ANNUAL REPORT
OF THE NATIONAL BANK OF THE REPUBLIC OF KAZAKHSTAN
FOR 2004

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List of Abbreviations Used

President of the Republic of Kazakhstan	President
National Bank of the Republic of Kazakhstan	National Bank
Agency for the Regulation and Supervision of the Financial Market and Financial	Agency for the Regulation and Supervision of the Financial Market and Financial
National Fund of the Republic of Kazakhstan	National Fund
Government of the Republic of Kazakhstan	Government
Ministry of Finance of the Republic of Kazakhstan	Ministry of Finance
Ministry of Justice of the Republic of Kazakhstan	Ministry of Justice
Agency to Combat Economic Crime and Corruption of the Republic of Kazakhstan	Agency to Combat Economic Crime and Corruption
Agency for Civil Service Affairs of the Republic of Kazakhstan	Agency for Civil Service Affairs
Commonwealth of Independent States	CIS
Eurasian Economic Community	EurAsEC
Common Economic Space	CES

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INTRODUCTION

Kazakhstan's economy continued its dynamic development in 2004, which was due to a great extent both to progress in the reforms that are being implemented and favorable conditions in the global economy.

In 2004 significant results were also achieved in the development of the country's financial sector. At the beginning of the year all regulatory and supervisory functions in the financial market were shifted from the National Bank to the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions.

The separation of regulatory and supervisory functions was dictated by the special status of the National Bank, which is the only central bank in the CIS whose operations are concentrated entirely on the performance of functions that are typically the responsibility of a traditional central bank.

The new realities led to a shift in the emphasis of the National Bank's policies. As of January 1, 2004 the main goal of the National Bank became ensuring price stability, and to achieve this the National Bank continued its performance of the following tasks:

1) developing and implementing the state's monetary policy;
2) ensuring the functioning of payment systems;
3) performing foreign exchange regulation and foreign exchange control;
4) assisting in ensuring the stability of the financial system.

Within the framework of the monetary policy being carried out by the National Bank, special attention was given to maintaining a low inflation rate. With regard to exchange rate policy, the floating exchange rate regime for the tenge, in which fluctuations in the exchange rate depend on supply and demand, was kept in place, and this helped maintain the price competitiveness of Kazakhstani goods in foreign markets and increase the country's integration into the global economic space.

In this connection, the improvement in the world economy, which grew by 4.6 percent in 2004, was a factor of considerable importance that helped reinforce the positive trends in Kazakhstan's economy.

In 2004 the United States posted economic growth of 4.6 percent, countries in the euro area recorded growth of 1.8 percent, and after a prolonged recession, Japan's economy grew by 2.1 percent. Growth in corporate profits among companies and fluctuations in oil prices were the main factors affecting world equity markets.

In 2004 world prices for crude oil reached record levels. According to World Bank data, the average spot price for crude oil in August was US$42.1 per barrel, which was the highest price ever posted in the entire history of the publication of oil price quotations.

Overall, in 2004 the average world prices for crude oil were 25.6 percent higher than in 2003.

Favorable economic conditions also contributed to a considerable stabilization of the economic situation in all of the CIS countries in 2004. The growth rates for the main macroeconomic indicators were relatively high. For example, according to estimates, average growth in GDP among Commonwealth countries in 2004 was 8 percent (the figure for 2003 was 8 percent), growth in industrial output was 7 percent (8 percent), retail trade grew by 13 percent (10 percent), and investments in fixed capital were up 14 percent (16 percent).

The improvement in the macroeconomic situation in the majority of CIS countries, as well as political and financial stability in Kazakhstan, helped to reinforce the economic growth trends in the Republic that have been seen for five years running now. The aggregate growth in GDP over the past five years is around 52 percent, which has enabled Kazakhstan to become one of the world leaders in terms of economic development.

The decisions by Standard & Poor's in May 2004 and Fitch Ratings in 2004 to assign Kazakhstan an investment rating (following the Moody's Investor Services rating agency in September 2002) served as recognition of the improvement in Kazakhstan's economic situation. In addition, in July 2004 the Moody's rating agency upgraded its projection based on Kazakhstan's ratings from "stable" to "positive."

Furthermore, the Organization for Economic Cooperation and Development upgraded its rating of the Republic from level 5 to level 4, which serves as confirmation of the progress that the country has made in reforming the economy, the positive changes in various sectors of the economy, improvement in the investment climate, and also the enhancement of the country's business reputation in the world arena. This rating indicator is taken into account by export-import banks and export credit insurance agencies of economically developed countries when considering whether to provide support for projects in these countries.

I. ECONOMIC DEVELOPMENT

1.1. The Real Sector of the Economy[1]

According to current data, in 2004 ***gross domestic product (GDP)*** totaled 5,542.5 billion tenge in current prices. Real GDP grew by 9.4 percent compared to 2003. These indicators are significantly higher than the projected GDP estimates provided as part of the Medium-Term Plan for Socio-Economic Development for 2004–2006 (projected GDP was 4,877 billion tenge, with real growth of 7 percent).

The growth in GDP was due to an increase in real production output in all sectors of the economy: 10 percent in industry, 0.1 percent in agriculture, 11.2 percent in construction, 12.2 percent in transportation and communication services, and 10.4 percent in trade and other services.

The production of goods accounted for 45 percent of GDP, while services accounted for 50.6 percent.

Industrial output in 2004 increased by 10.1 percent compared to 2003, with an increase of 12.7 percent in the mining and extraction industry, 8.9 percent in manufacturing, and 3.5 percent in the production and distribution of electricity, gas, and water (Appendix 1 to Section I, Subsection 1.1, Figure 1.1.1). The mining and extraction industry accounted for a larger proportion of industrial output (52.5 percent) than manufacturing (40.4 percent). The increase in world oil prices had an impact on the high rates of growth in the mining and extraction industry. An expansion in investments and consumer demand stimulated the development of manufacturing sectors.

The increase in production output in the mining and extraction industry in 2004 was due to growth in the extraction of natural gas by 25.3 percent, in crude oil and casinghead gas by 13.4 percent, iron ore by 6.3 percent, and coal and lignite by 2.3 percent.

The metallurgical industry and the production of finished metal products account for more than 40 percent of manufacturing output, and the production of foodstuffs, including beverages and tobacco, accounts for more than one-fourth.

In 2004 gross production output in agricultural totaled 693.3 billion tenge, which is 0.1 percent more than in 2003; the output of animal husbandry products increased by 5.3 percent (in connection with a rise in the number of livestock and poultry and their productivity), while crop production fell by 2.5 percent (as a consequence of a decline in the yield of all grain and legume crops compared to 2003 due to summer drought conditions in the northern regions of the country).

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[1] based on data from the Republic of Kazakhstan Statistics Agency

Investment activity on the part of domestic and foreign capital contributed a great deal to the country's economic growth. The implementation of large-scale investment projects with the participation of foreign investors in the oil extraction industry, further implementation of measures within the framework of the Strategy for the Republic of Kazakhstan's Industrial and Innovation Development for 2003–2015, as well as the implementation of a number of industry programs, allowed to maintain the investment in the economy at a high level. Throughout 2004 as a whole investments in fixed capital increased by 10.6 percent to 1,530.6 billion tenge. The main sources of investments in fixed capital were economic entities' equities (65.2 percent) and foreign investments (22.6 percent), while budget funds accounted for 12.2 percent. Priority sectors for investment are oil and natural gas extraction (accounting for 35.3 percent), real estate transactions (18.5 percent), transportation and communications (15.2 percent), and manufacturing (9.8 percent). The proportion of foreign investments earmarked for the establishment of fixed assets at enterprises in the mining and extraction industry fell (from 74 percent to 54.7 percent).

Under the conditions of growth in industrial output, the volume of freight shipments increased by 9.0 percent to 1,840.0 million tons of freight. The volume of services provided by communications enterprises grew in 2004 by 32.0 percent, with an increase of 21.1 percent in services provided to the public, totaling 150.8 billion tenge and 51.1 billion tenge, respectively.

The economically active population aged 15 years or older in 2004 (according to preliminary data) totaled 7.8 million, which is 166,000, or 2.2 percent, more than in the previous year. The number of people employed in the economy in 2004 increased by 2.6 percent to 7.2 million. The number of unemployed people in 2004 compared to 2003 fell by 2.2 percent to 657,400. The unemployment rate was 8.4 percent, and the number of registered unemployed people as a proportion of the economically active population was 1.5 percent.

In 2004 the ***average monthly nominal wage*** throughout the economy as a whole (according to preliminary data) was 28,270 tenge and rose by 21.7 percent compared to the previous year, and by 13.9 percent in real terms (Appendix 1 to Section I, Subsection 1.1, Figure 1.1.2). The growth in wages was due to an increase in economic activity in the country resulting from strong economic growth, as well as the social policy being pursued by the state, under which a pay raise was provided for employees in the budget sphere and for civil service employees. The increase in labor compensation for hired workers in 2004 relative to the previous year was observed for all types of economic activity. Wages at enterprises in industry, trade, transportation, and communications rose by 19–21 percent; wages in health care, education, and health rose by 23–25 percent; and wages for civil servants rose by 44 percent.

The population's average per capita nominal money income in December 2004 was equal to 14,876 tenge, which is 20.6 percent higher than in December of the previous year. Real money income during this same period grew by 13.2 percent. The average per capita subsistence minimum rose by 7.4 percent, and was equal to 5,640 tenge in December 2004.

Throughout the Republic as a whole the population's nominal money income in 2004 exceeded the subsistence minimum by a factor of 2.3.

1.2. Monitoring of Enterprises in the Real Sector of the Economy

In 2004 the number of enterprises participating in monitoring increased from 1,176 to 1,302, including an increase from 938 to 1,015 for medium-sized and large enterprises. Income earned from product sales by monitoring participants as a proportion of total income from product sales among all enterprises in the economy increased from 57.8 percent in the fourth quarter of 2003 to 66 percent in the fourth quarter of 2004.

Efforts to improve the organizational and information-methodological support for the monitoring system continued in the following areas.

First, improvements were made in the survey indicators and questionnaires with the aim of making it easier for enterprises to fill them out and focusing primarily on the impact of the banking system on the country's economy. In this connection, questions were included in the questionnaires to assess the nature and intensity of a change in indicators such as:

- the enterprise's need for bank credits and services and the extent to which it is fulfilled;

- the enterprise's debt on bank credit;

- the size of the enterprise's bank deposit;

- the structure of sources of financing for investments and replenishment of the enterprise's working capital;

- the impact on the enterprise's economic activity of the tenge's exchange rate against the U.S. dollar, the euro, and the Russian ruble, and its anticipated level over the short term;

- the demand and prices for enterprises' finished products, raw materials consumed.

Second, on the basis of the updated system of survey questions, there has been an improvement in the analytical survey of the arising economic situation and the main trends in the real sector based on the results of enterprise monitoring, which is presented to the central and regional governments.

Third, with a view to increasing enterprises' interest in regular participation in National Bank monitoring and providing for a more representative sample of enterprises, work has been done to improve the information sent by the National Bank to the monitoring participants, namely quarterly forms for sectoral compilation of the most significant financial and economic indicators for the enterprise.

Fourth, organizational and methodological work has been undertaken to apply the results of enterprise monitoring (pertaining to the evaluation of financial stability and creditworthiness) for purposes of second-tier bank refinancing under a bill of exchange program to establish a market for the liabilities of first-class issuers in the real sector of the economy.

The results of quarterly enterprise surveys throughout the year allow one to draw the following conclusions about the arising economic situation and the main trends in the real sector of the economy.

The management conditions at enterprises remain positive. The majority of enterprises either experienced no negative effect or experienced a positive effect on economic activity in connection with the current change in the tenge’s exchange rate against the euro (68.9 percent of the enterprises surveyed in the fourth quarter of 2004), the Russian ruble (71.4 percent), and the U.S. dollar (69.6 percent). In addition, in the first quarter of 2005 the bulk of the enterprises surveyed expect a stabilization of the tenge’s exchange rate against those currencies.

The conditions of lending to enterprises continued to improve. In the fourth quarter of 2004 almost one-third (30.9 percent) of the enterprises surveyed used credits to finance their operations. Above all, these are enterprises in industry, construction, and trade. The continuing trend toward a shrinking of the gap between the actual interest rate and a level acceptable for enterprises points to greater interest on the part of enterprises in using credits. In addition, given active borrowing by second-tier banks in foreign markets, the gap between the actual rate and the acceptable level is shrinking the most with respect to credits in foreign currency.

The overwhelming majority of enterprises participating in the survey (more than 90 percent) noted that their need for banking services was being adequately met.

The situation with regard to prices for both finished products and raw materials and supplies is still relatively stable.

The economic and financial condition of enterprises has improved. During the year enterprises’ own capital continued to play a key role in the financing of both working assets and investments.

In addition, the trend toward a greater proportion of working assets in total assets continued, reaching 37.7 percent in the fourth quarter (this figure was 32.3 percent in the fourth quarter of 2003). Proceeds from product sales made up for 20.3 percent of funds placed in assets in the fourth quarter (this figure was 16.9 percent in the fourth quarter of 2003). These data are evidence of an increase in business activity among enterprises.

The per unit production cost declined (59.4 tyins per tenge of output in the fourth quarter, compared to 63.8 tyins in the first quarter), which played a role in the improved financial results – profitability of sales, assets, and equity capital. The profitability of sales (before taxes) remained at a fairly high level throughout the year (40–42 percent), which was due to growth in this indicator in the extraction sector (from 58.4 percent to 67.5 percent). There was a decline in this indicator in the manufacturing sector, however (from 34.1 percent to 26.7 percent). These data confirm that the extraction sector is highly attractive from an investment standpoint.

There was an improvement in the structure of capital in the real sector from the standpoint of ensuring the liquidity of current assets. Current assets cover current liabilities in full (the current liquidity ratio in the fourth quarter of 2004 was 1.7, compared to 1.5 in the fourth quarter of 2003).

At the same time, there are some negative factors at play. The impact of bank credits on the investment activity of enterprises remains negligible, which is linked to insufficient transparency in the real sector and continued risk of default on credits.

The average profitability of equity capital in the real sector grew during the year (from 12.3 percent to 15.4 percent) and was practically the same as the interest rates on bank credits, although this was due to the rise in the profitability of equity capital in the extraction industry (from 20 percent to 25 percent). There was a decline in this indicator in the manufacturing sector, however (from 13 percent to 11 percent), which was also true for some other sectors (excluding trade).

1.3. Fiscal Sphere[2]

Execution of the state budget in 2004 took place against the backdrop of continuing positive processes in economic development of the Republic of Kazakhstan's. As a consequence, according to preliminary data, the state budget deficit ended up being much smaller than the forecasted figure for 2004 and than the deficit recorded in 2003. The planned deficit was 112.9 billion tenge, while the actual deficit was 18.7 billion tenge (the figure for 2003 was 46.2 billion tenge), or 0.3 percent of GDP (it was equal to 1.0 percent of GDP in 2003).

Based on the results for 2004, state budget revenues totaled 1,305.1 billion tenge, or 23.5 percent of GDP (22.2 percent in 2003), which represents an increase in state budget revenues of 27.7 percent compared to 2003. This increase was tied to growth in tax receipts to 21.4 percent of GDP (the figure in 2003 was 20.5 percent of GDP), especially the corporate income tax, payments for the use of natural resources, as well as an increase in nontax revenue to 1.5 percent of GDP (the figure in 2003 was 1.0 percent of GDP).

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[2] based on data from the Ministry of Finance

The policy of reducing the tax burden on the economy was continued in 2004. The maximum personal income tax rate was lowered to 20 percent, while it used to be 30 percent, and the flat rate for the social tax (21 percent) was replaced by a regressive rate scale with a maximum rate of 20 percent and a minimum rate of 7 percent. The value-added tax rate was lowered from 16 percent to 15 percent.

In spite of this, receipts from these taxes increased in 2004 compared to 2003, with a 5.6 percent increase in personal income tax receipts, a 6.5 percent increase in social tax receipts, and a 5.0 percent increase in VAT receipts.

According to preliminary data, state budget expenditures totaled 1,323,8 billion tenge, or 23.9 percent of GDP (in 2003 this figure was 23.3 percent of GDP). The annual budget plan for 2004 was fulfilled by 97 percent in terms of financing. State budget expenditures exceeded the level of spending in 2003 by 24.6 percent. Thus, the state budget deficit totaled 18.7 billion tenge (in 2003 this figure was 46.2 billion tenge).

Spending on items related to the fuel and energy complex and the use of mineral resources increased by the largest margin (by a factor of 3.0), along with spending on housing and municipal services (by a factor of 2.0). There was also a significant increase in financing for agriculture, water resources, forestry, fishing, environmental protection, health care, culture, sports, tourism, and the information space. Spending on the servicing of government debt, on the contrary, declined.

Over the past several years there has been a steady increase in state budget spending, which is outpacing growth in GDP. The volume of spending increased from 23.2 percent of GDP (in 2000) to 23.9 percent of GDP (in 2004), or by a factor of 2.2 in nominal terms. Capital outlays, which increased in 2000–2004 by a factor of almost 7, account for the greatest growth among state budget expenditures, while growth in current spending during this period less than doubled according to the estimates. As a result, the proportion of current spending increased to 24.5 percent of total spending (this figure was 7.8 percent in 2000), while the proportion of current expenditures, as well as credits and share participation, fell to 72.7 percent (this figure was 87.8 percent in 2000) and 2.7 percent (4.4 percent in 2000), respectively.

Thus, over recent years fiscal policy has had a clearly pronounced expansionist orientation, aimed at increasing the state's participation in the investment process. This policy, while stimulating economic growth, is one of the main factors in the continuing inflationary pressure on Kazakhstan's economy.

Republican budget revenues in 2004 totaled 978.4 billion tenge, or 4.7 percent more than the figure set forth in the Law "On the Republican Budget for 2004." Tax receipts going to the republican budget increased by 35.3 percent compared to 2003. Nontax revenue increased by 84.4 percent during the year compared to 2003. Republican budget spending compared o the corresponding period grew by 28.7 percent, with increases seen in the main spending items. According to preliminary data, expenditures were financed in the amount of

995.6 billion tenge. As a result, the republican budget posted a deficit of 17.3 billion tenge (there was a deficit of 51.9 billion tenge in 2003).

In 2004 local budgets were executed with a deficit of 12.7 billion tenge (in 2003 there was a surplus of 6.3 billion tenge), with revenues totaling 609.4 billion tenge and expenditures in the amount of 622.1 billion tenge.

The internal government debt at the end of 2004 totaled 231.1 billion tenge, which represents an increase of 38.9 percent compared to 2003.

The growth in internal debt was due for the most part to an increase in medium-term treasury bonds issued by the Ministry of Finance, debt on which grew by 35.4 percent. At the end of 2004 they accounted for 88.9 percent of internal government debt. In spite of the fact that the volume of short-term bonds in circulation grew by a factor of 4.0, they accounted for 9.2 percent of the debt. The amount of debt on indexed treasury bonds fell by 50.3 percent and as a proportion of internal debt they dropped to 1.2 percent. The volume of domestic debt instruments denominated in foreign currency fell by 9.7 percent as a result of a strengthening of the exchange rate of the tenge, while their nominal value in U.S. dollars did not change.

External government debt fell by 19.8 percent for the year compared to 2003 and totaled US$2.7 billion.

1.4. Balance of Payments and External Debt

Strong economic growth and the dynamic rise in prices for energy resources in the global economy continued in 2004 and played a determining role in the results of foreign economic activity on the part of Kazakhstan residents.

Revival of business activity and growth in domestic demand in practically all of the regions of the world led to further expansion of world trade and higher prices for goods used in production. With a view to stimulating economic growth, central banks in developed countries kept lending rates at relatively low levels, which significantly expanded the opportunities for developing countries to attract foreign capital. The year 2004 was characterized by unprecedented growth in world prices for crude oil, stimulated by both robust demand on the part of the United States and Asian countries, in particular, and by limited oil reserves. Kazakhstan made full use of the competitive advantages provided by external factors, which can be seen in the results of residents' foreign economic activity in 2004 (Appendix 1 to Section I, Subsection 1.4).

The current account balance ended up with a surplus for the year (US$533 million), a result that had been recorded only once before, in 2000. Given the high growth rates for imports of goods and services and further widening of the negative imbalance on income and current transfers, the positive current account balance was the result of a sharp increase in proceeds from exports of goods, which in turn provided for an increase in the positive trade balance by a factor of 1.8 compared to 2003.

The foreign trade goods turnover in 2004 exceeded US$34 billion, which represents an increase by a factor of 1.5 compared to 2003. Exports of goods totaled US$20.6 billion, increasing by 56 percent on the year, while imports of goods grew by 45 percent to US$13.8 billion. A comparison of the effect of world prices and growth in physical volumes on the value figures for exports and imports of goods shows that given proportional growth indicators, the increase in the value of exports was due primarily to the price factor, while growth in quantitative deliveries was the dominant factor in the growth in the value of imports.

In 2004, in addition to receipts from current transactions, the inflow of resources into the country came from the large-scale attraction of foreign capital both in the form of foreign direct investment (FDI) and in the form of borrowed resources attracted in international capital markets. The volume of financing attracted in 2004 through direct investment operations also reached a record level. These results were determined in large degree by the trends in the world oil market. The gross inflow of FDI into Kazakhstan in 2004 was in excess of US$8.4 billion. Investments in the oil and gas sector had a major impact on the distribution of the gross inflow of FDI among various sectors. The extraction of oil and natural gas accounted for the bulk of the FDI (63 percent of the gross inflow of FDI), along with geological and prospecting activities (20 percent). The proportion of FDI going to the extraction of oil and gas increased by 17 percent compared to 2003.

In 2004 the net inflow of loans attracted by the private sector totaled US$4.3 billion. The Republic's banking sector was responsible for the bulk of the increase in the volume of foreign borrowing in the private sector. High domestic demand and the relatively low cost of borrowed resources in international capital markets stimulated the attraction of significant quantities of foreign capital. A strongly positive assessment of the investment opportunities in Kazakhstan helped reduce the cost of foreign capital for Kazakhstani borrowers. The major international ratings agencies assigned investment-grade ratings both to the Republic and to leading Kazakhstani banks. In 2004 second-tier banks attracted loans totaling US$6.3 billion, and as a result the banking sector's external debt grew during the year by more than US$3.2 billion. Debt owed by the nonbanking sector to unaffiliated creditors grew by more than US$1.0 billion, which was due primarily to an increase in long-term loans taken out by enterprises in the Republic by a factor of 1.4. During 2004 as a whole Kazakhstan's gross external debt increased by more than US$9 billion and at the end of the year it exceeded US$31.9 billion.

In addition to the growth in export revenue, the significant inflow of external financial resources gave rise to a substantial increase in residents' foreign assets and a significant improvement in the Republic's external liquidity indicators.

Appendix 2 to Section I, Subsection 1.4, presents the dynamics of the main indicators of Kazakhstan's external sector over the past four years.

The capital inflows gave rise to growth in the country's external debt.

The Republic's gross external debt as a proportion of GDP has been fairly high over recent years, reaching more than 70 percent. According to the classification of the International Bank for Reconstruction and Development, in terms of its debt level Kazakhstan is now classified as a country with moderate debt. At the same time, since intercompany debt, which in international practice is considered to have the lowest risk of default, accounts for more than half of the external debt, the ratio of gross external debt to GDP, not counting this type of debt, is 37.7 percent.

The ratio of debt service to exports of goods and services indicates the proportion of a country's export revenues that are earmarked for servicing external debt and enables one to assess a country's ability to repay its debt obligations in the event of a sharp decline in revenues from exports of goods and services (Appendix 3 to Section I, Subsection 1.4). In 2004, in spite of significant growth in exports of goods and services, there was an increase in debt service payments and this indicator rose slightly compared to 2003 and 2002 (38 percent in 2004 as opposed to 35.2 percent and 35.0 percent in 2002 and 2003, respectively).

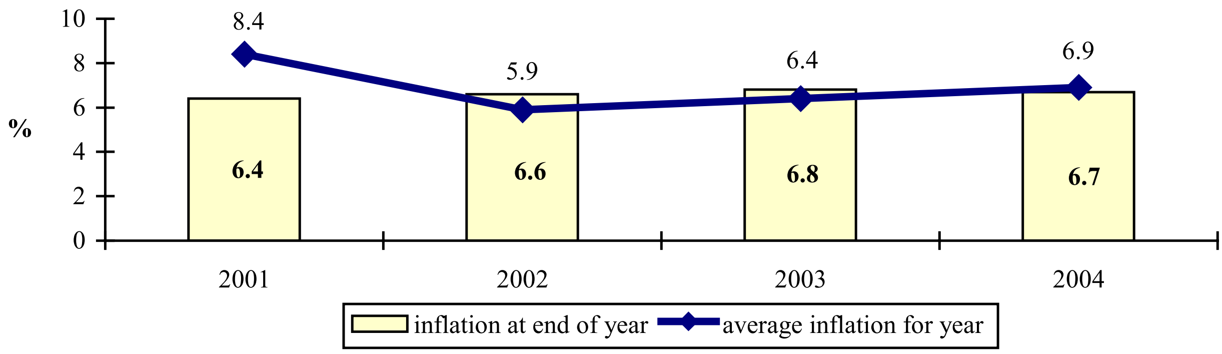
II. MONETARY POLICY AND MANAGEMENT OF GOLD AND FOREIGN EXCHANGE ASSETS

2.1. Monetary Policy

Continuing macroeconomic stability in the country, coupled with favorable foreign economic factors, helped sustain strong economic growth. The significant economic growth, accompanied by high consumer demand and investment activity, helped keep inflation at a stable level.

Under these conditions, in connection with the transfer of supervisory functions to the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions, ***the main goal*** of the National Bank since the beginning of 2004 has been to ensure price stability. Over the past several years inflation has remained steady at a relatively low rate – within the range of 6–7 percent calculated at year-end. In 2004 the National Bank continued to pursue a policy aimed at keeping inflation low. At the end of 2004 the annual inflation rate was 6.7 percent. Average annual inflation remained within the limits of the indicative indicators at 6.9 percent, while inflation has been rising over the past two years.

Dynamics of Inflation



There are three aspects that can be identified as typical characteristics of the dynamics of inflation in 2004.

First, the rise in prices was practically even across the board for all groups of consumer goods and services, without any clearly pronounced "leaders." In contrast to previous years, in 2004 there was a significant rise in consumer prices for only certain items (pork, eggs), and also in certain regions of Kazakhstan (especially for certain types of housing and municipal services in a number of regions).

Second, there was no seasonal decline in prices during the summer months. In previous years if there had not been a decline in prices, there was a least price stability in July or August (in July 2001 prices fell by 0.1 percent, in August 2002 they fell by 0.3 percent, and in July 2003 prices remained unchanged). In July and August 2004 consumer prices rose by 0.2 percent and 0.4 percent, respectively. The main reason for the decline in prices in previous years was a sharp reduction in the cost of fruit and vegetable products. While in 2000–2003 the decline in prices for these goods in July–September (the main harvest period) ranged from 10 percent to 17 percent, in 2004 there was a decline of just 7.4 percent.

Nevertheless, based on the results for the year, the rise in prices for fruits and vegetables was unexpectedly low at 5.9 percent, while in 1999–2003 the average increase was around 30 percent.

Third, there was a marked weakening of the volatility in monthly inflation rates. While in 2002 the maximum and minimum monthly growth rates of consumer prices were 1.4 percent in December and (-) 0.3 percent in August, in 2003 the corresponding figures were 1.6 percent in November and 0.0 percent in July, and in 2004 they were estimated at 1.1 percent in October and 0.2 percent in May and July.

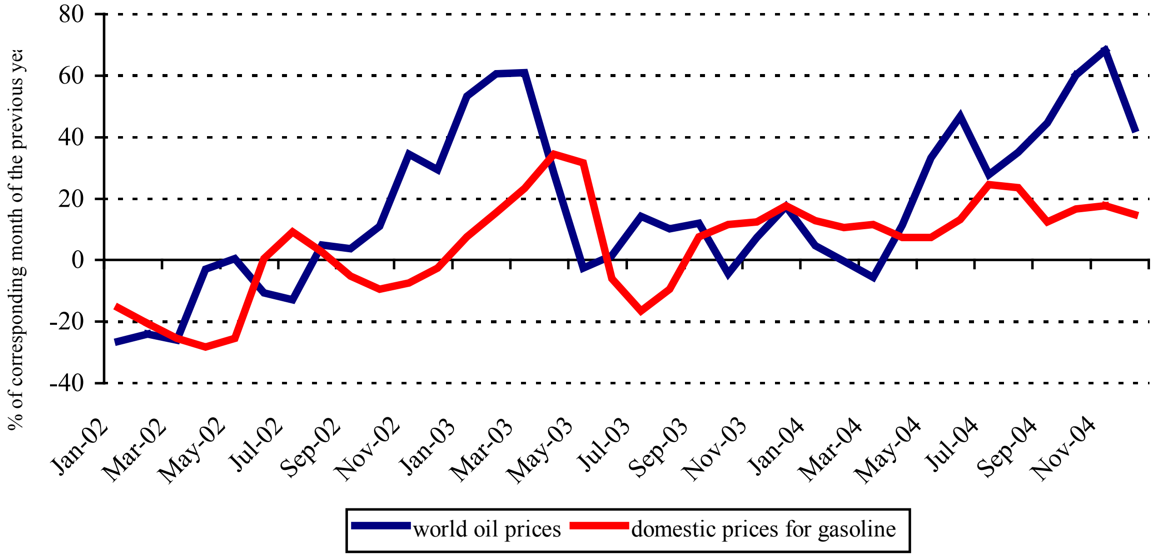
The price dynamics in 2004 were shaped by the effects of cost inflation (growth in spending on wages and purchased resources), demand inflation (growth in the income of economic entities), as well as "imported" inflation. In spite of this, inflation was kept at an acceptable level, although the impact of a number of factors (growth in real GDP, increase in the money supply, high world prices for raw materials resources) on inflation exceeded both the indicators of the previous year as well as expectations.

A significant increase in the population's purchasing power, linked to growth in personal money income and an overall increase in economic activity, is contributing to the continuing baseline inflation in Kazakhstan's economy. In 2004 wages increased by 13.9 percent in real terms. These growth rates are exceeding growth in labor productivity in real terms, at 6.6 percent (the ratio of real GDP to the employed population), and this results in higher prices.

A significant expansion of the money supply, one of the main reasons for which is growth in budget spending (which has increased by a factor of 2.2 over the past 4 years), has had a substantial impact on inflation over recent years, including 2004.

Another important factor that had an effect on consumer prices in 2004 was the "import" of inflation. According to data from the International Monetary Fund, world prices for Brent grade oil in 2004 rose by 38.5 percent. Taking the form of higher domestic prices for gasoline and fuel and lubricants, these prices give rise to significant inflationary potential in terms of higher prices for other goods and services in the future.

Dynamics of the Change in World Prices for Oil and Domestic Prices for Gasoline



On the other hand, a curb on the "import" of inflation was provided by lower prices for imported textile and sewn articles (by 3.0 percent).

In 2004 there was an unexpectedly sharp rise compared to 2003 in ***industrial producer prices, including prices for services of a production nature***, by 23.8 percent. Most of the price increase was due to higher prices for intermediate consumption products, which rose by 29.6 percent, while prices for producer goods, consumer goods, and services of a production nature increased by 4.7 percent, 3.9 percent, and 4.3 percent, respectively. Broken down by sectors of industry, prices increased in the mining and extraction industry (by 38.3 percent), manufacturing (by 13.5 percent), and in the production and distribution of electricity, gas, and water (by 2.5 percent). A key factor in the rise in prices in industry in 2004 was the increase in the price of gas condensate by 79.3 percent and oil by 40.6 percent. In connection with favorable foreign trade conditions, domestic producers' prices for nonferrous metals increased by 27.9 percent.

In addition, prices in agriculture rose by 4.0 percent, and in animal husbandry in particular, which posted an increase of 11.1 percent.

The rise in prices in the real sector of the economy contributed to a certain extent to higher consumer prices.

Monetary policy instruments. To achieve the inflation target, the National Bank carried out operations to absorb excess liquidity, the principal ones of which were issuing short-term notes, attracting bank deposits, and performing open-market operations, in addition to employing the mechanism of minimum reserve requirement. The base money level remained one of the key indicators.

Throughout the year the National Bank kept its ***main official rates*** weakly positive in real terms.

The policy of steadily lowering official rates which was typical over previous years was replaced by a policy of stabilizing and raising rates, given the failure to reduce inflation. The following were kept at the same level as the end of 2003: the official refinancing rate (7 percent) and the minimum reserve requirement rate (6 percent). The official rate for repo transactions fluctuated over the course of 2004. In August it was lowered from 4.5 percent to 3.5 percent, while the band of allowable deviations was expanded from ± 150 basis points to ± 200 basis points, and from October through December this rate was gradually raised to 4.25 percent, while the band for allowable deviations was kept at ± 200 basis points. The official rate for "overnight" loans was raised from 8.0 percent to 8.5 percent.

To curb the growth rate of inflation the National Bank took measures in 2004 to strengthen the regulating effects of official rates. Specifically, in order to expand the economic role of the refinancing rate, bills of exchange are being rediscounted in accordance with the official refinancing rate, while the bill trading system is being developed simultaneously.

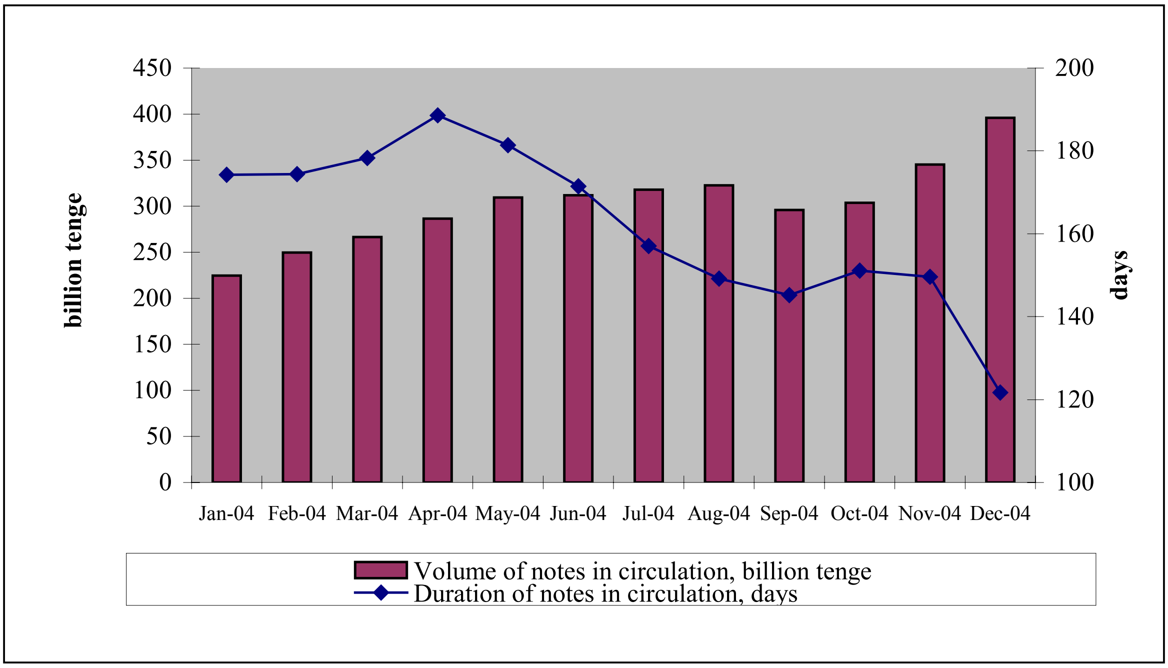
Short-term notes remained the main instrument used by the National Bank to sterilize excess liquidity.

During the year the National Bank issued short-term notes in the amount of 561.8 billion tenge (a decline of 8.3 percent compared to 2003). The largest issue of notes occurred in the fourth quarter, during which placements of varying size were carried out (40.1 billion tenge in October, 73.8 billion tenge in November, and 85.9 billion tenge in December). The liquidity of second-tier banks remained high throughout the year, which, in spite of a slight decline, was the reason for the continued large issues of short-term notes for the purpose of sterilizing excess liquidity.

The redemption of National Bank notes in 2004, including the payment of interest, totaled 374.8 billion tenge. Early redemption of short-term notes totaled 63.9 billion tenge, which was due to the operational replenishment of liquidity in the market. As a result, the volume of short-term notes in circulation doubled to 396.1 billion tenge (based on the discounted price).

The effective yield on short-term notes fell from 5.07 percent to 3.21 percent (the weighted average yield for the last month of the year). Duration indicators for short-term notes also fell during 2004 from 174.25 days at the end of January to 121.66 days at the end of December. The decline in the duration of short-term notes toward the end of the year was linked to a reduction in the time that short-term notes were in circulation, which was caused, in turn, by the National Bank's policy aimed at reducing the attractiveness of notes as an instrument for the investment of pension assets, and the gradual transition to regulation of the situation in the financial market through short-term rates.

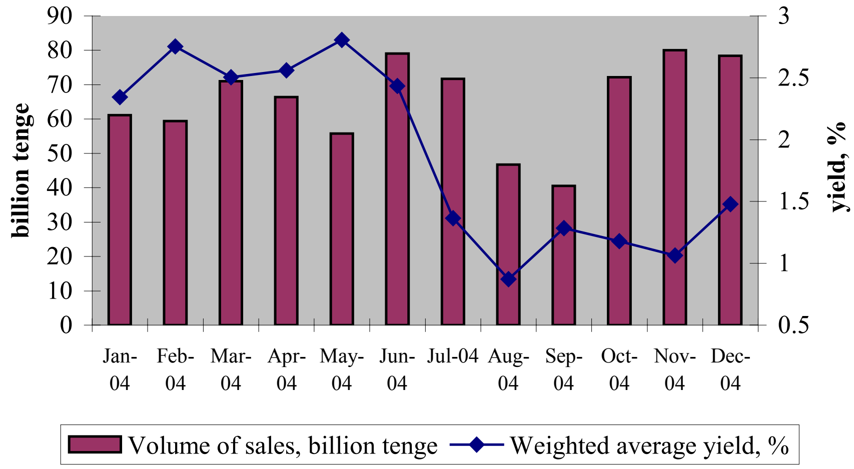
Short-Term Notes in Circulation (At the End of the Period)



Open-market operations continued to be an important type of operation for the National Bank. As in the past, however, the volume of these operations was limited by the small securities portfolio of the National Bank.

In 2004 the volume of repo transactions performed in the secondary government securities market increased by 60.1 percent to 782.4 billion tenge. The maturity for these transactions was 1.4 days, and the yield was 1.89 percent per annum.

Repo Transactions Performed by the National Bank



Reverse repo transactions in the amount of 26.0 billion tenge were performed, with a maturity of 7 days and a yield of 4.95 percent per annum.

The National Bank did not perform any transactions involving the sale of government securities in 2004. Purchases totaled 1.8 billion tenge, with a weighted average yield to maturity of 5.89 percent per annum. The time to maturity was 1,784 days.

In 2004 the National Bank devoted a great deal of attention to the instrument of ***attracting deposits from second-tier banks***. For the year the volume of tenge deposits attracted increased by a factor of more than 2.5 to 775.7 billion tenge, and the average term was approximately 2 weeks, with an average rate of 2.50 percent per annum. The National Bank also attracted deposits in tenge from the Ministry of Finance totaling 785.0 billion tenge at an average rate of 2.9 percent per annum and an average term of one month. At the end of 2004 tenge time deposits of second-tier banks at the National Bank had risen to 75.5 billion tenge, which represents an increase by a factor of 3.8 compared to the same period of the previous year.

General Agreements on the ***granting of "overnight" bank loans*** were in effect with seven second-tier banks as of January 1, 2005.

"Overnight" loans totaling 10.7 billion tenge were granted in 2004 (compared to 19 billion tenge in 2003).

The deadlines for the repayment of bank loans granted to banks for the financing of the "GRK ABS-Balkhash" Open Joint-Stock Company and the Kazakhstan Interbank Settlement Center were extended. Debt in the amount of 1.76 billion tenge owed by "KRAMDS Bank" JSC, which has completed the liquidation process, was cancelled. The repayment of loans in tenge totaled 10.9 billion tenge, and repayments on loans in U.S.

dollars totaled US$3.42 million (in 2003 these figures were 19.1 billion tenge and US$2.35 million, respectively).

At the end of 2004 the debt owed on foreign currency loans totaled US$0.886 million.

In 2004 there was continued development of the system for the circulation of bills of exchange, which plays a role to some extent in expanding the economic role of the official refinancing rate at which the National Bank performs the ***rediscounting of bills***.

General agreements on the rediscounting of bills have been concluded with seven second-tier banks. In 2004 there were 11 enterprises included on the list of first-class issuers. Bills of exchange of the seven enterprises were presented by discounting offices for rediscounting by the National Bank. A total of 669 bills of exchange in the amount of 5.7 billion tenge were accepted for rediscounting in 2004 (in 2003 these figures were 368 bills and 1.5 billion tenge, respectively). Bills of exchange in the amount of 4.2 billion were redeemed.

At the end of 2004 the National Bank's portfolio contained bills of exchange in the amount of 2.3 billion tenge (as of January 1, 2004 this figure was 770.7 billion tenge).

In 2004 the National Bank continued the floating ***exchange rate regime for the tenge***, which means that there are fluctuations in the currency's exchange rate depending on its supply and demand.

In 2004 the trend toward a stronger exchange rate for the tenge against the U.S. dollar continued. To even out fluctuations in the exchange rate, the National Bank participated in the domestic exchange market as a buyer. In 2004 net purchases of foreign currency by the National Bank totaled US$3.6 billion. In addition, the National Bank converted currency for the Ministry of Finance in the amount of US$1.0 billion for the purpose of replenishing the assets of the National Fund.

The National Bank intends to continue in the future to ***strengthen its influence through monetary policy operations***, to promote a further increase in the regulatory role of its basic rates, and to focus its efforts on coordinating rates for various types of monetary policy instruments. Open-market operations will be expanded and measures will be undertaken to enlarge its own securities portfolio and to develop new financial instruments.

To ease inflationary pressure, when necessary the National Bank may take measures to tighten monetary policy. One of these measures was raising the official refinancing rate at the beginning of 2005. As the inflationary potential in the economy declines, however, it is anticipated that this rate will be gradually lowered.

A tightening of monetary policy entails a change in the direction of the influence of the National Bank's official rates on market credit rates. While in previous years the

National Bank's measures were aimed at addressing the problem of getting banks more actively in terms of economy crediting, including the lowering of rates, given the need to prevent an "overheating of the economy," the lowering of rates is no longer an end in and of itself. The rates in the economy should be set on a market basis so that they are consistent with the risks and factors that arise from the actual situation.

To ease the severity of the problem of excess liquidity and to achieve more flexible regulation of banks' liquidity, the relevant changes will be made in the mechanism for setting minimum reserve requirements.

With a view to strengthening the regulation of interest rates in the financial market, there are plans to reduce significantly the time that short-term notes are in circulation. Given these conditions, the main instrument for sterilizing excess liquidity will be banks' deposits at the National Bank.

It is expected that in spite of the measures planned to limit liquidity, over the next three years the annual growth in monetary aggregates will mean that the existing economic growth rates will be maintained.

To enhance the effectiveness of the decision-making process, the National Bank will establish a ***consultative-advisory body on monetary policy*** with the participation of representatives of the National Bank and interested government bodies, Parliament, scientific groups, as well as the financial and real sectors of the economy.

To strengthen the regulatory properties of the official refinancing rate, the National Bank plans to put into practice a ***periodic (quarterly) review and setting of the official refinancing rate*** depending on the overall condition of the money market, loan supply and demand, the inflation rate, and inflationary expectations.

Monetary aggregates. In 2004 continued strong economic growth was accompanied by a significant expansion of the money supply. During this period the rate of growth in money base and cash in circulation (M0) was the highest in the last nine years, and the growth in the money supply was the highest in the last five years.

The ***money base*** level remained one of the key indicators used by the National Bank in the implementation of monetary policy. In 2004 money base expanded by 82.3 percent to 577.9 billion tenge. The main factor in its expansion was significant growth in the National Bank's net international reserves.

Continued high prices for oil in world markets contributed to a significant inflow of foreign exchange export earnings into the economy. There was an increase in borrowing by banks in world financial markets, and as a result, the supply of foreign currency in the domestic exchange market exceeded demand. Under these conditions the National Bank built up its foreign exchange assets (the National Bank's net foreign exchange reserves doubled in 2004). There was an increase in assets in gold (by 10.7 percent) in connection with transactions effected by the National Bank and a rise in the price of gold in world markets by 5 percent. As a result, in 2004 the National Bank's net international reserves increased by 87.1 percent and reached US$9.3 billion, which is the highest indicator posted since Kazakhstan gained independence.

On the other hand, the National Bank's purchase of foreign exchange in the domestic exchange market led to an increase in banks' liquidity. Therefore, in 2004 the National Bank continued simultaneously to pursue an active policy to sterilize the excess liquidity that had developed in the banking system by issuing short-term notes.

As a result, the National Bank's operations to sterilize excess liquidity made it possible in part to neutralize the significant growth in its net international reserves.

In 2004 the greatest shrinking of money base (by 5.8 percent) occurred as usual in January, which can be explained by the significant increase in balances on the government's accounts at the National Bank due to the seasonal decline in government spending. The two largest expansions in base money occurred in May, by 13.9 percent, and December, by 18.1 percent; this was tied to growth in the National Bank's net international reserves, while at the same time there was a decline in the National Bank's net domestic reserves.

Since January 1, 2004 the broad money supply(M3) survey has included credit union accounts, in addition to accounts of the National Bank and second-tier banks. Therefore, the analysis of the dynamics of the money supply is based on a money survey of deposit institutions, which includes a consolidated survey of the National Bank, second-tier banks, and credit unions.

The increase in the ***money supply*** in 2004 by 68.2 percent to 1,634.7 billion tenge occurred against the backdrop of a rise in business activity among economic entities. As a result, the level of monetization of the economy increased during the year from 21.1 percent to 29.5 percent, which is the highest indicator for the economy in recent years.

The increase in both net foreign assets of the banking system and credit unions (deposit institutions) and their domestic assets were the main factors in the growth of the money supply.

It should be noted that the growth in the net foreign assets of deposit institutions by 64.7 percent was due to an increase in the gold and foreign exchange assets of the National Bank, since the net foreign assets of second-tier banks declined.

The continuing growth in the volume of lending to the economy remained a significant factor in the growth of the money supply in 2004. The claims of deposit institutions on the economy in 2004 grew by 52.0 percent compared to the previous period. As a result, domestic assets of deposit institutions grew by 71.1 percent.

As a consequence of growth in residents' deposits at deposit institutions that outpaced the growth in cash in circulation, the upward trend in deposits as a proportion of the money supply continued. In 2004 this indicator rose from 75.5 percent to 77.6 percent.

The value of the money multiplier fell from 3.07 to 2.83. At the same time, it is fairly difficult to arrive at an unequivocal assessment of the importance of this change. On the one hand, the cash preference ratio, that is, the ratio of cash in circulation to residents' deposits at deposit institutions, fell from 0.33 to 0.30, which points to an increase in the population's preference to hold their available funds in the form of deposits. On the other hand, the reserve ratio, that is, the ratio of deposits of deposit institutions at the National Bank and cash in hand to residents' deposits at deposit institutions, increased from 0.11 to 0.16, which can be explained by growth in banks' deposits at the National Bank given the sterilization of excess liquidity in the banking system.

In 2004 ***cash in circulation*** increased by 56.8 percent to 410.9 billion tenge. This can be explained primarily by the continued strong economic growth, which helps increase the demand for money, including cash, growth in the nominal and real income of the population, and higher current spending by the state to pay wages.

Indeed, in 2004 GDP increased by 9.4 percent in real terms, while the real retail goods turnover through all sales outlets increased by 10.6 percent.

Growth in business activity among economic entities, in turn, led to an increase in the population's money income and average monthly wages. The growth in nominal and real money income of the population in 2004 compared to 2003 was 21.0 percent and 13.2 percent, respectively. Average nominal wages rose by 21.7 percent in 2004.

Growth in the population's money income and wages was also due to a rise in wages paid to employees of organizations supported by the budget and civil service employees, as well as the state's policy carried over from the previous year, which is aimed at increasing pensions on a differentiated basis and increasing social benefits as of January 2004. In addition, as of January 1, 2004 the minimum wage was raised by 32 percent. As a result, state spending on the payment of wages grew by 41.3 percent compared to the previous year, and state spending on social transfers increased by 13.5 percent.

Thus, in 2004 the expansion of money base can be explained by the significant increase in the National Bank's net international reserves. The active lending policy being pursued by second-tier banks contributed to growth in the money supply, while cash in circulation increased as a result of growth in the population's income and average monthly wages.

The gradual transition from targets for money base and gold and foreign exchange reserves to inflation targets, which is more consistent with the National Bank's main goal of lowering inflation, was made as part of the ***transition to inflation targeting principles***.

In the plan for preparing for the transition to inflation targeting, the National Bank established a three-year horizon for the planning of monetary policy, starting in 2000. The "core inflation" index has been calculated and an inflation survey has been published since 2004.

Another essential element of inflation targeting is a transmission mechanism model that enables one to increase the accuracy of inflation projections and evaluate the impact of measures being undertaken in the area of monetary policy on inflation.

A schematic diagram has now been developed and a model of money transmission in Kazakhstan has been devised (Appendix 1 to Section II, Subsection 2.1).

At the invitation of the National Bank, a mission from the International Monetary Fund made an official visit in September 2004 in the context of providing technical assistance in the introduction of inflation targeting principles in the Republic of Kazakhstan. The mission noted the significant progress that has been made by the National Bank in this direction. A report was presented based on the outcome of the meetings between members of the mission and representatives of the National Bank, the Agency of the Republic of Kazakhstan on Statistics, and commercial banks, which offered recommendations for further measures to introduce the inflation targeting regime in the Republic. Specifically, the following useful recommendations were made:

- a monetary policy committee should be set up with the participation of independent outside members among qualified candidates, with the authority to consider strategic issues in monetary policy, including inflation forecasting;

- with regard to the legal authorities of the National Bank, protection from arbitrary dismissal needs to be provided for the top management, with the exception of cases of serious negligence or unlawful behavior;
- the National Bank should focus attention on autonomous forecasting of indicators for the real sector of the economy, and GDP in particular.

2.2. Gold and Foreign Exchange Assets of the National Bank and Their Management

The dynamics of indicators of gold and foreign exchange assets. The National Bank's gross gold and foreign exchange assets as of January 1, 2005 totaled US$9.3 billion, which represents an increase of US$4.3 billion for the year. This change was due to an increase in assets in freely convertible currency by US$4.2 billion and assets in monetary gold by US$77.6 million.

Both internal and external factors had an impact on the growth in gross foreign exchange assets in 2004. For example, Kazakhstan's exchange market was influenced by the fact that the supply of freely convertible currency was greater than the demand. Net purchases by the National Bank on the Kazakhstan Stock Exchange totaled US$3.3 billion for the year, while net purchases in the over-the-counter market totaled US$308.4 million.

Another reason for the growth in gross foreign exchange assets was the receipt of foreign currency by the Ministry of Finance in the amount of US$1.7 billion. The largest sums were received in the form of tax payments by companies in the oil and gas sector, totaling US$1.6 billion, and from the Russian government for the leasing of the Baikonur complex in the amount of US$115.0 million.

At the same time, the National Bank made payments on external government debt in the amount of US$1.0 billion and sold US$1.0 billion to the National Fund.

Growth in the value of assets in precious metals, valued in U.S. dollars, was due to a rise in gold prices in world markets. The price of gold rose on the year from US$417.25 per troy ounce to US$438.00, or by 5 percent, which led to an increase in this reserve asset by US$43.0 million.

The National Bank purchased gold in the domestic market in the amount of US$34.7 million.

Based on the results of the transactions performed by the National Bank, net gold and foreign exchange assets increased on the year by US$4.3 billion to US$9.3 billion (Appendix 1 to Section II, Subsection 2.2, Table 2.2.1).

Management of the portfolio of gold and foreign exchange assets. The market value of assets placed under external management at the end of 2004 was equivalent to US$492.9 million, or 6 percent of the total market value of gold and foreign exchange assets[3].

In the process of the management of the portfolios of gold and foreign exchange assets and the National Fund in 2004, some new instruments were used, such as:

- 3-month Euribor futures;
- 3-month Euribor options;
- corporate bonds;
- IO – interest only mortgage bonds (MBS);
- currency straddle option;
- continuous call securities.

A new investment strategy, which entered into the force on October 1, 2004, was adopted pursuant to Resolution No. 115 of the National Bank Board of August 27, 2004 “On Approval of the Investment Strategy for Management of the National Bank’s Gold and Foreign Exchange Assets.” According to this strategy, gold and foreign exchange assets

[3] including the U.S. money market mandate type under external management up to December 31, 2004

have been divided up into a long-term portfolio of foreign exchange assets, a short-term portfolio of foreign exchange assets, a gold portfolio, and a liquidity portfolio.

The changes in the strategy for the management of gold and foreign exchange reserves can be characterized as a reaction to market expectations and concern over the decline in the return on fixed-return instruments in connection with the onset of a cycle of higher interest rates in the United States starting from the second half of 2004. No transfers of funds were made during the year from the short-term portfolio of gold and foreign exchange reserves to the long-term portfolio, in spite of a significant influx of U.S. dollars from transactions in the domestic market, and starting in the fourth quarter this was established officially by means of changes in the strategy that added to the investment portfolios a short-term portfolio of assets with 70 percent invested in U.S. dollars and 30 percent in euros, and by a benchmark portfolio based on short 3-month U.S. and German government treasury bills. These changes are a temporary solution in response to the situation that has developed, and the duration of the investment portfolios, in all likelihood, will be increased after the end of the monetary policy tightening cycle in the United States.

The long-term portfolio of gold and foreign exchange assets. The market value of the long-term portfolio of gold and foreign exchange assets at the beginning of 2004 was US$3.4 billion, and at the end of the year it was US$3.6 billion. Investment income (realized and unrealized) on the portfolio was US$231.1 million.

The return on the long-term portfolio of gold and foreign exchange assets for the year, expressed in U.S. dollars, was 6.86 percent. Given a return on the benchmark portfolio of 6.56 percent, the excess return was 30 basis points (Appendix 2 to Section II, Subsection 2.2., Figure 2.2.1).

In connection with the adoption of the new investment strategy, starting at the beginning of the fourth quarter the change was made to a new benchmark portfolio. Currencies such as the Canadian dollar, Danish krone, Australian dollar, Swedish krona, and Swiss franc were included in the benchmark portfolio. The inclusion of new currencies in the benchmark portfolio will make it possible to hold a larger number of active positions spread among countries and currencies, which offers the potential opportunity to increase the excess return.

In connection with the risk of a rise in inflation, instruments that protect assets against depreciation in the event of a rise in inflation, for example, the U.S. Treasuries Inflation-Linked index, were included in the portfolio.

The excess return on dollar subportfolios under external management in 2004, excluding the commission fee paid on the subportfolio under the management of Manager 1, was 19 basis points, while the excess return on the subportfolio under the management of Manager 2 was 143 basis points; when the commission fee is included, these figures are 7 basis points and 101 basis points, respectively. The excess return on the euro subportfolio under external management in the first half of 2004, excluding the commission fee, was

(-75) basis points, and when the commission fee is included, the figure is (-80) basis points. Due to the negative excess return of (-75) basis points since the portfolio was placed under external management, the decision was made pursuant to Resolution No. 88 of the National Bank Board of July 3, 2004, to terminate the Investment Management Agreement with Manager 3. The market value at the time the agreement was terminated, July 14, 2004, was US$158.7 million (Appendix 3 to Section II, Subsection 2.2).

Sectoral distribution of the long-term portfolio of gold and foreign exchange assets under internal and external management. The managers reduced the proportion of cash and cash equivalents during the year by 3.3 percent to 3.0 percent, the proportion of agency securities by 8 percent to 14.9 percent, the proportion of securities of international financial institutions by 0.7 percent to 0.2 percent, and the proportion of asset-backed securities by 0.8 percent to 7.2 percent; they increased the proportion of government securities by 11.3 percent to 71.1 percent (the proportion of U.S. inflation-indexed securities totaled 4.8 percent at the end of 2004) and the proportion of corporate securities by 1.8 percent to 3.7 percent. Appendix 1 to Section II, Subsection 2.2, Table 2.2.2, provides the distribution of foreign exchange assets under internal management on a yield curve by quarter in 2004.

The short-term portfolio of gold and foreign exchange assets. The overall return on this subportfolio was 4.26 percent, while the return on the benchmark portfolio was 4.16 percent, resulting in an excess return of 10 basis points (Appendix 1 to Section II, Subsection 2.2, Figure 2.2.2).

The excess return on the subportfolio under external management, excluding the commission fee, was 8 basis points. The excess return since management began was 170 basis points. With a view to reducing external management costs, Investment Management Agreement No. 482 of September 13, 2001 with the U.S. money market mandate type external manager (Manager 4) was terminated pursuant to Resolution No. 165 of the National Bank Board of December 15, 2004.

Gold and foreign exchange assets liquidity portfolio. The market value of this portfolio at the beginning of the fourth quarter of 2004 was US$1.3 billion, and at the end of the year it was US$551.8 million.

In connection with the large number of inflows and outflows from the short-term currency portfolio of gold and foreign exchange assets related to external payments, the purchase and sale of foreign exchange in the domestic market, Ministry of Finance payments, and external debt payments, a separate gold and foreign exchange assets liquidity portfolio was set up. This portfolio serves as a means for the implementation of monetary policy, and all flows and various payments are maid through it. It is not included in the valuation of the return on portfolios of gold and foreign exchange assets and it has no benchmark portfolio. The limit set for the minimum amount, which is US$300.0 million, was met.

Gold portfolio. The market value of the gold portfolio at the beginning of 2004 was US$725.9 million, and at the end of the year it was US$803.6 million. Receipts of gold during the year totaled 90,724.163 ounces.

The proportion of the gold portfolio in relation to the level of gold and foreign exchange assets at the end of the year was 9.3 percent.

III. FOREIGN EXCHANGE REGULATION AND CONTROLS

Liberalization of the foreign exchange regime is being carried out gradually, taking into account the specific features of Kazakhstan's economy, as well as internal and external factors that determine the sustainability of economic growth, and the government's economic policies.

The principal goal of the initial stage of liberalization of the foreign exchange regime was to increase the effectiveness with which foreign exchange assets are used by expanding the investment opportunities for residents of Kazakhstan. This gave rise to the need to ease the foreign exchange regulation regime with respect to investments in nonresidents' investment-grade securities and direct investments by residents abroad, which expand the Republic's production potential, foster conditions for penetration into promising new markets, and provide for the necessary level of control over investment objects.

These measures were carried out with the adoption of amendments to the current Laws "On Foreign Exchange Regulation" and "On Licensing" and a revision of the regulatory legal base of the National Bank.

The aim of further efforts to liberalize the foreign exchange regulation regime is to foster conditions for the subsequent lifting of restrictions on the performance of foreign exchange transactions and for a transition to the principles of full convertibility of the domestic currency starting in 2007.

The measures outlined in the Program for Liberalization of the Foreign Exchange Regime in Kazakhstan for 2005–2007 are set forth in the new Law "On Foreign Exchange Regulation and Foreign Exchange Controls," a draft of which is currently being considered by Parliament.

The plan is to carry out the Program for Liberalization of the Foreign Exchange Regime in parallel with improvement of the information base on foreign economic transactions, which will make it possible to ensure an effective transition from the permitting procedure required for the performance of foreign exchange transactions to a system of follow-up monitoring and selective controls.

Pursuant to the measures outlined in the Long-Range Plan for Cooperation in Foreign Exchange Regulation and Foreign Exchange Controls, approved by the Council of Directors of Central (National) Banks of EurAsEC Member States in November 2003, the National Bank has drawn up an Agreement among the Central (National) Banks and Governments of EurAsEC Member States on the fundamental principles of foreign exchange regulation and foreign exchange control policy for transactions involving the movement of capital. This draft, among other things, identifies a list of priority foreign exchange transactions with regard to which the EurAsEC member states intend to gradually liberalize current national foreign exchange regimes.

Licensing of transactions related to the use of foreign exchange assets. In 2004 the National Bank issued 1,523 licenses for the following types of transactions:

1) 1,325 for transactions involving the movement of capital, including 1,199 for export-import transactions, 41 for investments abroad, 35 for real estate transactions, and 50 for the granting of credits;

2) 79 to open accounts, including 69 for resident legal entities abroad and 10 for resident individuals abroad;

3) 119 for the performance of foreign exchange transactions.

The improvement of licensing and administrative procedures allowed for a comprehensive approach to the identification of legal offenders in the process of the licensing of foreign exchange transactions, which helped strengthen discipline in the fulfillment of obligations under foreign economic contracts and for the repatriation of funds.

The performance of export-import foreign exchange controls rose to a qualitatively new level with the introduction of an automated ***export-import foreign exchange control*** system. Access by branch offices to computerized analytical forms allows them to participate in the centralized system for maintaining information on administrative offenses.

In 2004, based on the results of processing data from the automated export-import foreign exchange control system, 1,800 possible violations were identified and sent on to branch offices of the National Bank, 2,650 were forwarded to the Agency to Combat Economic Crime and Corruption, and 3,240 were forwarded to the Customs Control Committee under the Ministry of Finance in connection with the failure to repatriate funds to the Republic, for the purpose of opening administrative and criminal cases. Reliable data on the amount of export proceeds not repatriated and imported goods are also provided to the Presidential Administration.

Administrative proceedings regarding violations of foreign exchange legislation. In 2004 the National Bank opened 620 cases involving administrative offenses in the area of foreign exchange legislation and statistical reporting. Of these, 462 cases were reviewed by the central administration of the National Bank, and fines totaling 23.8 million tenge were imposed in 70.2 of the cases. National Bank branch offices reviewed 83 cases, and fines totaling 1.98 million tenge were imposed in 79 of the cases (95 percent of those reviewed). A total of 71 cases were referred to judicial authorities, and penalties totaling 1.7 million tenge were imposed in 49 of these cases.

Thus, one of the results of the efforts by the National Bank (and its branch offices) to review cases involving administrative offenses in the area of foreign exchange legislation was the generation of 25.49 million tenge in republican budget revenues.

Foreign exchange control inspection. The National Bank, in addition to planning the activities of its branch offices related to the performance of audits through the approval of Inspection Plans, is responsible for the control and analysis of the results of the audits that were performed on the basis of reports and materials submitted by the branch offices. Thus, in 2004 a total of 205 reports based on the results of audits of branches of authorized banks were reviewed. All together, National Bank branch offices conducted 939 audits of second-tier banks, institutions performing certain types of banking operations, and other legal entities to determine their compliance with the foreign exchange legislation.

IV. INDICATORS OF CASH IN CIRCULATION

Steady development of sectors of the economy, as well as an increase in the population's income, are resulting in an increase in the demand for cash and are contributing to growth in the emission of cash and an increase in the turnover of cash moving through the cash departments of second-tier banks.

Emission operations of the National Bank. In 2004 a total of 485.5 billion tenge was put into circulation from the National Bank's reserve funds, and 339.8 billion tenge was withdrawn from circulation. The emission result was positive and totaled 145.7 billion tenge, which is 72.8 percent more than in 2003.

The increase in the emission indicator is tied to the large volumes of cash issued in the second half of the year. In January cash in circulation fell by 11.3 billion tenge. This is a relatively small negative emission result, and the cash that was released at the end of 2003 remained in circulation, for the most part. From June through August the emission of cash totaled 50.2 billion tenge, which is 37 percent more than the emission during the summer of the previous year. A distinguishing feature of 2004 is the increase in cash in circulation in November, although in previous years withdrawal of cash typically occurred in this month.

In terms of the regional breakdown, all of the oblasts, with the exception of the city of Almaty, posted positive emission results. The oblasts with the highest emission figures are still those with a developed industrial production sector: East Kazakhstan Oblast (40.4 billion tenge) and Karaganda Oblast (42.3 billion tenge). A decline in the emission result compared to the indicator for the previous year was posted only in West Kazakhstan Oblast. An increase in the release of cash compared to 2003 was seen in Aktyubinsk Oblast, which is a trend carried over from the previous year, and an increase was also observed in Mangistau and South Kazakhstan Oblasts.

During 2004 the National Bank released into circulation 14 types of jubilee and memorial coins (Appendix 2 to Section IV).

Maintaining banknotes and coins of the national currency in good physical condition. In 2004 worn banknotes and defective coins valued at 58.2 billion tenge were withdrawn from circulation. Banknotes in the 5,000 tenge denomination accounted for the largest share of the withdrawals.

Banknotes and coins that are no longer legal tender are still being withdrawn from circulation. Banknotes valued at 327.9 million tenge were withdrawn from circulation during the year. Old-format banknotes in 1,000 and 2,000 tenge denominations accounted for most of the withdrawals (106.8 million tenge and 175.4 million tenge, respectively). As a result, 0.9 percent of the total number of these banknotes printed remained in circulation as of January 1, 2005.

Worn banknotes totaling 112.3 billion tenge that were no longer valid as legal tender were destroyed during the year.

Cash turnover at banks. Throughout the year the cash turnover at banks increased each month. The most significant increases occurred in March, June, and December; contributing to this were two holidays in March, the beginning of the vacation season in June, and in December the final execution of the expenditure side of the budget and the New Year holidays.

The indicators describing the turnover of cash through banks' cash departments illustrate that the volume of cash disbursed continues to rise at a faster rate than the amounts received by banks' cash departments.

The cash received by banks' cash departments totaled 3,138.0 billion tenge, which represents an increase of 37.7 percent compared to the previous year. The volume of cash disbursed grew by 43.2 percent to 3,350.6 billion tenge. As one can see from Appendix 1 to Section IV, an increase in turnovers occurred for practically all of the cash turnover items. The exceptions were cash disbursed to transportation and communications enterprises, which was also seen in the previous year, and cash disbursed to pay for agricultural products and to insurance organizations.

The ratio of the return of cash to banks' cash departments fell by 3.7 percentage points to 93.7 percent.

On the income side of cash turnover, the following receipts remain the dominant items:

- from the sale of goods, services, and work performed (30.6 percent);
- from the sale of foreign currency (22 percent);
- going to deposit accounts held by individuals, which almost doubled compared to 2003 (11 percent).

The following account for the bulk of cash disbursed from banks' cash departments:

- cash disbursed to pay for goods, services, and work performed (21.8 percent);
- cash disbursed from deposit accounts held by individuals (15.4 percent);
- cash disbursed to fill up automatic teller machines, which increased due to the rise in the number of users of payment cards, growth in the network of automatic teller machines, and higher average wages and benefits (13.7 percent).

The "loans made to individuals and legal entities" item accounts for the greatest increase, by a factor of more than 1.5, in the total amount of cash disbursed, which reflects increased lending to the public by banks.

The strengthening of the national currency is reducing the population's inclination to hold funds in foreign currency. As a result, there is an increase in receipts going to deposits held by individuals and, consequently, cash disbursed from these accounts is also increasing, taking the place of foreign currency sales to some extent. Furthermore, the increase in the population's income is helping to bolster confidence in borrowers, which is reflected in the increase in the amount of lending.

The volumes of cash received and disbursed under items that reflect the sale of goods, work, and services are the largest of all of the cash turnover items. These volumes, together with the rate of growth for these items, raise doubts about banks' compliance with legal requirements regarding the performance of noncash payments between legal entities that exceed 4,000 times the monthly reference indicator. In this connection, the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions is faced with the task of conducting inspections of banks to determine their compliance with the requirements of the legislation pertaining to this limit.

V. FINANCIAL MARKET

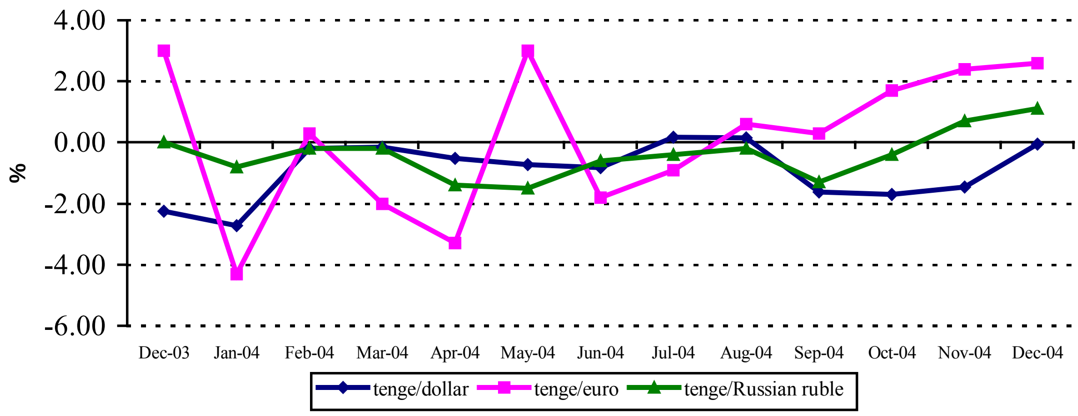
5.1. Foreign Exchange Market

The situation in the domestic foreign exchange market in 2004 was shaped by growth in receipts of export foreign exchange proceeds and borrowing by second-tier banks and the corporate sector in external markets, and it was also determined by conditions in the global foreign exchange market. Significant quantities of foreign currency entering the economy contributed to an increase in the transaction turnover both in the exchange and in the interbank market.

The weighted average exchange rate for the 12 months was 135.92 tenge to the dollar. The rate on the currency exchange at the end of the period was 130.00 tenge to the dollar. Since the beginning of the year the tenge strengthened against the U.S. dollar by 9.30 percent in nominal terms. The most rapid strengthening occurred in January and October (2.73 percent and 1.71 percent, respectively). During the year depreciation of the tenge was seen in July and August (0.17 percent and 0.16 percent).

The official exchange rate of the tenge against the euro and the Russian ruble also strengthened in 2004 by 5.3 percent and 1.7 percent, respectively.

Dynamics of the Exchange Rate of the Tenge against the U.S. Dollar, Euro, and Russian Ruble (% of previous month)



In 2004 the volume of exchange trades in the dollar position exceeded the same indicator of 2003 by 46.6 percent and reached US$9.3 billion.

The volume of transactions in the over-the-counter foreign exchange market increased by 20.2 percent to US$8.3 billion.

Transactions with Russian rubles and euros accounted for a negligible share of the turnover in the exchange and over-the-counter segments of the currency market. In the exchange market the volume of transactions with Russian rubles increased by a factor of 4.4 and reached 120.5 million Russian rubles. The volume of transactions with euros increased by a factor of 9.2 and reached 50.1 million euros. In the over-the-counter currency market the volume of conversion transactions with Russian rubles and euros increased by factors of 2.7 and 3.6 and reached 1,486.8 million Russian rubles and 102.9 million euros, respectively.

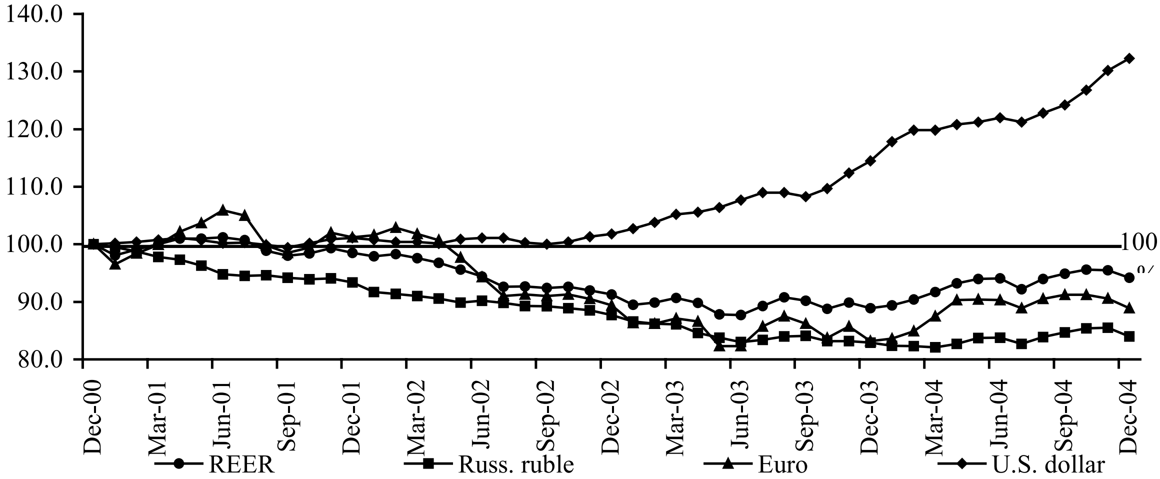
As in previous years, preference in the cash foreign exchange market was given to the U.S. dollar, and accordingly transactions involving the purchase of this foreign currency dominated this particular segment of the market. In 2004 the volumes of net sales of U.S. dollars at bureaux de change totaled US$2,661.9 million, which represents an increase of 16.9 percent compared to 2003.

The volumes of net sales of euros by bureaux de change increased by 44.1 percent to 397.5 million euros for the year. Purchases and sales of euros are negligible, however, and at the end of 2004, for example, these volumes were one-eighth of the volumes of dollar purchases and sales at bureaux de change.

The volumes of purchases and sales of Russian rubles by bureaux de change are practically the even, which can be explained by the predominance of the demand for this currency for tourist purposes and business travel expenses, rather than for savings.

The index of the real effective exchange rate (REER) of the tenge in December 2004 grew by 5.9 percent compared to December 2003. In 2004 the ***real strengthening of the tenge*** against the U.S. dollar was 15.3 percent, against the euro it was 7 percent, and against the ruble, 1.3 percent. In spite of the substantial upward trend in the strengthening of the tenge against the main currencies, on the whole the external competitiveness of Kazakhstani exports remained at a more favorable level than in 2001 and 2002.

Indices of Real Exchange Rates, % (December 2000 = 100%)



5.2. Interbank Money Market

In 2004 short-term borrowing in the interbank money market remained one of the main instruments for regulating the current liquidity of banks.

Given the strengthening of the tenge's exchange rate against the U.S. dollar, there was an increase in the level of banks' activity related to the placement of short-term tenge deposits. In 2004 the total volume of interbank deposits in the domestic currency that were placed rose by 27.0 percent compared to 2003 and reached 577.9 billion tenge. In December 2004 the weighted average interest rate on interbank tenge deposits that were placed fell from 2.78 percent to 2.10 percent, compared to December 2003.

Banks were very active in the interbank market in terms of the placement of deposits in euros, since with the weakening of the U.S. dollar investments in euros remained attractive. Deposits placed in euros totaled 5.0 billion euros, which is 3.5 times higher than the volume placed in 2003.

The opposite trend was seen in terms of dollar deposits. The placement of dollar deposits fell by 38.6 percent to US$26.9 billion, while the weighted average interest rate on the dollar deposits that were placed rose from 1.31 percent to 2.16 percent. In spite of the decline in the volume of deposits placed, however, in 2004 dollar deposits remained the main instrument in the interbank money market for short-term borrowing in foreign currency.

The volume of transactions involving other types of interbank borrowing in foreign currency was negligible.

5.3. Deposit Market

In 2004, against the backdrop of stable development of the financial sector, growth in the population's income, and the functioning of a deposit insurance system, the situation in the country's deposit market was favorable and was characterized by steady growth in the resource base of banks and credit unions due to the influx of money being placed in deposits by individuals and legal entities. In 2004 deposits of residents at deposit institutions grew by 71.2 percent to 1,255.4 billion tenge (the foreign exchange equivalent was more than US$9.6 billion). The ratio of residents' deposits in deposit institutions to GDP in 2004 compared to 2003 increased from 15.9 percent to 22.7 percent.

Deposits of legal entities more than doubled, totaling 814.3 billion tenge, while deposits of individuals grew by 31.5 percent to 441.2 billion tenge (Appendix 1 to Section V, Subsection 5.3, Figure 5.3.1).

An important element in the development of the deposit market in 2004 was the significant growth in domestic currency deposits given the increase in confidence in tenge-denominated instruments in connection with the strengthening of the tenge's exchange rate against the U.S. dollar. Tenge deposits increased by 84.6 percent to 715.7 billion tenge, while deposits in foreign currency increased by 56.2 percent to 539.7 billion tenge. As a result, tenge deposits as a proportion of total deposits grew from 52.9 percent to 57.0 percent (Appendix 1 to Section V, Subsection 5.3, Figure 5.3.2). Nevertheless, growth in deposits in foreign currency was significant, primarily due to deposits placed by legal entities.

Throughout 2004 the upward trend in the growth of deposits placed in banks by the population (including nonresidents) continued. The average monthly increase in deposits in 2004 was 8.7 billion tenge, compared to 7.2 billion tenge in 2003. As a result, deposits held by the population grew by 30.5 percent to 448.0 billion tenge, or by more than 3.4 billion tenge.

In terms of the structure of the population's deposits, the faster growth in tenge deposits compared to deposits in foreign currency is also viewed as a positive trend. Tenge deposits almost doubled on the year, while the population's deposits in foreign currency declined by 10.2 percent. As a result, the proportion of deposits held by the population in tenge increased from 37.5 percent to 57.0 percent.

In 2004 the weighted average interest rate on time deposits in tenge held by individuals fell from 10.9 percent to 9.3 percent, while the rate for foreign currency deposits declined from 5.9 percent to 5.6 percent (Appendix 2 to Section V, Subsection 5.3).

5.4. Credit Market

5.4.1. Credits to the Economy. Against the backdrop of favorable macroeconomic conditions and continuing growth of the resource base, the credit market remained one of the dynamically developing segments of the financial market in 2004. The volume of bank credits to the economy grew by 51.7 percent to 1,484.0 billion tenge (approximately US$11.4 billion). The ratio of bank credits to the economy to GDP grew in 2004 compared to 2003 from 21.2 percent to 26.8 percent.

The rise in the exchange rate of the tenge against the U.S. dollar became a major factor in the change in the structure of bank credits by type of currency. Credits in the domestic currency in 2004 grew by 64.0 percent to 714.0 billion tenge, while those in foreign currency increased by 41.9 percent to 769.9 billion tenge (US$5.9 billion). As a result, tenge credits as a proportion of the total increased from 44.5 percent to 48.1 percent.

Positive changes also occurred in 2004 in the structure of credits in terms of maturities, with growth in long-term credits (with maturities of more than 1 year) exceeding growth in short-term credits. Long-term credits increased by 60.3 percent to 975.4 billion tenge, while short-term credits increased by 37.5 percent to 508.6 billion tenge. Long-term credits as a proportion of the total increased from 62.2 percent to 65.7 percent (Appendix 1 to Section V, Subsection 5.4.1, Figure 5.4.1.1).

In spite of the fact that corporate customers continue to be the main borrowers in the credit services market, credits to enterprises as a proportion of the total volume of credits to the economy in 2004 fell from 87.5 percent to 79.5 percent, while the proportion of credits to individuals grew from 12.5 percent to 20.5 percent (Appendix 1 to Section V, Subsection 5.4.1, Figure 5.4.1.2). This is due primarily to the significant expansion of certain banking products, such as mortgage and consumer lending. In 2004 mortgage and consumer credits grew by a factor of 3.4 and 2.3, respectively, to reach a total of 99.4 billion tenge and 144.4 billion tenge, respectively.

In 2004 the volume of bank credits to small business grew by 47.0 percent to 288.4 billion tenge, or 19.4 percent of the total volume of credits to the economy.

The dynamics of credit rates were characterized by a gradual decline. In December 2004 compared to December 2003 the weighted average interest rate on credits in domestic currency to individuals fell from 20.3 percent to 19.5 percent, while the rate on credits to legal entities declined from 14.9 percent to 13.7 percent (Appendix 2 to Section V, Subsection 5.4.1).

5.4.2. Mortgage Lending. By the end of 2004 the total volume of mortgage credits issued by second-tier banks reached 99.4 billion tenge, which represents an increase by a factor of 3.4 for the year. As a result, mortgage credits as a proportion of the total volume of credits issued by banks to individuals reached 32.7 percent, as opposed to 24.2 percent in 2003.

Mortgage credits in domestic currency in 2004 increased by 70.0 percent to 11.4 billion tenge, while those in foreign currency almost quadrupled to 87.9 billion tenge. As a result, credits in foreign currency as a proportion of the total increased from 77.2 percent to 88.5 percent.

In 2004 “Kazakhstan Mortgage Company” (KIK) JSC acquired mortgage housing credits in the amount of 22 billion tenge, and since the launching of the mortgage lending program it has acquired credits in the amount of 31 billion tenge. The balance of loan debt as of January 1, 2005 on 14,145 credits increased by a factor of 3.3 to 26 billion tenge, while the plan called for 17.5 billion tenge.

KIK’s bank partners are 8 banks and 2 financial institutions performing certain types of banking operations, which are located in all of the regions of the Republic. In 2004 agreements were signed for joint cooperation under the KIK program with “Temir Bank” JSC, “Kazkommertsbank” JSC, and “Halyk Bank of Kazakhstan” [Narodny Bank Kazakhstana] JSC.

Credits offered under the KIK program as a proportion of the total volume of mortgage lending are increasing (Appendix 1 to Section V, Subsection 5.4.2, Table 5.4.2.1). In December 2001 they accounted for just 2 percent of the total volume of mortgage credits, in December 2002 this figure was 13 percent, and in October 2004 it had reached 29 percent. A further increase in the market share of KIK is expected in the future as a result of an increase in the number of partner banks and the volume of credits purchased under the State Program for the Development of Housing Construction for 2005–2007.

The volume of bonds placed totaled 26 billion tenge at the end of the year, including 19 billion tenge placed in 2004 (an increase of 171 percent compared to 2003). This program for the placement of mortgage bonds is unique and one of the most progressive in the CIS. Investor demand for KIK bonds, as a rule, significantly exceeds supply, which points to increased activity among institutional financial organizations, such as second-tier banks, pension funds, and insurance organizations (Appendix 1 to Section V, Subsection 5.4.2, Figure 5.4.2.2).

Against the backdrop of the development of market approaches, KIK proceed to the implementation of the State Program for the Development of Housing Construction for 2005–2007, the main goal of which is to complete 12 million square meters of affordable housing using progressive forms of lending.

In 2004 the National Bank placed KIK shares under trust management with the Ministry of Finance and measures are being undertaken to sell KIK shares to the Ministry of Finance.

5.5. Government Securities Market

The government securities market is continuing its active development within the country’s financial market. The main issuers, the Ministry of Finance and the National Bank, are in pursuit of different goals in issuing their securities. The main goal of the Ministry of Finance in issuing government securities is to finance the republican budget deficit. The goal of the National Bank in issuing notes is to regulate the liquidity of second-tier banks.

Recently a situation has developed in which budget receipts generated from taxes, due to a substantial increase in export foreign exchange earnings resulting from higher prices for energy resources in the world market, have reduced the need to use government securities issues to cover the budget deficit.

On the other hand, the significant influx of foreign currency is forcing the National Bank to increase its issue of notes to sterilize the excess liquidity, which leads to significant expenses for the National Bank associated with servicing these notes.

Under these conditions, with a view to preventing a rise in inflation, the National Bank and the Ministry of Finance need to work more closely to coordinate their actions in the area of issuing securities in order to solve problems related to sterilization of excess liquidity.

One of these problems was caused by the fact that pension savings funds, given a shortage of long-term government securities issued by the Ministry of Finance, invested heavily in short-term notes. This led to a weakening of the effect of the National Bank's monetary policy on bank liquidity. Under these conditions, the Ministry of Finance is planning in 2005 to issue a new financial instrument, government long-term treasury savings bonds (MEUZhKAM), intended for placement among pension savings funds, which will ease the urgency of this problem somewhat.

The following situation took shape in the Ministry of Finance government securities market in 2004 as a whole.

In 2004 the volume of government securities placed compared to 2003 grew by 20.1 percent to 126.2 billion tenge. During the year the Ministry of Finance placed 3-month, 6-month, and 12-month MEKKAM bonds, as well as all types of medium-term treasury bonds, with the exception of 3-year and 9-year MEOKAM bonds. Actual demand for these bonds exceeded the established supply by a factor of 1.8 on average.

The qualitative development of the government securities market that was launched the previous year continued throughout 2004. Medium-term instruments with maturities of more than 5 years were issued, with the exception of 9-year MEOKAM bonds: 6-year, 7-year, 8-year, and 10-year MEOKAM bonds were issued.

In addition, the Ministry of Finance revised the structure of government securities in terms of their maturities and on September 8, 2004 the Rules for the Issue, Placement, Circulation, Servicing, and Redemption of Government Treasury Bonds of the Republic of Kazakhstan were approved pursuant to Government Resolution No. 941; according to these rules the following types and maturities of treasury bonds are to be established since January 1, 2005:

- short-term treasury bonds (MEKKAM) with maturities of 3, 6, 9, and 12 months;

- medium-term treasury bonds (MEOKAM) with maturities of more than 1 year and up to 5 years;

- long-term treasury bonds (MEUKAM) with maturities of more than 5 years;

- medium-term indexed treasury bonds (MOIKAM) with maturities of more than 1 year and up to 5 years;

- long-term indexed treasury bonds (MUIKAM) with maturities of more than 5 years;

- long-term treasury savings bonds (MEUZhKAM) with maturities of more than 5 years.

The placement of government securities increased on the year by 20.1 percent, and this was accompanied by a reduction in the number of auctions held (from 35 to 28), which was due to an increase in the volume of treasury bonds placed at a single auction.

The issue of Ministry of Finance government securities in 2004 in excess of their redemption in 2004 (a net emission of 54.6 billion tenge) led to a 41.1 percent increase in the volume of these securities in circulation (to 229.5 billion tenge). The Ministry of Finance did not perform any early redemptions in 2004.

Short-term 3-month and 6-month MEKKAM bonds went out of circulation, as well as 24-month MEIKAM bonds. On the whole, the structure of securities in circulation as of December 31, 2004 appears as follows: short-term MEKKAM bonds (only 12-month bonds) account for 9.2 percent of the total, medium-term MEOKAM bonds (with maturities of between 2 and 10 years) account for 89.6 percent, and medium-term MEIKAM bonds (with maturities of between 3 and 7 years) account for 1.2 percent.

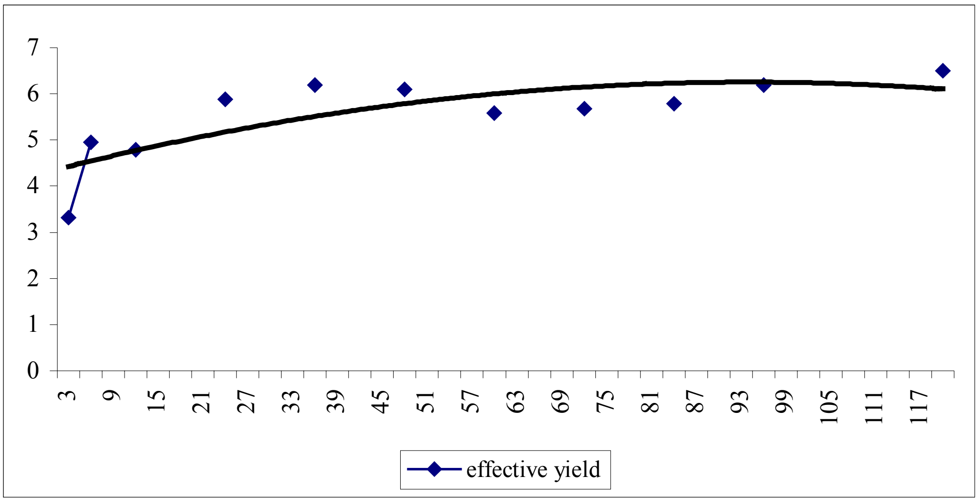
A broad spectrum of instruments in the government securities market will provide a reliable reference point for returns of investors and will broaden their investment opportunities.

Indicators of the return on financial transactions are the most important indicators in the financial market. They tell issuers and creditors the price of borrowing funds, they allow participants to make decisions about selling and buying credit resources, and they also provide an assessment of the financial consequences of carrying out such decisions. Factors that influence the setting of interest rates (determinants) are the long-term economic growth rate, inflationary expectations, the duration of loans, the nature of the distribution of payments over time, and various risks.

In 2004 indicators of the return on financial transactions in the government securities market were characterized by a downward trend. For example, the yield on 12-month MEKKAM bonds fell from 5.10 percent to 4.79 percent, the yield on 5-year MEOKAM bonds dropped from 6.18 percent to 5.58 percent, the yield on 6-year MEOKAM bonds went from 6.19 to 5.68 percent, the yield on 7-year MEOKAM bonds fell from 6.19 percent to 5.78 percent, and the yield on 8-year MEOKAM bonds declined from 6.30 percent to 6.19 percent (based on the last auctions). The yield on the other types of securities remained at the previous level and was as follows: 3.32 percent on 3-month MEKKAM bonds, 5.88 percent on 2-year MEOKAM bonds, 6.09 percent on 4-year MEOKAM bonds, and 6.50 percent on 10-year MEOKAM bonds.

The following graph illustrates the yield curve for government securities as of January 1, 2005.

Yield Curve for Government Securities as of January 1, 2005



It was constructed on the basis of data from the last auctions for each type of security. For the most part, it includes auctions held in 2004, with the exception of the auction of 3-year MEOKAM bonds, which took place in October 2003.

The yield curve illustrates two circumstances: first, there is a certain discrepancy among interest rates by maturities, and second, the market anticipates a further decline in rates on short-term securities.

Furthermore, all of the interest rates are negative in real terms, which creates problems for financial institutions whose assets contain large quantities of government securities.

VI. PAYMENT SYSTEMS

The positive assessment of Kazakhstan's payment systems by international financial institutions such as the International Monetary Fund, the World Bank, and the Bank for International Settlements, and the determination that they are in compliance with international principles and standards, have meant a qualitatively new stage in cooperation between the National Bank and these institutions within the context of further enhancement of the payment systems infrastructure.

In 2004 representatives of the National Bank, within the framework of the Bank for International Settlements International Working Group for the Development of the Payment Systems Infrastructure, took part in the drafting of recommendations for central banks regarding further improvement of existing payment systems.

This past year the National Bank, in conjunction with the Kazakhstan Center for Interbank Settlements Republican State Enterprise (KCIS), held an international seminar in the city of Almaty for representatives of central banks of CIS and Baltic countries, which was attended for the first time by managers and leading experts of divisions dealing with payments from the Bank for International Settlements, the World Bank, and the National Bank of Switzerland. In the course of the seminar the World Bank presented a new project for cooperation and interaction with central banks of CIS countries aimed at the development of payment systems. The project entails an assessment by the World Bank of payment systems functioning in CIS countries and the drafting of recommendations for their development and improvement.

The recognition of Kazakhstan's payment systems in the world arena means that the National Bank has an additional responsibility to maintain the functioning of the payment systems at a high level, taking into account constantly changing requirements for the safe and efficient performance of payments and money transfers. In this connection the National Bank presented proposals for making additions to the Republic's legislative acts with regard to defining the authorities to oversee (monitor) the functioning of payment systems, as well as compliance by second-tier banks and institutions performing certain types of banking operations with the requirements of regulatory legal acts of the National Bank in the area of effecting payments and money transfers. In view of the experience of central banks of European Union countries, in 2004 a great deal of attention was devoted to organizational issues related to assigning functions involving the oversight (monitoring) of the functioning of payment systems (including the need to establish a separate subdivision). Within the framework of efforts to bring Kazakhstan's payment systems closer into line with European Union standards, this past year work was launched in conjunction with the Kazakhstan Association of Financiers to reform the structure of bank accounts assigned by second-tier banks to their customers.

Based on the experience of the leading central banks of European countries, and taking into consideration the suggestions of second-tier banks, a new payment instrument has been introduced as part of the KCIS clearing system – the electronic debit notice, the distinguishing feature of which is the ability by the bank receiving the money to present it directly for payment. With a view to establishing a legislative basis for the use of this instrument in payment systems, in 2004 the relevant additions were made to the regulatory document of the National Bank governing the procedure for the functioning of the KCIS clearing system.

This past year was also characterized by more active efforts by the National Bank to develop cooperation not only with the central banks of CIS countries in general, but also with their separate subdivisions whose functions cover issues related to payment systems, and also with commercial banks. With a view to sharing information pertaining to payment systems issues on a regular basis, a draft Agreement on Cooperation Between Payment Systems Subdivisions of the Central Bank of the Russian Federation and Payment Systems Subdivisions of the National Bank of Kazakhstan was prepared, which has been sent to the Central Bank of the Russian Federation for review. Within the context of expanding business ties and establishing contacts with Russian banks, the Kazakhstan Association of Financiers and the Association of Russian Banks participated in a number of conferences on payment systems issues that were organized in the city of Almaty.

In addition to the measures described above, heightened attention was given to developing the payment card market in Kazakhstan. Specifically, work was done to ensure the continuous functioning of automatic teller machines and the assessment of their actual technical condition. Work was undertaken to establish a national payment card. Kazakhstan Post Joint-Stock Company [Kazpochta AO] took part in a pilot project, together with the National Processing Center Joint-Stock Company. The "KazCard" national payment card is intended to become an efficient payment instrument for the performance of noncash settlements within the country; it is aimed at the broadest segments of the population and is intended to cover the market for small payments in retail trade.

The expansion of noncash payments using payment cards is one of the top priorities for the National Bank. In 2004 the National Bank forwarded to the government proposals concerning amendments and additions to a number of regulatory documents. With a view to stimulating the development of the infrastructure for the payment card market, Government Resolution No. 707 of June 25, 2004 was adopted, in accordance with which equipment for the servicing of payment cards was included in the List of Fixed Assets Imported by a Lessor for Placement under Financial Leasing Contracts Whose Importation Is Exempt from the VAT.

With a view to expanding noncash payments in the trade and services sphere, Government Resolution No. 1328 of December 15, 2004 "On Approval of Categories of Trade (Service) Organizations Required to Accept Payments Using Payment Cards When Performing Commercial Transactions (Providing Services) on the Territory of the Republic of Kazakhstan" was adopted.

In order to improve the procedure for the payment of wages from the state budget through the transfer of money to employees' card accounts opened at banks, Government

Resolution No. 30 of January 12, 2004 “On Amendments and Additions to Republic of Kazakhstan Government Resolution No. 1464 of September 28, 1999 ‘On Measures to Improve the Procedure for the Payment of Wages, Stipends, Pensions, Benefits, and Other Monetary Payments at the Expense of the State Budget’” was adopted.

Overall, given the continuing favorable trends in the country’s economic development, there has been an increase in the number and volume of payments effected through Kazakhstan’s payment systems.

In 2004 the number of payments made through Kazakhstan’s payment systems (the Interbank Money Transfer System and Interbank Clearing) increased by 35.7 percent to 17.4 million transactions, and the value of the payments grew by 34.1 percent to 30.0 trillion tenge.

6.1. Interbank Money Transfer System (IMTS). As of January 1, 2005 a total of 52 users were registered in the IMTS.

In 2004 the number of payments increased by a factor of 1.7 to 6.2 million transactions, and the value of the payments grew by 34.8 percent to 29.1 trillion tenge.

The growth in the volume of payments in the IMTS was due primarily to a 42.3 percent increase in the volume of payments on transactions with residents’ securities, a 65.9 percent increase in deposit transactions, as well as a 42 percent increase in the volume of payments for goods and intangible assets. The change in payments on these types of transactions accounted for 83.2 percent of the total change in the volume of payments in the IMTS for the year.

At the same time, the IMTS, which is oriented toward effecting high-priority payments for large sums, is fulfilling its mission: of the total volume of noncash payments effected through payment systems, the IMTS accounts for 35.6 percent of the total number of payments and 96.9 percent of the total volume of payments. Payment documents in amounts in excess of 100 million tenge account for 71.5 percent of the total payments in the IMTS.

6.2. Interbank Clearing

As of January 1, 2005 a total of 32 participants were registered in the Interbank Clearing system.

A total of 11.2 million payment documents with a total value of 942.8 billion tenge were processed in the system in 2004. Compared to 2003 the number of payment documents in this system increased by 22 percent, and the value of payments by 15.4 percent.

Growth in tax and other mandatory payments to the budget and payments from the budget (by 23.2 percent), in payments for goods and intangible assets (by 27.8 percent) and services provided (by 12.4 percent), and transfers of mandatory pension contributions (by 32.0 percent), as well as a decline in the volume of deposit transactions by 42.7 percent, contributed to the 15.4 percent increase in clearing payments. The change in these types of payments accounted for 94.9 percent of the overall change in the volume of payments in the system for the year.

The bulk of retail payments went through Interbank Clearing. This system accounted for 64.4 percent of the total number of noncash payments, representing 3.1 percent of the total volume of these payments. Payment documents in amounts of less than 10,000 tenge accounted for the bulk of these payments (65.4 percent of the total number of payment documents).

6.3. Payment Instruments

In 2004 second-tier banks and Kazakhstan Post Joint-Stock Company performed 63.3 million transactions valued at a total of 33.4 trillion tenge. Compared to 2003 the number of various payment instruments used increased by 30 percent, and the value of payments increased by 53.6 percent (Appendix 1 to Section VI, Subsection 6.3).

Payment orders and payment cards are the instruments used most commonly on the territory of Kazakhstan.

Payments effected by means of payment orders accounted for 40.9 percent of the total number of payments in 2004 and for 96.7 percent of the total volume of payments. The average value of a payment order was 1.2 million tenge, which was an increase of 15.2 percent.

The high proportion of transactions using payment cards (57.9 percent) and the low volume of payments (1.7 percent of the total) is due to the use of this payment instrument primarily for the withdrawal of small sums of cash (the average amount of a cash withdrawal transaction was 15,700 tenge).

Bills of exchange, payment request-orders, bank account direct debit, checks to pay for goods and services, and collection orders are used the least frequently.

Growth in the total number of payment instruments was due mainly to an increase in the number of payment orders by 6.7 million transactions and the number of transactions using payment cards by 7.9 million transactions. Growth in the volume of payments was due to an increase in the amount of payments using payment orders by 11.5 trillion tenge.

Payment cards. Kazakhstan's payment card market has expanded significantly and strengthened its positions over recent years. The number of banks issuing and servicing payments cards of both local and international payment systems is growing steadily. For example, as of January 1, 2005, 21 second-tier banks and Kazakhstan Post Joint-Stock

Company are licensed to issue payment cards, and 19 banks are actually issuing them. Last year only 17 of the 20 second-tier banks licensed to issue payment cards actually issued any.

Second-tier banks are issuing payment cards of the following local systems: Altyn Card – People's Bank of Kazakhstan Joint-Stock Company and ATFBank Joint-Stock Company; SmartAlemCard – TuranAlem Bank Joint-Stock Company; the local card of Citibank Kazakhstan Joint-Stock Company; Duet – Valyut-Transit Bank Joint-Stock Company; Caspian – Caspian Bank Joint-Stock Company; and the local card of Cessnabank Joint-Stock Company. In addition, Kazakhstani banks are issuing cards for the international systems Europay International and VISA International, and they distribute cards for the American Express International and Diners Club International systems, and DB Alfa-Bank Open Joint-Stock Company distributes Europay International Cards.

Currently in Kazakhstan there is on average one payment card for every six people. As of January 1, 2005 second-tier banks had issued 2.36 million payment cards, which is 22.3 percent more than the previous year. The number of payment cardholders increased by 20 percent on the year to 2.27 million, which represents 15.1 percent and 29 percent of the country's total population and economically active population, respectively.

The volume of transactions performed using payment cards of Kazakhstani issuers increased in 2004 by 42.9 percent to 566.1 billion tenge. One should mention here that the volume and number of noncash payments are growing more rapidly (by 66.3 percent to 24.2 billion tenge and by a factor of 2.2 to 2.1 million transactions, respectively) than are the volume and number of cash withdrawal transactions (by 42.0 percent to 541.9 billion tenge and by 24.2 percent to 34.6 million transactions, respectively).

Against the backdrop of the development of the payment card market, the payment card network being serviced is undergoing further expansion. For example, as of January 1, 2005 there were 2,354 commercial establishments in Kazakhstan that accept payment cards for payment, which is 7.8 percent more than at the same time the previous year. The number of automatic teller machines has increased by 28.5 percent to 1,124, as a result of the growth in the total number of cards in circulation and the number of cardholders. There was a slight decline in the number of POS terminals, which fell by 0.1 percent to 4,211 units, and the number of imprinters fell by 19.2 percent to 1,611 units. The reduction in the number of imprinters was tied to the updating of equipment by banks, and the withdrawal of outdated imprinters from use and their partial replacement with POS terminals.

VII. REGULATORY ACTIVITY

With a view to improving the legislation, work is continuing on regulatory legal acts governing key issues such as foreign exchange regulation and controls, payments and money transfers, and accounting and reporting practices of financial market entities.

In 2004 the National Bank prepared three draft laws which are currently being reviewed by Parliament:

1) "On Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on the Activities of Government Bodies Responsible for Regulation of the Financial Market";

2) "On Amendments to the Republic of Kazakhstan Law 'On Licensing' Pertaining to Foreign Exchange Regulation and Foreign Exchange Controls";

3) "On Foreign Exchange Regulation and Foreign Exchange Controls."

Presidential Decree No. 1495 of December 10, 2004 "On Amendments and Additions to Certain Presidential Decrees of the Republic of Kazakhstan," governing issues related to further improvement of the system of government administration in the Republic, as well as the structure of the National Bank, entered into force.

A total of 33 regulatory legal acts of the National Bank were registered with the Ministry of Justice, concerning:

- the performance of cash transactions with legal entities and individuals at branch offices of the National Bank;

- determination the validity of banknotes and coins of the Republic's domestic currency;

- financial reporting by second-tier banks, credit unions, mortgage companies, insurance (reinsurance) organizations and insurance brokers, organizations performing brokerage and dealer activities in the securities market, reporting by organizations involved in maintaining the system of registries of holders of securities, reports on the structure of the securities portfolios of second-tier banks and investments by second-tier banks in the capital of other legal entities;

- the performance of transactions at the National Bank in foreign currency surrendered to (received by) the state on various grounds;

- the Investment Strategy for the management of the National Bank's gold and foreign exchange reserves;

- the accounting of insurance and reinsurance transactions in the “general insurance” sector;

- the procedure for the rediscounting of bills of exchange by the National Bank;

- the setting and application of rates for National Bank operations;

- the accounting of exchange transactions with foreign exchange cash performed on the basis of a license issued by the National Bank;

- information that should be contained in a statement from a customer’s personal account concerning the movement of funds on the customer’s balance accounts;

- the granting of a license to issue payment cards to institutions performing certain types of banking operations;

- Accounting Standard 33 “Accounting and Disclosure of Information about Brokerage Transactions”;

- the functioning of the National Interbank Payment Card System based on microprocessor cards;

- the procedure for inspecting the activities of clearing organizations – institutions performing certain types of banking operations, and so on.

In addition, amendments and additions were made to regulatory legal acts of the National Bank governing:

- the organization of export-import foreign exchange controls;

- the use of payment cards and the performance of noncash payments and money transfers;

- the performance of clearing in the Republic;

- the application of the State Classification of the Republic of Kazakhstan – the uniform classification of the purpose of payments;

- the limit on payments on correspondent accounts of second-tier banks and institutions performing certain types of banking operations;

- correspondent relations among second-tier banks of the Republic of Kazakhstan, among second-tier banks and institutions performing certain types of banking operations, between the National Bank and second-tier banks, and also institutions performing certain types of banking operations;

- determination of the market exchange rate for currencies;

- organization and performance of inspections pertaining to foreign exchange legislation issues;

- rescheduling of debt owed by banks and other institutions to the National Bank on loans made to them;

- requirements for paper used for bills of exchange, manufactured within the Republic or imported into the country, and so on.

With a view to developing and improving the regulatory base of the National Bank as it pertains to the introduction of information technology standards, a number of documents have been approved concerning the administration and maintenance of an integrated automated information system.

During the year 90 draft regulatory legal acts and resolutions of the government were reviewed and opinions were issued on them; they dealt with the identification of a borrower bank to provide lending for agricultural production, the purchasing of financial services by government enterprises and organizations, the Program to Develop the Insurance Market and the Securities Market, operations involving financial instruments performed by the State Social Insurance Fund, the circulation of government treasury bonds, approval of the report on the formation and use of the National Fund, the Postal Savings System Program for 2005–2010, the sale of housing built by local executive government bodies as part of the state program to develop housing construction for 2005–2007, the program to combat legal offenses in the economic sphere, the registration and accounting of government and government-guaranteed loans, and so on.

VIII. INTERNATIONAL COOPERATION AND PUBLIC INFORMATION ACTIVITY BY THE NATIONAL BANK

8.1. International Cooperation

In 2004 the National Bank's international activity was determined in large part by the need for further strengthening of cooperation with countries in the far abroad, the CIS, and the Baltic countries, as well as international financial institutions.

Cooperation with countries in the far abroad. The 5th meeting of the Belgian Subgroup was held in June 2004, in conjunction with the World Bank and the International Monetary Fund, and it was attended by representatives of the financial sector from various countries, as well as the International Monetary Fund, the World Bank, the central banks of Belgium, the Czech Republic, Hungary, Luxembourg, Slovakia, Slovenia, Turkey, and Kazakhstan, in addition to representatives of oil companies. The situation in the world energy markets was discussed, with special emphasis on the extraction, distribution, and consumption of oil; there was also discussion of the structure of financial oversight and the role of central banks in monitoring and maintaining financial stability. Issues were raised concerning the effect of high oil prices, Kazakhstan's oil sector in general, the financial stability of the European Union, and the development of Kazakhstan's financial system and monetary policy.

Efforts to expand financial cooperation with China were undertaken in conjunction with ministries and departments. In December 2004 the first meeting of the Kazakhstan-China Subcommittee on Financial Cooperation was held, during which the expansion of banking cooperation and its impact on the dynamics of the foreign trade turnover were discussed.

Cooperation with CIS and Baltic countries. The International Conference "Integration of the Financial Systems of the CIS and Baltic Countries" was held in October 2004, and the participants discussed problems and prospects for the integration of the financial markets of the CIS and Baltic countries, as well as the principles and methods of international financial reporting standards in the banking sphere.

Within the framework of the 3rd meeting of the Subcommittee on Interbank and Investment Cooperation between the Republic of Kazakhstan and the Russian Federation in May 2004, problems related to cooperation in the development of the banking systems and financial markets of the two countries were discussed, in addition to the possibility of harmonization of the legislation governing foreign exchange relations, the banking sector, and the securities market.

In the course of the 4th meeting of the Subcommittee in November 2004 a number of issues were discussed concerning the fostering of favorable conditions for cooperation among banks in Russia and Kazakhstan: the setting of mutual limits for documentary and treasury transactions between the banks of the two countries, the establishment of an information field in the area of financial and economic cooperation, an increase in the volume of transactions in the national currencies of the two countries, mutually beneficial cooperation between Roseximbank Closed Joint-Stock Company and banking institutions in the Republic in the area of providing support for Russian and Kazakhstani producers of products for export, improvement of the two countries' legislation on the securities market, including that pertaining to the disclosure of information by the nominal holders of securities about the ultimate owners of securities, and the activities of foreign investment funds in Russia and Russian investment funds abroad, among other issues.

The 8th meeting of the intergovernmental commission of the Republic of Kazakhstan and the Russian Federation on economic cooperation was held in October 2004, during which there was discussion of issues pertaining to the functioning of authorized Kazakhstani institutions performing certain types of banking operations (bureaux de change) within the town of Baikonur and the settlement of mutual financial claims related to the internal foreign exchange debt owed by the former USSR to legal entities and individuals. Based on the outcome of the meeting, the Parties agreed to make amendments and additions to the Agreement between the Republic of Kazakhstan and the Russian Federation on the Status of the Town of Baikonur and the Procedure for the Formation and Status of its Executive Government Bodies of December 23, 1995, with regard to the resolution of banking issues, and also to continue working on the settlement of mutual financial claims and claims on accounts of the USSR Vneshekonombank [Foreign Economic Bank].

Cooperation within the framework of integration associations. During the year the Council of Governors of Central (National) Banks of EurAsEC Member States continued its work.

The Agreement on Cooperation in the Training of Personnel of Central (National) Banks of EurAsEC Member States was signed in March 2004, and the Agreement on Standardization of the Procedure for the Opening of Accounts by Residents of One EurAsEC Member State at Banks of Another EurAsEC Member State for Servicing the Activities of their Representative Offices was signed in June 2004.

With a view to establishing a common interstate securities market, the Agreement on Cooperation in the Securities Market was signed at a meeting of the Interstate Council of the EurAsEC in June 2004, in accordance with which measures have been identified to protect the interests of investors in the securities market, to establish a common data base for interstate securities markets, and to ensure "equal access to it by the parties." The Treaty on the Status of the EurAsEC Principles of Legislation and the Procedure for their Development, Adoption, and Implementation was also signed, in accordance with which government bodies of the parties are to monitor compliance with the principles of legislation through the performance of expert legal reviews of draft legislative and other regulatory legal acts with the aim of verifying their compliance with the principles of legislation of the EurAsEC.

The Report on the Analysis of Medium-Range Programs for the Socio-Economic Development of EurAsEC Member States and Recommendations for the Coordination of Conditions for the Development of the Economies and Actions of EurAsEC Member States in the Implementation of Economic Reforms over the Medium Term were drafted and are in the approval stage, in addition to the Conceptual Framework for Cooperation in the Foreign Exchange Sphere and the Procedure for the Coordination of the Main Macroeconomic Indicators of Economic Development.

Work was done under the auspices of the CIS Executive Committee. In September 2004 the Conceptual Framework for Cooperation and Coordination of the Activities of CIS Member States in the Foreign Exchange Sphere was approved pursuant to a decision by the CIS Council of Heads of Government. Work was continued under the Plan for the Implementation of the Most Important Measures Aimed at Developing and Increasing the Effectiveness of Cooperation among CIS Member States in the Economic Sphere in 2003–2010.

Within the framework of meetings of the High-Level Group and working groups of experts in monetary policy, foreign exchange regulation and controls, macroeconomic indicators, and issues involving the movement of capital and investments, a number of documents were drafted that form the regulatory legal base for the Common Economic Space.

With the participation of National Bank representatives, work was done on drafting the Agreement on the List of Main Macroeconomic Indicators, the Agreement on the Mechanism for Monitoring the Implementation of Measures to Bring the Macroeconomic Indicators of Member States of the Common Economic Space into Alignment, the Agreement on Common Approaches to the Implementation of Monetary and Foreign Exchange Policy, the Agreement on the Mechanism for Monitoring the Implementation of Measures to Standardize Statistical Methodology and to Coordinate Government Statistical Authorities, the Agreement on Principles for Foreign Exchange Regulation and Foreign Exchange Control Policy, and the Agreement on the Harmonization of Norms for the Transport of Foreign Exchange by Individuals Crossing Borders between Member States of the Common Economic Space.

In September 2004 the Council of Heads of Government approved the establishment of the Development Fund of the Shanghai Cooperation Organization (SCO). During the year the National Bank worked actively on the development of a mechanism for the establishment and functioning of the SCO Development Fund. Draft charter documents outlining the principles for the functioning of the Fund were prepared and submitted to the parties for their review.

Work continued on the settlement of the debt of former USSR states based on the results of trade and economic relations in 1992–1993 (before and after the transition to correspondent accounts). Representatives of the National Bank took part in a meeting of experts on debt settlement issues, together with representatives of the Republic of

Azerbaijan, the Republic of Belarus, and Georgia, and a decision to submit this issue to the Heads of State for consideration was adopted based on the outcome of this meeting.

A meeting of the interagency commission on the inventory of international treaties concluded by the Republic of Kazakhstan from 1991 through 1995 was held in February 2004, and as a result treaties whose terms have been fulfilled were renounced.

Technical assistance. In May 2004 representatives of the National Bank took part in a meeting of Technical Assistance Coordinators in the city of Basle, Switzerland; based on the results of the meeting, a report was prepared on the accords that were reached with regard to arranging for further practical training and seminars for National Bank employees.

In March 2004 a meeting was held between representatives of the Cash Transactions and Safe Deposit Center of the National Bank and representatives of the Central Bank of the Netherlands, during which practical recommendations were offered regarding the circulation of cash and rules for the accounting, storage, and handling of cash at central banks.

Work was done related to the drafting and signing in December 2004 of a Memorandum of Understanding between the National Bank and the Asian Development Bank with regard to providing technical assistance in financial sector management.

A number of meetings were held with the participation of interested government bodies and USAID representatives regarding a Memorandum of Understanding between the Republic of Kazakhstan government and the government of the United States of America under the Kazakhstani-American Program for Economic Cooperation. During the course of these meetings there was discussion of attracting a grant under this Program to improve the activities of the National Bank in the area of monetary policy.

Cooperation with international financial institutions. In 2004 the National Bank completed the use of a line of credit provided by the EBRD.

In connection with the government's decision to attract a loan from the Islamic Development Bank for the "Rural Water Supply in Karaganda Oblast in Kazakhstan," a commitment letter was prepared that establishes the relevant loan payments.

Work was done on meeting the Republic of Kazakhstan's obligations to pay subscriptions to the authorized capital of international financial institutions. An acceptance certificate was signed with the Ministry of Finance for bills of exchange issued against subscriptions to the authorized capital of international financial institutions.

Work was done on the issue of the Republic of Kazakhstan's ratification of the Articles of Agreement of the International Monetary Fund.

8.2. Public Information Activity of the National Bank

The following periodicals of the National Bank were published: the Bulletin of the National Bank, the Statistical Bulletin, the Balance of Payments, the Economic Survey, and the Annual Report (in Kazakhstani and Russian). The quarterly Inflation Survey has been posted on the National Bank's website since the beginning of 2004.

With a view to explaining the key elements of the National Bank's monetary policy, 525 announcements were placed in the domestic and foreign mass media, including 159 on television, 50 on the radio and in news bulletins of Kazakh Radio, and 224 in the press, including 14 in the foreign mass media and 92 on news agency wires. In connection with the spinning off of the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions from the National Bank, the total number of announcements fell by 43 percent.

Four pages ran in the newspapers *Yegemen Kazakhstan* and *Kazakhstanskaya Pravda* under the heading "The National Bank Informs, Explains, Comments" (with 20 articles and interviews).

A total of 17 press conferences were held, including one joint press conference with the State Mortgage Credit Guarantee Fund, one with the State Pension Savings Fund, and one with the National Processing Center and Kazakhstan Post.

Thirty press releases were distributed and 26 public relations events were launched by the National Bank in the cities of Astana and Almaty and in various regions of Kazakhstan, including meetings with students, representatives of second-tier banks, and financial officers from large and medium-sized enterprises; as well as professional mastery competitions among bank tellers, open houses, exhibits of rare historical materials, documents, and coins, and so on.

Kazakhstani and Russian mass media that carry reports on Kazakhstan's financial sector and banking system were monitored and 15,352 reports and stories were analyzed.

IX. IMPROVEMENT OF ACCOUNTING AND FINANCIAL REPORTING

The National Bank has retained the functions of regulating the accounting and financial reporting system at financial institutions through the adoption of regulatory legal acts, in spite of the establishment of the independent Agency for the Regulation and Supervision of the Financial Market and Financial Institutions. The National Bank continues to control observance of the requirements of the legislation on accounting and financial reporting and accounting standards by financial institutions.

In 2004 work continued on improving the automation of accounting at second-tier banks, insurance (reinsurance) organizations, and pension savings funds. For example, individual control measures were approved for the maintenance of ancillary accounting records and the Main Ledger that had been incorporated into the automatic information system of the Housing Construction Savings Bank of Kazakhstan Joint-Stock Company, insurance (reinsurance) organizations, and pension savings funds. In addition, in 2004 seven second-tier banks made the change to international accounting standards with regard to automation of the banking information system, and nine banks still need to make the change to these international standards.

According to the Rules for the Identification of Organizations Whose Financial Statements Are Compiled in Accordance with International Financial Reporting Standards as of January 1, 2003 (Government Resolution No. 119 of February 3, 2002), organizations that are regulated and supervised by the National Bank have been compiling financial statements in accordance with the requirements of international financial reporting standards since January 1, 2003. In connection with this, in 2004 the National Bank worked on carrying out the process of converting financial market participants to international financial reporting standards. Specifically:

- financial reporting forms were approved for the following financial market participants: second-tier banks, insurance (reinsurance) organizations, insurance brokers managing an investment portfolio, organizations maintaining the system of registries of holders of securities, organizations engaged in the investment management of pension assets, pension savings funds, organizations engaged in transfer-agency activities, organizations engaged in brokerage and dealer activities, credit unions and mortgage companies, and institutions performing certain types of banking operations;

- regulatory legal acts were drafted on conducting the accounting of transactions with foreign exchange cash performed on the basis of a license issued by the National Bank, and insurance and reinsurance transactions in the "general insurance" sector. An Accounting Standard for Brokerage Activity was approved;

- letters were sent out containing recommended guidelines regarding the initial application of international financial reporting standards by all financial institutions, the recording by second-tier banks of transactions involving loans to customers and deposits received from customers that are individuals and legal entities, the recording of transactions with documentary letters of credit, the procedure for the formation of general provisions, the recording in financial statements of negative investment income by pension savings funds and organizations engaged in the investment management of pension assets, and for the accounting of transactions involving authorized capital.

In addition, the National Bank participated in the drafting of Law No. 562 of June 11, 2004 “On Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on Accounting and Financial Reporting.”

With the aim of the effective introduction of international financial reporting standards, raising the professional level of accounting department employees, and sharing experience, a number of seminars and meetings were held with representatives of foreign financial institutions. As part of training activities on transition of financial institutions to international financial reporting standards, lectures were held for employees of pension savings funds, pension asset management companies, and second-tier banks, as well as insurance organizations.

X. SERVICES PROVIDED TO FINANCIAL INSTITUTIONS

10.1. Management of the National Fund

The market value of the National Fund's foreign exchange portfolio at the end of 2004 was US$5.1 billion, including US$1.3 billion in the stabilization fund (25.65 percent) and US$3.8 billion in the savings portfolio (74.35 percent). The market value of securities and other financial instruments in the Fund's portfolio is based on data from the National Fund's custodial bank, ABN AMRO Mellon Global Securities Service (Appendices 1 and 2 to Section X, Subsection 10.1).

The market value of assets placed under external management at the end of 2004 was equivalent to US$2.9 billion, or 57 percent of the total market value of the National Fund[4].

The National Fund's net assets as of January 1, 2005 totaled 666.5 billion tenge.

In connection with the strengthening of the tenge's exchange rate against the Fund's base currency, the investment performance in tenge was negative at (-) 14.2 billion tenge. The negative exchange rate differential was 48.5 billion tenge (Appendix 3 to Section X, Subsection 10.1, Figure 10.1.1).

According to data from the National Fund's custodial bank, ABN AMRO Mellon Global Securities Service, investment income (realized and unrealized) generated for the year, calculated in U.S. dollars, was equal to US$313.0 million.

Receipts paid into the National Fund from the Ministry of Finance totaled 152.8 billion tenge, 19.8 billion tenge of which (the equivalent of US$150.0 million) was received in foreign currency.

Of the funds received in tenge, a total to 132.7 billion tenge was converted into U.S. dollars for subsequent investment in foreign financial instruments. The average exchange rate used in the conversion was 135.66 tenge to the dollar.

The reconversion of U.S. dollars back into tenge totaled of 232.3 million tenge to enable the Fund to pay the National Bank's claims for reimbursement of expenses arising from the trust management of assets. The average exchange rate used in the reconversion was 136.38 tenge to the dollar.

The balance of cash on the National Fund's account in tenge as of January 1, 2005 was 44.9 million tenge.

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[4] including the U.S. money market mandate type under external management up to December 31, 2004

The total expenses related to management of the National Fund (incurred by the National Bank and presented for payment by the Ministry of Finance) in 2004 reached 695.5 million tenge.

In accordance with notices received from the Ministry of Finance on the approval of expenditures, payment to cover expenses related to management of the Fund on National Bank claims was made in the amount of 524.2 million tenge.

Return on the management of the National Fund's assets. The National Fund's return from January 1 through December 31, 2004 was 7.61 percent. The National Fund's return from its inception through the end of 2004 was 19.79 percent, which in annual terms is 5.16 percent. The return was calculated in the base currency of the National Fund, U.S. dollars (Appendix 3 to Section X, Subsection 10.1, Figure 10.1.2).

The return on the stabilization portfolio from January 1 through December 31, 2004 was 1.45 percent, which is 0.23 percent higher than the return on the benchmark portfolio (Appendix 4 to Section X, Subsection 10.1).

Taking into account the management results, and with the aim of reducing external management costs, the decision was made to place the U.S. money market mandate type external management portfolio, as the simplest and most liquid, entirely under the management of the National Bank. Pursuant to the Board's Resolution No. 164 of December 15, 2004, the decision was made to terminate Investment Management Agreement No. 1 of January 30, 2003, which was concluded between the National Bank and the U.S. money market mandate type external manager.

The return on the savings portfolio from January 1 through December 31, 2004 was 9.33 percent. The return on the benchmark portfolio was 9.46 percent (75 percent – SWGB excluding Japan Index, 60 percent USD hedged (90 percent) plus SWGB Japan Index 60 percent USD hedged (10 percent) and 25 percent MSCI World excluding Energy). The excess return on the savings portfolio in 2004 was negative at (-) 0.13 percent (Appendix 6 to Section X, Subsection 10.1).

The negative excess return on the savings portfolio was due to the following reasons:

- the poor performance of the global tactical distribution mandate type external manager, with an excess return on the portfolio of (-) 3.65 percent for the year; this can be explained above all by the negative excess return on active positions in foreign exchange distribution, and also by the high level of allowable risk for this mandate; the tracking error target risk is 5 percent (with a maximum of 7 percent);

- the poor performance of the global stocks mandate type external manager, with an excess return on the portfolio of (-) 0.53 percent for the year. The main reason for the negative excess return was an improper selection of stocks for investment within sectors.

The return on the benchmark portfolio from January 1 through December 31 was 7.88 percent for bonds and 14.21 percent for stocks.

10.2. Custodial, Brokerage, and Other Activities on Servicing National Bank Customers

In 2004 the National Bank continued its custodial servicing of the State Pension Savings Fund Joint-Stock Company and the Kazakhstan Development Bank Joint-Stock Company. As of January 1, 2005 assets held on a custodial basis totaled 153.5 billion tenge, which is 14.9 billion tenge more than the previous year. Receipts for the year totaled 21.1 billion tenge, and the return of repaid investments totaled 1,089.4 billion tenge.

The placement of resources of the State Pension Savings Fund [GNPF] Closed Joint-Stock Company in investments totaled 1,101.9 billion tenge, which is 743.4 billion tenge more than in 2003.

National Bank income from providing custodial services grew by 6.8 percent to 85.0 million tenge, and reimbursed expenses totaled 21.4 million tenge.

In 2004 the National Bank provided brokerage services to the Kazakhstan Development Bank Joint-Stock Company. The volume of securities purchased under the brokerage agreement for the year grew by 38.4 percent to 48.1 billion tenge, while income from providing this service remained at the previous level of 0.8 million tenge.

Trust services were provided to the Kazakhstan Deposit Guarantee Fund Joint-Stock Company, the Kazakhstan Mortgage Company Joint-Stock Company, the National Processing Center Joint-Stock Company, the Insurance Payment Guarantee Fund Joint-Stock Company, the State Insurance Corporation for the Insurance of Export Credits and Investments Joint-Stock Company, the Kazakhstan Investment Fund Joint-Stock Company, the Kazakhstan Housing Construction Savings Bank Joint-Stock Company, the National Innovation Fund Joint-Stock Company, and the Kazakhstan Mortgage Credit Guarantee Fund Joint-Stock Company.

Customer assets under trust management with the National Bank totaled 39.9 billion tenge as of January 1, 2005, which is 3.0 billion tenge less than in 2003 (Appendix 1 to Section X, Subsection 10.2). Funds placed in trust with the National Bank fell by 0.8 percent to 45.0 billion tenge for the year. Funds withdrawn from trust totaled 48.0 billion tenge (this figure was 7.3 billion tenge in 2003). Income from providing asset management trust services as of January 1, 2005 totaled 28.8 million tenge, and reimbursed expenses totaled 14.4 million tenge.

XI. ORGANIZATION AND INTERNAL ACTIVITY

11.1. Organizational Structure

The structure and total number of permanent staff positions (3,580 units) of the National Bank were established by Presidential Decree No. 1271 of December 31, 2003 "On Approval of the Statute and Structure of the National Bank of the Republic of Kazakhstan."

In 2004 the structure of the National Bank underwent some changes (the number of departments and branch offices was cut) related to the transfer of supervisory functions to the newly established Agency for the Regulation and Supervision of the Financial Market and Financial Institutions and the establishment of the Banknote Factory of the National Bank of the Republic of Kazakhstan Republican State Enterprise based at a branch office of the National Bank.

At the end of the year the organizational structure of the National Bank consisted of 8 departments, 11 independent divisions, 1 independent section within the central administration, 17 branch offices, the Representative Office of the National Bank in the Russian Federation, and 6 subsidiary institutions (Appendix 1 to Section XI, Subsection 11.1).

The National Bank is the 100-percent founder of five joint-stock companies and one of the founders of the National Processing Center Joint-Stock Company (the National Bank's stake is 80.6 percent).

11.2. Personnel Policy and Personnel Training

The number of the National Bank's permanent staff positions declined by 5.2 percent compared to the previous year, while the actual number of people on staff fell by 6.0 percent in connection with the reorganization of the National Bank (the establishment of the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions).

The number of permanent staff positions at the joint-stock companies increased by 84.9 percent, while the actual number of people on staff rose by 87.5 percent, which was tied to an increase in the principal activities of the Kazakhstan Mortgage Company and the Kazakhstan Mortgage Credit Guarantee Company due to the development of the mortgage lending and mortgage credit guarantee systems in accordance with the State Program for the Development of Housing Construction for 2005–2007 (Appendix 1 to Section XI, Subsection 11.2, Table 11.2.1).

The turnover rate for personnel at the National Bank rose by 0.4 percentage point to 12.9 percent. Significant growth in this indicator occurred within the central administration of the National Bank, with an increase of 1.5 percentage points. Accordance to data from a sociological survey of employees, low wages are the main reason for leaving. This factor was mentioned by some 40 percent of those surveyed, who went on to find jobs at organizations with higher employee compensation: second-tier banks, other financial institutions, national companies, and the oil refining sector.

The turnover rate at the joint-stock companies declined by 14.3 percentage points.

In terms of the educational level of National Bank employees, those with higher education account for 58.3 percent of the total, those with specialized secondary education for 19.7 percent, and those with secondary education for 22.1 percent. At the joint-stock companies these figures are 94.8 percent, 4.5 percent, and 0.7 percent, respectively.

Employees with between 10 and 20 years of job experience account for the largest share of the personnel within the central administration and at branch offices, representing 28.3 percent and 38.1 percent of the total, respectively.

In 2004 the National Bank announced five competitions to fill 45 vacant administrative civil service positions. A total of 26 people were hired to fill the vacancies based on the competition results. Fourteen people were added to the personnel reserve of the Agency for Civil Service Affairs. Seven managers of subdivisions and branch offices of the National Bank were added to the political civil service reserve.

A total of 136 administrative civil service employees went through the certification process.

With regard to employees pursuing education and training, there were 772 people at the National Bank taking courses and engaged in practical training (including 80 representatives of outside organizations), 150 were studying at training centers in the Republic of Kazakhstan, 180 were studying abroad (including 28 in CIS countries), and 351 employees of branch offices of the National Bank were taking official state language courses.

With the participation of representatives of Deutsche Bundesbank, the European Commission, and the R-Style Ukraine company, four seminars on budget planning and control, risk management problems in the context of information technologies, international financial reporting standards, and macroeconomic and financial stability issues were organized for employees of the National Bank, the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions, second-tier banks, and other organizations.

Meetings were held with Deutsche Bundesbank representatives to discuss cooperation in the training and professional development of National Bank employees in 2005, in the course of which an accord was reached on holding four practical training sessions at Deutsche Bundesbank and one seminar at the National Bank.

In 2004, 19 representatives of central banks were received within the framework of cooperation among EurAsEC member states, with the aim of sharing experience on pressing issues in the operation of central banks.

During the course of a working meeting of members of the Coordinating Council of EurAsEC Member States, within the framework of a cooperation agreement, a uniform training policy was adopted and topics for future seminars were identified.

Based on the results of an individual scholarship competition that was held, 3 winners were chosen from among 46 participants: 2 students from the Al-Farabi Memorial Kazakh National University and 1 student from the S. Toraigyrov Memorial Pavlodar University.

A total of 68 students of higher education institutions received professional practical training at subdivisions within the central administration of the National Bank, including 26 students in the MBA program at T. Ryskulov Memorial Kazakhstan Economics University.

In 2004 the first 88 students graduated from the master's degree program. All of the graduates found jobs, and 53 percent of them found positions in government agencies.

A total of 84 master's degree students are enrolled in the 2004–2005 academic year in 1- and 2-year programs, which represents 41.4 percent of the total number of applicants; 32 of these students (38.1 percent) are studying on full scholarships. Training is being offered in the following areas of specialization: financial analyst, with 38 students; insurance and actuarial science, with 12 students; master's degree in public administration, with 21 students; and banking, with 13 students.

Labor compensation and social payments for personnel. During the year the National Bank's actual payroll expenses, including the social tax, fell by 7.2 percent to 3.5 billion tenge in connection with the reduction in the National Bank's staff.

At the joint-stock companies these expenses increased by 65.3 percent in connection with an increase in the number of employees (Appendix 1 to Section XI, Subsection 11.2, Table 11.2.2).

The average monthly wages per National Bank employee increased by 4.9 percent, which was due to the pay raise for specialists engaged in the management of the National Bank's gold and foreign exchange reserves, and the introduction of a supplemental bonus payment for them.

In 2004 the base salary paid to employees of the central administration and branch offices of the National Bank, not counting medical benefits, holiday bonuses paid out of payroll savings, and the annual bonus (to match second-tier banks that do not offer these payments to most of their employees), averaged 55,540 tenge. This indicator is significantly less (by a factor of 2.7) than the average monthly wages paid to employees of second-tier banks, which is the cause of the high turnover rate among National Bank personnel.

At the joint-stock companies the average monthly wages fell by 5.3 percent in connection with an increase in specialists as a proportion of the total number of employees.

Work was done to improve regulatory legal acts governing labor compensation for National Bank employees, personnel evaluations, loans granted by the National Bank, National Bank personnel training, and sending employees on official business trips.

With the aim of motivating personnel to stay healthy and to protect the property interests of employees related to compensation for injury to life or health resulting from an accident and/or illness, the National Bank provided medical insurance and accident and sickness insurance for its personnel.

During the period that the medical insurance contract was in effect (from August 7, 2003 through August 19, 2004), 2,363 employees utilized the services at a total cost of 61.8 million tenge.

During the period that the accident and sickness insurance contract was in effect (from August 11, 2003 through August 9, 2004), a total of 69 accidents occurred, for which the insurance company paid out 2.5 million tenge to employees.

As of August 2004 the National Bank was no longer providing insurance for employees because the competitions that were held were nullified due to the failure of the bids to meet the qualifications requirements or the documentation requirements, or because the price of the bids exceeded the amount specified in the plan. According to the explanation of the Financial Control and Government Purchasing Committee under the Ministry of Finance, in the event that a competition winner is named, government purchasing contracts need to be concluded for one financial year (from January 1 through December 31).

In addition, the National Bank provided charitable assistance to pensioners who are former employees of the bank (1,124 people) in the amount of 28.9 million tenge.

Work continued on improving the processes related to automation of accounting and payment of employee wages.

In connection with the introduction of a civil service personnel management information system, data on administrative civil service employees have been transferred to the Agency for Civil Service Affairs.

In the future work will need to be continued on the implementation of measures to promote the more efficient operation of the National Bank, including measures to retain and develop personnel potential to enable the National Bank to achieve its current, future, and strategic goals. In connection with this, the medium-range Personnel Management Strategy for 2004–2007, which identifies the tasks facing the National Bank to improve human resources management and the labor compensation system for employees, will be carried out with the aim of reducing personnel turnover.

11.3. Development of Information Technologies

With the aim of further development of the integrated automated information system of the National Bank (IAIS), projects were carried out in the following key areas:

- development of the new IAIS subsystems "Expert," "Personalized Recordkeeping of Computers and Software at the National Bank," "Recordkeeping of Telephone Calls";

- upgrading of existing IAIS subsystems in terms of the development and improvement of functional capabilities and centralization of subsystem data bases with the aim of increasing information security and reliability;

- development of the "Electronic Document Handling" subsystem (upgrading of the security module, circulation of the subsystem at branch offices of the National Bank, development of technical specifications for the creation of an electronic archive);

- creation of a subsystem for the centralized maintenance of regulatory and reference information (RRI) of the National Bank and upgrading of existing system to provide integration with it.

The "Expert" subsystem is used at the Cash Transactions and Safe Deposit Center and branch offices of the National Bank. As a result of the introduction of this subsystem, a uniform data base has been established for the results of expert inspections of questionable banknotes, the sharing of data with branch offices pertaining to the collection of results of expert inspections of questionable banknotes has been automated, and an opportunity has been created for the timely compilation of summary reports on the results of expert inspections performed at branch offices of the National Bank.

The development/upgrading of software for 13 applications was performed based on requests received from subdivisions within the central administration of the National Bank and the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions.

Work was done on holding an open competition to select a supplier for the banking information system.

Within the framework of efforts to establish a common information space in the Republic, the National Bank participated in the implementation of government programs and work was done on researching promising new technologies and on the further development of a corporate network and a quality management system for the information technology subdivision in accordance with international quality management standard version ISO 9001:2000.

With a view to incorporating advanced experience from around the world that will make it possible to improve the quality of user services, software has been developed and introduced that automates the process of the receipt and monitoring of the fulfillment of user requests. A total of 12,426 orders were prepared and filled during the year. Work is currently underway on the development of a program that will make it possible to speed up the performance of work on demand and to set up a feedback system for employees who have submitted requests, with a view to determining their satisfaction with the service performed.

Work on the maintenance and administration of existing information systems was done on 36 IAIS subsystems that are used within subdivisions and at branch offices of the National Bank.

Work on setting up work stations and on the installation of client applications on computers being upgraded was performed efficiently within all of the maintained subsystems.

The administration and operation of the existing information systems consisted of keeping the server equipment, the active equipment of the structured cable network, data bases, and mail systems in good working order. Work was done on the development and modernization of various areas of operation within the information technology subdivision that are aimed at improving the quality of administration and eliminating deficiencies that have been identified with regard to reliability, productivity, security, and greater convenience.

Overall, 3,220 pieces of computer equipment were serviced and used, compared to 3,851 in 2003. This figure includes 72 servers, 2,264 personal computers, 101 notebook computers, 659 laser printers, 31 high-speed Genicom printers, 47 scanners, and 46 pieces of other types of hardware; and in terms of communications equipment, this includes 20 automatic telephone exchanges and 96 fax machines.

Work was done to retire worn and outdated servers and personal computers in connection with their replacement with new ones. Scheduled maintenance work was performed on computer equipment, automatic telephone exchanges, Combimux data transmission systems, terminal rooms, and dealing systems, with follow-up checks to verify the quality of the service and maintenance work performed. The Compaq PIII laptop computers used within the central administration and at branch offices of the National Bank were updated in order to make the changeover to the standard Windows XP operating system.

11.4. Internal Audit

In 2004 a total of 43 scheduled audits were performed, including 11 within the central administration, 19 at branch offices and organizations, and 13 of information systems.

The planned audit of the "Management and Analysis of the Portfolios of Gold and Foreign Exchange Assets and the National Fund, Risk Management" automated information subsystem was not performed due to the fact that the competition to select a supplier of automation equipment for the National Fund was nullified.

An unscheduled audit of contingent income and expense on the monetary activity of the National Bank was performed, along with an unscheduled inventory of the property of the Banknote Factory of the National Bank Republican State Enterprise.

The results of the audits indicated in general that the National Bank's subdivisions are carrying out the task and functions assigned to them.

An integral part of each audit was an evaluation of the status of the internal control system at the unit being audited, and if it was found to be lacking the appropriate recommendations were made.

An analysis of the dynamics of the outcome of audits of the activities of National Bank subdivisions revealed a reduction in the number of violations, deficiencies, and problems compared to the indicators for the previous year by 5.8 percent, 22.9 percent, and 46.2 percent, respectively.

The reduction in the violations, deficiencies, and problems identified was the result of work that was done to improve the status of internal control, including in the information technology area, and to improve the regulatory legal base of the National Bank.

At the same time, there was an increase in the number of violations and deficiencies identified in the operation of branch offices and organizations of the National Bank, the bulk of which concern violations in the area of government purchasing of goods, work, and services.

In 2004 work continued on improvements in the methodological base for internal audits at the National Bank. Specifically, a new version of the Rules for the Organization of Internal Audit at the National Bank was prepared, along with methodological recommendations for the performance of audits in five auditing areas, a self-assessment questionnaire for National Bank subdivisions to evaluate their own monitoring, and requirements for the procedure to be followed in imposing preventive controls on government purchasing of construction and renovation work at branch offices of the National Bank.

With a view to improving internal auditing methods, the Methodological Recommendations for Audits of the Internal Control System were revised.

A risk section was also established within the internal audit subdivision and proposals were prepared regarding the establishment of a Risk Committee within the National Bank.

Collaboration between the outside auditor (Deloitte and Touche LLP) and subdivisions of the National Bank in the auditing of the annual financial statements for 2003 and 2004 was coordinated.

11.5. Financial Management Activity

In 2004 income within the National Bank system declined by 10.5 billion tenge (18.0 percent) to 48.0 billion tenge. Expenses grew by 11.0 billion tenge (26.7 percent) to 52.4 billion tenge (Appendix 1 to Section XI, Subsection 11.5, Table 11.5.1). After deductions were applied to the special reserve accounts, the undistributed loss of the National Bank for the year totaled 6.4 billion tenge. The profits of the National Bank's subsidiaries totaled 1.6 billion tenge, including 860.3 million tenge at republican state enterprises and 733.5 million tenge at joint-stock companies.

In accordance with Article 10 of the Law "On the National Bank of the Republic of Kazakhstan," undistributed losses of the National Bank for a financial year are compensated for in full by reserve capital.

Monetary activity. During 2004 the National Bank performed transactions in the foreign and domestic markets, as a result of which the average volume of gold and foreign exchange assets grew from US$4.4 billion to US$6.4 billion (by 43 percent), and net income on monetary activity was 1.2 billion tenge, which is 24.0 billion tenge (95.3 percent) less than in the previous year.

Net income on transactions ***in the foreign market*** grew by 3.9 billion tenge (34.1 percent) to 15.2 billion tenge.

Management of the National Bank's gold and foreign exchange assets is characterized by the following indicators:

- *the result for the gold portfolio* was a decline in net expenses by 2.5 billion tenge (97.8 percent) as a result of a reduction in expenses on swap transactions. In connection with a 5 percent rise in world gold prices and gold purchases in the domestic market, the average market value of the National Bank's gold portfolio grew by US$47.1 million (6.9 percent) from US$685.9 million to US$733.0 million. This includes an increase in the market value of gold placed on deposit by US$7.6 million (1.6 percent) to US$484.1 million.

- net income *on the foreign exchange portfolio* increased by 946.7 million tenge on the year (6.6 percent). In accordance with the new Investment Strategy for the Management of Gold and Foreign Exchange Reserves, a change was made in the structure of gold and foreign exchange assets, which made it possible to maintain a fairly high return even with the decline in the exchange rate of the dollar.

In terms of the short-term portfolio, in the fourth quarter of 2004 more than 30 percent of the assets were invested in euro-denominated government securities.

In *the long-term portfolio*, the basket of currencies was expanded to include the Canadian dollar, the Danish krone, the Australian dollar, the Swedish krona, and the Swiss franc.

There was a reduction in net income on assets *under external management* by 1.5 billion tenge (70.4 percent) compared to the previous year, due to a reduction in the assets placed under outside management on average from US$655.2 million to US$588.8 million and a decline in the return from 7.92 percent to 1.44 percent.

On average assets *under internal management* increased by 51.8 percent to US$4.7 billion. As a result, net income increased compared to the previous year by 19.8 percent to 14.6 billion tenge.

Net expenses on transactions ***in the domestic market*** grew by 17.7 billion tenge (by a factor of 9.8) to 16.1 billion tenge. Transactions related to the management of liquidity in the domestic market account for most of the growth. For example, at the end of 2004 the volume of National Bank notes in circulation compared to the previous year increased by 195.6 billion tenge (97.5 percent) to 396.1 billion tenge. In connection with this, net expenses on the management of excess liquidity grew by 5.3 billion tenge (57.6 percent) to 14.4 billion tenge, while the weighted average effective yield on short-term notes declined from 5.0 percent to 3.5 percent per annum (Appendix 1 to Section XI, Subsection 11.5, Table 11.5.2).

In terms of transactions with the government, there was a decline in expenses by 138.9 million tenge (7.6 percent), which was due to a reduction in the interest rate on deposits from 3.9 percent to 2.7 percent on average. At the same time, the average volume of government deposits increased by 14.6 billion tenge (31.3 percent).

During the year provisions for securities in foreign currency, for deposits placed with nonresident banks, for writing off debts on correspondent (nostro) accounts in foreign currency, and for loans made to individuals were created and cancelled in the amount of 107.3 million tenge and 114.9 million tenge, respectively. As a result, net income was earned in the amount of 7.5 million tenge, which is 99.9 percent less than the figure posted for the previous year.

Based on the results of transactions that were performed with gold and foreign exchange assets, realized income for the year totaled 22.5 billion tenge, which is 83.4

percent higher than the figure for the previous year, including 139.6 million tenge earned on transactions with foreign currencies and 22.3 billion tenge on transactions with gold.

Throughout 2004 the situation in the foreign exchange market was characterized by a strengthening of the tenge against the U.S. dollar. The nominal strengthening of the tenge against the dollar by 9.3 percent and growth in gold and foreign exchange assets led to an *unrealized loss* from revaluation of the dollar portfolio not secured by accumulated revaluation in the amount of 20.4 billion tenge.

The result of **nonmonetary activity** by the National Bank in 2004 was net expenses in the amount of 7.6 billion tenge, which represents a decline of 1.0 billion tenge (11.6 percent).

Income from nonmonetary activity fell compared to the previous year by 379.3 million tenge (24.2 percent) to 1.2 billion tenge (Appendix 2 to Section XI, Subsection 11.5). The main reason for the decline in income was the exclusion of revenues generated by the Banknote Factory in the amount of 306.0 million tenge (58.8 percent) from income in 2004 in connection with its reorganization and the establishment as of April 1, 2004 of the Banknote Factory Republican State Enterprise. In 2003 the Banknote Factory's revenues accounted for 33.1 percent (520.0 million tenge) of total income from nonmonetary activity.

There was an increase in the following types of income:

- income on cash transactions (the sale of gold and silver coins), which grew by 59.2 million tenge (108.2 percent) in connection with the release in the second half of the year of nine different types of silver coins and the release in November of new gold coins that are in high demand among the public;

- income from reimbursement of the National Bank's expenses related to transactions with nonfinancial institutions (trust and custodial activity), which grew by 121.3 million tenge (24.3 percent). The reason for the increase was growth in the assets of the National Fund and customers of the National Bank and a corresponding increase in the volume of transactions performed with them.

Expenses on nonmonetary activity fell by 1.4 billion tenge (13.5 percent) to 8.8 billion tenge.

A reduction in contingent expenses by 1.3 billion tenge (84.3 percent) related to the recording in 2003 of the results of the reappraisal of the value of the Banknote Factory building in the amount of 825.4 million tenge, and the write-off of the value of a bloc of shares in the National Information Technologies Closed Joint-Stock Company in the amount of 438.0 million tenge, which were transferred at no cost to the State Property and Privatization Committee under the Ministry of Finance, had the greatest impact on the decline in expenses.

There was a decline in expenses on the manufacturing of banknotes and coins in the domestic currency by 429.6 million tenge (14.6 percent) in connection with the write-off at the end of 2003 of balances of coins held in a warehouse, as part of measures to introduce a policy of recording expenses on the manufacturing of banknotes and coins that is consistent with the practices of central banks.

Other expenses fell by 120.7 million tenge (22.9 percent) due to a reduction in expenditures on taxes and mandatory payments to the budget by 17.8 million tenge (10.3 percent) in connection with the exemption from the land tax, the property tax, and the motor vehicle tax granted to the National Bank as of January 1, 2004.

While there was an overall decline in the National Bank's expenses, there was an increase in expenses related to supporting the functioning of the National Bank.

For example, expenses on transactions with fixed assets, intangible assets, and commodity stocks grew by 192.1 million tenge (16.6 percent), primarily due to the acquisition of supplies related to maintaining cash equipment, security and fire alarm systems, and vehicles.

Administrative expenses grew by 115.0 million tenge (10.4 percent) due to an increase in expenditures for communication services provided by the Kazakhstan Interbank Settlement Center Republic State Enterprise to effect transfers and perform payments for the Ministry of Finance.

Capital outlays of the National Bank fell by 921.7 million tenge (25.9 percent) to 2.6 billion tenge (Appendix 3 to Section XI, Subsection 11.5).

The decline in capital outlays compared to the previous year was due to a reduction in expenditures on construction projects by 105.3 million tenge (54.3 percent), on the purchase of fixed assets by 285.7 million tenge (27.8 percent), and on transfers of funds to replenish the authorized capital of organizations by 1.0 billion tenge (50.1 percent).

During the year funds totaling 1.0 billion tenge were transferred to the authorized capital of the National Processing Center Joint-Stock Company, the Banknote Factory Republican State Enterprise, the Kazakhstan Actuarial Center Joint-Stock Company, and the State Pension Savings Fund Pension Savings Fund Joint-Stock Company.

Expenditures on major renovation work increased by 396.8 million tenge (by a factor of 25.5) in connection with the repair of utility systems in the administrative building of the Agency for the Regulation and Supervision of the Financial Market and Financial Institutions, and expenditures on the acquisition of intangible assets, for the further development of the integrated automated information system, increased by 115.9 million tenge (45.5 percent).

Organizations of the National Bank. Income generated by republican state enterprises operating under the National Bank from the sale of goods (work, services) totaled 5.6 billion tenge in 2004, and expenditures on the production of goods (work, services) totaled 4.3 billion tenge. The organizations' net income after payment of the corporate income tax to the budget increased by 712.8 million tenge (483.2 percent) to 860.3 million tenge (Appendix 4 to Section XI, Subsection 11.5).

The organizations' operations are characterized by more rapid growth in income (197.5 percent) than in expenditures (161.6 percent) and an increase in profits earned by the Kazakhstan Mint (in connection with an expansion of the production program for manufacturing coins) and the Kazakhstan Center for Interbank Settlements (in connection with an increase in the number of payments in the MT 100 format as a result of a change in the conditions for effecting payments within the Interbank Money Transfer System).

Joint-stock companies of which the National Bank is a founder. Income earned by the joint-stock companies totaled 3.6 billion tenge, and expenses were 2.9 billion tenge. Net income grew by 255.9 million tenge (53.5 percent) to 733.5 million tenge (Appendix 4 to Section XI, Subsection 11.5).

The effectiveness of the joint-stock companies' operations is characterized by an increase in the number of insurance companies participating in the insurance payment guarantee system, participation by financial institutions in the mortgage credit guarantee system, and the issuance of the KazCard national payment card.

In 2004 the National Bank acquired shares in the State Pension Savings Fund Joint-Stock Company in the amount of 320.0 million tenge.

In connection with the National Bank's sale in 2005 of shares in the Kazakhstan Mortgage Company Joint-Stock Company to the Ministry of Finance, the results of KIK's activities were not consolidated within the National Bank's financial statements.

STATISTICAL APPENDICES

Appendix 1 to Section I, Subsection 1.1

Figure 1.1.1

Indices of Industrial Output in Physical Terms in 2004 (Compared to 2003) and the Sectoral Structure of Industry in 2004

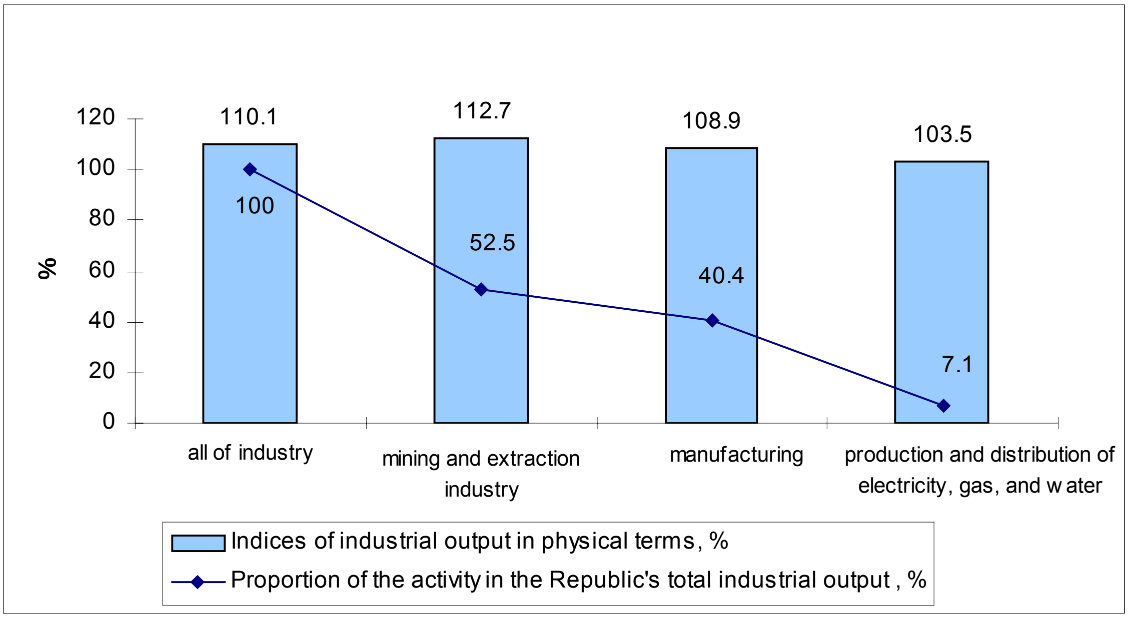
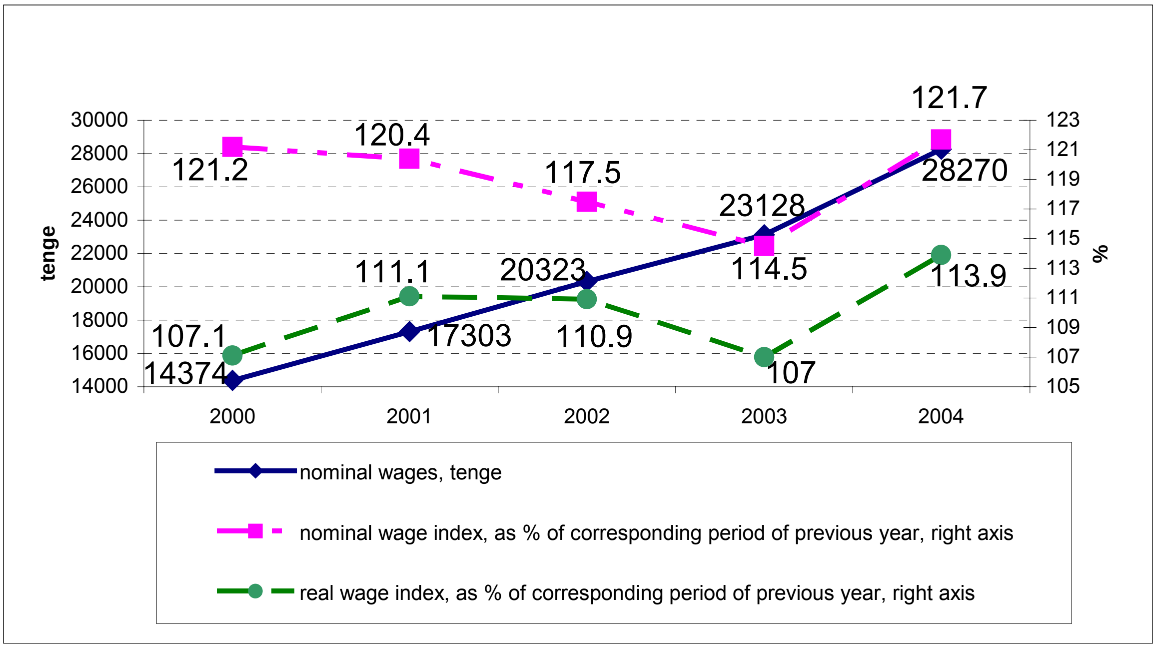


Figure 1.1.2

Nominal Wages in 2004 and Wage Indices in 2004



Appendix 1 to Section I, Subsection 1.2

Table 1.2.1

Dynamics of the Number of Monitoring Participants

	Quarter in which survey was performed				
	1st qtr. 2004	2nd qtr. 2004	3rd qtr. 2004	4th qtr. 2004	1st qtr. 2005
Number of participating enterprises	1176	1232	1248	1284	1302
of which: large and medium-sized	938	954	967	1015	1015
Number of large and medium-sized enterprises in the economy	4360	4369	4416	4423	4422
Proportion of large and medium-sized enterprises participating (line 2/line 3), %	21.5	21.8	21.9	22.9	23.0
Proportion of income from the sale of products by monitoring participants, %	57.8	58.7	56.4	61.7	66.0

Change in Economic Conditions and Financial Status in the Real Sector of the Economy in 2004 (Actual) and in the 1st Quarter of 2005 (Expected)

1. General economic conditions and factors thereof

Figure 1.2.1

1.1. Effect of the foreign exchange rate

Assessment of the effect of a change in the exchange rate on economic activity of enterprises in the 4th quarter of 2004.

Some 14.4 percent of the enterprises reported a positive effect of the change in the tenge's exchange rate against the U.S. dollar on economic activity, 3.5 percent reported a positive effect from the change against the euro, and 4.7 percent for the change against the Russian ruble. The numbers reporting a negative effect were 17.9, 10.3, and 6.6 percent of the enterprises, respectively. The majority of enterprises did not experience an effect from the change in the tenge's exchange rate, with 55.2, 65.4, and 66.7 percentage reporting no effect, respectively.

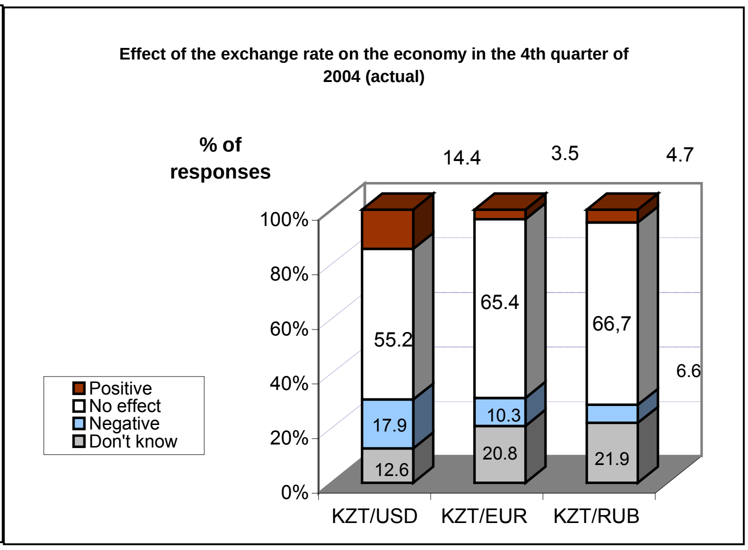


Figure 1.2.2

<table>
<tr>
<td>
<u>Assessment of the expected change in the exchange rate at the end of the 1st quarter of 2005</u>

1) 23.9 percent of the enterprises expect a strengthening of the exchange rate of the tenge against the U.S. dollar, 17.9 percent expect a strengthening against the euro, and 8.8 percent expect a strengthening against the Russian ruble;
2) 17.4, 12.6, and 7.1 percent of the enterprises expect a decline in the value of the tenge, respectively;
3) 32.6, 36.8, and 49.7 percent of the enterprises, respectively, believe that the tenge's exchange rate will remain unchanged in the 1st quarter of 2005.
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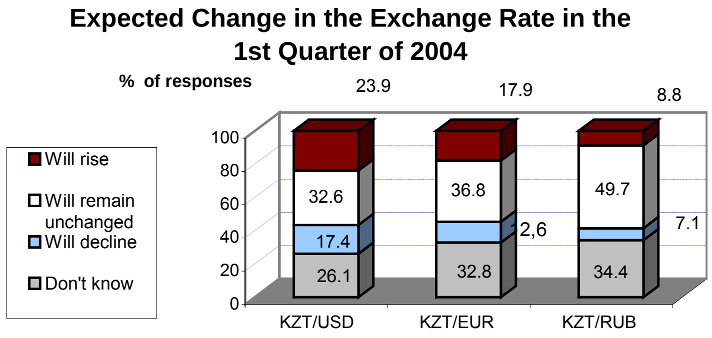

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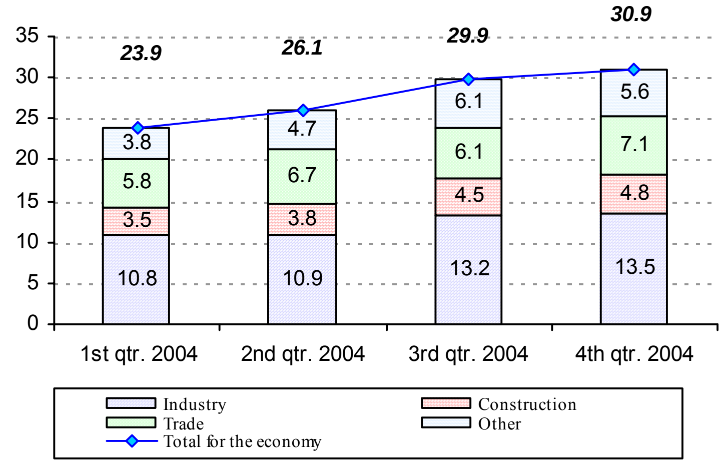
Appendix 2 to Section I, Subsection 1.2

1.2. Bank credits

Figure 1.2.3

In the 4th quarter of 2004, 66.5 percent of the enterprises surveyed had no need for bank credits, and 30.9 percent received credit; these were predominantly enterprises in industry, trade, and construction.



1.3. Assessment of sources of financing for working capital

Figure 1.2.4

In 2004 there was an increase in the number of enterprises using their own funds and/or bank credits for financing and replenishing working capital, which points to an improvement in the financial condition of enterprises and a greater positive influence by banks on the current operations of enterprises.

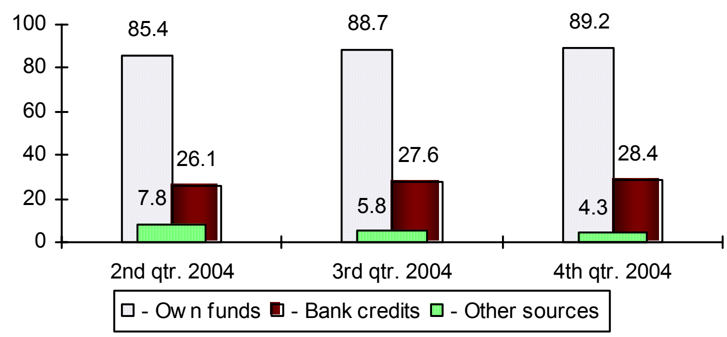
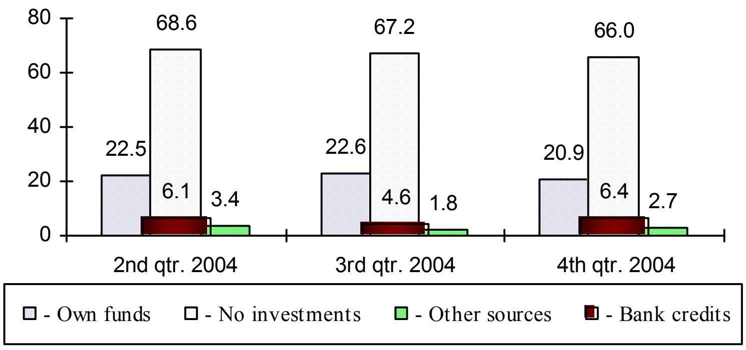


Figure 1.2.5

1.4. Assessment of sources of financing for investments

In 2004 there were no significant changes in the structure of sources of financing for investments in the real sector of the economy. Enterprises financed investments in large part using their own funds, which points to an improvement in their financial condition and has a positive impact on the financial stability of the real sector of the economy. At the same time, the impact of bank credits on these processes remains negligible.

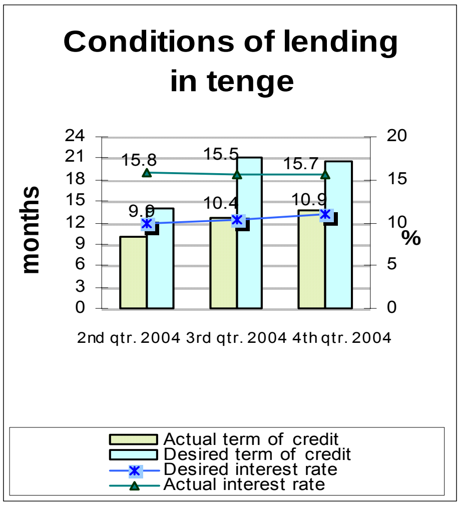


Appendix 3 to Section I, Subsection 1.2

Figure 1.2.6

1.5. Lending conditions

In 2004 there was no change in the average interest rate on credits in tenge, while there was a substantial change in the rate on credits in foreign currency. The narrowing of the gap between the actual interest rate and a level acceptable to enterprises (in both tenge and foreign currency) points to an improvement in lending conditions and should boost the role of credits in financing the economic activities of enterprises.



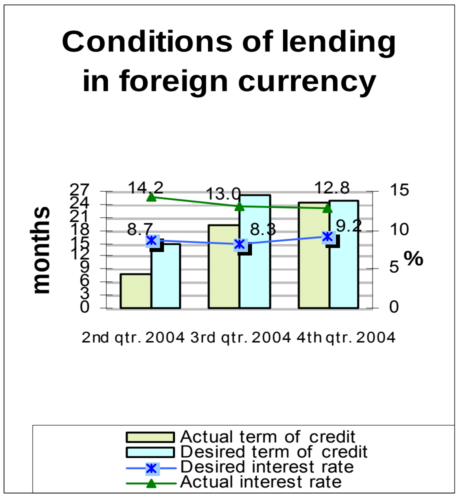


Figure 1.2.7

1.6. Assessment of enterprises' demand for banking services

In the 4th quarter of 2004, 28 percent of the enterprises had a high demand for banking services, and 23.1 percent had a good opportunity to obtain these services. Some 65.6 percent and 68.5 percent of the enterprises reported an average level of these indicators, respectively, and 6.1 percent and 7.1 percent reported low indicators. The satisfaction of the demand for banking services was estimated by 91.7 percent of enterprises as normal and by 7.5 percent as poor.

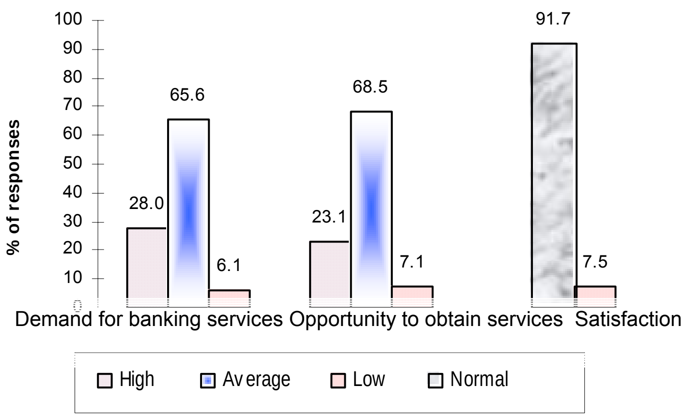
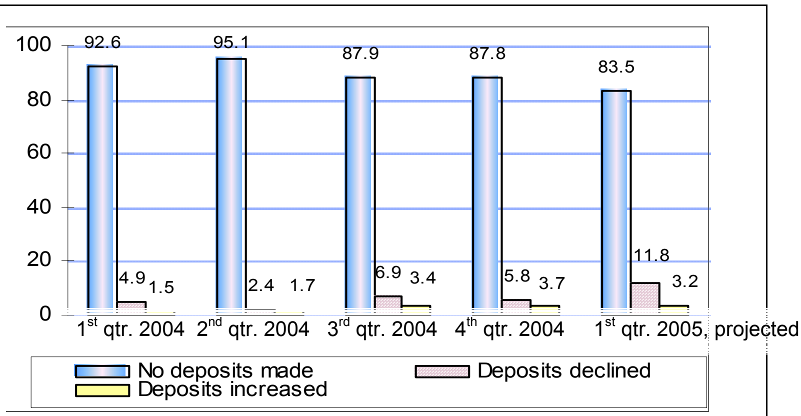


Figure 1.2.8

1.7. Placement of funds in deposits

In 2004 there was a significant decline in the proportion of enterprises with no holdings in bank deposits (from 92.6 percent to 87.8 percent), and there was an increase in the proportion of enterprises that reduced the size of their deposits. This trend will also continue into the 1st quarter of 2005.	

Appendix 4 to Section I, Subsection 1.2

2. Assessment of the change in prices for finished products, business activity, and the financial condition of the real sector of the economy

Figure 1.2.9

2.1. Dynamics of the rate of growth in prices for finished products

In 2004 the rise in prices for finished products in the real sector of the economy was linked above all to the increase in prices for finished products in the extraction industry.

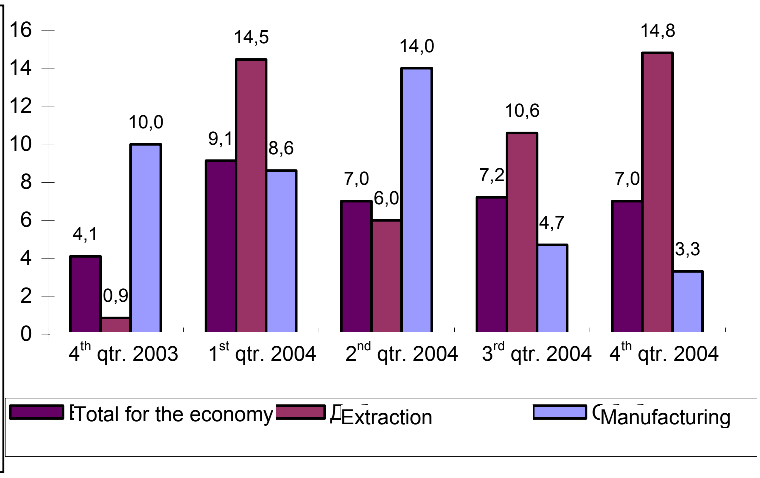


Figure 1.2.10

2.2. Assessment of solvency and liquidity

In 2004 working assets not only covered current liability in full (a current liquidity ratio is greater than 1), but they also allowed for a minimum guarantee of investments. The ability of the real sector to cover liabilities using all assets remained at an acceptable level: the total solvency ratio (1.7) was slightly below the normal level (>=2) only in the 2nd quarter.

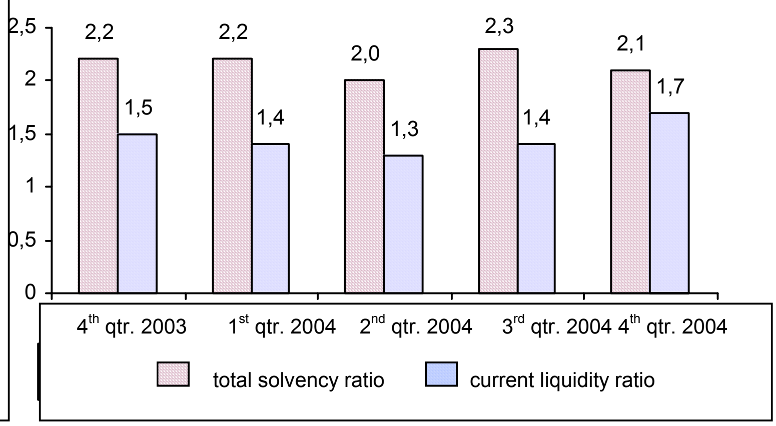
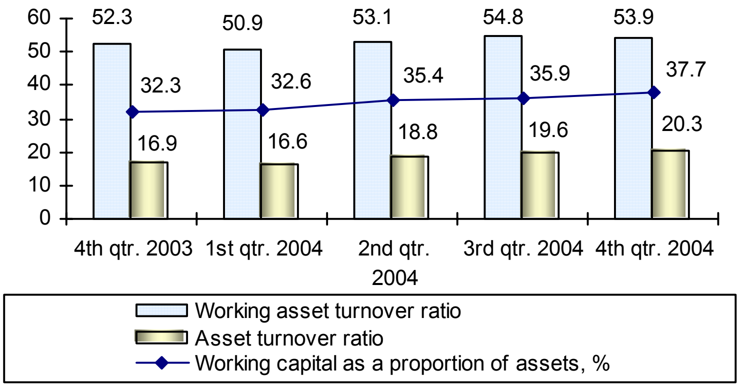


Figure 1.2.11

2.3. Assessment of business activity

In 2004 there was a steady improvement of business activity of enterprises: there was an increase in working capital as a proportion of total assets (to 37.7 percent in the 4th quarter); earnings from product sales made up for 20.3 percent of funds placed in assets and 53.9 percent of funds placed in working assets.



Appendix 5 to Section I, Subsection 1.2

Figure 1.2.12

2.4. Assessment of the profitability of sales

In 2004 the profitability of sales (before taxes) remained at a fairly high level, which was due primarily to the high level of this indicator in the extraction sector (67.5 percent in the 4th quarter). There was a decline in this indicator in manufacturing (from 37.2 percent in the 4th quarter of 2003 to 26.7 percent in the 4th quarter of 2004). The extraction industry continues to be more attractive from an investment standpoint.

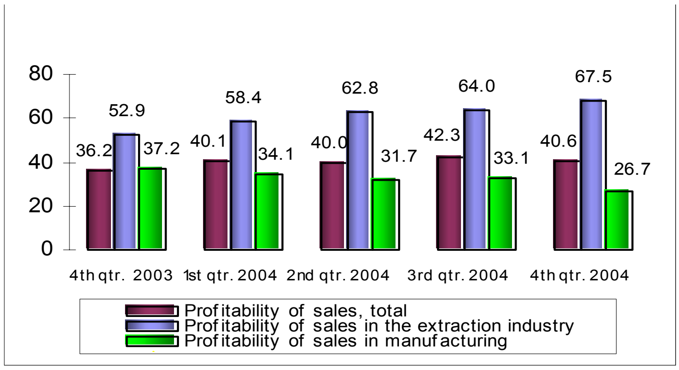


Figure 1.2.13

2.5. Assessment of the profitability of equity capital

The average profitability of equity capital in the real sector grew during the year (from 12.3 percent to 15.4 percent) and was practically the same as the interest rates on bank credits, although this was due to a rise in the profitability of equity capital in the extraction industry (from 20 percent to 25 percent). There was a decline in the indicator in manufacturing (from 13 percent to 11 percent), which was true for other sectors as well (with the exception of trade).

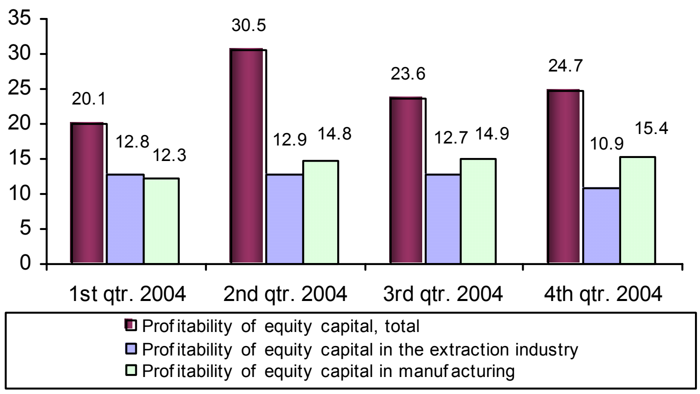
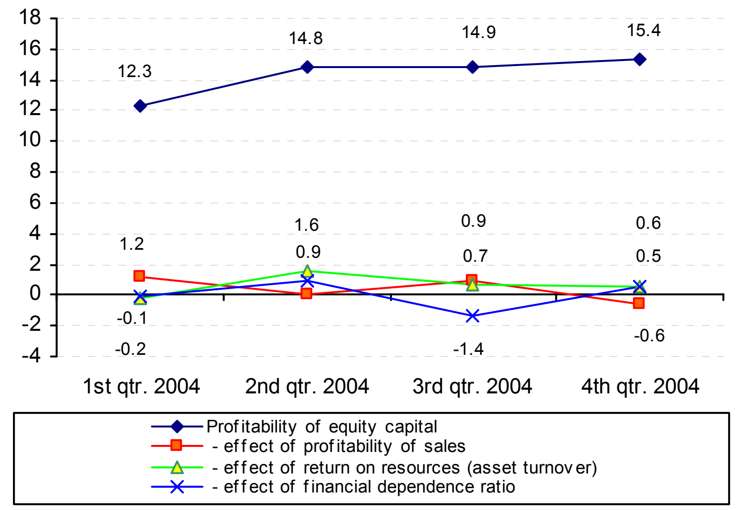


Figure 1.2.14

2.6. Effect of factors on the profitability of equity capital

In the 4th quarter of 2004 the main factors had varying effects on the profitability of equity capital: 1) the profitability of equity capital rose by 0.6 percent due to higher rates of growth in assets compared to equity capital (which was tied to an increase in the proportion of attracted funds and a corresponding rise in the financial dependence ratio); 2) the profitability of equity capital rose by 0.5 percent due to an increase in the turnover of assets; 3) the profitability of equity capital fell by 0.6 percent due to a decline in the profitability of sales. As a result, the profitability of equity capital fell by 0.5 percent in the 4th quarter (0.6 + 0.5 – 0.6).



Appendix 1 to Section I, Subsection 1.4

The Balance of Payments of the Republic of Kazakhstan: Analytical Presentation

millions of U.S. dollars

	2001	**2002**	**2003**	**2004**	**2004**			
					I	**II**	**III**	**IV**
A. Current account	-1389.5	-1024.3	-270.1	532.9	281.9	-269.2	96.9	423.2
Trade balance	983.4	1987.1	3679.0	6785.6	1422.3	1171.5	1923.6	2268.2
Exports	8927.8	10026.9	13232.6	20603.1	4108.2	4666.2	5694.4	6134.4
Imports	-7944.4	-8039.8	-9553.6	-13817.6	-2685.9	-3494.7	-3770.8	-3866.2
Balance of services	-1374.4	-1997.9	-2040.4	-2985.9	-586.3	-726.0	-783.3	-890.3
Exports	1260.2	1540.4	1712.3	2001.1	437.0	496.6	567.3	526.8
Imports	-2634.6	-3538.3	-3752.7	-4987.0	-1023.3	-1196.0	-1350.6	-1417.1
Balance of income	-1237.0	-1127.4	-1744.0	-2778.6	-496.6	-609.8	-878.7	-793.4
Interest payments on credits and loans attracted	-197.1	-213.1	-274.7	-406.9	-74.4	-109.4	-90.0	-133.1
Direct investor income	-1147.2	-1014.8	-1446.5	-2296.7	-386.5	-466.2	-752.8	-691.1
Interest on reserves and assets of the National Fund	193.6	200.3	191.7	258.5	49.6	54.6	59.1	95.1
Other (net)	-86.2	-99.8	-214.7	-333.5	-85.3	-88.8	-95.1	-64.3
Current transfers	238.5	113.7	-164.7	-488.2	-57.4	-104.8	-164.7	-161.3
B. Capital and financial account	2428.7	1239.3	2756.1	4592.5	300.1	1295.4	473.3	2523.7
Capital transfers	-185.0	-119.8	-27.8	-20.3	2.4	-5.6	-11.7	-5.3
of which: migrants' transfers	-197.9	-136.0	-45.5	-24.8	0.8	-6.8	-12.8	-6.0
Financial account	2613.7	1359.1	2783.9	4612.7	297.6	1301.0	485.0	2529.1
Direct investment	2860.6	2163.8	2209.8	5548.3	884.9	707.6	970.0	2985.9
financing (net)	4652.7	3681.3	4462.7	9781.7	1271.7	1051.2	1572.2	5886.5
repayment	-1792.1	-1518.0	-2252.9	-4233.4	-386.8	-343.7	-602.2	-2900.7
Portfolio investment	-1317.5	-1246.7	-1891.0	-421.8	-165.2	183.7	-95.3	-675.4
of which: Eurobonds of the government	-102.7	-237.1	54.3	21.2	169.4	56.4	14.3	-219.0
Financial derivatives (net)		0	15.9	-46.4	-39.4	12.9	-33.1	13.2
Other medium- and long-term investments	463.1	758.1	2196.5	1689.6	166.3	394.9	143.1	985.3
Trade credits	-59.7	98.3	36.5	260.1	8.5	36.0	75.9	139.8
Guaranteed by the Republic of Kazakhstan government	-70.1	-26.1	-0.8	77.9	0.4	17.6	46.5	13.3
Other (net)	10.4	124.4	37.4	182.3	8.1	18.4	29.4	126.4
Loans	316.1	661.3	1885.0	1429.5	157.8	359.0	67.3	845.5

Attracted by the Republic of Kazakhstan government	54.6	3.4	57.4	-69.0	-22.3	-16.9	23.8	-53.6
Financing	161.9	120.3	204.2	196.4	36.3	31.9	51.0	77.2
Debt repayment (accrued)	-107.3	-116.9	-146.9	-265.4	-58.6	-48.8	-27.2	-130.8
Other (net)	261.5	658.1	1827.6	1498.5	180.0	375.9	43.5	899.0
Miscellaneous (net)	206.7	-1.7	275.0	0.0	0.0	0.0	0.0	0.0
Other short-term capital	607.4	-316.07	252.8	-2157.1	-879.3	1.9	-499.7	-779.9
C. Errors and omissions	-654.5	320.2	-952.5	-1126.4	154.8	-27.2	-444.2	-809.7
D. Total balance	384.7	535.1	1533.5	3999.0	736.8	999.0	126.0	2137.2
E. Financing (utilized)	-384.7	-535.1	-1533.5	-3999.0	-736.8	-999.0	-126.0	-2137.2
NBK reserve assets	-384.7	-535.1	-1533.5	-3999.0	-736.8	-999.0	-126.0	-2137.2
IMF credit	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Appendix 2 to Section I, Subsection 1.4

	2001	2002	2003	2004
Current account balance (millions of dollars)	-1390	-1024	-270	533
- as a % of GDP	*-6.3*	*-4.2*	*-0.9*	*1.3*
Exports of goods and services (millions of dollars per year)	10188	11567	14945	22604
- as a % of GDP	*46.0*	*47.0*	*50.2*	*55.5*
Imports of goods and services (millions of dollars per year)	10579	11578	13306	18805
- as a % of GDP	*47.8*	*47.1*	*44.7*	*46.1*
Real effective exchange rate (change in index as a percentage of December of the previous year)	-1.5	-7.4	-2.5	5.9
Trade conditions (change in average index for the year as a percentage of the previous year)	-5.3	1.5	0.4	16.5
Net inflow of foreign direct investment (millions of dollars per year)	2861	2163	2209	5548
- as a % of GDP	*12.9*	*8.8*	*7.0*	*12.2*
Gross external debt (millions of dollars at year-end)	15157	18197	22884	32017
Public and publicly guaranteed external debt	3800	3481	3623	3366
Intercompany debt	8879	10709	11999	16651
External debt of the banking sector	488	1352	3514	6858
Other debt liabilities	1990	2655	3748	5142
International reserves of the National Bank (millions of dollars at year-end)	2508	3141	4962	9280
- in months of imports of goods and services	*2.8*	*3.2*	*4.4*	*4.5*

Appendix 3 to Section I, Subsection 1.4

Absolute and Relative Parameters of the Republic of Kazakhstan's External Debt

Indicator	2001	2002	2003	2004	Debt (IBRD) Low	Debt (IBRD) Moderate

A. Absolute parameters (millions of U.S. dollars)

1. Gross external debt (at year-end)	15 157.5	18 197.3	22 883.7	32 017.4		
of which: intercompany debt	*8 879.3*	*10 709.7*	*11 998.8*	*16 651.1*		
2. Gross external debt, excluding intercompany debt (at year-end)	6 278.2	7 487.6	10 885.0	15 366.3		
3. Aggregate accrued payments on repayment and servicing of long-term debt	3 834.2	4 094.9	5 258.6	8 648.0		
excluding repayment and servicing of intercompany debt	1 690.4	2 260.7	2 659.0	3 972.6		
4. Exports of goods and nonfactor services	10 228.4	11 633.5	15 039.6	22 728.2		

B. Relative parameters

1. Gross external debt per capita (U.S. dollars)	1 021.3	1 224.8	1 530.3	2 124.0		
excluding intercompany debt	423.0	504.0	727.9	1 019.4		
2. Ratio of gross external debt to GDP (%)	68.5	74.5	76.9	78.6	<48	48-80
excluding intercompany debt	28.4	30.7	36.6	37.7		
3. Ratio of gross external debt to exports of goods and nonfactor services (%)	148.2	156.4	152.2	140.9	<132	132-220
excluding intercompany debt	61.4	64.4	72.4	67.6		
4. Ratio of payments on debt repayment and servicing to exports of goods and nonfactor services (%)	37.5	35.2	35.0	38.0	<18	18-30
excluding intercompany debt	16.5	19.4	17.7	17.5		
5. Ratio of interest payments to exports of goods and nonfactor services (%)	6.8	5.8	4.7	4.0	<12	12-20
6. Ratio of long-term debt to gross external debt	92.4	89.9	87.6	88.8		

For reference:

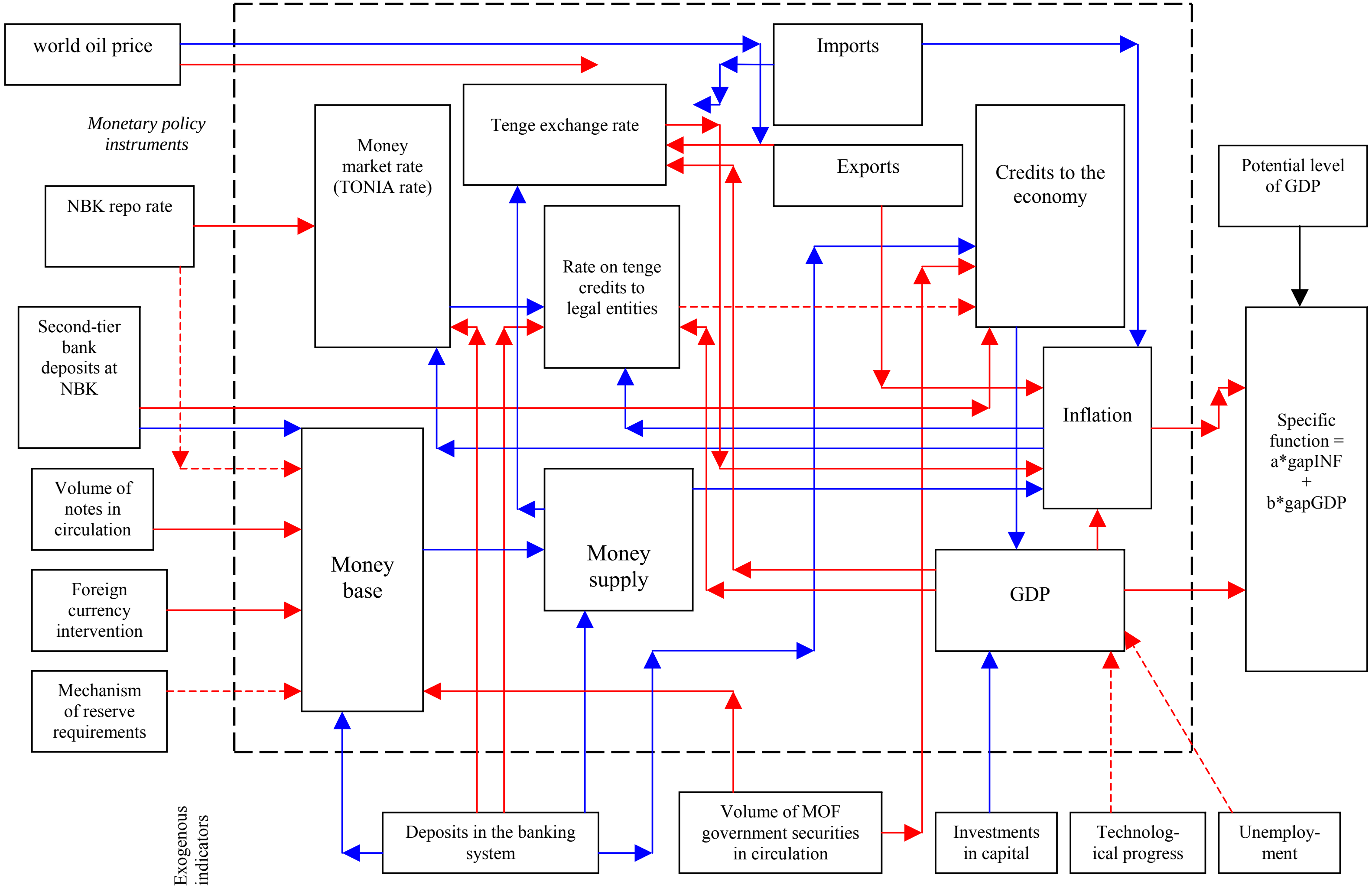
Population (thous. people)	14 842	14 858	14 890	15 074.2
GDP (billions of U.S. dollars)	22.125	24.414	29.76	40.75

Appendix 1 to Section II, Subsection 2.1

Diagram of Kazakhstan's Transmission Mechanism*

Exogenous indicators:

*The dotted lines with arrows indicate connections that the model shows as insignificant, but which theoretically should take place



Appendix 1 to Section II, Subsection 2.2

Table 2.2.1

	Indicators (in millions of U.S. dollars)	Amount	
		Jan. 1, 2004	**Jan. 1, 2005**
1.	**Gross gold and foreign exchange assets, total**	**4 962.106**	**9 280.494**
	Of which:		
1.1.	Monetary gold	725.916	803.562
1.2.	Assets in freely convertible currency and SDRs	4 236.192	8 476.931
a)	Foreign exchange cash (freely convertible currency)	3.461	3.299
b)	Deposits in freely convertible currency	767.964	1 085.720
c)	Credits in freely convertible currency backed by securities	325.090	539.924
d)	Securities, other than shares in freely convertible currency	3 133.659	6 840.441
e)	Financial derivatives and other accounts	6.018	7.547
2.	**External liabilities (freely convertible currency)**	**3.178**	**3.516**
	Of which:		
2.1.	Liabilities to international financial institutions	0.167	0.314
2.2.	Medium- and long-term credits	1.887	1.903
2.3.	Financial derivatives	0.746	0.050
2.4.	Other accounts	0.379	1.249
3.	**Net international reserves (1-2), total**	**4 958.928**	**9 276.977**

Table 2.2.2

Yield Curve Distribution of Foreign Exchange Assets under Internal Management

	<1 year	**1 – 3 years**	**3 – 10 years**
1st quarter	28.49%	62.04%	9.47%
2nd quarter	14.92%	82.05%	3.03%
3rd quarter	27.98%	66.14%	5.88%
4th quarter	10.07%	68.01%	21.92%

Appendix 2 to Section II, Subsection 2.2

Figure 2.2.1

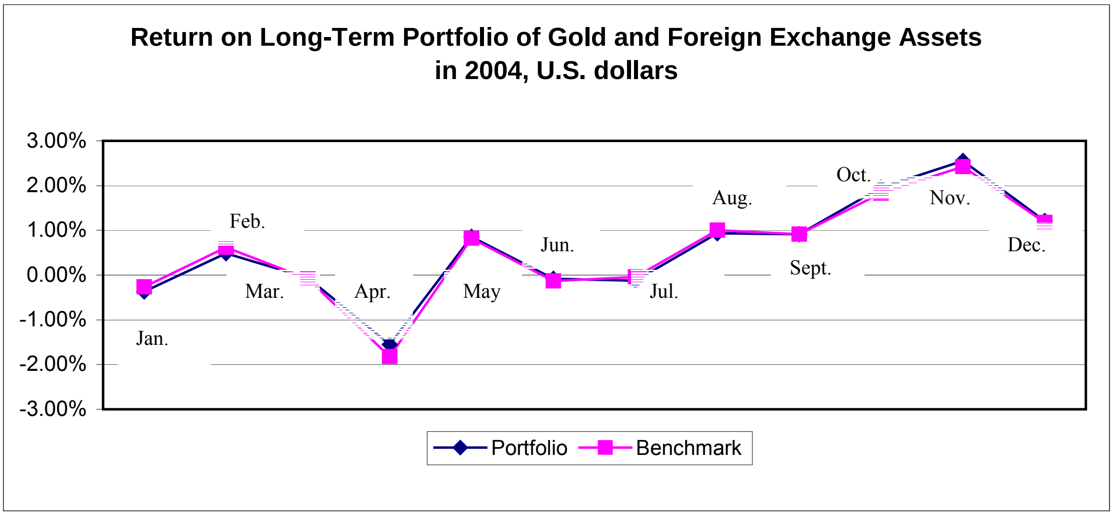
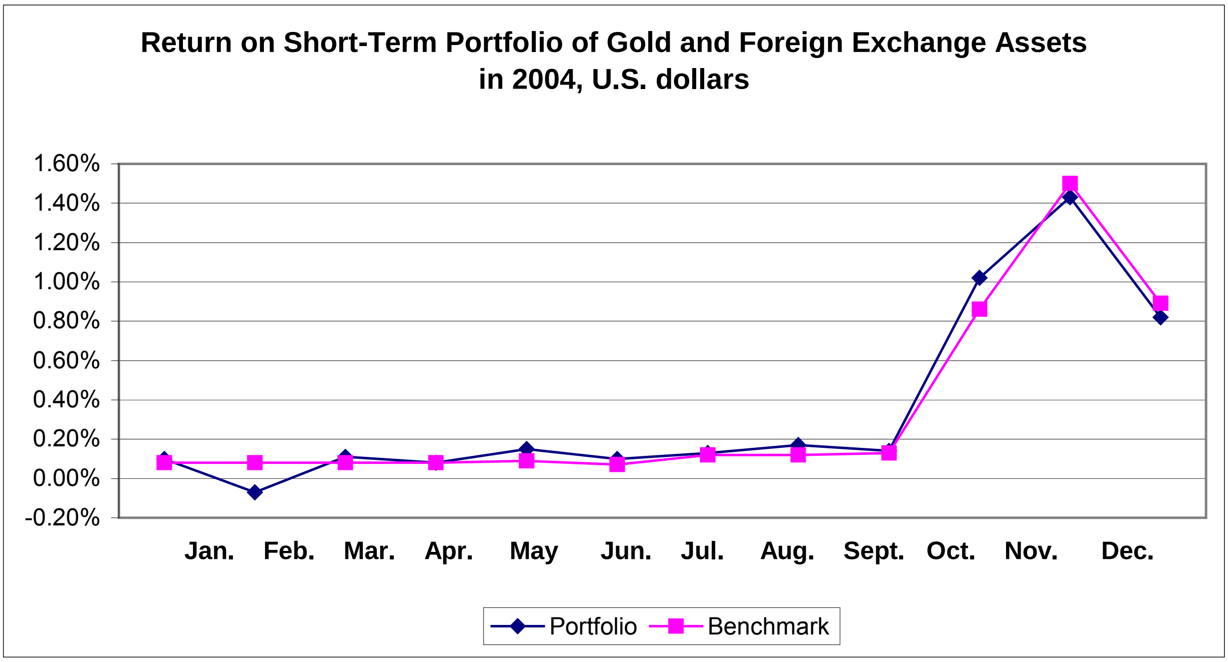


Figure 2.2.2



Appendix 3 to Section II, Subsection 2.2

Comparative Table of Excess Return by Gold and Foreign Exchange Portfolio Managers in 2004[5] (returns are calculated in the currency of each subportfolio)

millions of U.S. dollars

Manager	Market value	Portfolio return, %	Benchmark portfolio return, %	Excess return, %
Long-term portfolio of foreign exchange assets				
Subportfolio denominated in U.S. dollars				
Total	**1 367.45**	**1.57**	**1.00**	**0.58**
National Bank of the RK	1 036.30	1.50	1.00	**0.50**
Manager 1	160.49	1.28	1.10	**0.19**
Manager 2	170.66	2.42	1.00	**1.43**
Subportfolio of U.S. inflation-indexed securities*				
National Bank of the RK	172.14	2.46	2.55	**-0.09**
Subportfolio denominated in euros				
National Bank of the RK	1 318.99	2.99	3.20	**-0.21**
Manager 3**	158.70	0.62	1.37	**-0.75**
Subportfolio denominated in pounds sterling				
National Bank of the RK	182.77	4.49	4.64	**-0.15**
Subportfolio denominated in Canadian dollars*				
National Bank of the RK	108.99	1.20	1.32	**-0.12**
Subportfolio denominated in Danish kroner*				
National Bank of the RK	112.47	0.73	0.81	**-0.08**
Subportfolio denominated in Australian dollars*				
National Bank of the RK	111.82	1.28	1.45	**-0.17**
Subportfolio denominated in Japanese yen				
National Bank of the RK	73.53	0.23	0.43	**-0.20**
Subportfolio denominated in Swedish kronor*				
National Bank of the RK	75.60	1.52	1.60	**-0.08**
Subportfolio denominated in Swiss francs*				
National Bank of the RK	75.24	0.51	0.67	**-0.16**
Short-term portfolio of foreign exchange assets				
Total	3 694.86	4.26	4.16	**0.10**
Subportfolio denominated in U.S. dollars				
National Bank of the RK	2 528.45	1.84	1.33	**0.51**
Manager 4***	161.8	1.43	1.35	**0.08**
Subportfolio denominated in euros				
National Bank of the RK	1 166.41	0.50	0.54	**-0.04**

* - subportfolios introduced as of October 1, 2004;

** - market value at the time the Agreement with the given external manager was abrogated (July 14, 2004); the return on the portfolio and the return on the benchmark portfolio are shown for the first half of the year;

*** - market value at the time the Agreement with the given external manager was abrogated (December 31, 2004); the return on the portfolio and the return on the benchmark portfolio are shown for the year.

[5] Not including the commission fee paid to managers

Appendix 1 to Section IV

Cash Turnover at Second-Tier Banks

billions of tenge

Cash flows through banks' cash departments	**2004**	**2003**
Incoming cash at banks' cash departments	3 138.0	2 279.1
from the sale of goods, services, and work	959.7	744.0
from utility payments	67.8	59.3
from transportation enterprises	41.6	31.5
from communications enterprises	60.9	45.7
from hotel, gambling, and show business enterprises	4.5	3.2
from insurance organizations	2.4	2.3
from the sale of foreign currency	691.0	572.9
applied to deposit accounts held by individuals	345.7	173.5
taxes, fees, and customs payments received	74.7	51.0
loan repayments	52.8	31.5
removed from automatic teller machines	90.5	62.3
other receipts	746.4	501.9
Outgoing cash from banks' cash departments	3 350.6	2 339.1
to pay for goods, services, and work	728.7	543.6
for employee compensation	263.6	227.7
to pay for agricultural products	88.3	120.1
to transportation and communications enterprises	3.1	7.6
to insurance organizations	0.5	0.6
for the purchase of foreign currency	346.4	254.7
from deposit accounts held by individuals	517.0	290.6
loans to individuals and legal entities	33.1	13.1
for the payment of pensions and benefits	198.4	138.3
for filling automatic teller machines	459.5	320.8
other disbursements	712.0	422.0

Appendix 2 to Section IV

Anniversary and Memorial Coins Issued in 2004

1. Coin dedicated to the 2006 World Football Championship in Germany from the “Sports” series, with a face value of 100 tenge, made of silver with a purity of 925/1000

2. Coin dedicated to the 2004 Olympic Games from the “Sports” series, with a face value of 100 tenge, made of silver with a purity of 925/1000

3. Coin dedicated to the 100th anniversary of the Kazakhstan railroad, with a face value of 500 tenge, made of silver with a purity of 925/1000

4. Coin dedicated to the 100th anniversary of the birth of A. Kasteyev, with a face value of 50 tenge, made of nickel-silver alloy

5. Coin dedicated to the 100th anniversary of the birth of A. Margulan, with a face value of 50 tenge, made of nickel-silver alloy

6. “The Thinker” from the “Petroglyphs of Kazakhstan” coin series, with a face value of 500 tenge, made of silver with a purity of 925/1000

7. “Saker Falcon” from the “Red Book of Kazakhstan” coin series, with a face value of 500 tenge, made of silver with a purity of 925/1000

8. “Zhetigen” from the “Applied Arts” coin series, with a face value of 500 tenge, made of silver with a purity of 925/1000

9. “Stone Carvings” from the “Architectural and Historical Monuments” coin series, with a face value of 500 tenge, made of silver with a purity of 925/1000

10. “Half-Kopeck Coin” from the new “Coins from Old Imprints” series, with a face value of 500 tenge, made of silver with a purity of 925/1000

11. “Golden Deer” from the new “Gold of the Nomads” series, with a face value of 500 tenge, made of silver with a purity of 925/1000

12. “Tsar Midas” with a face value of 100 tenge, made of gold with a purity of 999/1000

13. “Tsar Krez” with a face value of 100 tenge, made of gold with a purity of 999/1000

14. “Marco Polo” with a face value of 100 tenge, made of gold with a purity of 999/1000

Appendix 1 to Section V, Subsection 5.3

Figure 5.3.1

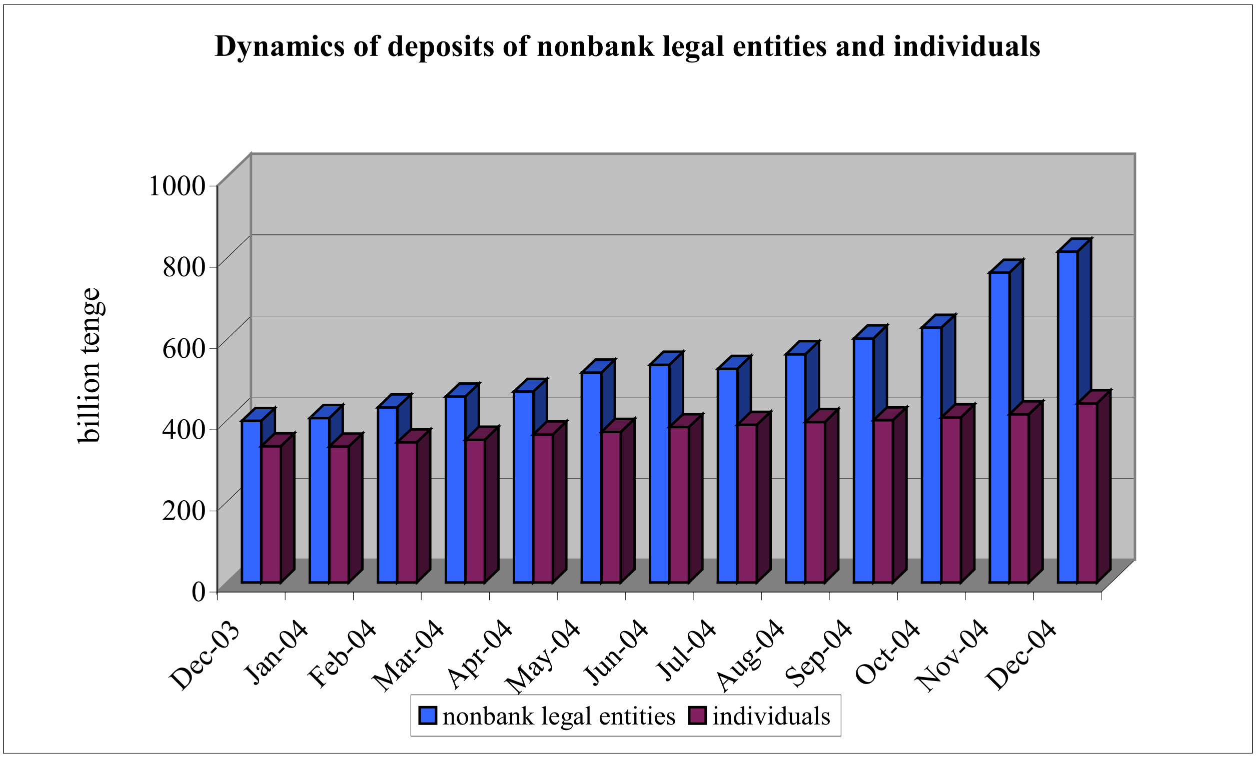
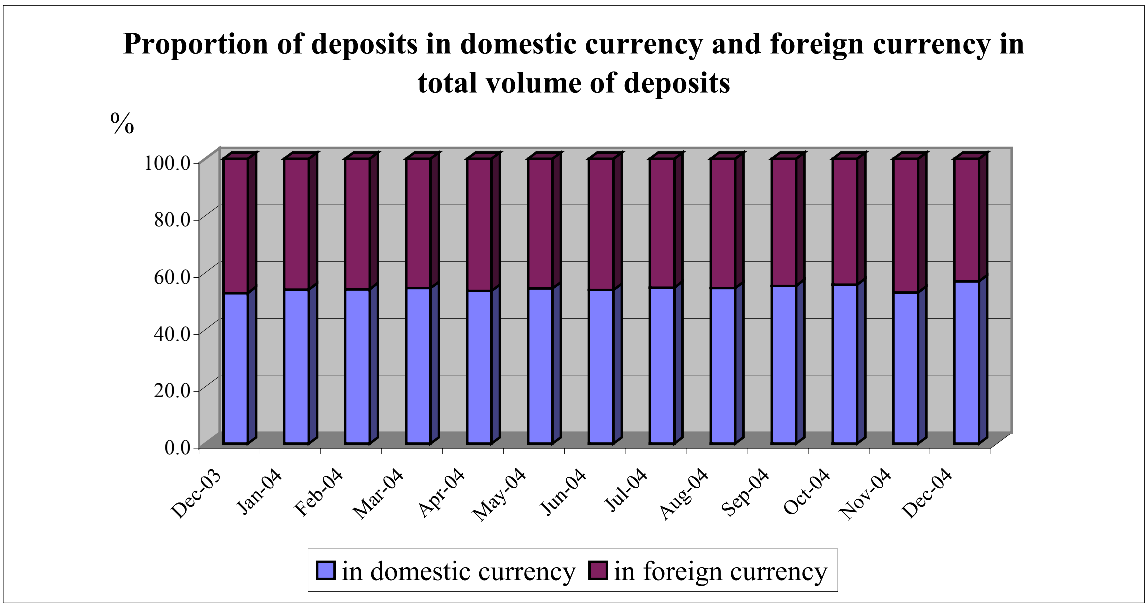
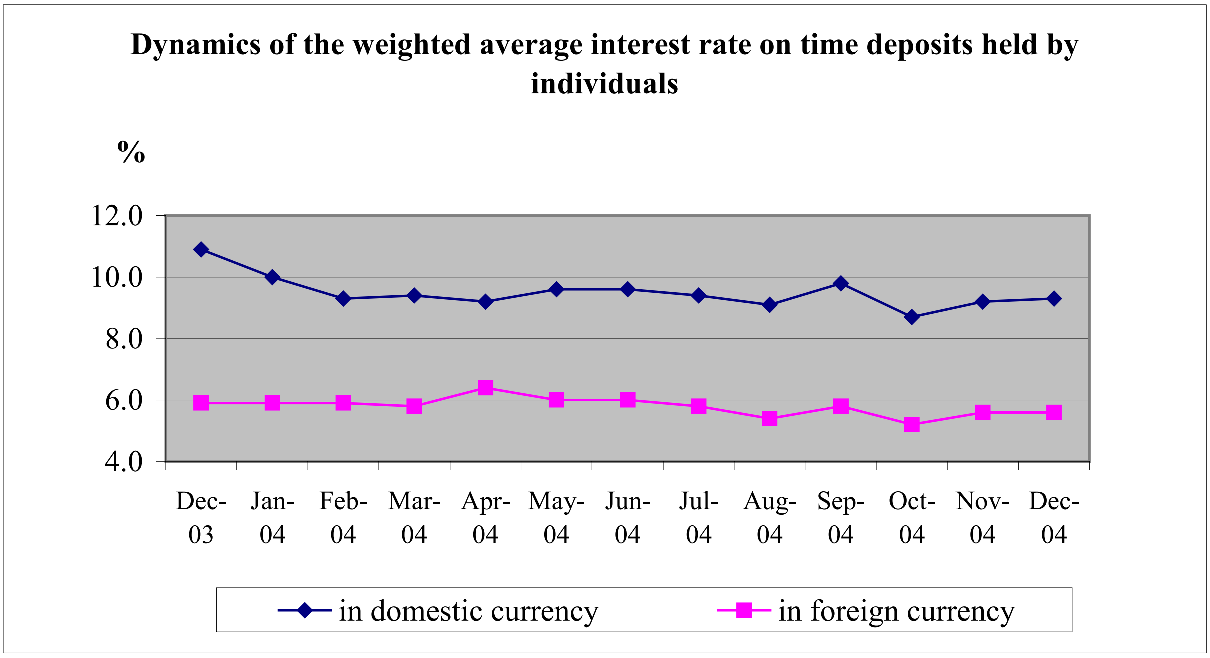


Figure 5.3.2



Appendix 2 to Section V, Subsection 5.3



Appendix 1 to Section V, Subsection 5.4.1

Figure 5.4.1

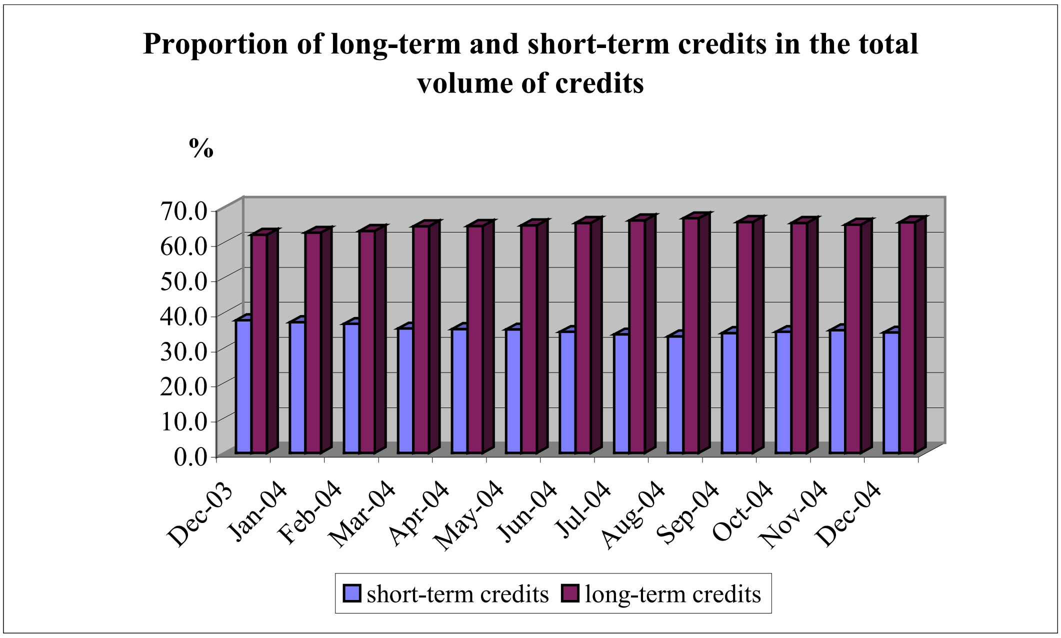
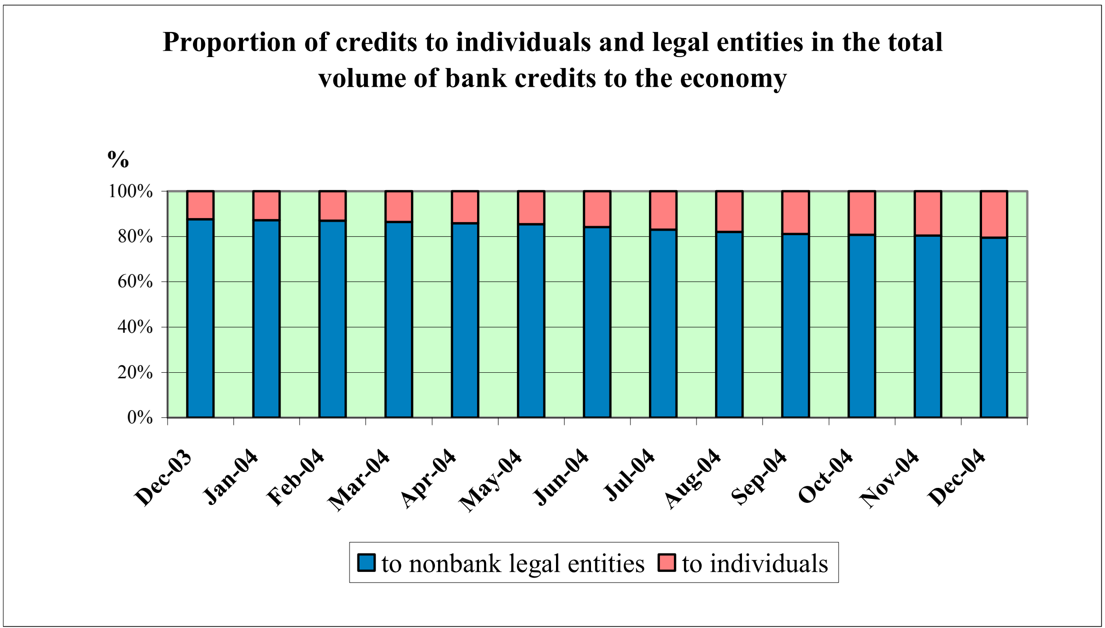
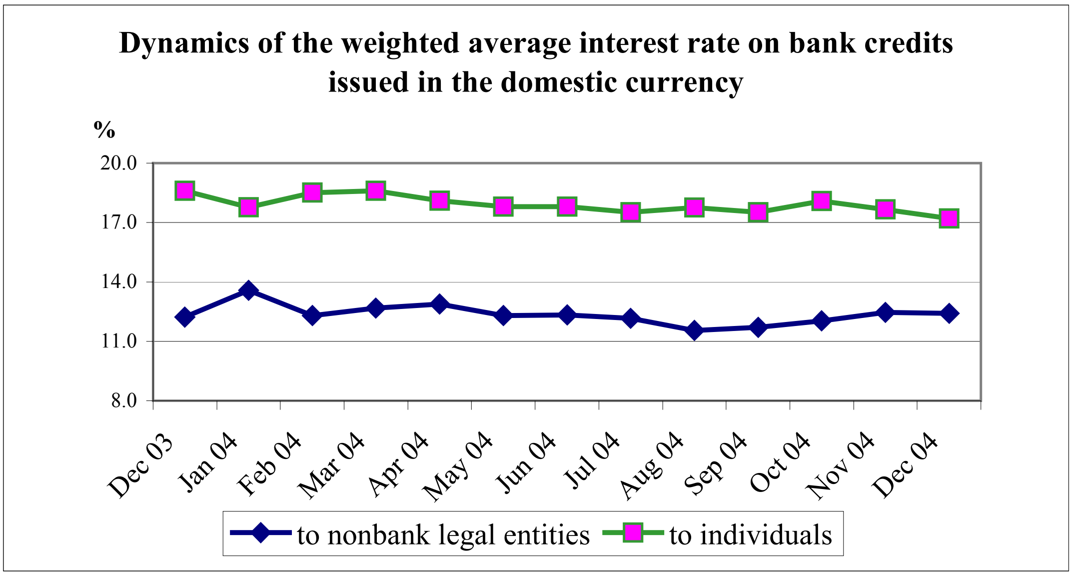


Figure 5.4.2



Appendix 2 to Section V, Subsection 5.4.1



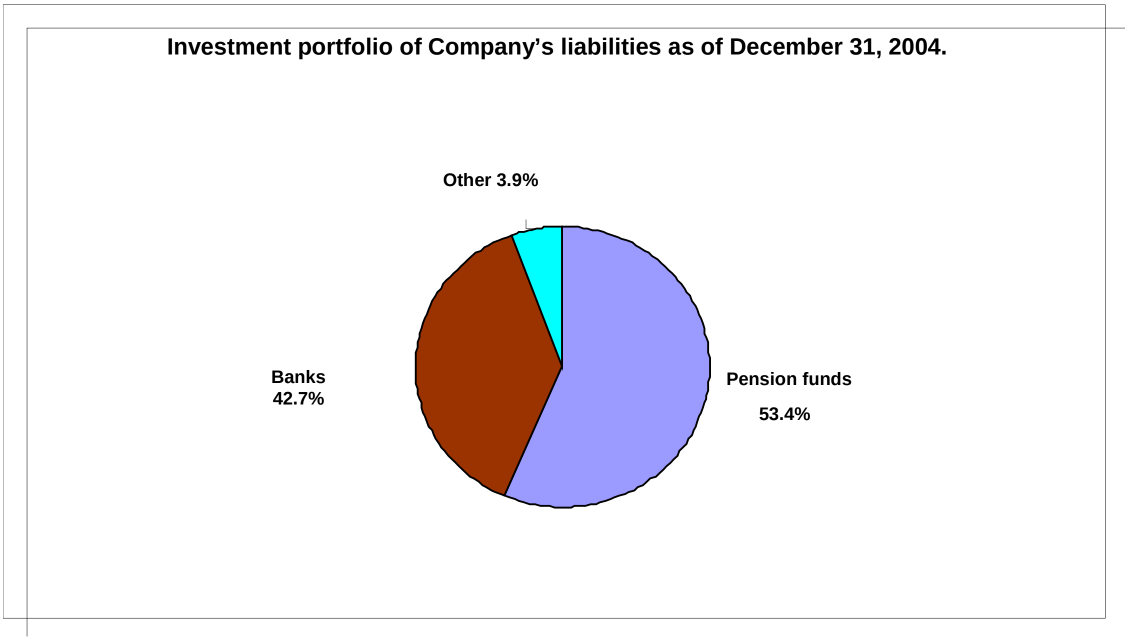
Appendix 1 to Section V, Subsection 5.4.2

Table 5.4.2.1

billions of tenge, at end of period

At year-end	Volume of mortgage credits issued			KIK's share, %
	Banks' own programs	KIK Program	Total	
December 2001	2.624	0.064	2.688	2
December 2002	7.632	1.098	8.730	13
December 2003	29.509	9.036	38.545	23
December 2004	101	26	127	29

Figure 5.4.2.2



Appendix 1 to Section VI, Subsection 6.3

Data on the Use of Payment Instruments

(in thousands of transactions and billions of tenge)

Payment instrument	2003		2004		Change	
	Number	**Amount**	**Number**	**Amount**	**Number**	**Amount**
Payment orders	19 177.4	20 774.5	25 862.9	32 269.2	34.9%	55.3%
Payment request-orders	131.5	46.6	96.0	93.5	-27.0%	by a factor of 2
Checks as payment for goods and services	246.8	191.7	215.9	205.9	-12.5%	7.4%
Direct debit from bank account	174.2	25.1	216.4	4.8	24.2%	-81.0%
Collection orders	200.3	288.0	263.6	223.9	31.6%	-22.3%
Paid bills of exchange	0.9	5.7	1.6	17.8	89.7%	by a factor of 3.1
Payment cards	28 748.3	396.2	36 611.7	566.1	27.4%	42.9%
Grand total	**48 679.4**	**21 727.7**	**63 268.1**	**33 381.2**	**30.0%**	**53.6%**

Appendix 1 to Section X, Subsection 10.1

Table 10.1.1

Structure of the Distribution of Assets by Type of National Fund Mandates

	millions of U.S. dollars	%
Money market	1 316.0	25.65
Fixed-return securities	2 450.6	47.76
Stocks	852.8	16.62
Global tactical distribution	511.2	9.96
Total	**5 130.6**	**100.00**

Table 10.1.2

Dynamics of the Distribution of Assets of the National Fund's Stabilization Portfolio

% (by value, in U.S. dollars)

U.S. dollars	Dec. 31, 2003	Dec. 31, 2004
Cash and money market instruments	76.30	93.02
Bonds	23.70	6.98
Total stabilization portfolio	**100.00**	**100.00**

Table 10.1.3

Dynamics of the Distribution of Assets of the National Fund's Savings Portfolio

% (by value, in U.S. dollars)

U.S. dollars	Dec. 31, 2003	Dec. 31, 2004
Cash and money market instruments	10.70	8.80
Fixed-return securities	67.76	64.70
Stocks	21.54	26.50
Total savings portfolio	**100.00**	**100.00**

Appendix 2 to Section X, Subsection 10.1

Table 10.1.4

Distribution of Assets in the National Fund' Savings Portfolio by Country

percent

Country	Dec. 31, 2003	Dec. 31, 2004
United States	34.2	34.5
Euro countries	40.8	41.7
Germany	10.8	14.2
France	12.5	11.2
Italy	4.7	4.1
Austria	1.9	1.5
Netherlands	3.6	4.0
Spain	2.2	1.9
Belgium	1.8	2.0
Portugal	1.1	0.0
Finland	0.8	0.9
Greece	0.6	0.6
Ireland	1.1	0.3
Euro currency*	1.4	1.0
Japan	7.3	7.9
Great Britain	7.6	7.6
Canada	2.2	2.3
Australia	1.6	0.8
Switzerland	0.9	1.1
Sweden	1.6	1.0
International financial institutions	0.6	0.5
Denmark	0.9	1.1
Other	0.6	1.5

[*] Cash and cash equivalents in euros.

Appendix 3 to Section X, Subsection 10.1

Figure 10.1.1

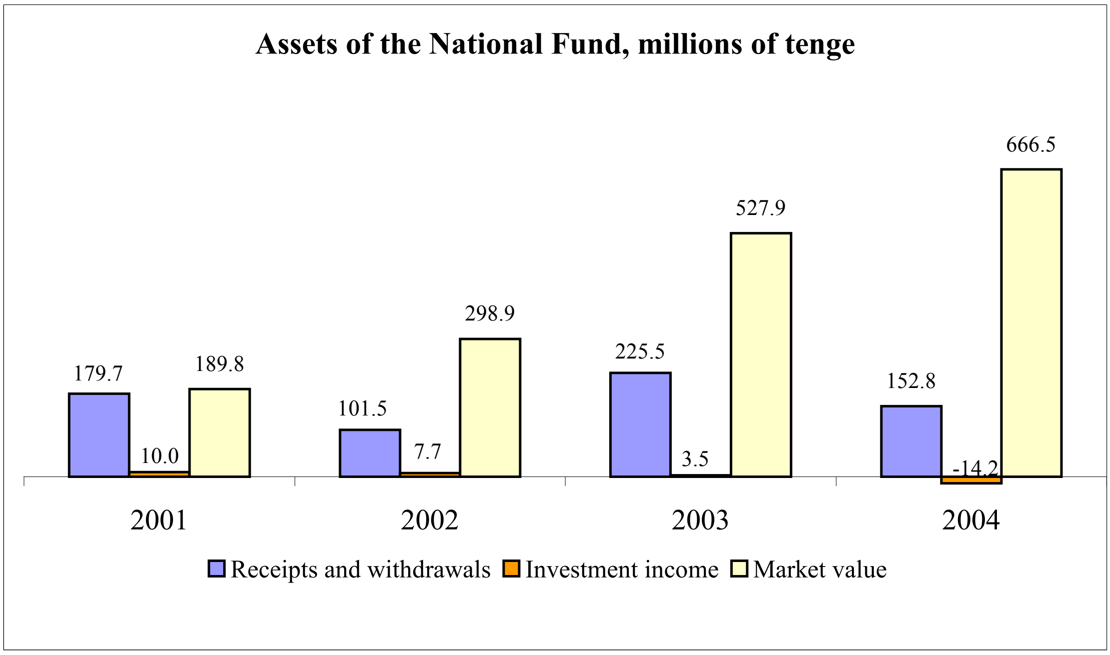
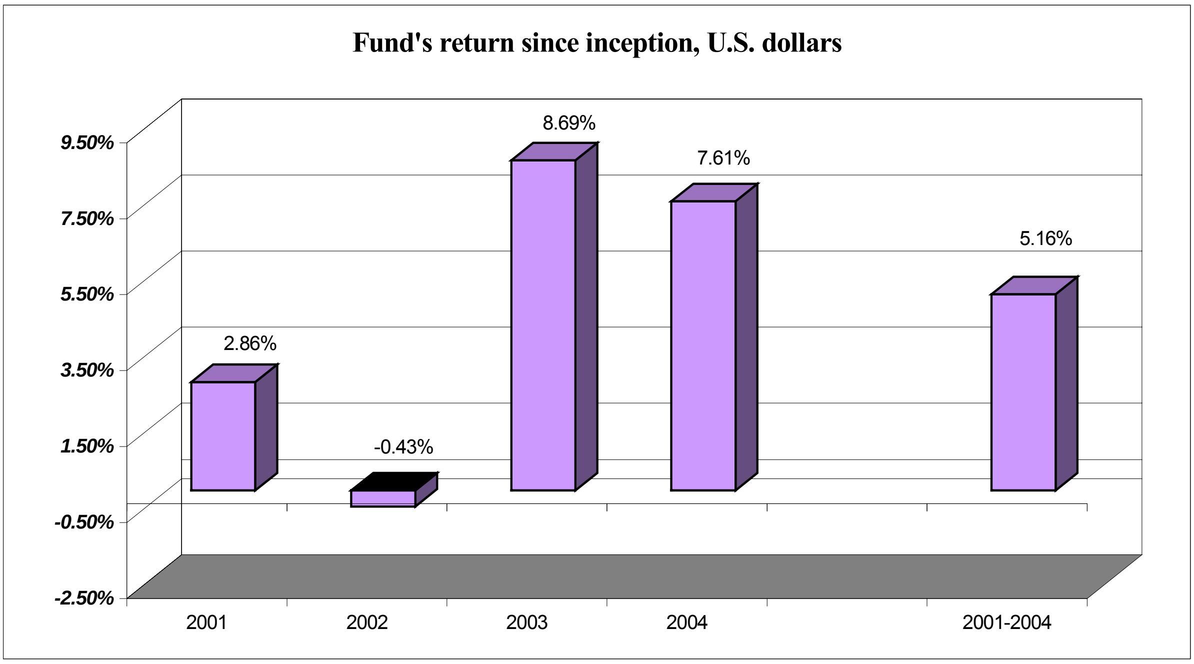


Figure 10.1.2



Appendix 4 to Section X, Subsection 10.1

Comparative Table of the Return on the Stabilization Portfolio Compared to the Benchmark Portfolio

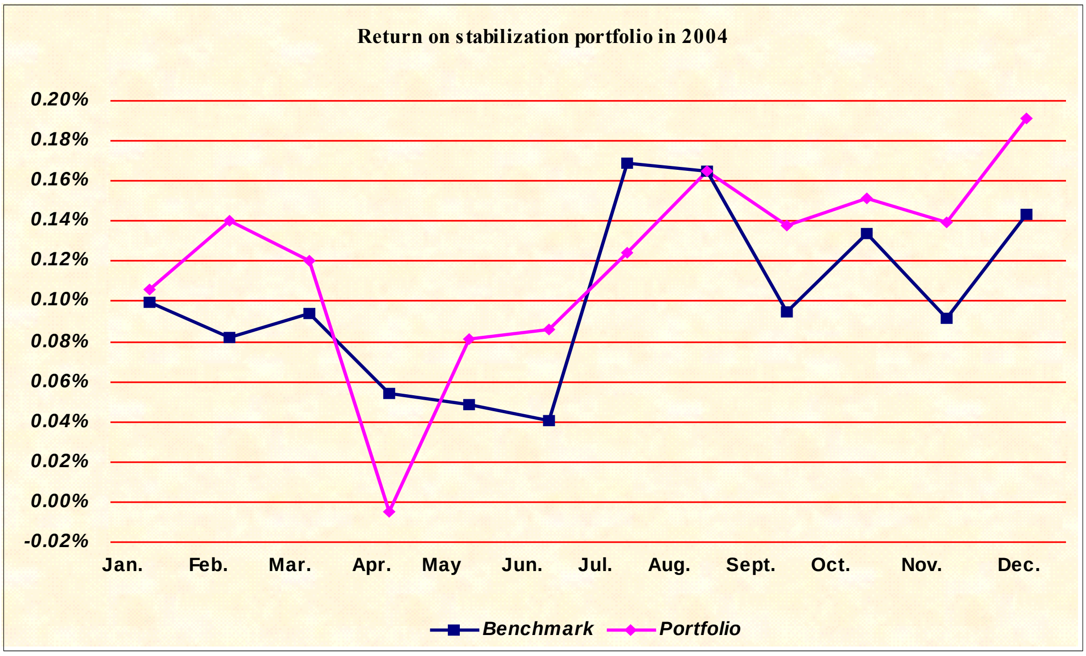
percent

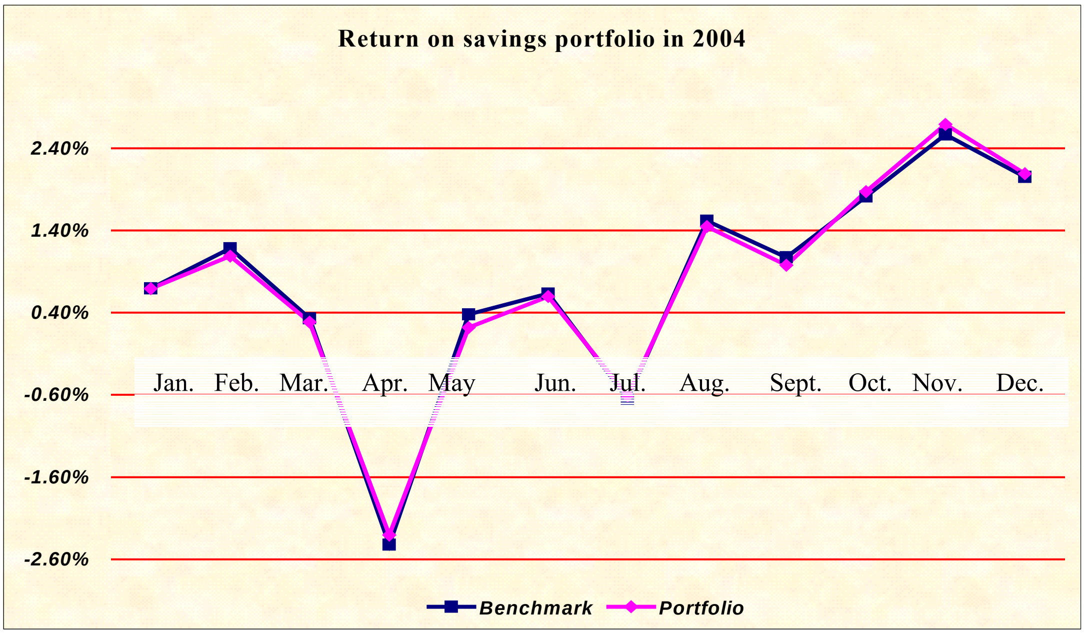
	Portfolio	Benchmark	Excess return
I quarter	0.38	0.28	0.10
II quarter	0.16	0.14	0.02
III quarter	0.42	0.43	-0.01
IV quarter	0.48	0.37	0.11
2004	**1.45**	**1.22**	**0.23**

Comparative Table of the Excess Return by Managers of the Stabilization Portfolio from January 1 through December 31, 2004

Manager	Market value, millions of U.S. dollars	Return on portfolio, %	Return on benchmark portfolio, %	Excess return, %
National Bank of the RK	1 162.5	1.45	1.22	0.23
Manager 1	153.5	1.50	1.22	0.28

Appendix 5 to Section X, Subsection 10.1





Appendix 6 to Section X, Subsection 10.1

Comparative Table of the Return on the Savings Portfolio Compared to the Benchmark Portfolio

percent

	Portfolio	Benchmark	Excess return
I quarter	2.08	2.22	-0.14
II quarter	-1.51	-1.43	-0.08
III quarter	1.82	1.94	-0.12
IV quarter	6.80	6.57	0.23
2004	**9.33**	**9.46**	**-0.13**

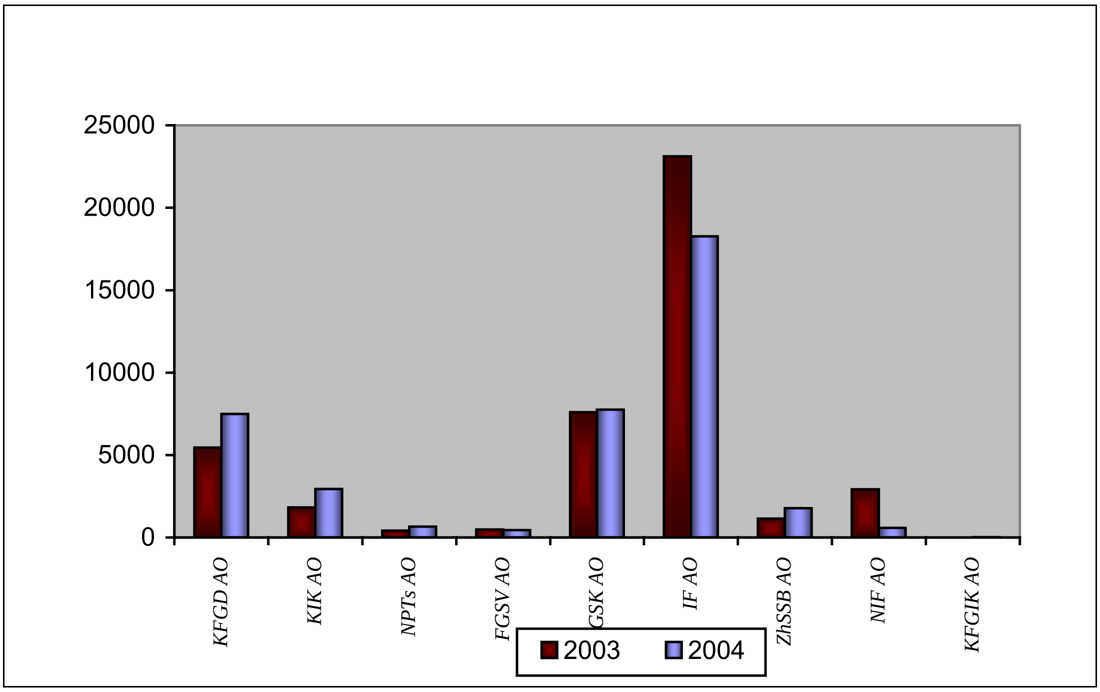
Comparative Table of Excess Return by Managers of the Savings Portfolio in 2004[6]

Manager	Market value, millions of U.S. dollars	Return on portfolio, %	Return on benchmark portfolio, %	Excess return, %
Global fixed-return bonds				
Manager 1	142.5	6.62	5.61	**1.01**
Manager 2[7]	178.8	8.41	7.88	**0.53**
Manager 3	180.2	8.23	7.88	**0.35**
Manager 4[8]	141.6	5.78	5.61	**0.17**
Manager 5	178.0	7.92	7.88	**0.04**
Manager 6	288.4	7.83	7.88	**-0.05**
National Bank of the RK	1 055.5	7.74	7.88	**-0.14**
Manager 8	285.5	7.72	7.88	**-0.16**
Global shares - passive				
Manager 10[9]	153.7	12.01	12.05	**-0.04**
Manager 11[10]	307.8	11.79	12.06	**-0.27**
Manager 12	286.3	13.68	14.21	**-0.53**
Global shares - active				
Manager 13[11]	104.9	4.59	4.32	**0.27**
Global tactical distribution of assets				
Manager 14	293.1	11.85	9.46	**2.39**
Manager 15	218.1	5.81	9.46	**-3.65**

[6] excluding the commission fee paid to managers
[7] the portfolio and benchmark returns are calculated from September 1, 2004
[8] the portfolio and benchmark returns are calculated from September 1, 2004
[9] the portfolio and benchmark returns are calculated to December 21, 2004
[10] the portfolio and benchmark returns are calculated from February 1, 2004
[11] the portfolio and benchmark returns are calculated from December 1, 2004

Appendix 1 to Section X, Subsection 10.2

Amount of Assets under Trust Management with the National Bank



[Expansion of abbreviations:
KFGD AO – Kazakhstan Deposit Guarantee Fund Joint-Stock Company
KIK AO – Kazakhstan Mortgage Company Joint-Stock Company
NPTs AO – National Processing Center Joint-Stock Company
FGSV AO – Insurance Payment Guarantee Fund Joint-Stock Company
GSK AO – State Insurance Corporation Joint-Stock Company
IF AO – Investment Fund Joint-Stock Company
ZhSSB AO – Housing Construction Savings Bank Joint-Stock Company
NIF AO – National Innovation Fund Joint-Stock Company
KFGIK AO – Kazakhstan Mortgage Credit Guarantee Fund Joint-Stock Company]

Appendix 1 to Section XI, Subsection 11.1

Organizational Structure of the National Bank and Joint-Stock Companies as of December 31, 2004 (3,522 units)

Chairman of the National Bank of the Republic of Kazakhstan

Deputy Chairmen of the National Bank of the Republic of Kazakhstan (4 positions)

Subdivisions within the central administration of the National Bank of the Republic of Kazakhstan

- Research and Statistics Dept. (42 units)
- Balance of Payments and Foreign Exchange Regulation Dept. (45 units)
- Legal Dept. (36 units)
- Monetary Operations Dept. (52 units)
- Accounting Dept. (56 units)
- Information Technology Dept. (93 units)
- Internal Audit Dept. (47 units)
- Personnel Dept. (50 units)
- Cash Operations Division (29 units)
- International Relations Division (9 units)
- Payment Systems Division (26 units)
- Administrative Support Division (20 units)
- Transactions Division (37 units)
- Budget Planning and Control Division (22 units)
- Division for the Introduction of Automated Banking Information Systems (10 units)
- Security Division (17 units)
- Document Support and Control Division (21 units)
- Facilities Administration (43 units)
- Coordination Division (City of Astana) (10 units)
- First Division (4 units)

Representative office and branch offices of the National Bank of the Republic of Kazakhstan

- NBRK Representative Office in the Russian Federation (1 unit)
- 16 regional branch offices (928 units)
- Cash Transactions and Safe Deposit Center (branch office) (381 units)

Organizations of the National Bank of the Republic of Kazakhstan

- Kazakhstan Center for Interbank Settlements of the NBRK RSE (67 units)
- Bank Service Bureau of the NBRK RSE (69 units)
- Kazakhstan Mint of the NBRK RSE (336 units)
- Motor Pool of the NBRK RSE (167 units)
- Almaty Building Maintenance Center of the NBRK RSE (KP) (383 units)
- Banknote Factory of the NBRK RSE (357 units)

[RSE – Republican State Enterprise]

Joint-stock companies

- Kazakhstan Deposit Guarantee Fund JSC (15 units)
- National Processing Center JSC (22 units)
- Kazakhstan Mortgage Company JSC (86 units)
- Kazakhstan Actuarial Center JSC (10 units)
- Insurance Payment Guarantee Fund JSC (9 units)
- Kazakhstan Mortgage Credit Guarantee Fund JSC (17 units)

Appendix 1 to Section XI, Subsection 11.2

Table 11.2.1

Number of Personnel at the National Bank and Joint-Stock Companies

	Number at year-end				Turnover rate, %	
	Staff, units		Established, people			
	2003	2004	2003	2004	2003	2004
1	2	3	4	5	6	7
Central administration	859	675	798	608	13.1	14.6
Branch offices	1712	1309	1693	1300	10.3	10.6
Total:	**2571**	**1984**	**2491**	**1908**	**11.2**	**11.8**
Organizations under the NBRK (republican state enterprises)	977	1379	965	1341	16.4	14.8
Total for the NBRK:	**3548**	**3363**	**3456**	**3249**	**12.5**	**12.9**
Joint-stock companies	86	159	72	135	42.1	27.8
Total:	**3634**	**3522**	**3528**	**3384**	**13.0**	**13.4**

Table 11.2.2

Payroll Expenses Including Social Tax, and Average Monthly Wages

	Actual payroll expenses, including social payments, insurance for personnel, and social tax, millions of tenge			Average monthly wages per employee, tenge		
	in 2003	in 2004	as % of 2003	in 2003	in 2004	as % of 2003
1	2	3	4	5	6	7
Central administration	1655.9	1325.9	80.1	132 399	165 054	124.7
Branch offices	1367.4	1120.8	82.0	54 605	58 526	107.2
Total:	**3023.9**	**2446.7**	**80.9**	**79 839**	**89 710**	**112.4**
Organizations under the NBRK (republican state enterprises)	703.1	1012.8	144.0	54 648	57 390	105.0
Total for the NBRK:	**3726.4**	**3459.5**	**92.8**	**73 430**	**77 049**	**104.9**
Joint-stock companies	195.4	322.9	165.3	210 909	199 816	94.7
Total:	**3921.8**	**3782.4**	**96.4**	**75 776**	**81 125**	**107.1**

Appendix 1 to Section XI, Subsection 11.5

Table 11.5.1

Operating Results of the National Bank

million tenge

	2003				2004				difference (2004/2003)	
	NBK	Republican state enterprises	Closed joint-stock companies	Total	NBK	Republican state enterprises	Closed joint-stock companies	Total	+/-	%
Income *	55 159.4	1 876.8	1 531.7	58 567.9	38 827.2	5 584.6	3 620.3	48 032.1	-10 535.8	18.0
Expenses *	38 682.1	1 624.5	1 053.7	41 360.3	45 256.7	4 250.0	2 879.8	52 386.5	11 026.2	26.7
Undistributed profit/loss	**16 477.3**	**252.3**	**478.0**	**17 207.6**	**-6 429.4**	**1 334.6**	**740.5**	**-4 354.3**	**-21 561.9**	**125.3**
Revaluation of retired fixed assets					73.4			73.4	73.4	100.0
Corporate income tax		104.9	0.4	105.3		474.3	7.0	481.3	376.0	357.1
Balance of undistributed profit/loss **	**16 477.3**	**147.4**	**477.6**	**17 102.3**	**-6 356.1**	**860.3**	**733.5**	**-4 762.3**	**-21 864.6**	**127.8**

* - income and expenses for the National Bank's monetary activity are on a net basis

** - losses are compensated for out of reserve capital

Table 11.5.2

Income and Expenses of the National Bank from Monetary Activity

million tenge

№	Item	Net result		Difference	
		2003	2004	+/-	%
1	**Foreign market**	**11 295.3**	**15 151.6**	**3 856.3**	**34.1**
1.1	**Management of gold and foreign exchange assets**	11 726.9	15 151.2	3 424.3	29.2
1.1.1	Gold portfolio	-2 533.4	-55.8	2 477.6	97.8
1.1.2	Foreign exchange portfolio	14 260.3	15 207.0	946.7	6.6
1.1.2.1	Under external management	2 088.5	619.2	-1 469.3	70.4
1.1.2.2	Under internal management	12 171.8	14 587.8	2 416.0	19.8
1.2	Other	-431.6	0.4	432.0	100.1
2	**Domestic market**	**1 643.6**	**-16 052.0**	**-17 695.6**	**by a factor of 9.8**
2.1	Transactions with the government	-1 821.0	-1 682.1	138.9	7.6
2.2	Liquidity management (sterilization of excess liquidity	-9 124.4	-14 377.4	-5 253.0	57.6
2.3	Establishment and elimination of provisions	12 589.0	7.5	-12 581.5	99.9
3	**Realized revaluation**	**12 262.6**	**22 485.1**	**10 222.5**	**83.4**
4	**Unrealized revaluation**		**-20 396.1**		**100.0**
	Result from monetary activity	**25 201.5**	**1 188.6**	**-24 012.9**	**95.3**

Appendix 2 to Section XI, Subsection 11.5

Income and Expenses of the National Bank on Nonmonetary Activity

million tenge

№	Item	2003	2004	Difference	
				+/-	%
1	**Total income**	**1 569.9**	**1 190.6**	**-379.3**	**24.2**
1.1	**Current income**	**1 385.1**	**1 086.8**	**-298.3**	**21.5**
1.1.1	On cash transactions	54.7	114.0	59.2	108.2
1.1.2	Reimbursed expenses	498.2	619.5	121.3	24.3
1.1.3	On transactions with unrefined precious metals and precious stones	6.0	0.3	-5.7	94.5
1.1.4	Other income	826.1	353.0	-473.1	57.3
	including the Banknote Factory	520.0	214.0	-306.0	58.8
1.2	**Contingent income**	**179.8**	**86.4**	**-93.4**	**51.9**
1.3	**Elimination of provisions established previously**	**5.0**	**17.4**	**12.4**	**248.3**
2	**Total expenses**	**10 188.9**	**8 808.6**	**-1 380.3**	**13.5**
2.1	**Current expenses**	**8 696.7**	**8 573.7**	**-123.0**	**1.4**
2.1.1	On the manufacture of banknotes and coins in the domestic currency and their delivery	2 938.4	2 508.8	-429.6	14.6
2.1.2	On the payment of commissions for National Bank transactions	46.1	38.3	-7.8	17.0
2.1.3	On transactions with fixed assets, intangible assets, and commodity stocks	1 159.4	1 351.5	192.1	16.6
2.1.4	Other	526.2	405.5	-120.7	22.9
2.1.5	On personnel	2 737.6	2 864.3	126.7	4.6
2.1.6	On insurance for personnel	36.0	29.9	-6.1	17.0
2.1.7	On the training and retraining of personnel	60.5	63.3	2.8	4.6
2.1.8	On business travel	83.4	88.1	4.7	5.6
2.1.9	Administrative expenses	1 109.1	1 224.1	115.0	10.4
2.2	**Contingent expenses and expenses on the establishment of provisions**	**1 492.2**	**234.9**	**-1 257.3**	**84.3**
	Result from nonmonetary activity	**-8 619.0**	**-7 618.0**	**1 001.0**	**11.6**

Appendix 3 to Section XI, Subsection 11.5

Capital Expenditures of the National Bank

million tenge

№	Item	2003	2004	Difference	
				+/-	%
1	Construction projects	193.9	88.6	-105.3	54.3
2	Reconstruction and expansion of existing production facilities	17.7	0.5	-17.2	97.2
3	Major renovation resulting in an increase in the value of fixed assets	16.2	413.0	396.8	by a factor of 25.5
4	Acquisition of fixed assets	1 029.0	743.3	-285.7	27.8
	- computer equipment	551.2	227.0	-324.2	58.8
	- motor vehicles	130.7		-130.7	100.0
	- security and alarm systems	73.1	140.3	67.2	91.9
	- equipment for the mechanization of cash transactions	5.0	165.1	160.1	by a factor of 33
	- machinery and equipment	134.6	6.1	-128.5	95.5
	- communications equipment	52.3	115.3	63.0	by a factor of 2.2
	- other stock	82.2	89.5	7.3	8.9
5	Acquisition of intangible assets	254.6	370.5	115.9	45.5
6	Other expenditures	2 048.6	1 022.4	-1 026.2	50.1
	Total capital expenditures	**3 560.0**	**2 638.3**	**-921.7**	**25.9**

Appendix 4 to Section XI, Subsection 11.5

Operating Results of National Bank Subsidiaries

million tenge

№	Item		Income				Expenditures				Net after-tax income			
			2003	2004	Rate of increase (decline) +,-	%	2003	2004	Rate of increase (decline) +,-	%	2003	2004	Rate of increase (decline) +,-	%
	Republican state enterprises		**1876.8**	**5584.6**	**3707.8**	**197.5**	**1624.5**	**4250.0**	**2625.5**	**161.6**	**147.5**	**860.3**	**712.8**	**483.2**
1	KMD		651.9	1276.4	624.5	95.7	589.5	1076.9	487.4	82.6	27.6	136.2	108.6	393.4
2	KTsMR		668.0	1109.4	441.4	66.0	450.1	579.0	128.9	28.6	150.3	363.9	213.6	142.1
3	BSB		191.8	277.4	85.6	44.6	189.5	261.6	72.1	38.0	0.5	10.8	10.3	2060.0
4	Avtobaza		199.4	440.6	241.2	120.9	230.0	237.5	7.5	3.2	-30.5	141.9	172.4	565.2
5	AETsZ		165.7	274.9	109.2	65.9	165.4	260.4	95.0	57.4	-0.4	9.7	10.1	2525.0
6	BF *			2205.9				1834.6				197.8		
	Joint-stock companies		**1531.7**	**3620.3**	**2088.6**	**136.3**	**1053.7**	**2879.8**	**1826.1**	**173.3**	**477.6**	**733.5**	**255.9**	**53.5**
7	KFGD		514.9	562.8	47.9	9.3	66.0	204.8	138.8	210.3	448.9	357.9	-91.0	-20.2
8	KIK**	NBRK's	452.8	2127.0	1674.2	369.7	310.0	1773.2	1463.1	471.9	142.8	353.8	211.0	147.7
9	KATs	stake	10.1	6.9	-3.2	-31.6	20.6	18.5	-2.2	-10.6	-10.5	-11.6	-1.1	10.4
10	FGSV	100%	347.0	56.8	-290.2	-83.6	345.9	52.7	-293.2	-84.7	0.7	4.2	3.5	500.0
11	KFGIK		0.4	145.1	144.7	36175.0	2.9	58.4	55.5	1913.7	-2.5	86.6	89.1	3564.0
12	NPTs (NBRK's stake – 80,6%)		206.5	68.3	-138.2	-66.9	308.3	190.1	-118.3	-38.3	-101.8	-121.7	-20.0	19.6
13	NPF GNPF (NBRK's stake – 64%)***			653.4				582.1				64.3		

** - functioning as a republican state enterprises since April 1, 2004*
*** - In connection with the National Bank's sale of KIK shares to the Ministry of Finance in 2005, the operating results of KIK have not been consolidated within the National Bank's financial statements.*
**** - the National Bank acquired shares in GNPF AO in 2004*

KMD – Kazakhstan Mint
KTsMR – Kazakhstan Center for Interbank Settlements

BSB – Bank Service Bureau
AETsZ – Almaty Building Maintenance Center
BF – Banknote Factory
KFGD – Kazakhstan Deposit Guarantee Fund
KIK – Kazakhstan Mortgage Company
KATs – Kazakhstan Actuarial Center
FGSV – Insurance Payment Guarantee Fund
KFGIK – Kazakhstan Mortgage Credit Guarantee Fund
NPTs – National Processing Center
NPF GNPF – State Pension Savings Fund Pension Savings Fund