

November 2019

*The growth of the economy of Kazakhstan in the third quarter of 2019 intensified, reaching 4.6% yoy, which was facilitated by large-scale budget injections and continued high investment activity against the background of negative dynamics in oil prices. Inflation risks were not fully realized – high devaluation expectations of the population and weakening of the national currency were not adequately reflected in the official statistics in regard to the consumer prices growth. Based on the current dynamics of the main macroeconomic factors, we expect GDP to grow by 4.4% in the base case for 2019, inflation at 5.5%, and the national currency rate at – 389.5 tenge per dollar at the end of the year.*

**Economic growth accelerated to 4.6% yoy in the third quarter due to government spending.** The growth of the economy of Kazakhstan this year was headed for a gradual acceleration, amounting to 3.8% yoy in the first quarter, 4.4% yoy in the second and 4.6% yoy in the third. The latter indicator corresponds to the level of 2014, when the oil price was close to \$100 per barrel. However, the average level of oil prices for 9M2019 amounted to about \$65 per barrel, which is 11% lower than the same indicator a year earlier. At the same time, oil production also decreased slightly against the background of maintenance works at the country's largest oil fields. Accelerated economic growth amid falling oil prices is explained by the increase in government spending, which increased by almost 20% yoy – the highest growth since 2012. It should be noted that the financing of these expenditures is carried out at the expense of the same oil revenues accumulated in the National Fund earlier. Among major industries, no fundamental changes took place against the background of a large volume of investments, the sectors of construction, trade and transport were actively growing. Against this background, a slowdown in industrial output has been evident as part of the general global trend due to declining demand for raw materials and finished goods.

**Agriculture is a weak chain in the Kazakhstan economy.** The only industry that finished the reporting period in the negative zone was agriculture. A weak grains crop has taken agriculture to the negative zone for the first time since 2013, although for the year as a whole the situation may improve due to the small decrease at the moment by 0.5% yoy.

**The increase in real wages in the public sector offset the decline in the private sector.** The average salary in September of this year amounted to almost T189 thousand, which is T28 thousand or 17% higher than in September 2018. At the same time, retail trade showed a slowdown to 5.5% from 7% a year earlier amid increasing demand for foreign currency. Consumer lending growth is still above 20% yoy.

**Inflation risks are not fully realized.** High devaluation expectations of the population and the weakening of the national currency by more than 10% yoy compared to the same period last year did not have a corresponding reflection in the data of official statistics on the consumer price index. Inflation for 9M2019 remained at the level of last year at 3.3%. While the weakening of the tenge against the US dollar in January-September of the current year amounted to almost 12% yoy, and the similar change to the ruble amounted to more than 6% yoy, the contribution of non-food products to inflation, on the contrary, decreased.

**The current account deficit in 1H2019 expanded to \$1.9bn compared to \$1.5bn in 1H2018.** According to the updated NBK data, a small negative current account balance of \$163mn in the first quarter of 2019 was covered by a deficit of \$ 1.757bn in the second quarter. The expansion of the current account deficit was facilitated by a decrease in the trade surplus of 7.5% yoy to \$11.4bn. At the same time, the nominal export volume grew by 0.8% yoy and amounted to \$ 28.3 billion, while the volume imports grew by 7.2% yoy and amounted to \$16.0bn. The reduction in the deficit in the balance of services by 6.7% yoy and primary income by 3.6% yoy in the first half prevented a widening of the current account deficit.

**The national currency follows the decline in oil prices.** In the third quarter, the national currency weakened by 1.4% from an average of 380.9 tenge in the second quarter to 386.1 tenge per dollar in the third. Kazakhstan tenge followed oil quotes, which in August almost approached their annual lows of \$56.2 per barrel (54.9 at the beginning of the year). Also, as in the second quarter of 2019, in the third quarter, the Kazakhstan tenge continued to experience the influence of a drop in oil prices against the background of the greater stability of the Russian ruble against the US dollar. This, in turn, shifted the quotation for the RUBKZT pair to an annual maximum of 6.07 tenge (6.12 tenge per Russian ruble at the end of October).

**Monetary conditions, despite an increase in the base rate, remain neutral.** In September of this year, the regulator decided to raise the base rate to 9.25%, attributing such a decision to food inflation, expanding domestic demand and price volatility in global oil markets, as well as uncertainty due to trade differences between the US and China and a slowdown in the global economy. Rates on money market instruments continue to move up. The yield on short-term notes with a maturity of 182-364 days increased to 10.00% -10.20%. The weighted average yield was 9.31% in August of the current year (9.02% in June 2019 and 8.61% in August last year). The actions of the regulator will restrain the flow of funds into the real sector of the economy due to the cost of credit, which in turn will reduce the inflationary pressure on the economy. In addition, an increase in interest rates on money market instruments with a maturity of 6-12 months will facilitate the further transfer of large volumes of liquidity to longer periods.

**The international reserves of the NBK decreased by 7%, while the share of gold increased to 63%.** According to preliminary data from the NBK, the consolidated international reserves of Kazakhstan in September 2019 amounted to \$

88.1 billion, having decreased by 0.9% since the beginning of the year due to a decrease in the NBR gold reserves by 6.9% to \$ 28.8 billion. The NBK has experienced a decrease in the most liquid part of gold reserves - since the beginning of the year, assets in hard currency decreased by 35.0% to \$ 10.7 billion, although over the past month they have grown by 12.0%. The volume of gold in the reserves of the NBK as of the end of September this year increased by 25.5% from the beginning of the year to \$ 18.1 billion, or 62.7% of the total gold reserves. At the end of September of this year, the assets of the National Fund (NF) increased by 2.3% from the beginning of the year and reached \$59.3bn. Direct tax revenues from enterprises of the oil sector increased by 0.7% YoY and amounted to T2.128bn.

**In the base scenario we expect GDP to grow by 4.4% by the end of 2019, inflation at 5.5%, and the national currency rate at - 389.5 tenge per dollar.** As a result of escalation of trade disagreements between the largest economies – the United States and China, lasting for the second year, and the growth of uncertainty about the actions of world central banks that could spill over into currency wars, a slowdown in global economic growth is expected. In particular, in October, the IMF once again lowered its forecast for global economic growth for 2019 from 3.3% to 3%. Quotations of “black gold” this year are extremely weakly responsive to reduced production under OPEC+ agreements and geopolitical instability in important oil-producing countries, indicating a weakening demand. Accordingly, our expectations for oil prices are shifting down from \$65 to \$63.8 barrel this year.

Thanks to numerous government measures to stimulate consumption, domestic demand in the Kazakhstani economy largely compensates for the deterioration of the external environment and supports economic growth in the short term. The risks of accelerating price growth in the consumer market under the influence of increasing budget expenditures, accompanied by a depreciation of tenge, stubbornly do not want to materialize fully in the growth of inflation so far. The forecast for GDP growth in 2019 and 2020 was 4.4%. Expectations of the tenge exchange rate to US dollar were revised downward from 385 to 389.5 at the end of this year (baseline scenario). We implemented the scenario forecasts of the main macroeconomic indicators for 2020 with a symmetrical deviation from the baseline scenario, assuming an average annual oil price of \$62 per barrel in 2020.

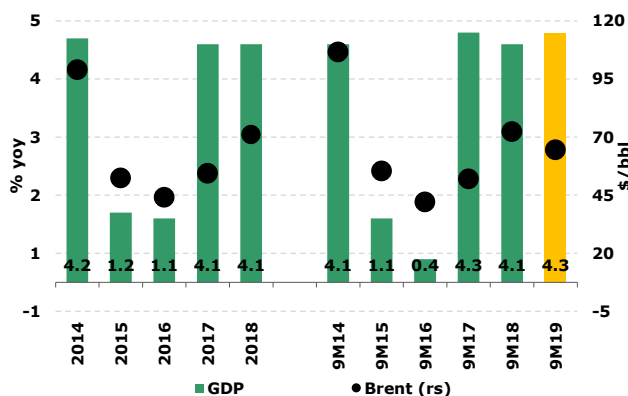
Main macroeconomic indicators	2017	2018	Base		Pessimistic		Optimistic	
	Fact	Fact	2019	2020	2019	2020	2019	2020
Oil Brent, average, USD/bbl.	54,0	71,0	63,8	62,0	62,0	52,0	65,0	72,0
Real GDP, % yoy	4,1	4,1	4,4	4,4	4,0	3,6	4,5	4,6
Exchange rate USDKZT, eop	332,0	384,2	389,5	397,0	394	412	385	388
Exchange rate USDKZT, average	326,0	344,7	386,9	393,3	389,1	403	384,6	386,5
CPI, % change yoy	7,1	5,3	5,5	5,5	5,7	6,0	5,3	4,9
Government debt, KZT bn eop	13,5	15,4	16,7	18,3	16,9	18,7	16,7	18,1
Government debt, % GDP	25,4	24,9	24,4	24,1	25,0	25,3	24,2	23,3
Budget balance consolidated, % GDP	-2,7	-1,3	-2,0	-2,0	-2,1	-2,4	-2,0	-1,8
Current account, % of GDP	-3,1	-0,2	-1,5	-1,8	-1,6	-2,3	-1,4	-1,2

**Fiscal stimulus strengthened the economic growth**

The growth of the economy of Kazakhstan for the nine months of 2019 accelerated to 4.3% yoy from 4.1% yoy for 9M2018 (Fig. 1), while in July-September, the growth of the economy was at the level of 4.6% yoy compared with 4.4% yoy in the second quarter and 3.8% yoy in the first. As we have already noted, the acceleration of the economic growth this year is going contrary to a less favorable external environment – oil prices fell by more than 10% yoy, while oil production fell due to repairs at the largest oil fields – Kashagan, Karachaganak and Tengiz. Over the nine months of this year, 67 million tons of oil were produced (67.3 million tons in 9M2018). The increase in oil prices, which was observed in 2017 and 2018, was replaced by a noticeable weakening; as a result the cost of a barrel of oil averaged \$64.5 for 9M2019, which is lower than \$72 per barrel in the same period a year earlier. Deflation in both the oil and other commodity markets is driven by concerns over the falling demand for raw materials, the negative effects of trade wars, and the strengthening of the US dollar in which the majority of commodities are traded.

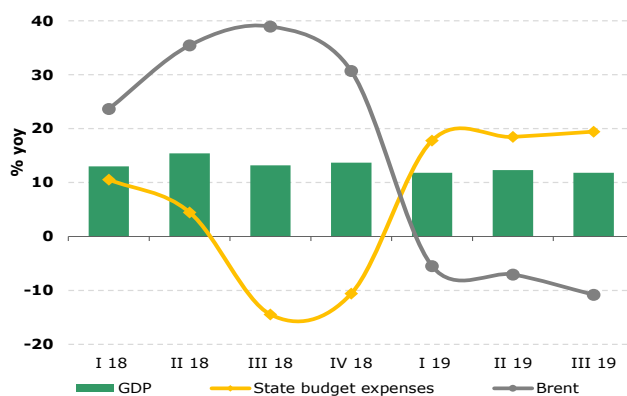
The deterioration of external conditions was more than offset by a strong increase in the state budget expenditures, which increased by almost 20% in annual terms nominally, compared with a two-digit reduction (-12%) in the second half of 2018 (Fig. 2). Nominal GDP growth rates are also slightly lower, on average about 1 pp weaker than last year and make up 12%. The increase in government spending this year is the largest in the last 8 years, not counting 2017, when their growth was associated with saving banks. In addition to the increase in direct payments for social security of the population, household incomes increase due to tax amnesty, forgiveness of consumer loans, maintaining low fuel prices in the domestic market, reducing utility tariffs and increasing the availability of housing. Incentive measures are financed by increasing the transfer from the National Fund from T2.6 trillion in 2018 to T3.1 trillion in this year and the growing budget deficit from T0.8 trillion to T1.5 trillion.

Figure 1. Oil prices and GDP



Source: CS MNE

Figure 2. Fiscal stimulus



Source: CS MNE

**All major industries, excluding agriculture are in positive zone, investments grow strong**

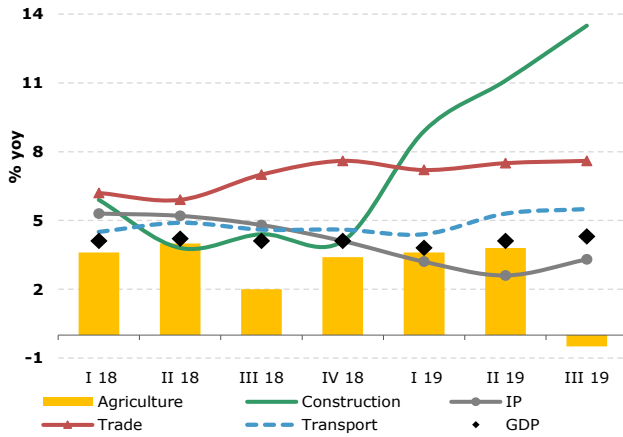
Acceleration of the economic growth at the industry level is mainly due to the construction and trade. The volume of construction works in 9M2019 increased by 13.5% yoy, and such strong growth rates have not been observed since 2006. The main contribution to the growth of construction is due to the expansion of capacities in the oil industry and investments in residential real estate and infrastructure.

The industrial output shows rather weak indicators this year – an increase of 3.3% yoy for 9M2019, which is noticeably worse than 8.3% yoy for 9M2017 and 4.8% yoy for 9M2018. In the main components of the manufacturing sector, there is an increase of 3.5%, in the mining sector – by 3.1% yoy.

Under the influence of climatic factors the current year was not the best for agriculture, as obsolete agricultural technologies used in crop production lead to a high dependence of crops on weather conditions. This year, 19.3 million tons of grain were harvested (as of 10/22/2019), which is more than 10% lower than last year, the yield indicator accordingly decreased from 14.6 c/ha to 12.7 c/ha. A weak crop in agriculture this year means a rise in the cost of raw materials for the food industry, which subsequently should result in an increase in the cost of food.

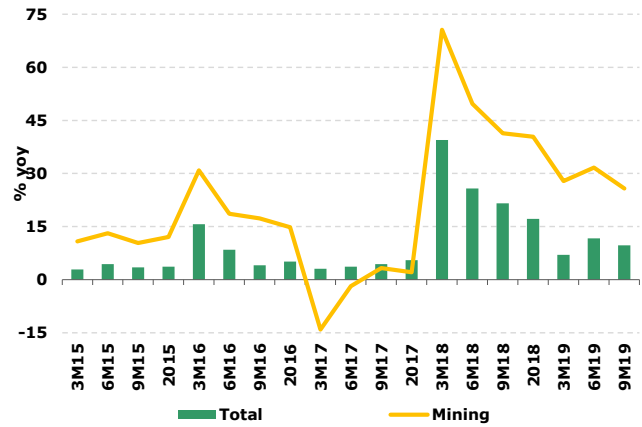
The rapid growth of investments in the mining industry, which was observed last year, corrected slightly, but remained strong – in 9M2019 its volume grew by 25.8% yoy (41.4% yoy in 9M2018). Given that the mining industry accounts for approximately 40% of all investments, the overall growth in investment activity is directly dependent on the mining sector. As a result, investment in fixed assets increased by 9.7% yoy (Fig. 4).

Figure 3. Strong growth of construction



Source: CS MNE

Figure 4. Investment boom in mining



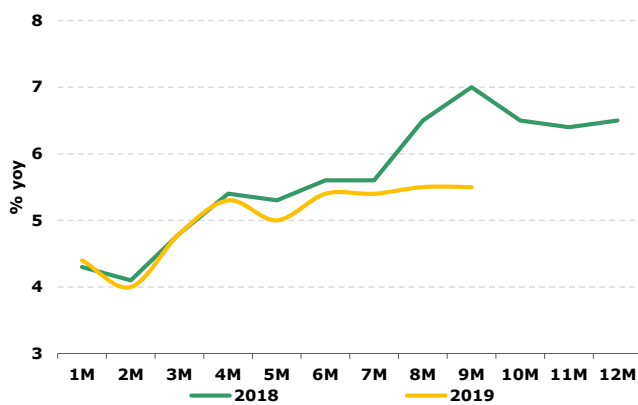
Source: CS MNE

**Retail trade slowed amid rising wages**

Growth in the retail trade turnover moderately weakened to 5.5% yoy in January-September compared with a 7% growth over 9M2018 (Fig. 5). The main components, food and non-food products, show similar dynamics, having increased by 6% yoy and 5.2% yoy, respectively. Despite the fact that retail sales growth is still ahead of economic growth this year, its dynamics look noticeably lower than potential in our opinion. The slowdown in trade turnover growth can be attributed to the rise in the devaluation expectations, which provoked an increase in demand for foreign currency. For example, in 8M2019, the population acquired \$3.4 billion, which is \$1 billion or 40% more than a year earlier. Thus, instead of an increase in consumer spending, increased devaluation expectations stimulated the foreign exchange market, although higher salaries and measures to increase household incomes should have a positive effect on consumption. In turn, the demand for bank consumer loans shows a growth of more than 20% yoy and remains an important channel for supporting retail turnover.

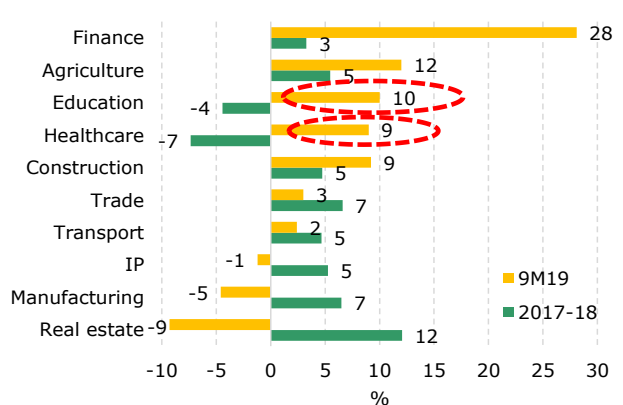
This year, the state organs decided to pay more attention to the salaries of the population, whose growth was systematically behind inflation (Fig. 6). First of all, from the beginning of the year, the minimum wage was immediately increased by 50% to T42.5 thousand. Since June, salaries in education and healthcare spheres have been increased: taking into account that these industries account for more than 30% of those employed to determine the average wage in the country, the public sector has become the main driver of wage growth this year according to the official statistics. For nine months, real salaries in education increased by 10%, in healthcare by 9%. In addition to the public sector, a significant increase in real wages occurred in the financial sector (+28%). The average salary in September of this year amounted to almost T189 thousand, which is by T28 thousand or 17% higher than in September 2018. Against this background, it is noteworthy that, despite the declared acceleration of economic growth, real wages in the manufacturing sector decreased by almost 5%, and in industry - fell by 1%, and there was a drop in other sectors. It is not yet clear whether there has been a peak in wage growth in the private sector, or whether growth will continue. However, it is increasingly difficult to count on this, given the significant deterioration in the external environment in the current year. Thus, fiscal stimulation, which includes an article such as the raise of salaries in the public sector, plays an important role in increasing household incomes.

Figure 5. Retail sales



Source: CS MNE

Figure 6. Real wages



Source: CS MNE

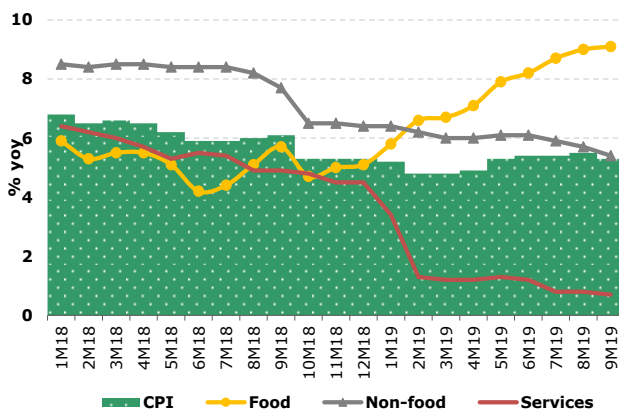
**Inflation risks unrealized**

According to the results of the nine months of 2019, inflation amounted to 3.3%, which corresponds to the same value for 9M2018. In annual terms, the inflation rate in September slowed to 5.3% from the peak of the current year at 5.5% in August. The main contribution to the price increase for the nine months of this year was made by food products (2.4pp out of 3.3%). Non-food products added 1ppt, which is 30% lower than last year, while services, under the influence of government interventions, subtracted -0.1pp from the total increase in consumer prices. Thus, the main increase in prices falls on food products. In turn, the effect of the reduction and freezing of tariffs for housing and communal services along with the artificial maintenance of low prices for fuel is close to exhaustion.

This year, the dynamics of inflation is largely determined by the unprecedented measures of state support of population incomes, including raising salaries of state employees, pensions, improving housing affordability, writing off bad consumer loans, lowering tariffs and many other measures. Due to the suppression of inflation via tariffs, inflation risks have not yet been realized, and the fall in wages in the private sector offset the increase in wages to state employees. Thus, the net change remained zero, in turn, a strong increase in mortgage lending due to the affordable mortgages can be considered as a factor limiting current consumption (long-term deferred demand). However, it cannot be said that the inflation pattern is completely transparent: we recall that the weakening of the tenge against other currencies, in particular against the dollar in January-September of this year amounted to almost 12% yoy, a similar change to the ruble amounted to more than 6% yoy. At the same time, as noted above, the contribution of non-food products to inflation, on the contrary, decreased, which seems illogical, given the high dependence on imports of finished products. Although inflationary expectations of the population have departed from the peak values of the current year, they are nevertheless at an elevated level, indicating continued pressure on consumer prices.

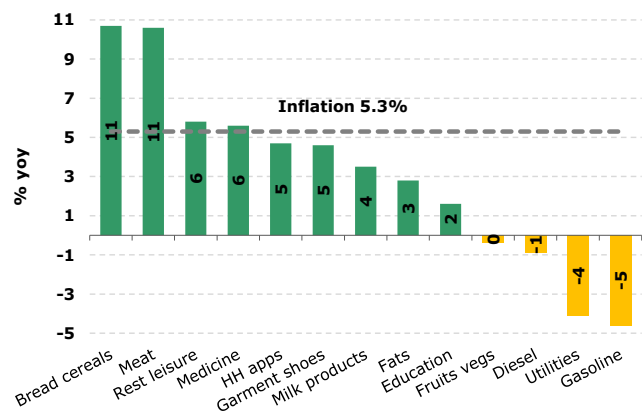
Due to the fact that inflation risks are latent at the moment and there is likelihood that they will not manifest themselves, we adhere to our basic inflation forecast for the current year of 5.5%, which corresponds to a comfortable level within the framework of the National Bank's operating corridor of 4-6%. We consider the increase in the base rate by the regulator in September to be quite an adequate solution, demonstrating the monetary authorities' commitment to the inflation targeting policy and the seriousness of their intentions to manage inflationary expectations, albeit with a temporary increase in costs due to more expensive loans.

Figure 7. Food drove inflation



Source: CS MNE

Figure 8. Components of inflation



Source: CS MNE

**Interest rate policy**

During the first two months of the third quarter of this year, the base rate of the regulator remained at 9.0%. However, in September, the regulator decided to raise the base rate by 0.25%, emphasizing that food prices contributed the most to inflation in August, while prices for non-food products and services showed moderate growth. According to the regulator, expanding domestic demand remains a major factor of the inflation. The NBK indicates that growth in consumer lending along with growth in real wages, growth in retail sales, as well as growth in budget spending on the social sphere contribute to the expending of the aggregate demand. On the supply side, growth in economic activity is also observed, which is higher than the NBK expectations. The NBK emphasizes that amid rising investment, GDP growth will be in the positive zone, indicating inflationary pressure on the economy. The regulator connects the external negative background with the volatility of oil prices, differences in trade policies of leading countries and with a slowdown in the global economy, which, in turn, reduces the demand for Kazakhstan exports. The NBK notes that monetary conditions remain neutral.

The average rate on automatic REPOs in the 3rd quarter amounted to 8.53% (8.16% in 2Q2019), while the range of change in rates was 8.01-10.11% (7.96% -9.04% in 2Q 2019). As of the end of September, the rate on automatic REPOs was at the level of 8.76% (9.04% in 2Q 2019). In 3Q 2019, there was a decrease in the volume of automatic REPO transactions by 14.4% yoy to T14.375bn. The maximum volume of automatic REPO transactions fell at the beginning of September and amounted to T419bn a day.



The volume of one-day swaps USDKZT in the 3rd quarter of 2019 increased by 51.1% yoy to T1.856bn. The average rate on one-day swaps increased from 7.18% in the second quarter of this year to 8.19% in the third. The maximum volume for one-day swap transactions falls at the end of the quarter and amounts to T106.4bn.

The volume of two-day swaps USDKZT in the 3rd quarter of this year decreased by 11.7% yoy to T5.670 billion. The average rate on two-day swaps amounted to 8.23%, increasing by 0.96 bp. The maximum volume for two-day swaps falls at the end of August and amounts to T140.5bn.

Figure 9. Money market rates

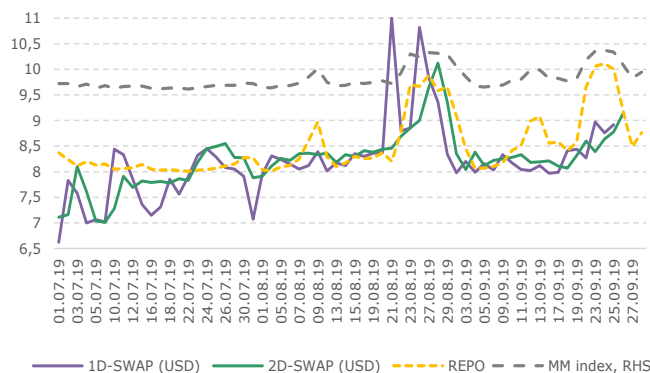
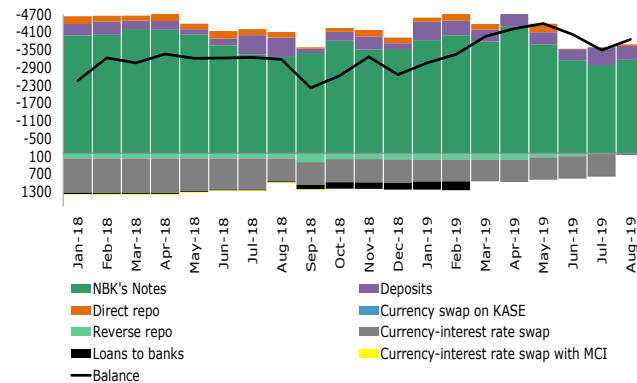


Figure 10. Withdrawal of excess liquidity



Source: NBK, Halyk Finance

Source: NBK, Halyk Finance

The composite MM index at the end of the 3rd quarter of this year was at the level of 8.79% with an average value of 8.48% (8.50% at the end of the 3Q2018 with an average value of 8.47%). The total volume of transactions in the money market in the third quarter of 2019 decreased by 13.5% yoy (-10.0% yoy) and amounted to T16.231bn.

The volume of liquidity withdrawals through NBK notes at the end of August this year amounted to T3.159bn, while the effective yield was 9.31% (9.02% in June 2019 and 8.61% in August last year). Since the beginning of this year, there has been an upward trend of interest rates on the NBK notes from 8.64% to 9.31% with a relative decrease in sterilized liquidity by 10.3%. In August 2019, the NBK notes increased by 5.6% mom (share of 94.7%), while deposits decreased by 66% mom (share of 4.8%). The yield on short-term notes with a maturity of 182-364 days increased to 10.00%-10.20%.

Rates on money market continue to move up. The yield on short-term notes with a maturity of 182-364 days increased to 10.00%-10.20%. The weighted average yield was 9.31% in August of the current year (9.02% in June 2019 and 8.61% in August last year). The actions of the regulator will restrain the flow of funds into the real sector of the economy due to the cost of credit, which in turn will reduce the inflationary pressure on the economy. In addition, an increase in interest rates on money market with a maturity of 6-12 months will facilitate the further transfer of large volumes of liquidity to longer periods.

**FX policy**

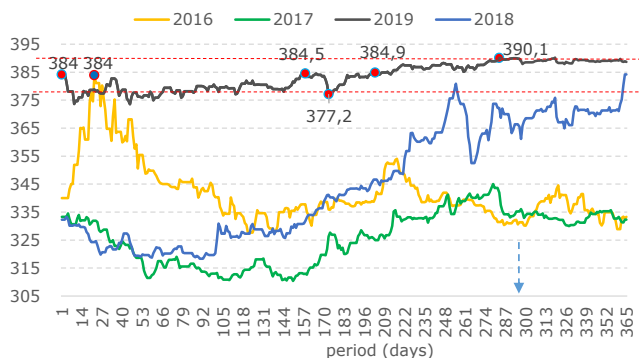
In the third quarter of this year, tenge weakened by 1.4% yoy to an average quarterly value of 385.8 tenge per US dollar. The national currency followed oil quotes, which in August amounted to \$56.2 per barrel, approaching an annual minimum of \$54.9 per barrel at the beginning of the year. For the third quarter, the price of oil corrected to an average quarterly level of \$ 62.0 per barrel, losing 9.4% of its value in the quarter. The correlation of the national currency and oil quotes was negative (-64%).

Unlike the Kazakhstan tenge, the Russian ruble weakened only 0.2% from an average of 64.5 rubles in the second quarter to 64.6 rubles per US dollar in the third. The correlation coefficient with the Russian ruble for the Kazakhstan tenge in the third quarter was 77%. Despite the new U.S. sanctions against the Russian Federation in the third quarter of this year, the ruble was supported by demand for ruble denominated sovereign assets, despite the fact that the Ministry of Finance of the Russian Federation allocated 664.3 billion rubles for the purchase of foreign currency. With the plan for the placement of domestic government bonds (DGB) for the third quarter of 2019 in the amount of 300 billion rubles at face value, the Ministry of Finance of the Russian Federation placed DGB in the amount of 370 billion (-50% qoq). At the same time, the share of foreign nominal holding amounted to about 30%. Meanwhile, the nominal holding of Kazakhstani debt in tenge by foreigners was reduced from T172.6bn in April to T61.6bn in October of this year. We believe that the tenge's support from further weakening during the third quarter was ensured by the presence of the regulator in the foreign exchange market in the form of direct foreign exchange interventions and indirect interventions in the form of currency conversion from the National Fund for transferring a targeted and guaranteed transfer to the budget.

A drop in oil quotes, together with a weaker decrease in the Russian ruble against the US dollar, shifted the quotation for the RUBKZT pair to an annual maximum of 6.07 tenge in the third quarter and 6.12 tenge per Russian ruble at the end of October. According to the Ministry of Finance of the Russian Federation, in the fourth quarter of 2019, the size of the planned placement of DGBs at par will amount to 420bn rubles, which is 40% more than the department's plans for the past third quarter. We also believe that the demand for DGBs will remain high, despite the mitigation of the key rate of the CB of RF,

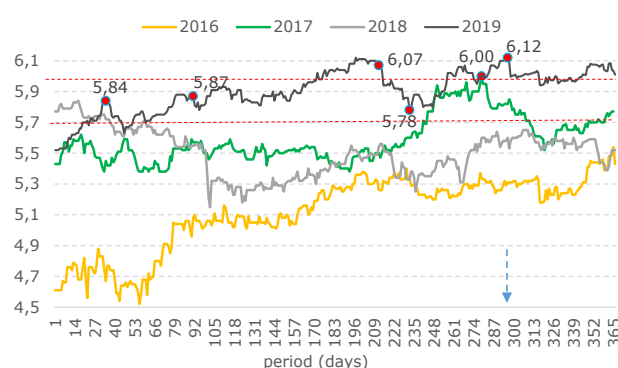
foreign investors will expand their investments in ruble-denominated stock instruments due to the high margin in carry trade operations. The strengthening of the Russian ruble will also be facilitated by a decrease in the volume of currency purchases by the Ministry of Finance of the RF on the foreign exchange market in the fourth quarter of this year. We believe that the volume of purchases of Russian currency will decrease by 20-25% from last year, which will support the ruble exchange rate by the end of this year. The Russian ruble will be formed at the level of 64-65 rubles per US dollar. Such levels for the USDRUB FX rate, in turn, will form the rate for the RUBKZT in a narrow corridor of 6.0-6.1 tenge.

Figure 11. Change in USDKZT FX rate



Source: NBK, Halyk Finance

Figure 12. Change in RUBKZT FX rate



Source: NBK, Halyk Finance

Unfortunately, we cannot analyze the expectations of the population regarding the devaluation of the national currency, because the NBK removed this question from its questionnaire or left it, but does not publicly disclose this information. Data on the sales of foreign currency by exchange offices shows that the sale of US dollars for 9 months of the current year increased by 43.4 yoy and amounted to T1.433bn. We believe that this can serve as an indicative sign of the "devaluation" expectations stance of the population at levels comparable to polls in June of this year, when 67% of respondents expected a rise in US currency value. Based on this, we can conclude that the population will continue to increase their savings in the US currency in the fourth quarter of 2019.

We believe that oil quotes will be formed at the level of \$ 62 dollars per barrel by the end of the year, although we do not exclude higher values at the moment. At such levels, the national currency exchange rate at the end of the year will amount to 389.5 tenge per US dollar.

**Export and import in January-August 2019 (according to the Committee on Statistics and the State Revenue Committee)**

The volume of imports from Kazakhstan in January-August 2019, according to preliminary data of the Statistics Committee, increased by 13.2% yoy to \$24.5bn, while export volumes decreased by 4.5% yoy up to \$37.6bn. Foreign trade turnover for 8 months of this year increased by 1.8% yoy to \$62.1bn.

In the analyzed period, a noticeable increase of the share of the export structure is observed in China (+ 2.1pp) to 14.0% and in Turkey (+ 2.0pp) to 4.0%. For 8 months of this year, there has been a reduction in the share of Italy by 4.1pp to 14.8% and the Netherlands by 3.8pp to 7.3%. In the structure of imports, there is a decrease in the share of the Russian Federation by 4.0pp to 35.4%, by 2.2pp to Germany to 1.9pp to 3.5%. The Republic of Korea increased its share in the structure of imports by 7.8pp to 9.6%.

The concentration of Kazakhstan exports in the five major countries-trading partners (with a share of ≥ 5%) for the 8 months of 2019 amounted to 52.3% and decreased by 1.5 pp in the same period last year. The concentration of imports of the largest 5 trading partner countries of Kazakhstan (with a share of ≥3.8%) for the 8 months of 2019 increased by 4.4 pp to 69.7% in the analyzed period.

In January-August 2019, the share of mineral products in the structure of Kazakhstan's exports decreased by 2.3 pp to 72.2%. In nominal terms, the volume of exports of mineral products decreased by 7.4% yoy to \$27.1bn. According to the Committee on State Revenues of the Republic of Kazakhstan, in January-August 2019, the physical volume of exports of crude oil and oil products decreased by 4.7% yoy and amounted to 44.1 million tons. In nominal terms, this export item decreased by 11.3% yoy to \$21.6bn.

A noticeable decrease in crude oil and gas condensate exports in January-August 2019 was observed to Italy (-19.5% yoy to 11.1 mln tons), the Netherlands (-38.5% yoy to 4.2 million tons), as well as Switzerland (-25.4% yoy to 2.6 million tons). At the same time, the export of crude oil to China increased by 87.9% yoy to 1.6 million tons, to the Republic of Korea - by 15.2% yoy to 3.7 million tons. The most noticeable increase in export volumes is observed to Turkey by 6.2 times to 2 million tons. The six largest importers of Kazakhstan's crude oil account for 66.9% of all exports.

The share of exports of metals and products from them has not changed compared to the same period last year and amounted to 14.5%. However, in monetary terms, a decrease of 4.6% to \$5.4bn is observed. The expansion of exports of metals in physical terms is accompanied by a decrease in their value at the global markets (excluding lead). Deliveries of untreated

zinc increased by 11.8% yoy, unprocessed lead by 40.2% yoy, unprocessed aluminum by 4.0% yoy, and refined copper by 18.4% yoy.

Figure 13. Geographic structure of exports,%

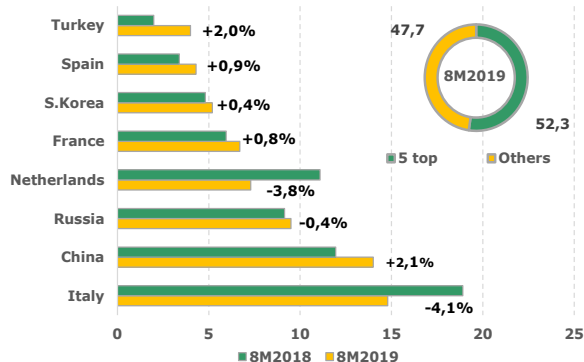
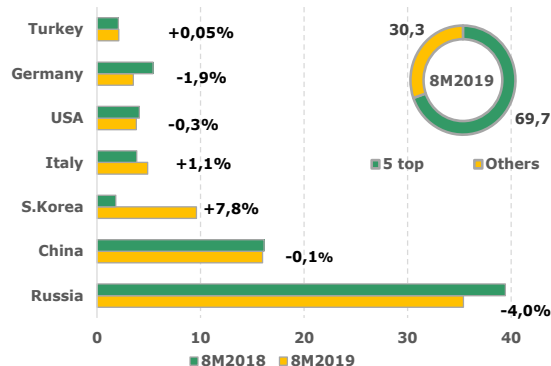


Figure 14. Geographical structure of imports,%



Source: SC of MNE, Halyk Finance

Source: SC of MNE, Halyk Finance

The concentration of exports for these two largest export items (oil and gas sector and metals) increased in January-August 2019 to 86.7% compared to 84.5% in the same period last year.

The third-largest item of Kazakhstan's export "animal and vegetable products, prepared food products" increased in the analyzed period to 5.4% from 4.8% in January-August 2018. In nominal terms, the increase was 7.4% yoy up to \$2.0bn. In January-August 2019, there was a significant increase in the export of cattle meat by 18.2 times to 1.3 thousand tons (according to the State Revenue Committee). About 87.9% of the total cattle meat export was exported to Iran. According to preliminary data from the Statistics Committee, the export of meat and meat products in January-August 2019 amounted to 16.4 thousand tons or \$37.6mn (for 12M2018: 20.9 thousand tons or \$50.6mn) against imports of 136.9 thousand tons or \$208.4mn (for 12M2018: 210.3 thousand tons or \$289.7mn).

Figure 15. Structure of export of goods

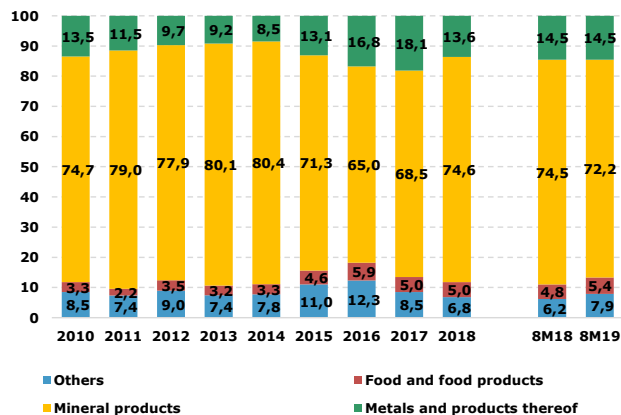
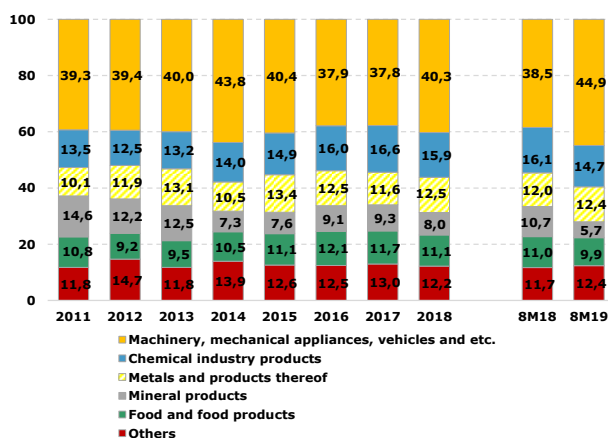


Figure 16. Structure of imports of goods



Source: SC of MNE, Halyk Finance

Source: SC of MNE, Halyk Finance

Exports of wheat and a mixture of wheat and rye decreased by 10.6% yoy to 3.3mn tons, however, in value terms, exports grew by 6.8% yoy to \$610mn. About 44% of the total export of Kazakhstan wheat imported by Uzbekistan. Growth in barley exports amounted to 2.1% yoy to 844 thousand tons or \$161mn (+ 19.5% yoy). The share of barley exports to Iran amounted to 95.6% of the total barley exports in the period. Rice export increased by 45.7% yoy to 45 thousand tons or \$13.5mn (+ 34.4% yoy). The main importing countries of Kazakhstani rice were Uzbekistan (50.4%) and Tajikistan (39.2%).

The largest point of Kazakhstan imports (44.9%), according to the Statistics Committee for 8 months of this year, is "imports of machinery, equipment, vehicles, instruments and apparatus", which over the year increased in nominal terms by 32.2% to \$11.0bn. Over the 8 months of this year, there has been a slight decrease in the share of imports of chemical products and related industries (including rubbers and plastics) to 14.7% from 16.1%. Import volumes reached \$3.6bn (+ 3.6% yoy).



In the structure of imports in the analyzed period, there is a slight increase in the share of metals and products from them by 0.4% to 12.4% compared to the same period last year. In value terms, metal imports grew by 17.0%yoy and amounted to \$3.0bn.

**Balance of payments for the first half of 2019**

Current account of the Republic of Kazakhstan in the first half of 2019 according to the updated data of the NBK hit a deficit of \$1.920mn (deficit of \$1.470mn in 1H2018). The negative balance of \$163mn in the first quarter of 2019 expanded to \$1.757mn in the second quarter. Current account deficit for the first half of the current year widened by a decrease in the trade surplus of 7.5% yoy to \$11.4 bn. At the same time, the nominal growth in export volumes was 0.8% yoy (\$ 28.6 billion), while imports grew by 7.2% yoy to \$17.2bn. The deficit in the balance of services in the first half of this year decreased by 6.7% yoy to \$1.8bn and in the balance of primary income of 3.6% yoy to \$11.6bn helped reduce the current account deficit. The reduction of the positive balance in the secondary income balance by 37.1% yoy to \$158mn, on the contrary, slightly contributed to the expansion of the current account deficit.

Figure 17. Expansion of the current account deficit, \$bn

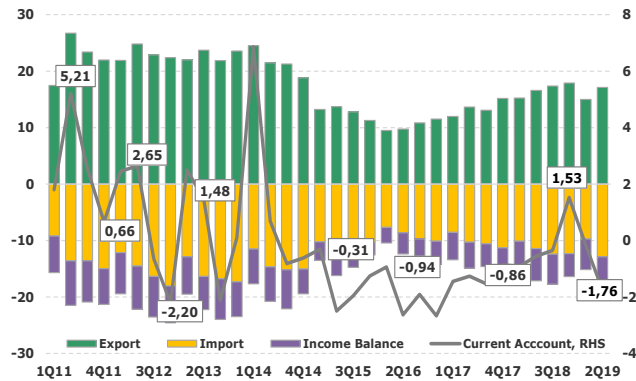
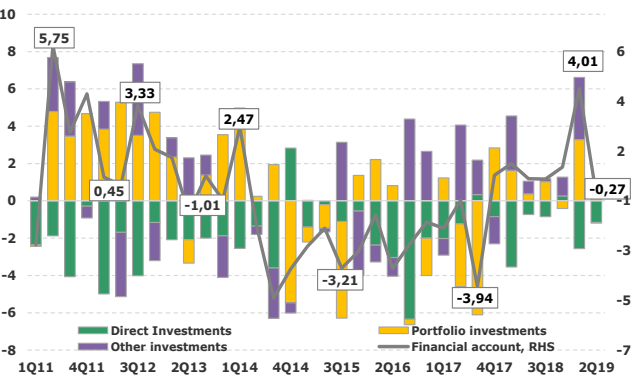


Figure 18. Inflow to the financial account, \$bn



Source: NBK, Halyk Finance

Source: NBK, Halyk Finance

According to the NBK reporting for the first half of 2019, FDI income (foreign direct investment) amounted to \$10.2bn (+ 27.7% yoy). Most of the FDI income to be paid comes from the crude oil and natural gas production sector (63.0%), metal ore production (6.3%), and transportation and warehousing (6.0%). The largest recipient countries for FDI income are the Netherlands at \$3.7bn, the United States at \$3.1bn and China at \$799mn.

Primary income receivable items show a negative trend for all types of income, except portfolio investments, which grew by 6.8% yoy to \$658.7mn. Remuneration on reserves and assets of the National Fund decreased by 5.6% yoy up to \$631mn.

The relative deficit of the current account to GDP in the first half of this year amounted to 1.1% (\$ 1.9 billion), increasing from a deficit of 0.8% (\$1.5bn) in the first half of 2018.

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

According to the NBK statistics for the first half of 2019, a significant outflow of capital in the amount of \$3.7billion is observed within the financial account, which is 2.7 times more than the outflow of capital in the first half of last year. The outflow of capital within the financial account for the entire last year amounted to \$2.6bn. At the same time, for the first time in 7 quarters, there is an inflow of capital in the second quarter of this year in the amount of \$270mn. However, the size of the inflow of the second quarter is not comparable with the volume of outflow in the first quarter current year at \$4.0 bn.

According to the direct investment account, in the first half of this year there is an inflow of financial resources in the amount of \$3.7bn compared to an inflow of \$4.3bn in the same period in 2018. At the same time, the net acceptance of liabilities amounted to \$ 916 million, and the net acquisition of financial assets amounted to \$2.8bn.

Gross FDI inflows in the first half of 2019 amounted to \$12.1bn (-3.1% yoy). About 53.4% of all investments were directed to the crude oil and natural gas production sector, 10.5% went to the metallurgical industry, and 11.4% of them went to the wholesale and retail trade. The main geography of gross FDI flows to Kazakhstan is represented by the Netherlands (28.1%), the USA (24.6%), Switzerland (8.3%) and China (7.6%). The annual growth in gross FDI in these countries amounted to: the Netherlands (+ 12.1%), the USA (+ 28.0%), Switzerland (-18.5%), China (+ 63.4%).

The outflow of financial resources of portfolio investments increased 2.1 times in annual terms and amounted to \$4.2bn. The outflow was facilitated by an increase in the net acquisition of financial assets in the amount of \$3.1bn in the first half of 2019 against the observed inflow under this article in amount of \$614mn last year in the same period. The net acquisition of residents' liabilities to non-residents as part of portfolio investments decreased from \$2.6bn in the first half of last year to \$ 1.1 billion in the reporting period. According to the updated NBK data on the balance of payments for the first half of 2019, there is an outflow under other investments in the amount of \$3.3bn (-8.2% yoy).

The relative indicator of the outflow of financial resources in the financial account to GDP, according to our estimate, increased from 0.8% (\$1.4bn) in the first half of 2018 to 2.1% (\$4.0bn) in the first half of 2019.

Within the analyzed period, the expansion of the acquisition of assets by residents in a financial account over their acceptance of obligations to non-residents continues.

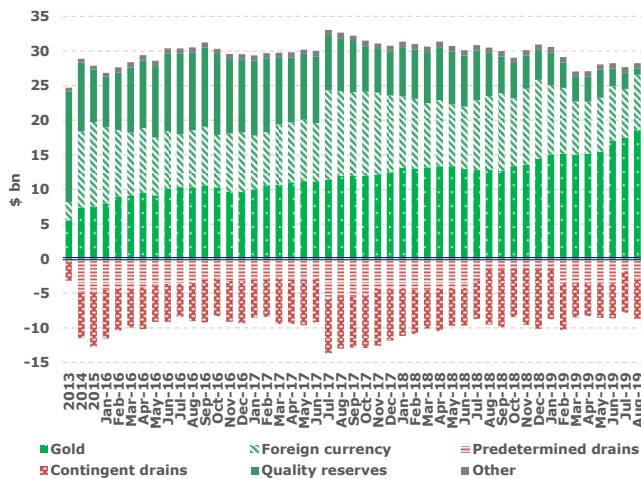
**Consolidated International Reserves**

Consolidated international reserves in September 2019, according to preliminary data from the NBK, amounted to \$88.1bn. From the beginning of the year, consolidated reserves decreased by 0.9% mainly due to a decrease in the NBR gold reserves by 6.9% to \$28.8bn.

As part of the NBK’s reserves, there is a decrease in the most liquid part of gold reserves, hard currency assets, the volume of which since the beginning of the year decreased by 35.04% to \$10.7bn. At the same time, the share of assets in hard currency increased in September to 37.3% from 34.0 % in August. Monthly growth of assets in hard currency was facilitated by the receipt of funds in bank accounts from the placement of sovereign debt in the amount of 1.15bn Euros. The decrease in reserves in hard currency since the beginning of the year was due to the withdrawal of deposits in foreign currency by bank customers abroad.

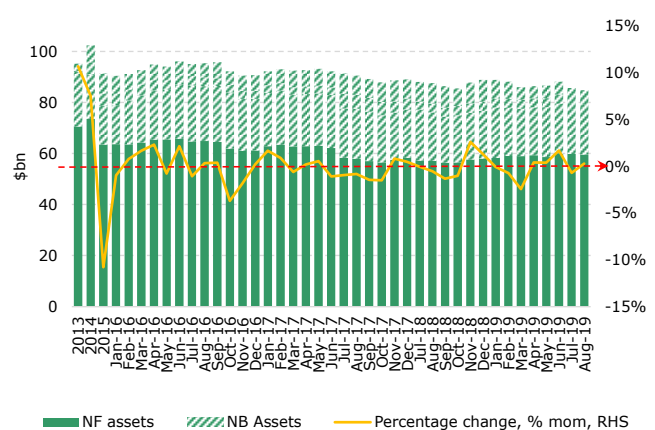
Gold in the NBK's asset structure has grown by 25.5% since the beginning of the year and amounted to \$18.1bn, or 62.7% of the total gold reserves. According to the IMF, the physical volume of gold of the NBK in August 2019 amounted to 12.13 million troy ounces or 377.3 tons (+ 7.7% from the beginning of the year). The nominal growth in the share of gold in the gold and foreign currency reserves was facilitated by the positive dynamics of prices on global markets from \$1,282 at the beginning of the year to \$1,547 in early September (the highest since November 2013). The reduction in physical volumes of gold from 12.22 million ounces in July to 12.13 in August was mainly due to the transfer of part of the assets in gold to the NF, which also contributed to an increase in the liquid part of hard currency. According to the NBK report for September of this year, net international reserves decreased by 7.0% from the beginning of the year and amounted to \$28.3bn.

Figure 19. International Reserves of the NBK



Source: NBK, IMF, Halyk Finance

Figure 20. Consolidated Reserves of Kazakhstan



Source: NBK, Halyk Finance

As part of the short-term conditional net expenses of the NBK in foreign currency, in August 2019, the liabilities continued to decrease by 51.2% from the beginning of the year to \$5.7bn. As of the end of August 2019, in the structure of the provided short-term expenses, a short position is reduced from \$2.2bn in June to \$1.5bn in August, which according to the IMF classification corresponds to a currency swap, which in turn reflects a reduction in the size of the NBK’s reserves.

Since the beginning of this year, the assets of the National Fund (NF) increased by 2.3% to \$59.3bn (-0.3% mom). According to the Ministry of Finance of the Republic of Kazakhstan, revenues to the NF in January-September increased by 2.6 times in annual terms and amounted to KZT2.973bn (\$ 7.7bn). Direct tax revenues from enterprises in the oil sector increased by 0, 7% YoY to T2.128bn. In January-September of this year, the NF recorded investment income of T805 billion against a loss of T408bn in the same period last year. Fund expenses for January-September increased by 2.4% in annual terms and amounted to T2.588 billion or \$6.7bn (+ 10.1% m / m). Over the 9 months of this year, the balance of revenues to the Fund was positive and amounted to T384.8 billion (\$994mn at an average rate for the 2nd quarter of 386.9). In January-September of the current year, the amount of guaranteed transfer to the budget decreased by 12.2% YoY to T2.207bn or \$5.7bn. The size of the targeted transfer directed to the budget amounted to T370bn or \$956mn.

The increase in NF assets was due to an increase in corporate tax revenues of 6.7% yoy, an increase in excess profits tax revenues by 91.5% yoy, and also due to a decrease in the guaranteed transfer to the budget by 12.2% yoy.

**Banking sector**

The situation in the banking system is described in detail in a publication devoted to this topic: [Banks of Kazakhstan in September 2019](#).

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