, as a result, the growth of repatriation of income on direct investments of nonresidents, which affected the deepening of the deficit in the primary income account and had a restraining effect on the further expansion of the current account surplus.

### Financial account (excluding reserve assets of the NBK)

The financial account experienced a capital outflow of \$1.1 billion in 1Q2022 compared to an inflow of \$301 million in 1Q2021. Capital outflow from the financial account in 1Q2022 was supported by a reduction in capital inflows from the portfolio investment account from \$2.5 billion to \$80 million, and also due to the expansion of the outflow of short-term capital flows from \$3.3 billion to \$5.7 billion. In the direct investment account, on the contrary, an increase in inflow was observed from 181.4 million (outflow) to \$3.0 billion. Medium-term and long-term investments in Kazakhstan expanded from \$1.3 billion in 1Q2021 to \$1.6 billion in 1Q2022. Errors and omissions see an inflow of \$1.7 billion compared to an outflow of \$1.3 billion.

### International reserves of Kazakhstan are declining

Consolidated international reserves at the end of the first quarter of 2022, according to the NBK, amounted to \$85.9 billion. Reserves decreased by 4.3% QOQ (-5.3% YOY) due to a 3.6% QOQ reduction in the nominal volume of the NBK's gross gold reserves to \$33.1 billion (-1.1% YOY), as well as due to a fund by 4.7% QOQ to \$52.7 billion (-7.7% YOY).

As part of the NBK's reserves, assets in hard currency decreased by 4.4% QOQ to \$10.4 billion (-14.1% YOY). According to the IMF, as of the end of March 2022, in the structure of the gold reserves, there is a decrease in assets in the Central Bank by 15.0% YOY to \$5.0 billion (-2.4% QOQ). Assets and deposits in hard currency decreased by 45.0% YOY and amounted to \$2.9 billion.

The NBK's gold holdings shrank by 3.3% since the beginning of the year to \$22.8 billion, up 6.2% YOY. Since the beginning of the year, the price of gold (XAU spot) has grown by 5.9% and as of the end of March reached \$1,937 per troy ounce. Given the dynamics of the value of gold on the international market, the reduction occurred due to a reduction in its physical volume. The share of assets in gold at the end of March this year amounted to a record 68.7%, having increased from a share of 68.5% at the beginning of the year. Foreign exchange interventions during the first three months of the year contributed to the reduction of assets in hard currency and gold. Net sales of the NBK for the three months of this year amounted to \$1.5 billion, and in March, net sales amounted to \$990.5 million. Since the NBK's hard currency has decreased by \$1.2 billion since the beginning of the year, it can be assumed that the NBK sold monetary gold to provide itself with the liquidity needed for interventions. This is also indicated by the reduction in the volume of gold reserves in gold by 7.0% YOY (-8.5% QOQ) to 11.84 million troy ounces (368.3

tons). In total, since November last year, the NBK has sold foreign currency in the form of interventions in the country's foreign exchange market in the amount of almost \$2 billion.

Fig. 17. International reserves of the NBK

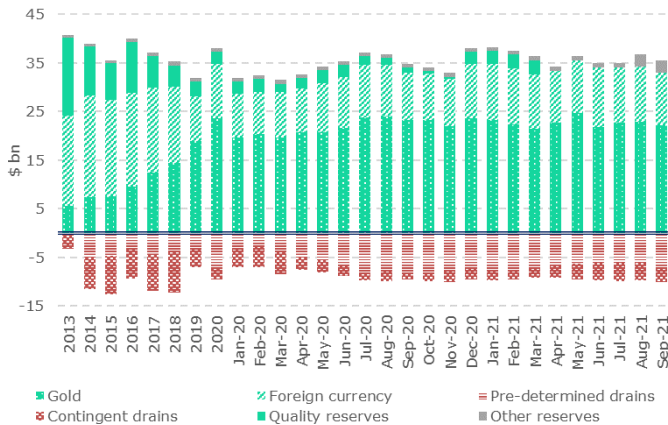
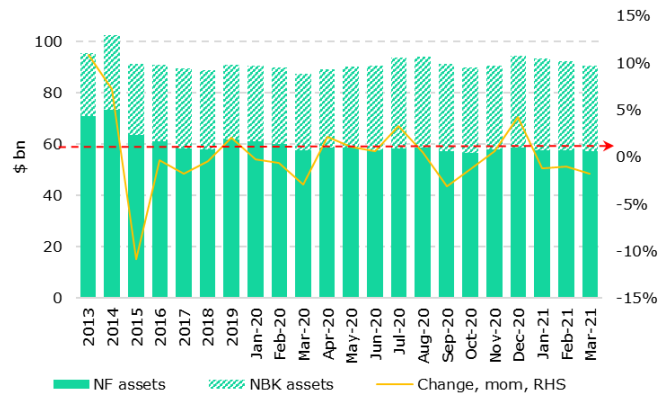


Fig. 18. Consolidated reserves of Kazakhstan



Source: IMF, Halyk Finance

Source: NBK, Halyk Finance

Receipts of funds in the NF in January-March of this year, according to the Ministry of Finance of the Republic of Kazakhstan, increased 4 times to KZT1.1 trillion (\$2.4 billion) compared to the corresponding period last year. Direct tax revenues from oil sector enterprises also quadrupled to KZT1.05 trillion (\$2.31 billion). A significant increase in revenues is observed from CIT (growth by 3.8 times) and from the tax on the extraction of minerals (by 6.5 times). The share of the Republic of Kazakhstan in the division of production under concluded contracts increased by 3 times. In total, the share of these items in the structure of receipts is 87.5%. Among the fund's revenues, there is a return of a targeted transfer from the republican budget in the amount of KZT30 billion. In 1Q2022, the fund's expenses decreased by 3.9% YOY and amounted to KZT1.04 trillion, or \$2.3 billion. The size of the guaranteed transfer, transferred to the budget in 1Q2022 increased by 22.8% YOY and amounted to KZT985 billion (\$2.16 billion). The size of the targeted transfer decreased by 81.6% YOY and amounted to 50.7 billion (\$111 million). For 1Q2022, the balance of receipts to the Fund was positive and amounted to KZT53.3 billion (\$117 million).

Recall that according to the revised budget for 2022, the guaranteed transfer to the budget will be KZT4,030 billion, while the targeted transfer is KZT550 billion. Thus, the total transfer to the country's budget revenues will be KZT4,580 billion (\$10 billion), which is slightly higher than the total amount of the transfer in 2021 in the amount of KZT4 500 billion.

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