
November 16, 2022

Disruptions in the oil and gas industry and subdued consumer activity led to a slowdown in the economy of the Republic of Kazakhstan in 9M2022 to 2.8% yoy from 3.6% yoy in 1H2022 and 4.6% yoy in 1Q2022. Despite the acceleration of inflation and external uncertainty, fundamental conditions for the economic activity remain favorable so far. Continuing relatively high prices for hydrocarbons, stimulating budget support for the economy against the backdrop of expanding investment activity, and a close-to-record grain harvest are the main drivers of growth in the period. Due to continued geopolitical tensions, rising production costs and expansion of government spending, consumer inflation accelerated in September to 17.7% yoy, which is in line with the maximum figure achieved in the previous inflation acceleration cycle in 2015-2016. Amid accelerating inflation, the NBK raised the base rate by 50bp in July to 14.5%, while kept it at that level in September. In October, in view of further inflation growth to 18.8% yoy, the NBK raised the base rate to 16.0%.

Continued favorable pricing environment for energy products (~70% in the structure of exports in 9M2022) led to a 2.2-fold increase in the trade account surplus to \$29.3 bn, which in turn led to an expansion of the current account surplus to \$7.9 bn. The current account surplus was offset by an outflow from the financial account of \$9 billion. Despite the favorable dynamics of external accounts, the tenge had depreciated by 10.5% YTD to 476.9 tenge per US dollar (depreciation by 2.5% qoq).

Macroeconomic dynamics in the Republic of Kazakhstan, according to our forecasts, will develop as follows: GDP growth rates this year will amount to 2.9% yoy, inflation dynamics will accelerate to 19%-20% yoy, and the exchange rate will be 480 tenge per 1 US dollar at the end of 2022.

The recovery of industrial production driven by oil output and the expansion of the budgetary impulse will ensure the growth of Kazakhstan's GDP by 2.9% in 2022. Despite the correction in the third quarter of 2022, oil prices remained at their highest levels in recent years (\$99.2 per barrel in 3Q2022). This has had a positive impact on both export earnings and state budget revenues. A significant increase in budget revenues in 9M2022 ensures the implementation of the stimulus policy, mitigating the effects of external geopolitical shocks and supporting domestic demand. Scheduled and unscheduled repairs in the oil and gas sector, together with the limitation of oil production under the OPEC+ agreement, have constrained oil production, while at the same time, its production volumes remained at levels close to last year's. The forecast volume of oil production in Kazakhstan in 2022 will be about 85.7 million tons against 85.9 million tons last year. As a result of sanctions against the Russian Federation, there is an influx of foreign and Russian companies into the republic, along with an increased tide of migrants, which also stimulates business activity in the country.

Tightening monetary conditions against the backdrop of accelerating inflation. During 3Q2022, the NBK tightened the monetary policy only in July, raising the base rate by 50bp to 14.5%. In 3Q2022, consumer inflation accelerated throughout the quarter. Despite inflation accelerating to 17.7% yoy in September, the NBK kept the base rate at 14.5%. Only in October, when consumer inflation accelerated to 18.8% yoy, did the NBK raise the base rate immediately by 150bp to 16%, while the real interest rate became negative at 2.8%. In addition to the growth in food prices by 22.2% yoy in September (23.1% yoy in October) and non-food products by 17.0% yoy (17.9% yoy in October), the expansion of spending of the state budget by 18.9% yoy, growth in investment activity by 7.0% yoy, as well as a significant increase in net exports 2.3 times in 9M2022 also contributed to elevated inflation. Despite the growth of the economy on the consumption side, household purchasing activity remains subdued (retail trade growth increased by only 1.4% yoy in 9M2022). High inflation rates, depreciation of the national currency and geopolitical uncertainty in the world contribute to the gradual transition of households and businesses toward the savings model, which affects the slowdown in the Kazakhstani economy.

Tenge - weakening against the backdrop of correction in oil prices and strengthening of the US dollar. As of the end of September, the national currency depreciated by 10.5% since the beginning of the year and reached 476.9 tenge per US dollar (-2.5% qoq). In 3Q2022, the exchange rate of the national currency at the moment reached 484.2 tenge, with an average value of 475.3 per US dollar. The weakening of the national currency took place against the backdrop of an adjustment in the cost of oil and an increase in the US dollar. Thus, oil prices corrected by 12% qoq, with an average value of \$99.2 per barrel (\$99 per barrel in 1Q2022, \$112.7 in 2Q2022). The US dollar exchange rate (DXY index) has increased since June 2022 by 7.1% qoq (+17.2% ytd and 19% yoy) to 112.1. At the same time, a significant inflow of foreign currency on the current account at the level of \$7.9 billion was offset by an outflow on the financial account of \$9 billion. Given further tightening of monetary policy by the US Federal Reserve, the continued high exchange rate of the US dollar and the outflow of capital of non-residents from

government securities of Kazakhstan, the tenge exchange rate at the end of 2022 will be at the level of 480 per US dollar.

Main macroeconomic indicators	2020	2021	Base		Worse case		Best case	
			2023	2024	2023	2024	2023	2024
Oil Brent, average, USD/bbl	42.3	70.4	100.0	80.0	90.0	60.0	110.0	100.0
Real GDP, % yoy	-2.5	4.3	2.9	3.2	2.4	1.6	3.4	4.1
Exchange rate USDKZT, eop	420.7	431.7	480.0	510.0	490.0	530.0	470.0	490.0
Exchange rate USDKZT, average	413.0	426.0	462.1	495.0	464.2	510.0	460.5	480.0
CPI, % change yoy	7.5	8.4	19-20	11.5	21-22	13.5	18-18.5	9.5
Base rate, %	9.0	9.8	16.5-17	12.5	15.0	14.5	16-16.25	10.5
Budget balance consolidated, % GDP	-4.0	-3.0	-2.6	-3.0	-2.8	-3.6	-2.4	-2.7
Current account, % of GDP	-3.7	-4.0	4.2	3.5	3.8	1.7	5.0	5.6

Disruptions in the oil industry affected the growth of the economy of Kazakhstan

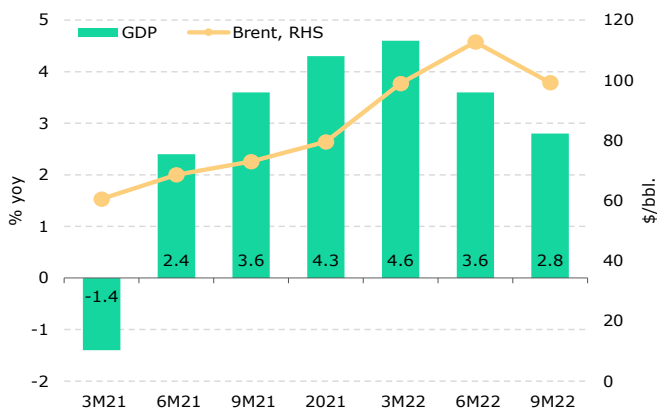
In the third quarter of this year, economic growth slowed down to 2.8% yoy after rising by 4.6% yoy in 1Q2022 and 3.6% yoy in 1H2022. Kazakhstan's economy has not seen such subdued growth since 2016, not counting the pandemic 2020. A number of negative factors caused a slowdown in business activity in the republic. A significant constraint on economic growth in 3Q2022 was the oil sector, which experienced a decline in oil production due to repair work at three largest oil fields in the country at once. In addition, oil quotes in the third quarter corrected to below \$100 per barrel, returning to the level of the 1st quarter of this year.

Despite the uninterrupted operation of the Caspian Pipeline Consortium (CPC) for two decades, this year there have been repeated interruptions in the transportation of oil through it from Kazakhstan to the port of Novorossiysk. We believe that restrictions on CPC operations as a form of Russia's pressure on Europe make no strategic sense, since deliveries of Kazakh oil through CPC account for less than 10% of the total balance of hydrocarbon consumption in European countries. In turn, the RF is a CPC shareholder and benefits from the transit of liquid hydrocarbons through its territory. According to the Ministry of Energy of the Republic of Kazakhstan, the restoration of full-fledged work of the CPC was to take place in October this year.

In relation with the decision taken by the OPEC+ countries to limit oil production, Kazakhstan's quota for October will be 1.7 million barrels per day, i.e. will remain at the level of August. The decision to cut oil production by countries participating in the OPEC+ agreement was taken in the face of an expected slowdown in global economic growth, which led to a widening imbalance between supply and demand in the oil market. In addition, OPEC lowered its forecast for growth of demand for hydrocarbons for the current and next years. Taking into account the new cap on oil production, as well as repair work at the key fields of the country, the total oil production in the republic this year is likely to be lower than the forecast of the Ministry of Energy of the Republic of Kazakhstan for this year at 85.7 million tons.

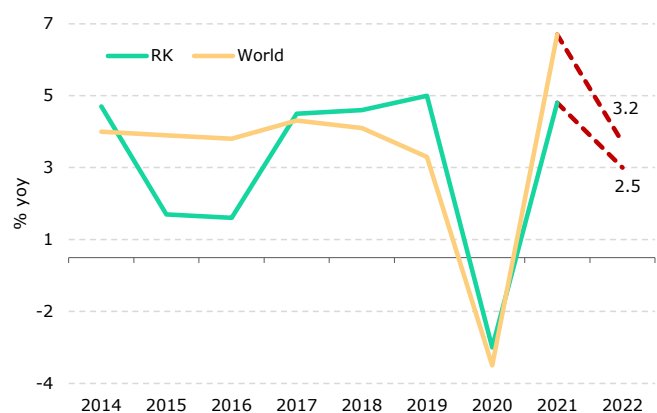
Against the backdrop of a correction in the cost of energy resources in global markets, the national currency weakened to 475.42 on average over 3Q2022 and reached its historical minimum. In the context of persisting geopolitical tensions in the world, the weakening of regional currencies against the US dollar coupled with capital outflow from emerging markets, inflation accelerated to 17.7% yoy in September and equaled the growth rates in the previous price growth cycle in 2015-2016. In order to support economic growth rates, the Government resorted to budgetary stimulation of domestic demand. Thus, in 9M2022 state budget expenditures increased by 18.9% yoy to T14.9 trillion (T12.5 trillion in 9M2021). At the same time, despite the administrative measures taken to regulate prices and the tightening of monetary policy, pro-inflationary pressure on the economy persisted, including due to the budgetary impulse. In turn, the growth in consumer prices, combined with the weakening of the national currency, had a dampening effect on the household consumer activity in 3Q2022.

Fig. 1. GDP vs oil prices



* GDP accumulated Source: BNS

Fig. 2. World economy and GDP of RK (IMF forecast)



Source: BNS

Given the escalation of war situation in Ukraine and taking into account significant economic influence of the RF on regional economies, the IMF in October adjusted the forecast for global GDP growth in 2022 with a slowdown to 3.2% from 6.0% in 2021. In 2023, a significant part of the world's countries will teeter on the brink of recession, and global growth rates will slow down to 2.7%. The growth forecast for Kazakhstan's economy has also been revised down to 2.5% in 2022 from 2.9% in the original forecast. The forecast for an economic downturn in Russia for the current year has been revised down to 3.4% from 8.5%. According to the Fund's estimates, the average price of oil will be

\$98 per barrel this year (\$111 per barrel in the previous forecast) and \$85.5 per barrel in 2023 (\$96 per barrel in the previous forecast).

Sanctions against Russia have a twofold effect on the economy of Kazakhstan. On the one hand, the activities of the Russian banks in the republic are being curtailed, volatility of currencies and acceleration of inflation rates are observed, on the other hand, there is a relocation of companies from the Russian Federation to the Republic of Kazakhstan, trips of Russian citizens to the republic have become more frequent and there has been an inflow of capital from Russia to Kazakhstan, which, in turn, provided some support to domestic demand.

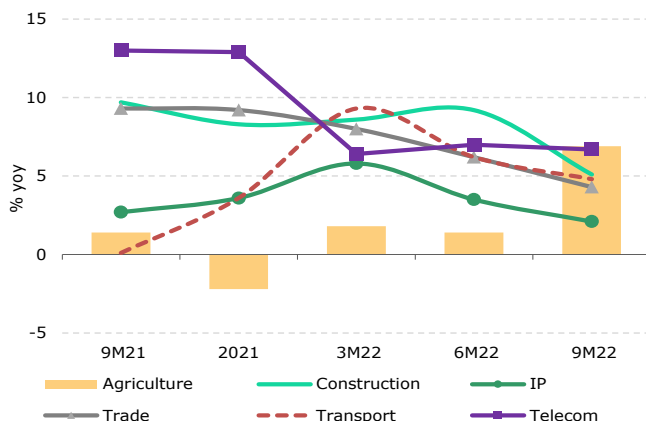
The slowdown in economic sectors continued

During the entire 3rd quarter, external demand as a whole remained quite favorable for the economy of the republic. Oil quotes, although they corrected close to the first quarter prices, nevertheless were at a very comfortable levels both for the oil industry and for the country's budget. The average price of Brent oil in the third quarter of this year was at \$99.2 per barrel (-12% qoq), while in 9M2022 its average price was \$103.6 per barrel, which is the highest reading since 2014. Continuing strong demand and a relatively high cost of energy contributed to the growth of Kazakhstani exports by about a half.

In January-September, industrial production growth slowed to 2.1% yoy compared to 3.5% yoy in 6M2022 and 5.8% yoy in 1Q2022. The volume of output in the mining industry increased by just 0.1% yoy over the period (+1.9% yoy in 6M2022). Crude oil production in 9M2022 decreased by 1% yoy (+1.3% yoy in 6M2022), which was affected by a partial shutdown of oil production at the Kashagan field, which produces almost 20% of all oil in the country and the planned repairs at the Karachaganak field, that provide approximately 13% of the total oil production.

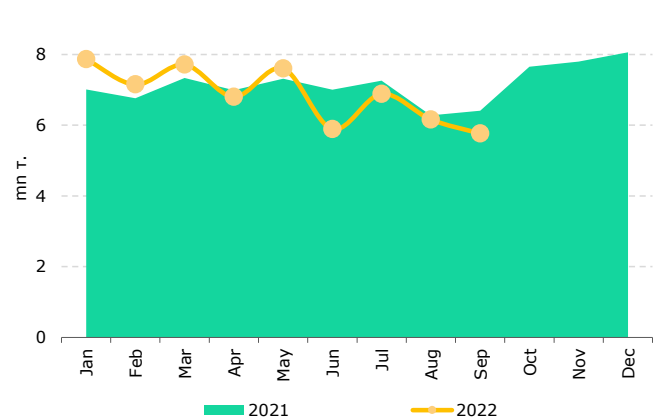
Growth in the manufacturing industry also demonstrated a slowdown, standing at 4.6% yoy in 9M2022 versus 5.8% yoy in 1H2022 and 6.5% yoy in 1Q2022. across all sub-sectors, although it should be noted that output growth is still positive – oil refining products (+4% yoy), chemical industry (+10.7% yoy), metal products (+4.7% yoy) and machine building (+7.6% yoy). The number of passenger cars produced in 9M2022 amounted to 71.4 thousand units (+29.8% yoy).

Fig. 3. Branches of economy



Source: BNS

Fig. 4. Oil output



Source: BNS

The agriculture sector showed the highest growth rates in 9M2022 (+6.9% yoy) due to an increase in gross crop output (+11% yoy). According to the statement of the relevant department, the grain harvest amounted to 21.6 million tons, which is almost by a third more than a year earlier and is the highest figure since 2011. The dynamics of gross livestock output, on the contrary, slowed down to 1.1% yoy (+3.8% yoy in 9M2021).

It should be noted that this year the performance of the sectors of the Kazakhstani economy is affected by the effect of the high base of last year, which is expressed in more moderate growth rates. Thus, the volume of domestic trade in January-September increased by 4.3% yoy (9.3% yoy in 9M2021). The growth rate of transport services was at the level of 4.8% yoy. In the telecommunications sector, growth slowed to 6.7% yoy in 9M2022 from 13% yoy in 9M2021. Growth dynamics in the construction industry also slowed down. Thus, in 9M2022, the volume of construction works increased by 5.1% yoy compared to 9.7% yoy in the same period last year. At the same time, the construction of non-residential buildings increased by 14% yoy (40% of the total volume), housing construction by 8.8% yoy, and infrastructure by 6.3% yoy (42% of the total volume).

Expansion of investments in the Republic of Kazakhstan

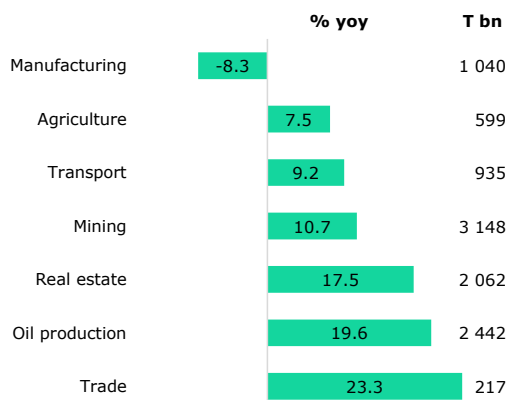
Against the backdrop of a slowdown in the growth rates of economic sectors, investment activity, on the contrary, demonstrated an acceleration of dynamics, turning into one of the significant drivers of economic growth. Thus, investment in fixed assets in 9M2022 increased by 7% yoy compared to 2.6% yoy in 1H2022. In nominal terms, investment amounted to T9.9 trillion, up from T8.7 trillion in 9M2021.

The growth of investments is still mainly driven by the commodity sector. The growth rate of investment in fixed assets in the extractive industry over 9M2022 increased by 10.7% yoy to T3.1 trillion (32% of the total). Whereas, investments in the non-commodity sector showed a more moderate growth by 4.4% to T4.8 trillion. Among them, of note investments in real estate operations (+17.5% yoy) with investments of T2.1 trillion (21% of the total). More than half of the total investment have occurred in the country's three largest cities.

Positive dynamics of investment growth was also noted in construction (+22.9% yoy), trade (+23.3% yoy), transport (+9.2% yoy) and agriculture (+7.5% yoy).

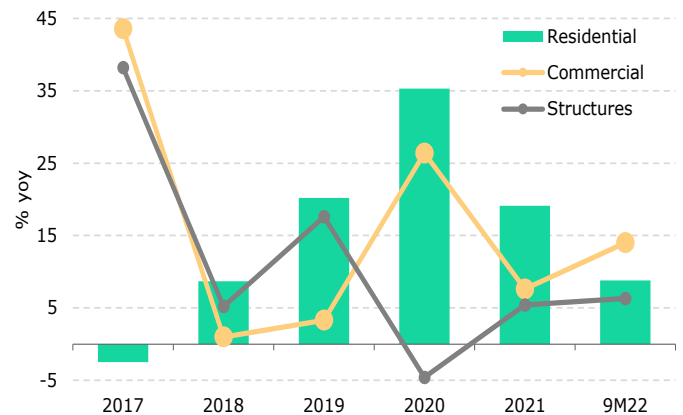
Growth rates of investments in the manufacturing industry were negative (-8.3% yoy), which was enabled by the high base effect of last year, when the industry's investment dynamics exceeded 80% yoy. The volume of investments in nominal terms was at the level of KZT1 trillion and was only KZT35 billion less than in the last year.

Fig. 5. Investment by sector (9M2022)



Source: BNS

Fig. 6. Construction by segments



Source: BNS

Household consumption is under pressure from inflation and the weakening of the national currency

After continuous growth for three quarters in a row, the decrease in nominal average wages in the third quarter of this year amounted to 7.8% qoq, and wages amounted to KZT300 thousand (\$631). This decrease was due to seasonal factors, while in general, for 9M2022, wage growth in the republic amounted to 24.1% yoy (+9.4% yoy in real terms). The highest wage growth rates were recorded in the construction industry – by 37.9% yoy (+21.6% yoy in real terms) and in the transport sector – by 31.6% yoy (+16.0% yoy in real terms). In general, wage growth is observed in all sectors of the economy, both in the public and in the private sector. Thus, the growth of wages became one of the significant factors in the growth of production costs and has translated to an increase in prices, which showed double-digit growth rates.

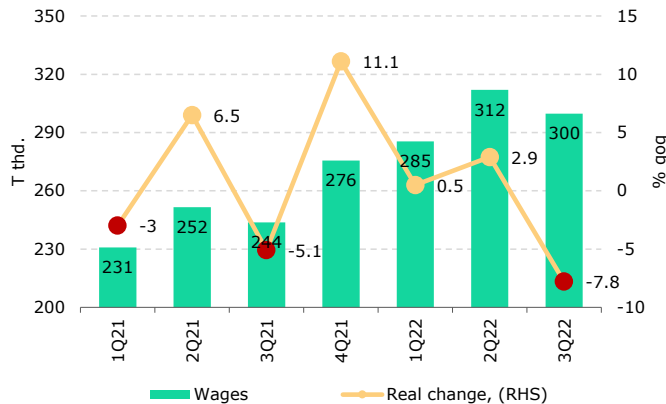
Household consumption in the current year remains restrained. In January-September, the growth of retail trade turnover in real terms amounted to only 1.4% yoy (+15.7% yoy in nominal terms), which was slightly higher than 1.2% in 1H2022. In nominal terms, retail trade turnover amounted to T10.6 trillion (T9.2 trillion in 9M2021), of which T3.8 trillion fell to food sales, and T6.8 trillion to non-food products.

Decrease in the sale of food products for 9M2022 amounted to 1.5% yoy, while a decrease in turnover was noted in about half of the regions of the republic. In turn, sales of non-food products increased by 3.1% yoy, which is also a rather modest outcome. Under normal conditions, the turnover of retail trade grows annually by about 5%-6%. Thus, despite the double-digit growth in wages and consumer lending (+27.7% yoy), monetary factors – inflation close to a record high, the weakening of the national currency and the growing attractiveness of savings in the form of deposits predetermined more restrained household consumption.

The trough of the decline in consumption was apparently passed in the first quarter of this year (-3.3% yoy), after which consumer demand recovered and reached a plateau in the third quarter. In the last quarter of the year, the retail trade turnover tends to grow. We believe that in 4Q2022 retail turnover will enter a growth trajectory, although

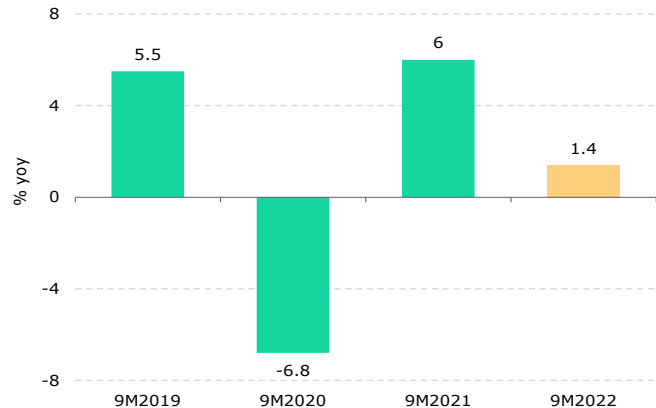
the dynamics will be restrained. At the same time, the weakening of the national currency and further acceleration of inflation may significantly affect the behavior of consumers.

Fig. 7. Dynamics of wages and retail trade



Source: BNS

Fig. 8. Retail trade



Source: BNS

Inflation rates remained high

Consumer inflation accelerated to 1.8% mom in September from 1.4% mom in August (+1.1% mom in July 2022). In annual terms, the growth rate of consumer inflation accelerated to 17.7%. Since the beginning of this year, the annual growth rate of consumer prices has shown continuous growth. Recall that the last time consumer inflation was at such a high level was in July 2016, when it reached a maximum of 17.7% yoy. Price growth rates for food products in September accelerated to 22.2% yoy (+19.2% yoy in June), and for non-food products - up to 17.0% yoy (+13.2% yoy in June). Price growth was also noted for paid services, the cost of which increased by 12.3% yoy (+9.2% yoy in June).

Since the beginning of the military conflict in Ukraine, the situation in the consumer market has been significantly different from previous periods. Despite a good harvest, food price increases accelerated across all commodities except fruits and vegetables, which is not typical for this time of year.

The rise in prices for non-food products was affected by the weakening of the national currency, which since the beginning of this year has lost 10% of its value against the US dollar and 44% against the Russian ruble. Given the high dependence of the domestic market on consumer imports, the rise in prices for non-food products in Kazakhstan has the potential for further growth.

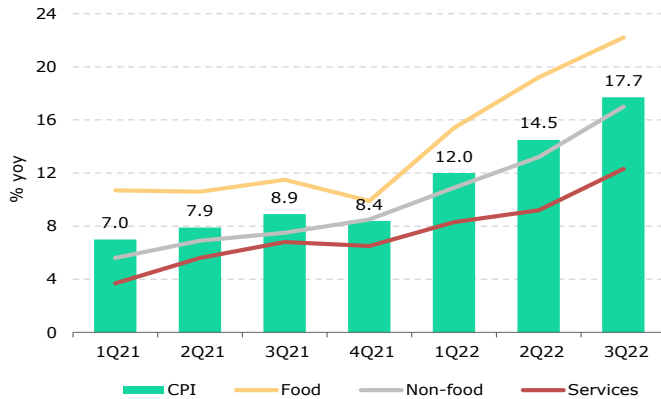
A significant increase in the cost of paid services in September was due to the hype in the housing rental market, provoked by a significant influx of citizens from the RF, as well as against the background of a seasonal increase in demand from students of outer regions. In addition, the cost of educational services and certain types of public services has risen significantly.

The double-digit growth (+18.9%) of the state budget expenditures this year, with a focus on the growth of wages of state employees (+23%), created significant inflationary pressure on the economy on the demand side. Geopolitical tensions due to conflict in Ukraine also form pro-inflationary pressures in the world and are partially transmitted to the economy of Kazakhstan. The growth rate of consumer inflation has accelerated to the maximum level since 2016 of 17.7% yoy, and there are no signs of its slowdown yet.

The situation with food prices in the world began to stabilize. According to the World Food Organization (FAO), the food price index showed a decline for 6 months in a row. As a result, food prices increased by only 5.5% yoy in September this year. Prices for such components of the index as dairy products rose by 20.7% yoy, for cereals by 11.2% yoy and meat by 7.7% yoy. Butter and sugar products have already moved into the deflationary zone, shrinking by 9.5% yoy.

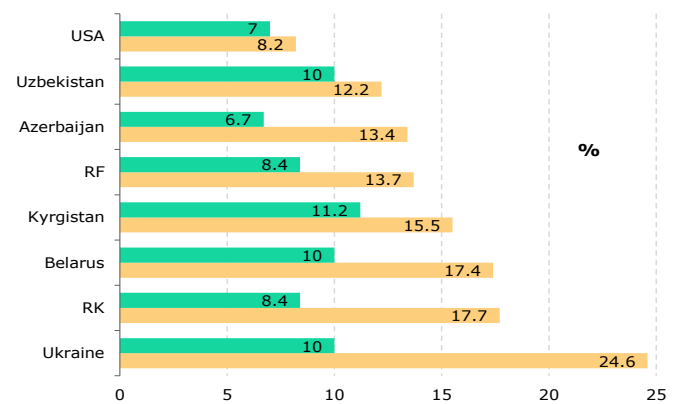
The sharp rise in prices in Kazakhstan (17.7% yoy) currently looks irrational among the countries-trading partners of the republic, while inflation rates are higher only in Ukraine (24.6% yoy). In Belarus, which is under Western sanctions, consumer inflation in September amounted to 17.4% yoy, while in Russia, having peaked in April at 17.8% yoy, it has already slowed down to 13.7% yoy. Against this background, in addition to high inflation rates, Kazakhstan is also distinguished by the depreciation of the national currency, which has weakened against the US dollar by more than 13% since the beginning of 2021, while in Uzbekistan the sum has lost only about 5% of its value, and in other CIS countries national currencies have even strengthened against the US dollar.

Fig. 9. Consumer inflation in RK



Source: BNS

Fig. 10. Inflation in RK and other countries



Source: BNS, Bloomberg

Despite the tightening of the NBK’s monetary policy, double-digit wage growth, amid persistently low unemployment and persistent external shocks, are helping to further unwind the inflationary spiral. If the current rates of consumer inflation remain unchanged, the maximum value of 2008 of 20.1% yoy can be reached already this year.

Interest policy – the base rate does not keep pace with inflation

During 3Q2022, the NBK raised the base rate only in July to 14.50%, keeping the liquidity management band symmetrical at +/-1%. The increase in the base rate took place against the backdrop of an almost doubling of inflation rates from 8.5% in January to 15% in July and 16.1% in August. At the same time, economic growth rates showed a gradual slowdown from 4.6% in 5M2022 to 3.3% in 7M2022.

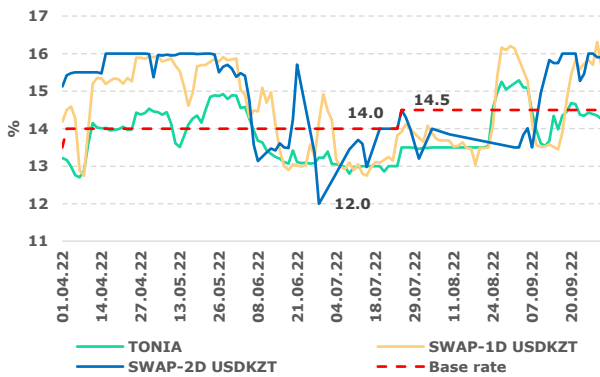
Despite the tightening of the NBK’s monetary policy in July, the pace of consumer lending remained at a high level. Thus, in 7M2022, the growth rate of consumer lending to individuals accelerated to 11.9% (18.2% yoy in 7M2021), while the growth rate in annual terms amounted to 32.5% (25.1% yoy). Along with the growth in consumer activity of households, there is an expansion in the investment activity of businesses from 1.5% yoy in 3M2022 to 2.6% in 6M2022 and 4.5% in 7M2022 a significant impetus to the expansion of aggregate demand. The increase in the cost of energy products contributed to the growth of net exports of the Republic of Kazakhstan in 6M2022 by 2.7 times to \$20.2 billion. At the same time, such macroeconomic dynamics was accompanied by a 34.3%. External shocks related to the military conflict in Ukraine, the acceleration of global inflation due to rising energy prices, and disruptions in supply chains also created a high inflationary background.

In September, the NBK decided to maintain monetary conditions in the country unchanged. The decision of the NBK to preserve the base rate was dictated by the fact that high inflation rates in the country were due to the adaptation of domestic prices to the external price shock, and the cumulative effect of the rate increase since the beginning of the year has not yet manifested itself in full. At the same time, the dynamics of the main macroeconomic indicators remained unchanged. Consumer inflation rates reached 17.7% yoy. High rates of investment activity were also observed in January-September and amounted to 7.0% yoy. Consumer lending expanded by 17.1% yoy in 9M2022 (28.3% yoy in 9M2021), while in annual terms the growth was 27.7% (32.8% yoy). The volume of net exports in Kazakhstan for 9M2022 increased by 2.3 times to \$28.4 billion due to sustained relatively high level of energy prices. At the same time, economic growth rates continued to slow down and reached 2.8% yoy in 9M2022. In 9M2022, state budget expenditures increased by 18.9% yoy. The weakening of the USDKZT pair remained at the level of 10.5% since the beginning of the year, while the weakening of the RUBKZT pair continued and for 9M2022 amounted to 44.0%. Such depreciation of the national currency against the currency of the main trading partner (36.7% in 8M2022) was translated into higher prices for non-food products (+17.0% yoy) and food products (+22.2% yoy). Thus, in 3Q2022 despite further slowdown in economic growth rates, aggregate demand, unanchored inflation expectations, the weakening of the national currency and the external inflationary background were the main factors behind further acceleration of inflation in the republic.

At the October meeting of the monetary policy committee, the NBK decided to raise the base rate to 16% while maintaining the symmetrical liquidity management corridor at the same level. The decision to significantly increase the rate was facilitated by the acceleration of inflation, which amounted to 18.8% yoy in October and exceeded the NBK’s forecast range of 16%-18% for 2022. Among the factors that influenced this decision, the NBK cited continued global price inflation pass-through, fiscal momentum, high inflationary expectations, rising production costs due to reorientation of supply chains, and continued robust domestic demand.

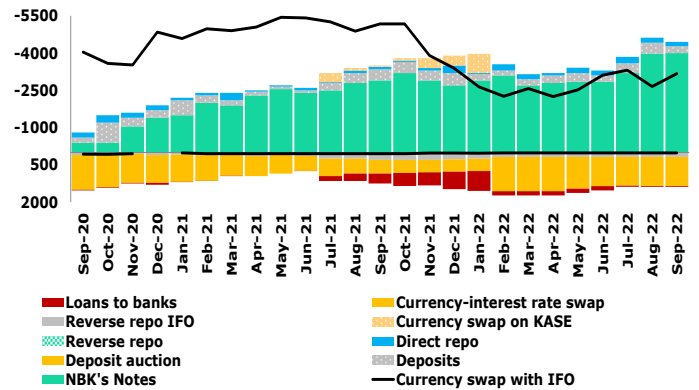
We believe that the potential for inflation growth in the republic, as well as in the world, has not yet been exhausted, and if the current external and internal macroeconomic dynamics continue, the consumer inflation rate will approach the maximum value of 20.1% yoy, which was registered in 2008. Judging by the rhetoric of NBK, the potential for raising the base rate at the next meetings of the monetary policy committee remains plausible and the regulator intends to continue tightening its policy, based on pro-inflationary risks. According to our current forecast, the dynamics of consumer inflation by the end of the year will be formed at the level of 19-20%, while the base rate will reach 16.5%-17%.

Fig 11. Money market rates, eop



Source: NBK, Halyk Finance

Fig 12. Withdrawal of excess liquidity



Source: NBK, Halyk Finance

Money Market - reducing demand

The rate on automatic REPO operations (TONIA) at the end of September 2022 was at the level of 14.7% (10.56% at the end of December 2021 and 13.4% at the end of June 2022) with an average value of 13.8% (13.9% in 2Q2022). The volume of transactions of automatic REPO in 3Q2022 decreased by 29.6% qoq (-10% yoy) and amounted to KZT31,380 bn, while the average value of daily transactions for the period amounted to KZT490.3 bn (KZT719.4 bn in 2Q2022). The maximum daily volume of transactions of automatic REPO operations fell on the last ten days of August and amounted to KZT980.1 billion.

The volume of transactions on overnight swaps on the USDKZT pair in 3Q2022 decreased by 38.1% qoq to KZT4 560.6 bn. At the end of 3Q2022, the overnight swap rate stood at 15.8% (14.5% at the end of 1Q2022) with an average rate of 14.1% (14.9% in 2Q22). The maximum volume of transactions of overnight swaps occurred at the end of August 2022 and amounted to KZT179.3 bn with an average quarterly value of KZT74.8 bn (average quarterly nominal value of transactions of KZT122.8 bn in 2Q2022). The volume of transactions of two-day swaps on the USDKZT pair in 3Q2022 decreased by 90.5% to T296.7 billion. As of the end of 3Q2022, the USDKZT two-day swap rate stood at 16% (15.7% at the end of 2Q2022) with a quarterly average of 14.2% (15.3% in 2Q2022). The maximum volume of two-day swaps fell on July 1 and amounted to T42 bn with an average quarterly value of T10.2 bn (an average quarterly value of the nominal volume of transactions was T54.6 bn in 2Q2022).

In 3Q2022, there was a decrease in the amount of withdrawn liquidity via NBK notes (54.3% in the structure of withdrawal instruments) by 4.1% qoq (-62.8% yoy) to KZT1,722 bn. September 2022 was at the level of 15.5% (9.96% in December 2021 and 13.7% in June 2022). The effective rate of NBK notes in September 2022 amounted to 14.5% with the placement volume of KZT1,722 bn versus the rate of 14.9% and the initial placement volume of KZT1,711.3bn in June this year. In general, the volume of excess liquidity in the system increased by 2.0% qoq (-38.7% yoy) and at the end of September amounted to KZT3,173 bn.

The decrease in money market transactions in 3Q2022 was accompanied by an increase in the money supply (M3) by 6.8% qoq and by 7.9% yoy, while in annual terms the money supply increased by 12.6% yoy and amounted to T32.5 trillion. Money supply growth slowed down compared to 13.4% in 9M2020 (+18.9% yoy) and 15.8% in 9M2021 (+19.3% yoy), but remains relatively high. Against the backdrop of a rise in the price of money in the republic (the base rate since the beginning of the year increased from 9.75% since the beginning of the year to 14.50% as of the end of September), quantitative easing is taking place through the expansion of the money supply. This expansion is supported by an increase in state budget expenditures (18.9% in 9M2022), i.e. "budget emission" reduces the effectiveness of the NBK's monetary policy.

In 3Q2022, the money market rate (13.8% average for 3Q2022) formed near the lower limit of the NBK liquidity management interest rate band of 13.5%, while the FX swap rate stood at 14.1%. Against the backdrop of a

slowdown in economic growth, relative stability of the national currency exchange rate during 3Q2022, and tighter monetary policy, the demand for liquidity in the money market declined over 3Q2022.

Exchange rate - weakening will continue

As of the end of September, the exchange rate of the national currency depreciated by 10.5% since the beginning of the year and amounted to 476.9 tenge per US dollar (depreciation by 12.0% yoy, 2.5% qoq). In 3Q2022, the exchange rate of the national currency at the moment reached 484.2 tenge, with an average value of 475.3 per US dollar. The weakening of the national currency took place against the backdrop of an adjustment in the cost of oil and an increase in the US dollar. Thus, the price of oil corrected by 12% qoq and amounted to \$88 per barrel, with an average value of \$99.2 per barrel (\$99 per barrel in 1Q2022, \$112.7 in 2Q2022). At the same time, the inflow of foreign currency via the current account amounted to \$7.9 bn, but was offset by the outflow from the financial account in the amount of \$9 bn. Thus, the total capital outflow for 9M2022 amounted to \$1.1 bn, which could not but affect the national currency exchange rate.

The US dollar exchange rate (DXY index) has increased since June 2022 by 7.1% qoq (+17.2% YTD and 19% yoy) to 112.1. The highest rate of USD occurred at the end of September and reached 114.1 (maximum value since March 2002). This strengthening of the main reserve currency indirectly affected the depreciation of the tenge against the US dollar. According to the Bloomberg consensus forecast, the DXY rate in 2023 will be at the level of 106, which will correspond to the maximum values since 2002. Given the growing geopolitical tensions in Ukraine, Armenia, the Middle East, North Korea and around Taiwan, high rates of inflation of production costs, as well as tightening of monetary policy in the largest economies of the world against the backdrop of a slowdown in their growth rates, the value of the US currency will remain at a relatively high level this year and next.

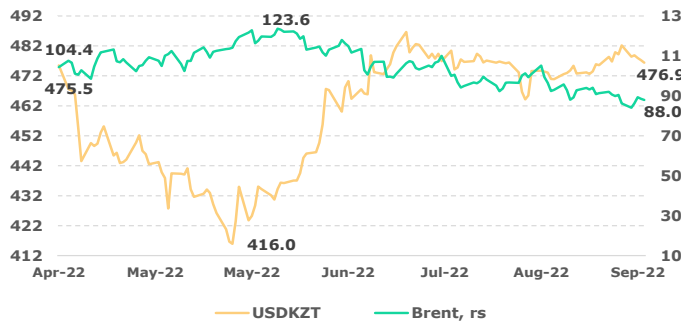
The volume of foreign exchange operations of the NBK for the NF in 3Q2022 increased by 12.1% qoq to \$684 million (-76.1% yoy). It should be noted that in August of the current year no foreign exchange operations were carried out for the NF. This happened against the backdrop of outstripping growth of state budget revenues by 31.1% yoy in 9M2022, while expenditures grew by 18.9% yoy. At the same time, there was a decrease in the budget deficit by almost 2.7 times to T602.9 bn. The NBK will carry out currency exchange operations in the amount of about KZT929.5 bn (about \$2 bn at an average forecast rate of 462.1 tenge per US dollar).

In the foreign exchange market in the segment of exchange trading for the USDKZT pair in 3Q2022, there was an increase in foreign exchange transactions by 4.7% qoq to \$6.5 billion (-24.4% yoy). The minimum volume of foreign exchange transactions on KASE fell in September and amounted to KZT1,999 million. The volume of purchases of US dollars in exchange offices for 3Q2022 decreased by 22% qoq to T343.8 billion (\$723 million at an average exchange rate of 475.2 tenge per US dollar). In 9M2022 the volume of purchases of US dollars increased by 4.4% yoy and amounted to T1,226.3 bn (\$2,675 mn).

Against the background of tightening the monetary policy of the US Federal Reserve and the ECB, there is a decrease in the interest of foreign investors in government securities of emerging markets and, as a result, there is an outflow of foreign currency. Thus, the volume of government securities owned by non-residents decreased by 20.6% qoq compared to 2Q2022 to T379.3 bn (-36.3% YTD, -51.9% yoy). A decrease in the amount of non-residents' holding of the state debt of the Republic of Kazakhstan will also be observed in 4Q2022. This, in turn, will not support the exchange rate of the Kazakhstani tenge.

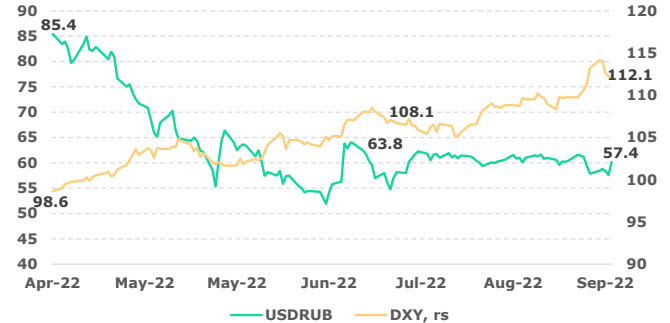
As of the end of September, the Russian ruble appreciated by 23.6% since the beginning of the year and amounted to 57.4 rubles per US dollar. The strengthening of the Russian ruble took place against the backdrop of an increase in the current account surplus to \$198.4 bn (\$75.2 bn in 9M2021). The expansion of the current account surplus of the Russian Federation in 9M2022 was facilitated by the growth of the surplus in the goods and services account to \$238 bn (\$107.9 bn in 9M2021). The increase in the cost of the main range of Russian exports (oil, gas, metals, etc.) against the backdrop of sanctions restrictions on imports led to the fact that Russian exports of goods and services in 9M2022 increased by 27.6% yoy, while imports decreased to 9.6% yoy for the same period. The financial account, including CBR reserve assets, saw a capital outflow of \$195.2bn (\$74.5bn in 9M2021). According to independent analysts, the outflow of capital from the RF in 2022 will exceed \$200 billion (estimated by the Central Bank at \$246 billion), provided that the relatively free movement of capital remains intact. Recall that the countries of the main trading partners from December 5, 2022 will impose sanctions against oil and oil products supplied by the RF by sea. The sanctions of the 8th EU package imply the introduction of a price ceiling for crude oil (from December 5, 2022) and petroleum products (from February 5, 2023). The Bloomberg consensus forecast for the Russian currency at the end of 2022 is 62 (median), with an average of 64 in 4Q2022. Analysts polled by the agency believe that the Russian ruble in 2023 will weaken to 80 per US dollar.

Fig 13. USDKZT vs Brent



Source: NBK, Bloomberg, Halyk Finance

Fig 14. USDRUB and USD index



Source: NBK Bloomberg, CBR, Halyk Finance

We believe that capital inflows from the current account in Kazakhstan will continue in 4Q2022 and, as of the end of 2022, will be at the level of about 4.2% of GDP (in 9M2022, the account surplus amounted to 3.9% of GDP). Current account capital inflows and NBK foreign exchange operations for the NF of \$2 bn will also support the Kazakhstan tenge. The outflow of capital from emerging markets, the slowdown in economic growth in the countries of trading partners, the strengthening of the US dollar will put pressure on the tenge towards weakening. Based on the emerging external macroeconomic dynamics, the exchange rate of the national currency will be at the level of 480 per US dollar by the end of this year.

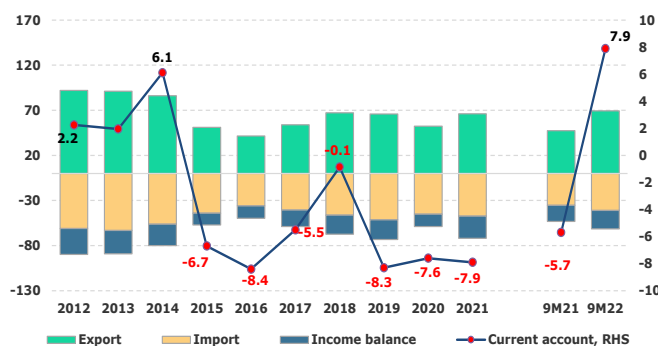
The current account for 9M2022 developed with a significant surplus

According to the preliminary NBK data, the current account of the Republic of Kazakhstan for 9M2022 developed with a surplus of \$7.9 bn (deficit of \$5.6 bn for 9M2021). The current account surplus in 9M2022 was driven by a 2.2x expansion in the trading account surplus to \$29.3 bn, a reduction in the services account deficit by 27.9% yoy to \$893 mn, and a decrease in the deficit in the secondary income account by 44.9% yoy to \$295 mn. At the same time, only the growth of the primary income account deficit by 16.8% yoy to \$20.2 bn had a restraining effect on further expansion of the current account surplus.

The increase in the trade account surplus to \$29.3 bn was driven by outpacing export dynamics by 47.9% yoy to \$64.0 bn over imports, which increased by 16.4% yoy to \$34.6 bn in 9M2022. Such foreign trade dynamics was last observed in 2013-2014, when export earnings for the same period amounted to \$62-63 bn, while imports reached \$31-\$35.7 bn. Brent oil price at \$103.7 per barrel on average for 9M2022 (\$67.4 bbl on average for 9M2021) contributed to the multiple growth of Kazakhstan's export earnings in the period. Recall that at the moment its price reached \$127.9 per barrel.

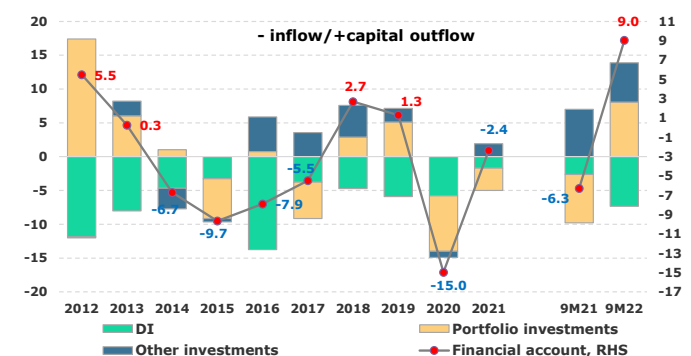
The deepening of the deficit of primary income received by non-residents from direct investments in 9M2022 by 18.8% yoy to \$19.0 bn (net) led to the expansion of the deficit in the balance of primary income by 16.8% to \$20.2 bn. Income on NBK reserves and assets increased by 15.6% to \$825 million in the period.

Fig. 15. Growth of current account surplus, \$ bn



Source: NBK, Halyk Finance

Fig. 16. Capital outflow of financial account, \$ bn



Source: NBK, Halyk Finance

The reduction in the deficit in the services account to \$893 million was due to outpacing growth in exports of services at the level of 29.7% yoy to \$5.5 billion compared to the growth rate of imports of services by 16.7% yoy to \$6.4 billion.

Financial account (excluding reserve assets of the NBK)

The financial account for 9M2022 saw a capital outflow of \$9.0 bn (an inflow of \$6.3 bn for 9M2021). Capital outflow for 9M2022 was recorded for portfolio investments in the amount of \$8.1 bn (\$7.2 bn inflow for 9M2021). Other short-term capital flows saw an outflow of \$7.9 bn (outflow of \$7.1 bn in 9M2021). Under medium-term and long-term investments, there was an outflow of \$444 mn compared to an inflow of \$3.5 bn in 9M2021. Capital inflows within the financial account were recorded for direct investments of \$7.3 bn (inflow of \$2.6 bn in 9M2021).

Consolidated international reserves - another contraction

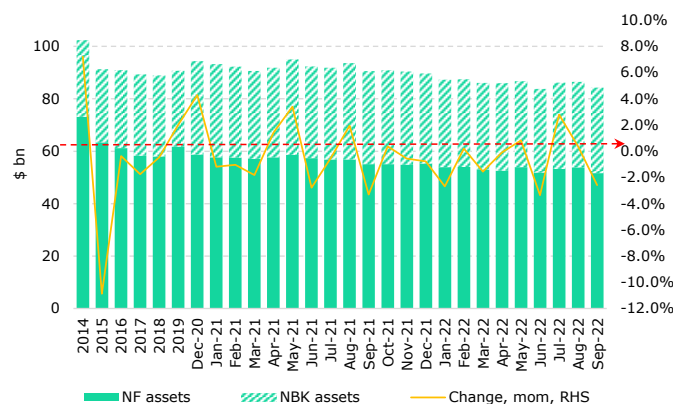
In the middle of the current year, the volume of consolidated international reserves (CIR) reached its lowest level since August 2012 and amounted to \$83.8 billion. In June and August, there was an increase of CIR to \$86.2 billion and \$86.5 billion, respectively. However, in September 2022, CIR decreased by 6.1% YTD and amounted to \$84.2 billion (-7.0% yoy).

Contraction of CIR occurred both due to a reduction in the nominal volume of the NBK’s gross gold reserves by 5.1% YTD to \$32.6 bn (-8.1% yoy), and due to a reduction in the National Fund’s assets by 6.7% YTD to \$51.6 bn (-6.3% yoy). Quarterly dynamics of CIR was multidirectional. Thus, the NBK’s gold reserves increased by 2.1% qoq, while the assets of the NF RK decreased by 0.5% qoq.

As part of NBK reserves, assets in hard currency grew by 26.6% qoq to \$12.1 bn (-9.6% yoy). According to NBK data for 3Q2022, in the structure of foreign exchange reserves, there was an increase of assets held in securities by 12.3% qoq to \$5.4 bn (-1.8% yoy). Assets and deposits in hard currency increased by 85.3% qoq (-19.5% yoy) and amounted to \$4.3 bn.

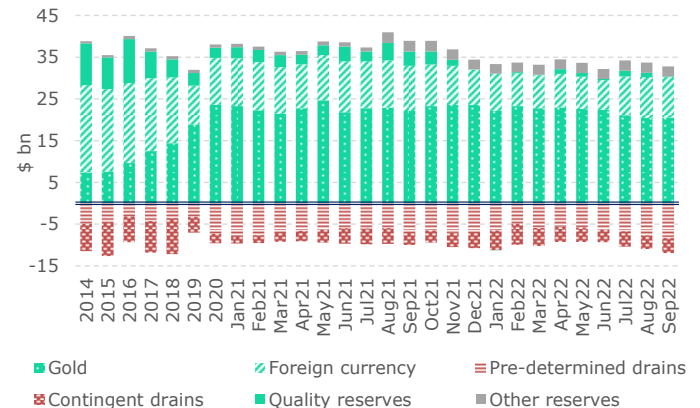
The NBK’s gold holdings shrank by 8.4% qoq (-12.9% YTD), down 7.2% yoy to \$20.5 bn. The decrease in gold reserves in gold was facilitated by a decline in its value by 9.2% since the beginning of the year to \$1,661 per troy ounce on global markets. In addition, since the beginning of the year, there has been a decrease of this asset in physical terms.

Fig 17. Consolidated reserves of Kazakhstan



Source: NBK, Halyk Finance

Fig 18. International reserves of NBK



Source: IMF, Halyk Finance

Thus, in December 2021, the physical volume of NBK gold amounted to 12.94 (402.5 tons) million troy ounces, and as of the end of September, its volume decreased by 5.2% since the beginning of the year to 12.27 (381.6 tons) million troy ounces. Such changes led to the fact that the share of NBK assets in gold at the end of September 2022 amounted to 62.9% (the lowest figure in the last 15 months), having decreased from 68.5% since the beginning of the year.

© 2022 Halyk Finance, a subsidiary of Halyk Bank.

For contact details see the information on Halyk Finance website www.halykfinance.kz or contact Halyk Finance office. All rights reserved. This document and/or information has been prepared by and, except as otherwise specified herein, is communicated by Halyk Finance. This document is for information purposes only. Opinions and views expressed in this document do not necessarily represent the opinions and views held by Halyk Finance, or other subsidiaries of Halyk Bank. The differences of opinion stem from different assumptions, sources information, criteria and methodology of valuation. Information and opinions expressed herein are subject to change without notice; and neither Halyk Finance, or Halyk Bank, or any of its subsidiaries or affiliates are under any obligation to keep them current. This document is not an offer or an invitation to engage in investment activity. It cannot be relied upon as a representation that any particular transaction necessarily could have been or can be effected at the stated price. This document does not constitute an advertisement or an offer of securities, or related financial instruments. Descriptions of any company or companies or their securities or the markets or developments mentioned herein are not intended to be complete. Views and opinions expressed in this document cannot substitute for the exercise of own judgment and do not attempt to meet the specific investment objectives, financial situation or particular needs of any specific investor. The information and opinions herein have been arrived at based on information obtained from sources believed to be reliable and in good faith. Such sources have not been independently verified; information is provided on the basis and no representation or warranty, either expressed or implied, is provided in relation to the accuracy, completeness, reliability, merchantability or fitness for a particular purpose of such information and opinions, except with respect to information concerning Halyk Finance and its affiliates. The securities described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. Options, derivative products and futures are not suitable for all investors and trading in these instruments is considered risky. Past performance is not necessarily indicative of future results. Foreign-currency denominated securities are subject to fluctuations in exchange rates that could have an adverse effect on the value or the price of, or income derived from, the investment. Halyk Finance and its affiliates, directors, representatives, employees, or clients may have or have had interests in issuers described herein. Halyk Finance may have or have had long or short positions in any of the securities or other financial instruments mentioned herein at any time and may make a purchase and/or sale, or offer to make a purchase and/or sale, of any such securities or other financial instruments at any time, as principal or agent. Halyk Finance and its affiliates may act or may have acted as market maker in the securities or other financial instruments described herein, or in securities underlying or related to such securities. Employees of Halyk Finance or its affiliates may serve or have served as officers or directors of the said companies. Halyk Finance and its affiliates may have or have had a relationship with or have provided investment banking, capital markets, advisory, investment management, and/or other financial services to the relevant companies. Halyk Finance relies on information barriers to avoid the appearance of conflict of interests within Halyk Finance or in its relations with clients, other issuers, and external investors.

The information herein is not intended for distribution to the public and may not be reproduced, redistributed or published, in whole or in part, for any purpose without the written permission of Halyk Finance. Neither Halyk Finance nor any of its affiliates accepts any liability whatsoever for the actions of third parties in this respect. This information may not be used to create any financial instruments or products or any indices. Neither Halyk Finance, nor its affiliates, nor their directors, representatives, or employees accept any liability for any direct or consequential loss or damage arising out of the use of any information herein.

© 2022, All rights reserved

Contacts:

Research department mail to: research@halykfinance.kz

Sales department mail to: sales@halykfinance.kz

Address:

Halyk Finance
Abay av., 109 «B», 5th fl
A05A1B4, Almaty, Kazakhstan
Contact. +7 727 357 59 77
www.halykfinance.kz

Bloomberg

HLFN

Refinitiv

Halyk Finance

Factset

Halyk Finance

Capital IQ

Halyk Finance