International Monetary Fund

IMF Executive Board Concludes 2012 Article IV Consultation with the Republic of Kazakhstan

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On June 18, 2012, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with the Republic of Kazakhstan.

Background

Real GDP growth reached 7½ percent in 2011. While growth of oil production slowed, high commodity prices helped spur domestic demand and activity in transport and communications. Agriculture recovered from a severe drought, but activity in construction and real estate remained flat. Official unemployment rate, at 5¼ percent, continued to be unaffected by real growth, as was the case at the time of the slowdown.

Driven by rising global food prices and large increases in public sector wages, inflation peaked at 9 percent in mid-2011, exceeding the official objective range of 6–8 percent. More recently, however, slowing international commodity prices, an exceptionally high harvest, and the use of administrative measures to limit food and fuel price increases helped to bring inflation below 5 percent. Core inflation, which excludes energy and food, remains subdued.

The current account surplus rose to 7½ percent of GDP, the highest level in recent years, as robust exports outpaced the demand–driven rebound in imports. Assets in the National Fund (NFRK) rose rapidly, and together with National Bank of Kazakhstan’s (NBK) international reserves, reached a comfortable level equivalent to 17 months of imports and 110 percent of broad money.

Fiscal and monetary policies have adapted to the economic recovery. An expansion of nonoil revenues from improved tax collection combined with a small decrease in the expenditure-to-GDP ratio resulted in a decline in the nonoil fiscal deficit. Key monetary indicators continued to grow at a slower rate than nominal GDP, and as inflation pressures subsided, the NBK signaled a more accommodative monetary policy stance, cutting its policy rate by 100 bps in early 2012. The tenge has started to show more flexibility, with the NBK intervening on both sides of the market to avoid undue exchange rate volatility in either direction.

The banking sector has still not fully recovered from the severe shock in 2007. Foreign liabilities have fallen drastically, aggregate liquidity is ample, and provisioning of overdue loans is still relatively high. Nevertheless, domestic banks′ burden of nonperforming loans has further increased, and BTA bank has embarked on a second debt restructuring with external creditors. So far, economic growth and government ad-hoc support to distressed borrowers in the construction, real estate and Small and medium enterprise (SME) sectors have not improved the quality of the loan portfolio, as activity in construction and real estate, the sectors subject to highest bank exposure, remains flat.

Executive Board Assessment

Executive Directors commended the authorities′ policies which, together with high commodity prices, yielded a strong economic recovery and helped rebuild external buffers. The authorities have appropriately responded to the upswing in the cycle by gradually tightening fiscal policy, sterilizing excess bank liquidity, and allowing greater exchange rate flexibility. Directors noted that the growth outlook is positive, but subject to downside risks. They called on the authorities to address vulnerabilities in the banking sector posed by the deterioration of asset quality, and further strengthen the macroeconomic framework.

Directors appreciated the preparation of plans to deal with a possible protracted global slowdown and a decline in oil prices. They stressed that achieving the nonoil medium-term deficit target remains a priority and spending plans should not unduly stimulate demand in the absence of a shock. They encouraged the central bank to closely monitor inflation, and to stand ready to tighten monetary policy if domestic demand picks up.

Directors underscored the need to address the continued rise in bank troubled assets, which presents a public sector contingent liability. They stressed that restoring banks′ health would support growth and economic diversification. Envisaged regulatory improvements should be complemented with strict enforcement to provide an incentive for banks to clean up their balance sheets. Directors noted that the new mechanism to manage troubled assets represents only a partial solution. A successful strategy would require action by the central bank to enforce realistic asset valuation and loss recognition, ensure adequate provisioning, replenish bank capital where needed, and close unviable banks. To mitigate further risks, a quick and definitive solution to the difficulties of BTA bank is a crucial priority. Directors welcomed the plan to adopt Basel III standards by year-end.

Directors considered that macroeconomic policymaking would benefit from improved medium-term frameworks and policy coordination. In the fiscal area, this would require broadening the tax base and fully integrating the oil fund and state entities' accounts into the fiscal framework. In the monetary sector, strengthening the transmission mechanism by deepening financial markets would allow the gradual unwinding of administrative price controls. Greater exchange rate flexibility would facilitate monetary management and the economy's response to external shocks. A well-capitalized and well-regulated financial system would be important to support these reforms.

Directors welcomed the authorities' ambitious plans to promote growth in the non-oil sector. The envisaged job-creating government investments, partly financed by oil savings, will however need to be complemented by enhanced private sector participation. Directors therefore called for sustained efforts to improve the business environment through strengthened governance and institutions and integrate Kazakhstan into the global economy. Along with improvements in the coverage of the social safety net, these reforms would promote greater social inclusiveness and help ensure that the oil wealth benefits the population as a whole.

Kazakhstan: Selected Economic Indicators, 2009–13

				Proj. 1/	Proj. 1/
	2009	2010	2011	2012	2013
	(Changes in percent)				
Real economy					
Real GDP	1.2	7.3	7.5	5.9	6.0
CPI (end-of-period)	6.2	7.8	7.4	6.6	6.8
	(In percent of GDP)				
Public finance					
Government revenue and grants	22.1	23.9	27.5	27.1	26.7
Government expenditures	23.4	22.0	21.5	21.7	21.7
General government balance 2/	-1.4	1.4	5.5	4.9	4.5
General government non-oil balance	-10.6	-10.3	-9.3	-9.7	-9.4
General government debt (end-of-period) 3/	10.2	10.7	10.5	9.9	8.7

	(Changes in percent)				
Money and credit 4/					
Base money	60.7	5.0	10.2	16.7	14.5
Broad money	17.9	15.7	14.1	15.4	15.5
Credit to the economy 5/	7.2	0.9	14.9	15.5	15.2
NBK refinance rate (eop; percent)	7.0	7.0	7.5	…	…
	(In percent of GDP)				
Balance of payments 6/					
Trade balance	13.0	19.4	25.4	26.1	23.3
Current account balance	-3.6	1.6	7.6	7.1	5.3
External debt	97.9	79.9	66.6	65.2	62.3
Excluding intra-company loans	54.8	44.5	34.4	31.8	28.4
Gross international reserves					
In billions of U.S. dollars, end of period	23.1	28.3	29.3	35.3	38.4
In months of next year's imports of goods	6.3	6.5	6.1	6.9	7.0
and nonfactor services					
	(Changes in percent)				
Exchange rate 7/					
Tenge vs. U.S. dollar (end of period)	-22.9	0.7	-0.4	…	…
Tenge vs. Russian ruble (end of period)	-19.4	1.4	4.7	…	…
Tenge vs. Euro (end of period)	-24.5	8.3	2.0	…	…
Real effective exchange rate (p.a) 8/	-6.7	3.3	-0.6	…	…

Source: Kazakhstan authorities and IMF staff estimates and projections.

1/ Staff projections.

2/ Privatization revenues are treated as a financing item.

3/ Gross domestic and external government debt, including government guaranteed debt.

4/ Reflects data available at the time of the mission.

5/ Source: Monetary survey of the banking system.

6/ The GDP in US. Dollar is calculated using the period average exchange rate average.

7/ A positive sign indicates appreciation.

8/ National Bank of Kazakhstan estimates.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

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