

National Bank
National Bank
of the Republic of Kazakhstan
of the Republic of Kazakhstan

Inflation Report 1st quarter 2006

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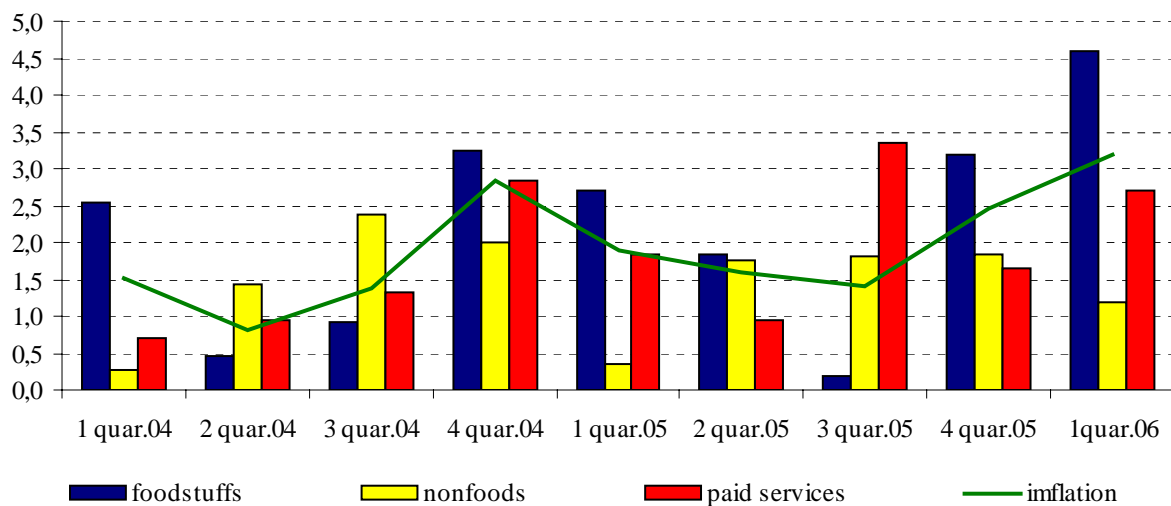
1. Inflation

a. Consumer prices

Acceleration of rise in prices in the consumer market as against both the previous quarter and compared with the corresponding period in the previous year was observed in the 1st quarter of 2006. For example, as per the results of the 1st quarter of 2006 the growth of consumer prices has reached the level of 3.2% (graph 1). Excess of the rate of inflation at the current year compared with indices of 2005 has been caused by higher monthly rates of inflation. It was particularly obvious in February 2006 when the monthly inflation rate was 1.5 %, and it has been the maximum monthly inflation rate since December 2003.

Graph 1

Dynamics of inflation and its components (% of the preceding period)



Source: The Agency of the Republic of Kazakhstan for Statistics

The prices of foodstuffs in January-March 2006 rose by 4.6%. The highest price advance in their structures fell to fruit and vegetable products and sugar. Besides, fish and sea-foods, meat products and dairy produce became more expensive. Prices of eggs were recorded as dropped.

Among nonfoods which appreciated by 1.2% in the 1st quarter of 2006, the garments and footwear, dishes, printed matters and medicine grew dear.

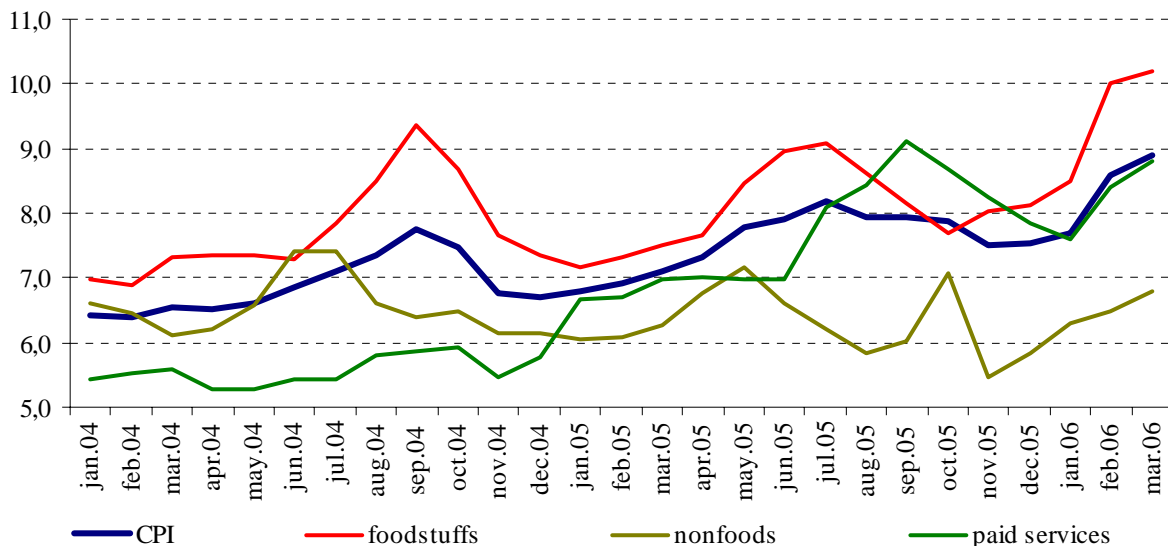
The rise of prices and tariffs of paid services to the population in the 1st quarter of 2006 reached the rate of 2.7%. Dynamics of prices of the housing and communal services was conditioned by appreciation of services for maintenance of housing, gas utilities and electric power supply. Also, the services of cultural and educational institutions, transport, communications and medical services rose in prices as well.

The higher growth rates of consumer prices in the 1st quarter of 2006 as against the corresponding period of 2005 caused the increase of inflation rate in annum terms from 7.5% in December 2005 up to 8.9% in March 2006 (7.1% in March 2005). Thus, the growth of consumer prices was primarily caused by the appreciation of foodstuffs and paid services to the population by 10.2% and 8.8% respectively, whereas nonfoods grew dear by 6.8% (Graph

2). In annum terms the main price appreciation covered sugar, fruit and vegetable products, rice, gasoline, gas utilities and transport services.

Graph 2

Dynamics of inflation and its components
(% of the corresponding month of the previous year)



Source: The Agency of the Republic of Kazakhstan for Statistics

The growth of consumer prices in January-March 2006 was affected by the situation in some markets of goods and services, mainly sugar and likewise fruit and vegetable products and transport services.

The sugar price increased in the 1st quarter of 2006 by 28.1% thus causing inflation, by National Bank's estimates at nearly 0.6% out of 3.2%. Dynamics of changes in sugar prices in the past proves that they were changing insignificantly. For example, in 2000 the sugar prices decrease by 3.0%, in 2001 they rose by 0.3%, in 2002 they boosted by 0.4%, in 2003 they did not change, in 2004 they increased by 1.9% and in 2005 by 0.6%. This year, however, the rate of domestic prices of sugar was greatly affected by the situation in the foreign markets including those in the Russian Federation.

E.g. in accordance with data of the International Monetary Fund, the average sugar price in the world market in 2005 compared with data for 2004 boosted by 20.4%. Sugar prices for the 1st quarter of 2006 rose by 19.6% up to 17.1 cents per pound. The last time the prices increase that high in 1981. Appreciation of sugar in the world market can be explained by the use of sugar for the production of alternative types of fuel and the common deficit of sugar too.

Regarding the Russian sugar market it should be noted that the domestic prices of sugar in Russia have been soaring since the end of 2005. The situation in the Russian sugar market is mainly attributed to the fact that Russia produces less sugar than it consumes and, respectively the country is dependent upon the world sugar prices. In this case sugar appreciates in Russia despite considerable reduction on import duties on it. As a result, the Russian market is more attractive for import of sugar than the markets of other CIS countries.

Appreciation of fruit and vegetable products by 19.5% in the 1st quarter of 2006 can be explained by seasonality reasons.

A number of macro-economic factors were affecting the dynamics of prices in the consumer market in the 1st quarter of 2006, and these factors have been influencing the inflation for already a long time. The affection of these factors causes the imbalance between

aggregate demand and aggregate supply in the economy. The rates of growth of aggregate demand outrun the rates of expansion of aggregate supply entailing the rise in prices in the economy.

The growth of aggregate demand is strengthened by the increase in revenues of all subjects of economy (population, enterprises, state) and the credit expansion of second tier banks and a significant inflow of foreign capital in the country.

The real money incomes of the population in January-March 2006 as compared with those in 2005 increased by 15.5%. The increase in incomes of the population is expressed in the growth of consumption and namely that of retail turnover. E.g. the growth of retail trade turnover in January-March 2006 as against the corresponding period of 2005 made 12.9%.

Despite the significant economic growth that has been observed for the recent years the rates of expansion of retail turnover outstrip the rates of growth of real GDP. For instance, the real GDP for the 1st quarter of 2006 rose by 7.7%.

The real wages in January-March 2006 as against the corresponding period of 2005 were raised by 15.1% and the labor productivity for the same period increased by 5.0%. Thus, the rates of growth of wages outstrip those of the labor productivity and this outstrip promotes the rise of inflationary pressure in the economy.

Besides, the increase in revenues of subjects of economy causes demand for money. The relevant increase of monetary offer is ensured by the expansion of banks' crediting of economy and the inflow of foreign capital.

E.g. for the 1st quarter of 2006 the growth of credits by the second tier banks made 5.4% including the rise of consumer credits' volumes by 12.2%.

Expansion of crediting of economy and the significant inflow of foreign exchange is mainly conditioned by the growth of volumes of borrowings of the second tier banks in the foreign market and likewise the increase of world prices especially those of oil as well. For example, as of the end of March 2006 the volume of gross liabilities of the second tier banks to nonresidents in the foreign market in freely convertible currencies reached the amount of USD17.7 billion having risen by 11.4% for January-March 2006. In March 2006 the average price of Brent crude oil in the world markets amounted to USD 62.3 per barrel having been risen by 9.7% as against December 2005. As compared with March 2005 the oil price grew by 17.3%.

Significant growth of demand against the high credit activity and liquidity of second tier banks and also the considerable inflow of foreign capital in the country entail the growth of monetary aggregates. E.g. the money supply in the 1st quarter of 2006 increased by 12.9% (the growth by 5.8% in the 1st quarter of 2005), money in circulation grew by 6.0% (reduction by 3.8% in the 1st quarter of 2005).

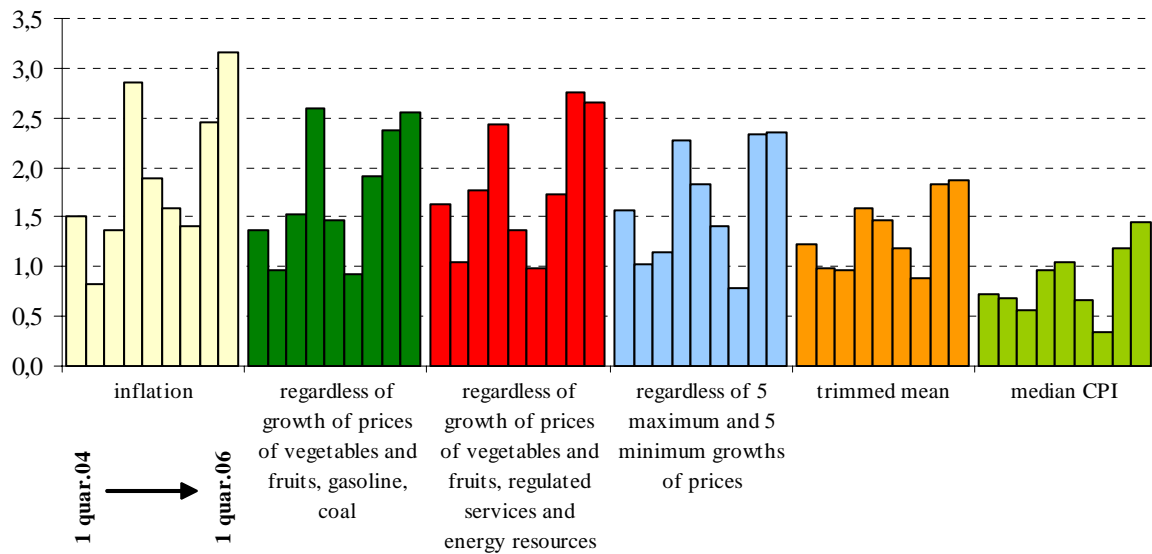
Aggregate demand "is warmed up" by significant budget expenses and it also promotes increase in the inflationary pressure. The expenditure of the state budget for January-March 2006 went up by 53.9% as compared with the corresponding period of the previous year.

b. Core inflation

The growth of general rate of prices in the consumer market in the 1st quarter of 2006 as against the previous quarter was accompanied by the growth of core inflation calculated by all the methods excepting the core inflation as per the variant 2 (Graph 3).

Graph 3

Inflation and core inflation in 2004-2005 (in % of the previous period)



Source: The Agency of the Republic of Kazakhstan for Statistics

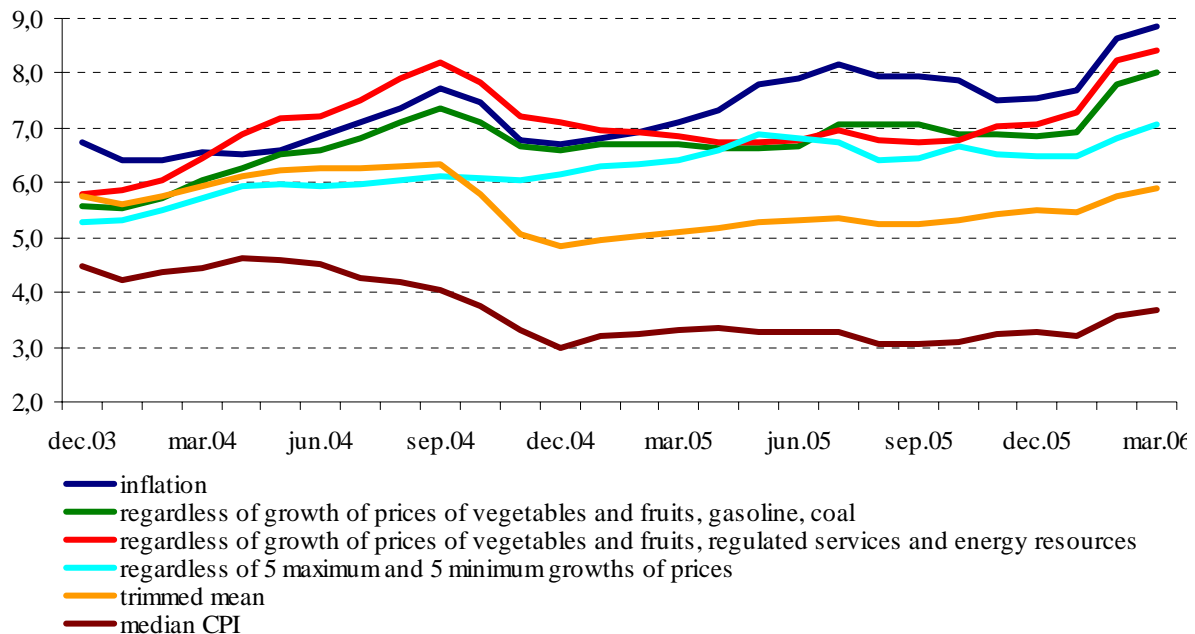
In January-March 2006 the rates of growth of general inflation outran the rates of growth of core inflation calculated by all the methods, as a result of a significant growth of prices of goods and services excluded at calculating it (fruits and vegetables, sugar, regulated services). In 2006 the high growth of prices of transport services, in its turn, made it possible for the core inflation under variant 2 to take place at a higher rate compared with that of variant 1.

Dynamics of core inflation by all the methods in annum terms was inclined to grow and at the same time the values of indices of core inflation did not exceed the index of general inflation (Graph 4).

Acceleration of growth rates of general inflation in the 1st quarter of the current year was specific to that period and better dependent on situations in some commodity markets. Dynamics of inflation was measured by a significant growth of prices of some types of foodstuffs and paid services to the population, i.e. the factors that affect consumer prices are not attributed to the category of long-term ones and are of local nature.

Graph 4

Inflation and core inflation (% in annum terms)



Source: The Agency of the Republic of Kazakhstan for Statistics

c. Prices in real sector of economy

Prices in industrial production

As per data of the Agency of the Republic of Kazakhstan for Statistics, in the 1st quarter of 2006 the producing enterprises increased prices by 6.4% (by 5.3% in the 1st quarter of 2005). The output appreciated by 6.6% and prices of production services rose by 3.3%. Out of products groups classified in accordance with the final end use of them the products of interim consumption appreciated by 7.1%, means of production by 4.3% and consumer goods by 3.5%.

In January-March 2006 the prices of output of mining industry increased by 9.5% (by 7.3% in January-March 2005). The prices grew dear mainly in recovery of oil and gas condensate. Prices of the producing enterprises for oil products in the 1st quarter of 2006 reduced by 0.7% due to the reduction of prices of motor gasoline by 2.5%, at the same time black oil appreciated by 4.7% and diesel fuel by 2.7%. All in all, the producers' prices of energy resources in January-March 2006 appreciated by 9.3% (by 5.5% in the 1st quarter of 2005).

Growth of producers' prices in the manufacturing industry in the 1st quarter of 2006 compared with the corresponding period of 2005 slowed down: 2.4% against 3.6%. Significant rise in prices of non-ferrous metals caused appreciation of them in the domestic market as well. E.g. zinc, untreated aluminium and copper. And on the contrary, rolled ferrous metals and ferroalloys depreciated.

For January-March 2006 the growth of prices of foodstuffs produced in the republic made 3.2%. The highest appreciation was registered at producing sugar. Fish and seafood, dairy produce and meat and meat products also grew dear.

Prices and tariffs in the production and distribution of electric energy, gas and water in the 1st quarter of 2006 went up by 2.4% (by 1.9% in the 1st quarter of 2005).

In March 2006 the annual rise of prices in the industrial production (March 2006 against March 2005) reached the rate of 21.5% (20.3% in 2005).

Prices in agriculture

In accordance with data of the Agency of the Republic of Kazakhstan for Statistics, the selling prices set by the producers of agricultural products in the 1st quarter of 2006 rose by 0.9% (by 1.3% in the 1st quarter of 2005). Dynamics of prices in agriculture was formed against the appreciation of livestock products by 2.5% and at the same time the crop production products fell in price by 0.3%.

Among the livestock products the prices of milk, pork, meat of cattle, horses and sheep appreciated to a greater extent in the 1st quarter of 2006. Poultry and eggs reduced in prices.

Reduction in prices of crop production products at the period analyzed was conditioned by cheapening of grain crops including wheat. At the same time there was a seasonal increase in prices of vegetables including crops under glass (tomatoes, cucumbers) potatoes, bulb onion, carrot.

Prices of agricultural products in March 2006 compared with those in March 2005 did not change (they rose by 0.4% in 2005). At the same time the livestock products grew dear by 9.4% (by 10.5% in 2005) and the crop production products became cheaper by 7.1 (by 7.2% in 2005).

Monitoring of enterprises

27.2% of polled enterprises (35.3% in the 4th quarter of 2005) noted the increase in demand for finished products in the 1st quarter of 2006 as against the previous quarter, and there was a simultaneous increase in a share of enterprises with a steady demand (from 48.7% up to 56.4%). Reduction of a share of enterprises with a steady demand (down to 44.2%) is expected in the 2nd quarter of 2006 and 35.5% of enterprises which participated in the head count, expected increase in demand.

The backset of situation concerning prices of finished products was observed in the 1st quarter of 2006 as against those in the 4th quarter of 2005. 29.5% of enterprises stated the price advance, whereas in the previous quarter their share was 24.2%. Besides, the share of enterprises with stable prices reduced from 68.9% to 65.6%. The 2nd quarter of 2006 is expecting some stabilization of situation concerning prices: the share of enterprises with stable prices will be reduced to 57.8% and the share of enterprises the price advance for the product of which is projected, will be decreased to 26.7%.

The situation regarding prices of raw and other materials did not improve in the 1st quarter of 2006 (as against that in the 4th quarter). The share of enterprises which noted the price advance increased from 54.1% up to 55.4% and 40% of polled enterprises noted a stability of prices, whereas the share of them in the previous quarter was 40.6%. 29.4% of enterprises were expecting a stability of prices in the 2nd quarter and 47.2% of enterprises polled were expecting a rise in prices.

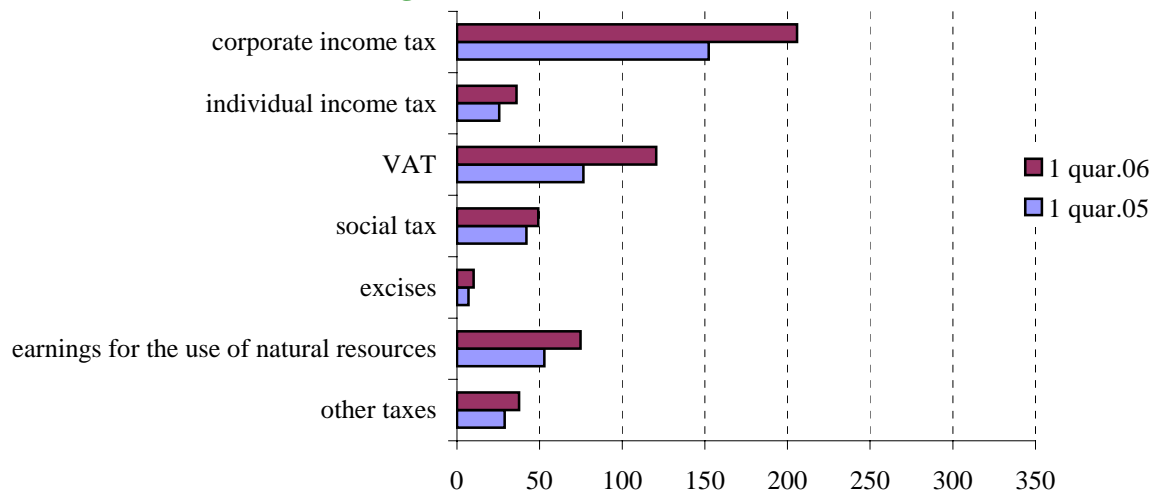
2. Fiscal policy

In accordance with data of the Ministry of Finance of the Republic of Kazakhstan, the revenues in the state budget for the 1st quarter of 2006 amounted to 556.8 billion Tenge. Compared with the indices of the corresponding period of the previous year they were increased by 40.6%.

The main volume of revenues in the state budget falls on tax revenues (95.9%) in the structure of which the largest are still the corporate income tax, VAT, social tax, revenues for the use of natural resources (Graph 5). As against those in the 1st quarter of 2005, the revenues on VAT at the period under consideration were increased by 57.8% due to the growth of charges from both the products of domestic production and imported goods. Excise duties were risen by 43.8%, collections from the individual income tax and revenues for the use of natural and other resources by 41.6% each. Earnings on the corporate income tax were increased by 35.1%.

Graph 5

Tax revenues in the state budget, billion KZT



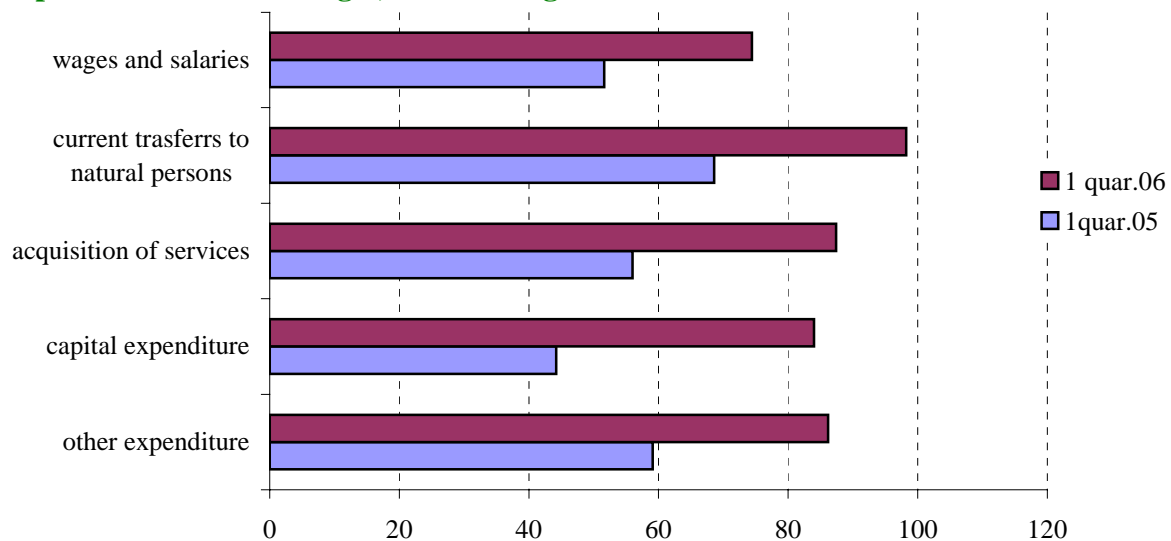
Source: The Ministry of Finance of the Republic of Kazakhstan

Non-tax revenues in the state budget increased by 26.5%. The growth of non-tax revenues was provided by the increase in taxes from the public property (by 6.8%) primarily due to the earnings of the rent for the use of the “Baikonyr” complex, penalties, fines, sanctions (by 3.4%) as well as other non-tax revenues (by 3.3 times as much).

Earnings from sales of fixed assets were increased by 3.5 times as much due to the growth of revenues from sales of the public property of the public institutions, goods sold from the public material reserve and from sales of land and intangible assets.

In the 1st quarter of 2006 the expenditure of the state budget were financed to the amount of 430.1 billion Tenge. As against the indices of the similar period of the previous year, the expenditure increased by 53.9%. Current expenses in the 1st quarter of 2006 increased by 51.3%, and capital expenditure increased by 90.2% (Graph 6).

Graph 6

Expenditure of state budget, billion Tenge

Source: The Ministry of Finance of the Republic of Kazakhstan

Expenses paid in cash (current transfers to natural persons and expenses on wages) which have a considerable influence on the dynamics of cash, share a great part in the structure of the budget expenditure. Wage-and-salary disbursements increased by 44.3% and transfers to natural persons increased by 43.2%.

As a result of revenues over expenditure the state budget was formed with the positive operational balance amounting to 126.7 billion Tenge, which is 8.7% more than in the 1st quarter of 2005.

The volume of net budget crediting (budget credits less redemption of them) in the 1st quarter of 2006 made 4.8 billion Tenge, whereas at the corresponding period of 2005 it was 1.3 billion Tenge. The growth was due to the increase in volume of extended credits by 26.5% and to the reduction of returns on redemption of them by 2.6 times as little.

The balance on operations with financial assets made 46.8 billion Tenge against 65.8 billion Tenge.

As a result, the state budget in the 1st quarter of 2006 was formed with a surplus amounting to 75.0 billion Tenge (49.9 billion Tenge in the 1st quarter of 2005) (Graph 7).

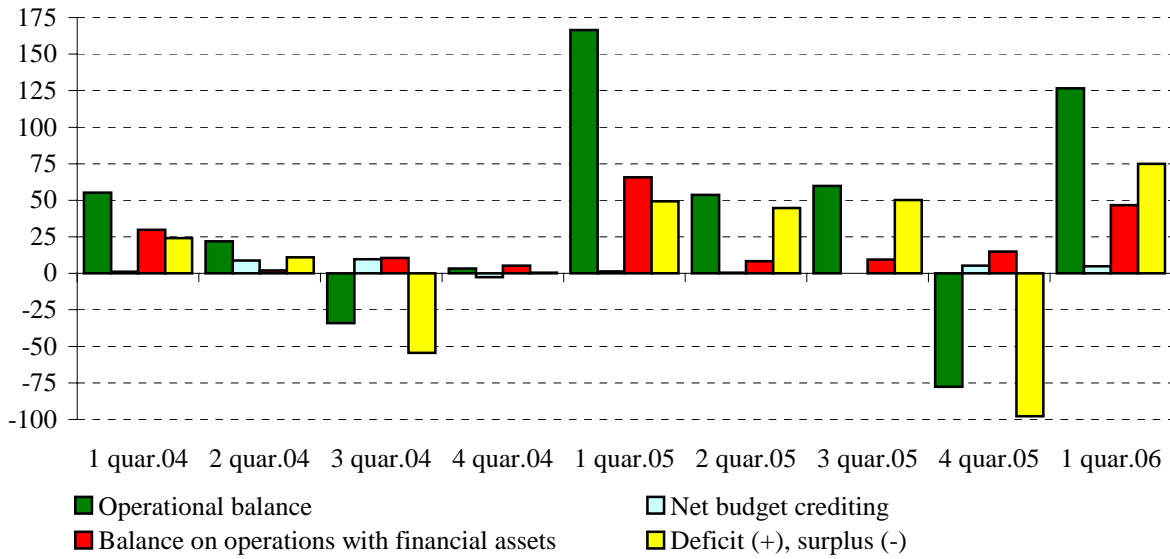
The sources of financing of a possible deficit were formed as follows: proceeds of loans to 38.9 billion Tenge and repayment of them to 22.9 billion Tenge. As a result, for the 1st quarter of 2006 temporarily free funds of the Government were increased by 91.0 billion Tenge.

The Governmental internal debt in March 2006 as against December 2005 increased by 4.3% amounting to 310.8 billion Tenge and it was secured by issuing the mid-term and long-term Treasury obligations.

The Government's foreign debt in the 1st quarter of 2006 compared with that in the previous quarter grew by 1.1% amounting to USD 1.8 billion (Graph 8).

Graph 7

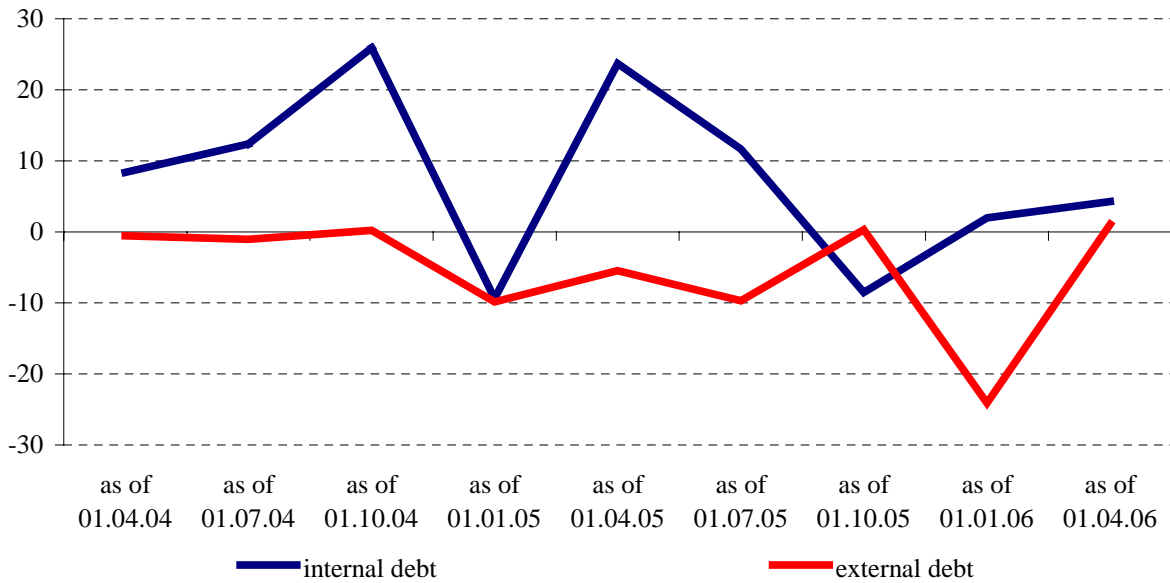
Administration of the state budget, billion Tenge



Source: The Ministry of Finance of the Republic of Kazakhstan

Graph 8

Dynamics of Government's debt (% of the previous period)



Source: The National Bank of the Republic of Kazakhstan

3. Monetary policy

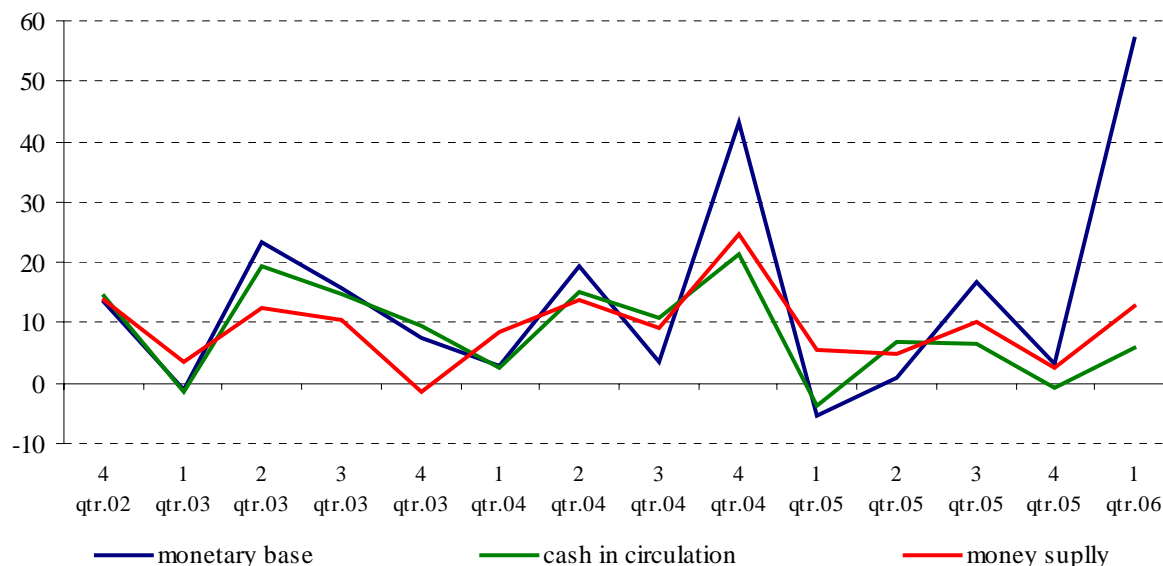
a. Monetary offer

As a rule, during the recent years a seasonal deceleration of rates of growth of monetary aggregates is seen in their conduct at the beginning of each year. The reason for such a deceleration is a considerable decrease in volumes of monetary aggregates in January and the subsequent gradual growth of them.

However the situation is different in 2006. After insignificant reduction of volumes of monetary aggregates in January, their growth in February and March showed the rates that excelled the indices of the corresponding months of the past years (Graph 9). As a result, the monetary base and money supply in February exceed their volumes as of the end of 2005 and money in circulation in March.

Graph 9

Dynamics of monetary aggregates (% of the previous period)



Source: The National Bank of the Republic of Kazakhstan

Monetary base

One of the special features of the 1st quarter of 2006 was the significant increase of monetary base by 56.9% amounting to 1040.4 billion Tenge. This increase was secured by the augmentation of net external assets of the National Bank, whereas its net internal assets were reduced.

In the 1st quarter of 2006 net international reserves of the National Bank were arisen by more than twice – by 56.8% amounting to USD11.1 billion. Purchase of foreign exchange by the National Bank in the domestic exchange market and inpayment of foreign exchange to the accounts of the Government, despite the operations on replenishment of assets of the National fund and servicing the foreign debt of the Ministry of Finance, caused the increase in net foreign exchange stock by 62.8%. Assets in gold increased by 19.8% as a result of operations fulfilled and the growth of its price in the world market by 13.8%.

Decrease in net internal assets of the National Bank in the 1st quarter of 2006 was conditioned by the decrease of requirements to the Government (by 3.1 times as less) as a result of a significant growth of residual amounts on the Government's accounts with the National Bank (by 2.9 times as much). Requirements to other sectors of economy except the Government reduced by 22.3%. Out of them the requirements to the financial institutions decreased by 13.9% due to the increase in volumes of short-term notes in circulation. Other net internal assets grew by 30.1% (Table 1).

Table 1

Dynamics of changes in assets and liabilities of the National Bank
(% of the previous quarter)

	1 quarter 05	1 quarter 06
Net external assets	1,9	50,3
Net external assets	-16,0	-36,1
Net internal credit	-18,8	-65,7
net requirement to the Government	-98,4	-212,2
net requirements to financial institutions	-3,3	-13,9
requirement to the rest economy	-15,7	-86,5
Other net internal assets	1,9	30,1
Monetary base	-5,5	56,9

Source: The National Bank of the Republic of Kazakhstan

Deposits of second tier banks in the National Bank, i.e. "tied-up" funds were growing to a greater extent in the structure of the monetary base in the 1st quarter of 2006. Their "tie-up" is expressed by the fact that at pursuing its monetary policy the National Bank uses time deposits of banks in the National Bank that serve as a principal instrument for regulating the interest rates in the financial market. In this case, though the growth of time deposits in the National Bank methodologically causes the increase in money supply, there is no actual growth of a monetary offer.

The monetary base, regardless of time deposits of the second tier banks, in the 1st quarter of 2006 rose by 15.8%.

Monetary survey of second tier banks

The 1st quarter of 2006 was characterized by the growth of the resource base of the second tier banks. Their assets increased by 11.9%. At the same time their net external assets reduced by 23.0%, whereas their internal assets increased by 15.3%.

Reduction of net external assets was caused by the reduction of requirements by 3.3% and simultaneous growth of liabilities to nonresidents by 7.5%.

Decrease in the volume of foreign exchange in cash by 18.4% and that of deposits in the nonresidents' banks by 30.4% entailed the reduction of requirements of banks to nonresidents, despite the fact that credits facilities and other financial requirements to nonresidents including those on securities rose by 6.9% and 11.9%, accordingly.

The growth of liabilities of second tier banks to nonresidents was secured by the increase of credits created in freely convertible currencies by 6.8% and likewise that of liabilities in other currencies by 2.1 times as much.

The volume of internal credit in the structure of internal assets of second tier banks increased by 5.9% and it was secured by the growth of requirements to the economy by 5.9% and to the Government by 4.5%. Other internal assets reduced by 14.1%.

The requirements to the National Bank in the structure of internal assets of the second tier banks in March 2006 as against December 2005 doubled due to the increase in deposits

lodging in the National Bank, by 2.9 times as much. The national currency in cash placed in tills of the banks reduced by 6.2%.

Deposits in the structure of liabilities of the second tier banks increased by 14.3%, whereas other liabilities reduced by 4.8% (Table 2).

Table 2

Monetary survey of second tier banks
(% of the previous quarter)

	1 quarter 05	1 quarter 06
Net external assets	-3,1	-23,0
requirements to nonresidents	26,9	-3,3
liabilities to nonresidents	15,4	7,5
Internal assets	7,3	15,3
Requirements to National Bank	0,1	102,5
Internal credit	9,2	5,9
net requirements to Government	11,2	4,5
requirements to economy	9,1	5,9
Other net internal assets	-8,8	-14,1
Liabilities	8,8	11,9
Deposits	11,4	14,3
Other	-9,5	-4,8

Source: The National Bank of the Republic of Kazakhstan

Money supply

The calculations of money supply have excluded the accounts of credit partnerships since 2006; therefore money supply is a consolidated review of the National Bank and second tier banks.

Money supply for the 1st quarter of 2006 increased by 12.9% amounting to 2332.6 billion Tenge. The growth of money supply was promoted by the increase in net external assets of the banking system (by 3.4 times as much), whereas internal assets reduced (by 1.0%).

The growth in the structure of net external assets took place by both the requirements of the banking system to nonresidents and by liabilities to them.

The growth of internal assets of deposit-related organizations was secured by the continuous high growth of volumes of crediting of economy, and as a result, these requirements of the banking system in the 1st quarter of 2006 increased by 5.5%. Net requirements to the Government reduced by 98.8%. Other net internal assets of the banking system decreased by 9.2% (Table 3).

The analysis of dynamics of main components of money supply, i.e. cash in circulation and deposits in the banking system proves that the latter out of the above-mentioned components predominated in the growth of money supply. The volume of cash money in circulation for the 1st quarter of 2006 increased by 6.0% amounting to 436.7 billion Tenge and deposits in the structure of money supply in the banking system rose by 14.7% amounting to 1895.9 billion Tenge. As a result, the share of the latter in the structure of money supply increased from 80.1% up to 81.3% (Table 4).

The higher rates of extension of money supply as against the rates of growth of money supply caused the reduction of money multiplier from 3.12 to 2.24.

Table 3

Dynamics of changes in money supply
(% of the previous quarter)

	1 quarter 05	1 quarter 06
Money supply	5,8	12,9
Net external assets	1,2	239,9
Internal assets	9,5	-1,0
net requirements to Government	-107,6	-98,8
requirements to economy	8,9	5,5
other net internal assets	-0,3	-9,2

Source: The National Bank of the Republic of Kazakhstan

Table 4

Dynamics of changes in components of money supply
(% of the previous quarter)

	1 quarter 05	1 quarter 06
Money supply	5,8	12,9
cash in circulation	-3,8	6,0
deposits of nonresidents	8,7	14,7

Source: The National Bank of the Republic of Kazakhstan

– **Cash in circulation**

Cash in circulation in the 1st quarter of 2006 increased by 6.0% amounting to 436.7 billion Tenge. At the corresponding period of 2005 it reduced by 3.8%. Data on turnover of cash in the second tier banks and organizations which fulfill some banking operations make it possible to identify the factors that effected the growth of cash (Table 5).

In the 1st quarter of 2006 the volume of cash in circulation was affected by the factors for both the increase and decrease of it.

The main factor that facilitated the decrease in volume of cash in circulation was the seasonality on business activities. For instance, the decrease in it in the 1st quarter of 2006 compared with that in the 4th quarter of 2005 entailed the reduction of operations using the national currency in cash for the acquisition and disposal of goods, works and services in the branches of economy. Besides, there was a reduction of allocation of cash for payment of wages and it can be explained by high additional payments during holidays and New-Year's Eve in the previous quarter.

The influence of these factors was fully made up for by the factors which promoted the increase of cash in circulation. Such factors in the 1st quarter of 2006 were the operation with foreign exchange, allocation of finds for payment of wages and allowances as well as other items of payment of cash in circulation.

The significant strengthening of the exchange rate of Tenge against the US dollar caused the increase in operations fulfilled by the population for selling foreign exchange and reducing the volume of operations for purchasing foreign exchange in view of the fact that the main volume of operations is made with the US dollars.

Indexation of pensions and allowances since January 1, 2006 paid from the republican and local budgets in the 1st quarter of 2006 as against that in the 4th quarter of 2005 entailed the increase in payment of cash money by 3.2%.

Table 5

Balance of payments and receipts of cash through banks' cash offices
(% of the previous quarter)

	1 quarter 05	1 quarter 06
Goods, services and works performed	-39,1	-51,0
allocation for payment	-26,5	-24,9
earnings from sales	-15,0	-10,6
Wages (with regard to funds in Bancomats, demand deposits and on the current accounts of natural persons)	-17,9	-16,9
Agricultural products	-62,1	-59,0
Operations with foreign exchange	-5,9	58,1
allocation for purchase of foreign exchange	-15,3	21,7
earnings from sales of foreign exchange	-5,0	-39,1
Time deposits of natural persons	75,9	-429,7
payments of deposits	36,5	10,4
incomings to deposits	-8,5	34,0
Pensions and allowances	6,4	3,2
Other items	-31,3	5,9
Aggregate balance of payments and incomings	-95,6	168,3

Source: The National Bank of the Republic of Kazakhstan

– **Deposits of residents**

Deposits of residents in the 1st quarter of 2006 increased by 14.7%, thus amounting to 1895.9 billion Tenge, and at the same time the increase can be seen on deposits of both the population (7.2%) and non-bank legal persons (entities) (18.8%). Simultaneously the share of other deposits which are one of the main sources of crediting of the real sectors of economy remained at the highest level – 67.8% of the deposit volumes (Table 6).

Table 6

Dynamics of changes in residents' deposits
(% of the previous period)

	1 qtr. 05	1 qtr. 06	Share, % ¹
Deposits of residents	8,7	14,7	100,0
Transferable deposits in Tenge	7,0	23,0	25,1
of population	-2,9	11,2	3,4
of non-bank legal persons	8,7	25,1	21,8
Other deposits in Tenge	6,9	22,5	37,0
of population	8,8	19,8	16,1
of non-bank legal persons	5,1	24,6	20,9
Transferable deposits in foreign exchange	70,2	-6,7	7,1
of population	0,6	-21,4	0,9
of non-bank legal persons	86,8	-3,9	6,1
Other deposits in foreign exchange	1,6	6,2	30,8
of population	5,5	-3,9	18,0
of non-bank legal persons	-0,5	14,7	12,8

Source: The National Bank of the Republic of Kazakhstan

¹ As of April 1, 2006

The dynamics of deposits was determined by primarily transferable and other Tenge deposits of non-bank legal persons, which, in the 1st quarter of 2006, increased by 25.1% and 24.6%, accordingly and provided more than a half of growth of all deposits of residents.

Special features in the structure of deposits in the 1st quarter of 2006 are the reduction of share in foreign exchange. This is primarily related to the fact that enterprises and population make efforts not to run the foreign exchange risk under conditions of a significant strengthening of Tenge.

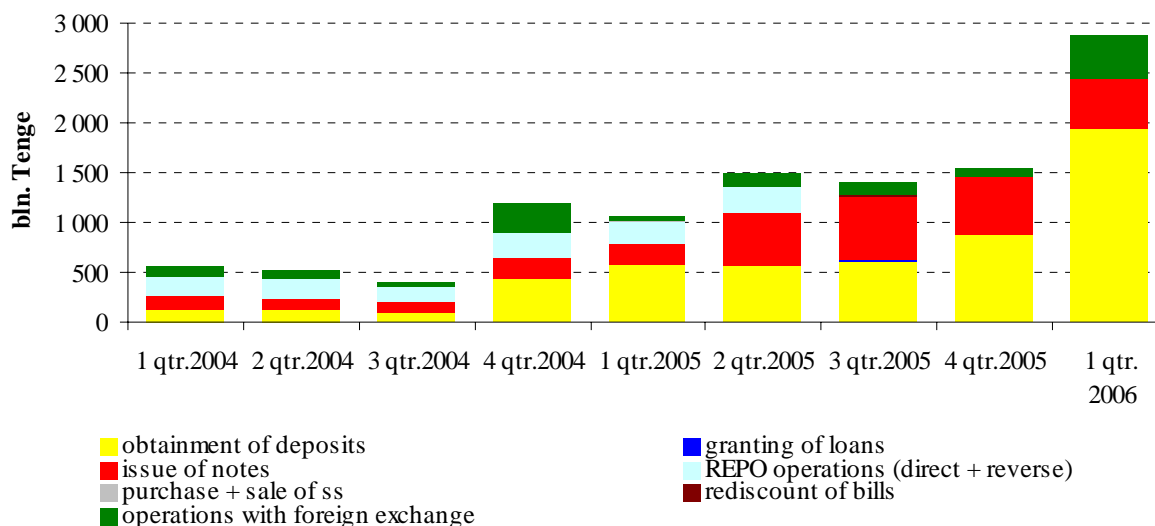
b. Instruments and operations of monetary policy

The monetary policy of the National Bank in the 1st quarter of 2006 was implemented under conditions of the continuous growth of liquidity in the financial market of Kazakhstan and, in particular at the second tier banks, as well as under conditions of a considerable excess of foreign exchange over the demand for it. Average daily residuals on the correspondent Tenge accounts with the banks in the National Bank in the 1st quarter of 2006 increased by 57.1% as against those in the previous quarter and by 2.8 times as much as compared with the 1st quarter of 2005. At the same time their maximum volume fell on March when they made over 158 billion Tenge on average per day.

As a whole, the gross volume of operations of the National Bank in the financial market in the 4th quarter of 2005 including the issue of short-term notes, acquisition of deposits, rediscount of commercial bills as well as the purchase and sales of foreign exchange made 2878.7 Tenge thus having increased by 86.7% compared with the previous quarter. At the same time the volume of operations in the money market rose by 67.8% and those in the foreign exchange market by 5 times as much (Graph 10).

Graph 10

Operations of the National Bank in the domestic financial market



Source: The National Bank of the Republic of Kazakhstan

In the 1st quarter of 2006 the volume of operations of the National Bank in the domestic financial market made 84.8%, whereas in the 4th quarter of 2005 it was 94.3%. At the same time the National Bank was acquiring the deposits of the second tier banks, issuing short-term notes, rediscounting the bills and fulfilled operations under the reverse repurchase agreements (REPO).

Operations with foreign exchange made 15.2% of the volume of operations fulfilled by the National Bank in the domestic financial market.

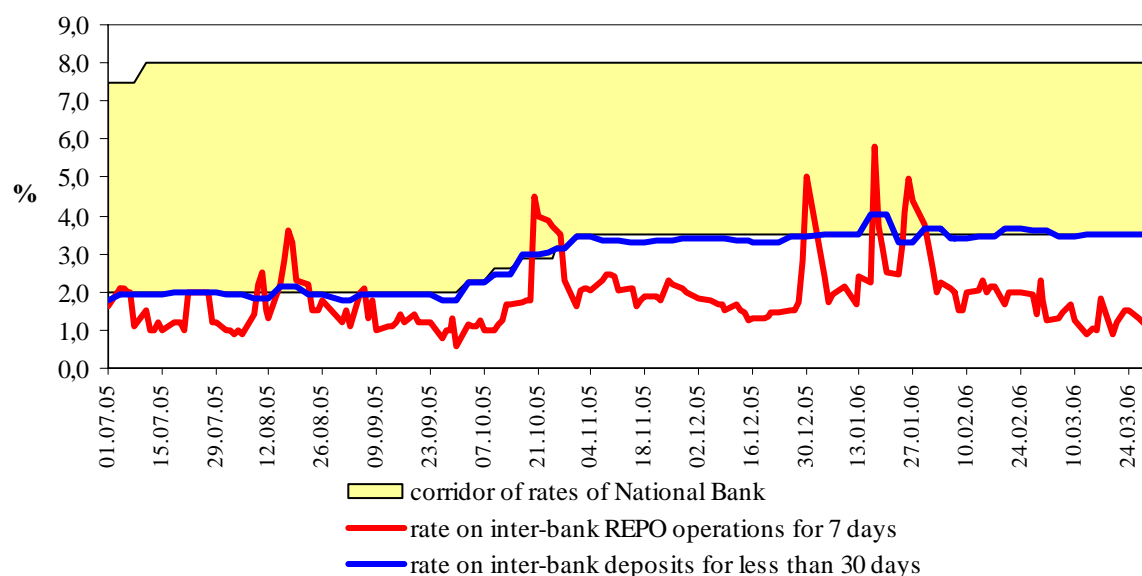
National Bank's rates

In the 1st quarter of 2006 the National Bank did not change the rates for its own operations: the official refinance rate remained at 8.0% and the rate on deposits obtained from the banks was 3.5%.

Thus, the limits for the corridor of rates of the National Bank which had been introduced since July 1, 2005 (the upper limit is an official refinance rate and the lower limit is the deposit rate) remained unchanged (Graph 11).

Graph 11

Limits of corridor of rates of the National Bank



Source: The National Bank of the Republic of Kazakhstan

The rates for operations in the inter-bank market comparable, through the dates with the rates which specified the corridor of the National Bank (7 days) in the 1st quarter of 2006, were located, with few exceptions, below the lower limit of the corridor of rates.

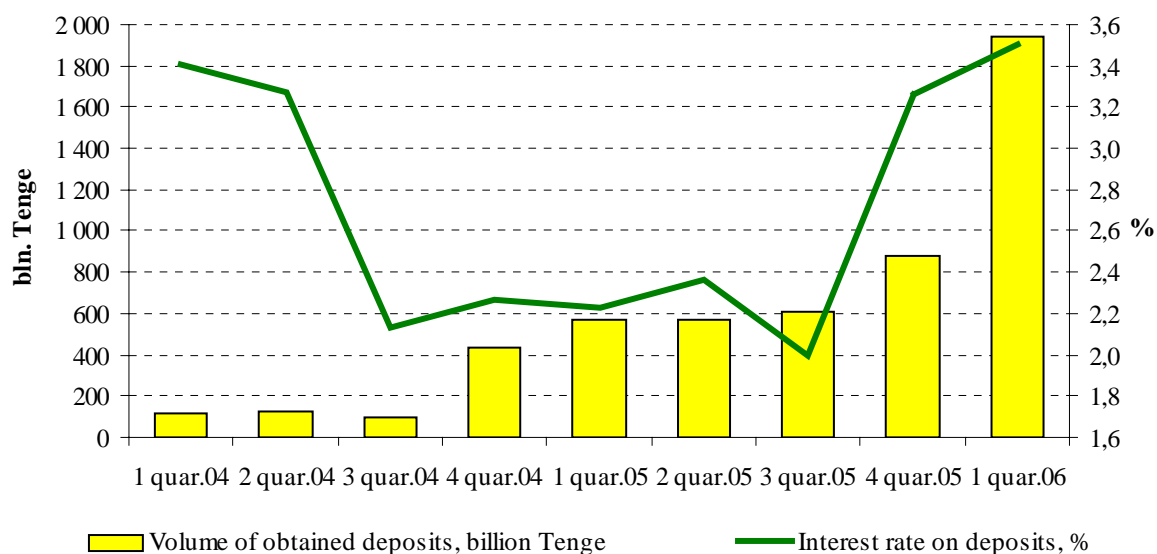
Obtainment of deposits

Obtainment of deposits has the largest scope in the operations of the National Bank. This is related to the short time spent for these operations, daily fulfillment of them, absence of restrictions to the maximum volume of obtainment and also high profitability of them.

IN the 1st quarter of 2006 the National Bank obtained Tenge deposits from the second tier banks to the amount of 1941.1 billion Tenge, and historically this amount is the maximum one. Compared with the previous quarter the volume of the deposits obtained increased by 2.2 times as much. The dates for obtaining the deposits were 7 days. The average weighted interest rate for the obtained deposits in the 4th quarter of 2005 rose up to 3.5% (3.26% in the 4th quarter of 2005) (Graph 12).

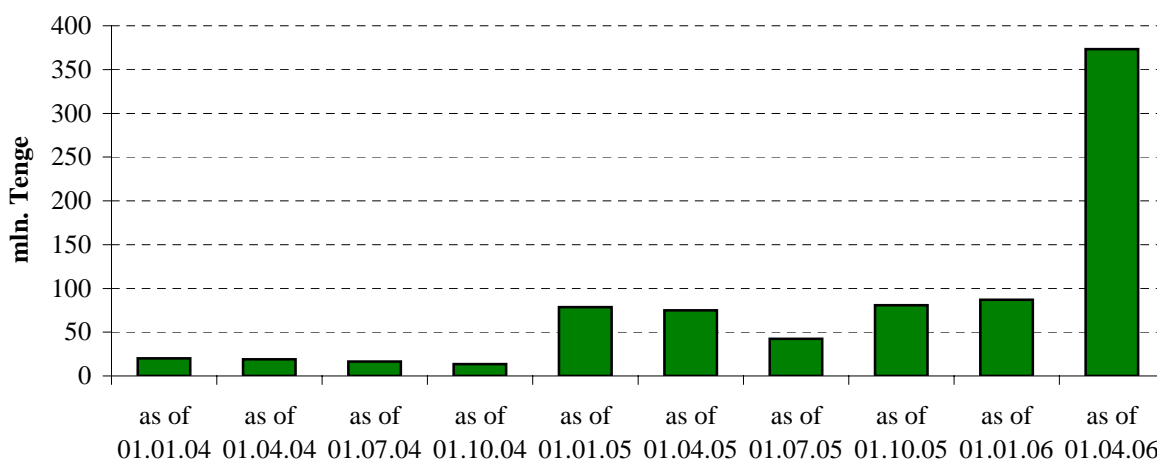
The volume of unpaid liabilities of the National Bank on the deposits obtained from the second tier banks as of the end of the 1st quarter of 2006 as against the volume of those liabilities as of the end of 2005 increased by 4.3 times as much amounting to 373.7 billion Tenge (Graph 13).

Graph 12

The volume and interest rates on the deposits obtained by the National Bank

Source: The National Bank of the Republic of Kazakhstan

Graph 13

The volume of unpaid liabilities of the National Bank on the deposits obtained from second tier banks

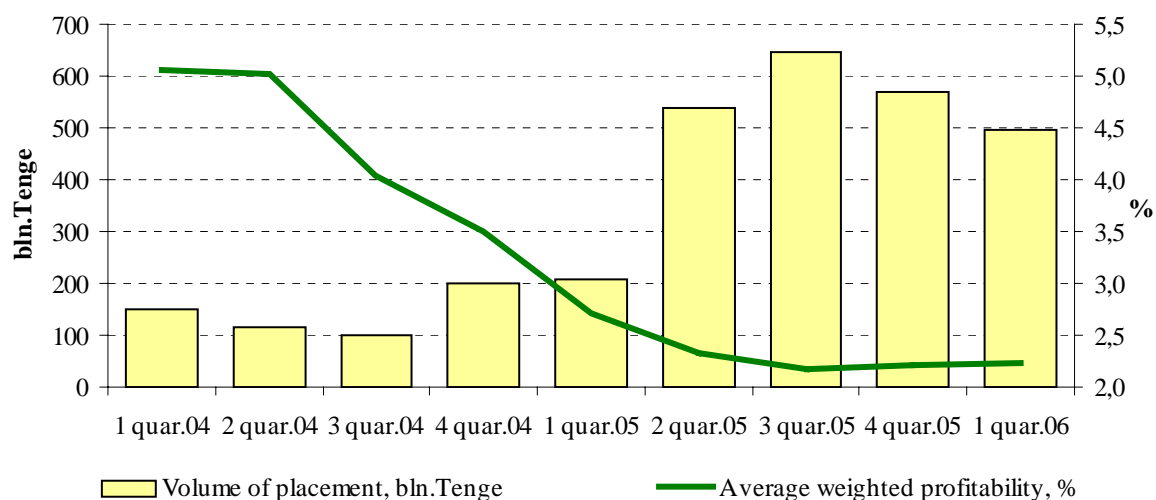
Source: The National Bank of the Republic of Kazakhstan

Issue of short-term notes

In the 1st quarter of 2006 the placement of short-term notes of the National Bank amounted to 495.9 billion Tenge, which is 12.9% less than that in the previous quarter. The notes were issued to be circulated for 28 days. The profitability on the notes placed increased a little – from 2.22% in the 4th quarter of 2005 up to 2.23% in the 1st (Graph 14).

Graph 14

The volume of placement of short-term notes of the National Bank and average weighted profitability on them (for the period)



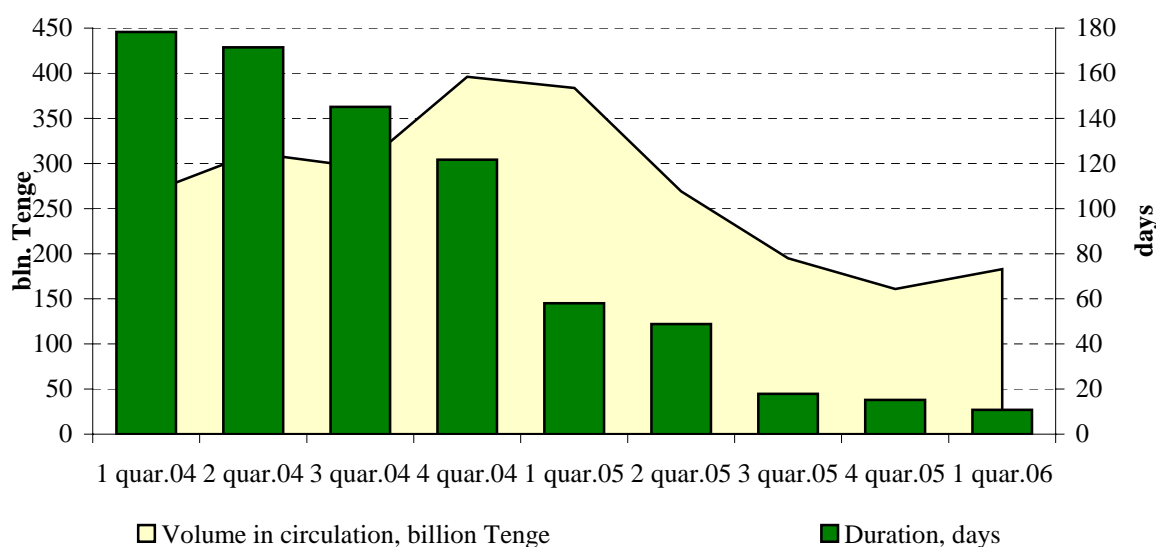
Source: The National Bank of the Republic of Kazakhstan

The trend towards reducing the volumes of issue of short-term notes was observed within the 1st quarter in January and February and that trend shifted to a significant increase of issue volumes in March. In March the issue made nearly 44% of all the notes issued in the 1st quarter.

The volume of short-term notes as of the end of March, 2006 amounted to 182.9 billion Tenge thus being 13.6% as much as that as of the end of 2005. The duration of notes in circulation as of the end of 2005 reduced to 10.8 days (Graph 15).

Graph 15

Short-term notes in circulation (as of the end of the period)



Source: The National Bank of the Republic of Kazakhstan

Granting of loans

In accordance with the current regulations the National Bank may grant bank loans as (1) refinancing loans to banks and (or) organizations which fulfill some types of banking, (2) special loans to banks and (or) legal persons to be granted by the National Bank as a lender of last resort.

At this case the refinancing loans may be granted for the period lasting for at most 1 month and both in national currency through operations under the reverse repurchase agreements and in foreign exchange (SWAP operations).

The volume of refinancing loans granted in the 1st quarter of 2006 as reverse REPO for 7 days at the official refinance rate (8.0%) amounted to 0.8 billion Tenge.

The special loans were not granted by the National Bank in the 1st quarter of 2006.

Exchange rate

The 1st quarter of 2006 was noted by the sharp reduction of the dollar exchange rate in the domestic foreign exchange market. Altogether, as per the results of the quarter the Tenge exchange rate against the US dollar strengthened by 4.01% – from 133.77 Tenge/US dollar to 128.40 Tenge/US dollar.

The trend towards the growth of the Tenge rate against the US dollar was conditioned by the situation in the world exchange markets as well as by the considerable supply of foreign exchange over the demand for it in the domestic foreign exchange market. One of the factors of a surplus supply was the stirring up of the second tier banks in the process of obtainment of foreign borrowings in the 4th quarter of 2005. For instance, the increase in liabilities of the second tier banks to nonresidents in the 4th quarter of 2005 amounted to USD 4854.2 millions.

In January 2006 in the world exchange market the US dollar exchange rate against Euro decreased from the rate of \$1.188 to \$1.210. The principal “nerve-racking“ factor was the replacement of the Head of the USA Federal Reserve System (FRS) and ambiguity of perspectives of the monetary policy of the USA as well as the growth of prices of oil on account of the aggravation of the situation concerning the Iranian nuclear programme. Against that background the exchange rate of Tenge against that of the US dollar in the domestic foreign exchange market nominally strengthened by 1.26% (from 133.77 Tenge/US dollar to 132.08 Tenge/US dollar).

Despite the fact that the situation in the world market in February, 2006 was characterized by several periods of weakening of the dollar rate against Euro, as per the outcomes of the month the dollar rate against the common European currency strengthened a little and approximated to the one and a half monthly maximum rate. During a month the dollar rate against Euro rose by 2% from the rate of \$1.210 to \$1.185, i.e. it made up for its fall in the previous month. The reasons for it were new statistical data that proved high rates of economic growth in the USA. The first statement by Mr. Ben Bernanke, the new Head of the USA FRS, made to the USA Congress was to the dollar’s favour. In his statement he pointed out that the USA FRS can re-raise the discount rate in order to reduce the effect from high inflation which accompanied the economic growth, and rising prices of energy resources.

In February the dynamics of the Tenge exchange rate against that of the US dollar in the domestic foreign exchange market was also characterized by staggering trends. For example, during the period from February 1 to 8 the Tenge rate against the dollar rate was devalued by 0.36% (from 131.89 Tenge/US dollar to 132.37 Tenge/US dollar), whereas during February 9 to 28 one could see strengthening of the Tenge rate against that of the US dollar (from 131.96 Tenge/US dollar to 130.35 Tenge/US dollar). All in all, within a month Tenge nominally strengthened by 1.31% (from 132.08 Tenge/US dollar to 130.35 Tenge/US dollar).

In March in the world exchange market the dollar rate against Euro was decreased by 2.7% from \$1.185 to \$1.217. The drop of the dollar became sustainable due to the topic of interest rates and statements by central banks of different countries about the conversion of a part of reserves from dollars to the European currency.

The Open Market Operations Committee of the USA FRS at one of its regular sessions on March 28 raised the rate on federal funds up to 4.75%. And the representatives of the European Central Bank stated that the current level of rates was very low. The cycle of raising the rates is about to finish, whereas in Europe it can be started shortly. That was the reason for negative mood of investors towards the US dollar. Meanwhile the Central Bank of Japan also announced the tightening of its monetary policy the goals of which were not traditional interest rates (in Japan they are practically equal to zero) but the volume of funds on the reserve accounts of banks with the Central bank.

The country of Middle East announced their intention to reject the American currency in their gold and currency reserves and commercial calculations in favour of the Euro. The Head of the Central bank of the UAE informed that the country was planning to convert up to 10% of its foreign exchange reserves (approximately 2.3 billion US dollar) from dollar to Euro. Investors expressed disquietude about the fact that the other regional banks could follow suit.

The negative attitude of investors towards the American currency was also observed in the domestic foreign exchange market to which the record volumes of bargaining at the KASE and in the over-the-counter inter-bank foreign exchange market in March can testify. In March the volume of stock exchange operations in the Kazakhstan's Stock Exchange in view of the transactions at the additional bargaining compared with those in February was increased by 53.8% up to USD 2805.8 millions. In March the volume of operations in the over-the-counter foreign exchange market increased by 20.8% amounting to USD 3900.3 millions.

Against the background of large volumes of bargaining the Tenge rate against that of the US dollar strengthened by 1.5% from 130.35 Tenge/US dollar to 128.40 Tenge/US dollar.

The average weighted exchange rate of Tenge for the 1st quarter of 2006 made 130.28 Tenge/US dollar thus having been strengthened by 2.21% as against the index of the 4th quarter of 2005. During the 1st quarter the Tenge rate against the US dollar was changing within the ranges of 127.40-133.85 Tenge per dollar (Graph 16).

The position of the common European currency in the international financial market influenced the dynamics of the Tenge exchange rate against the European currency. For the 1st quarter of 2006 the official Tenge exchange rate against the Euro strengthened by 2.29% and made 154.91 Tenger per Euro as of the end of the period.

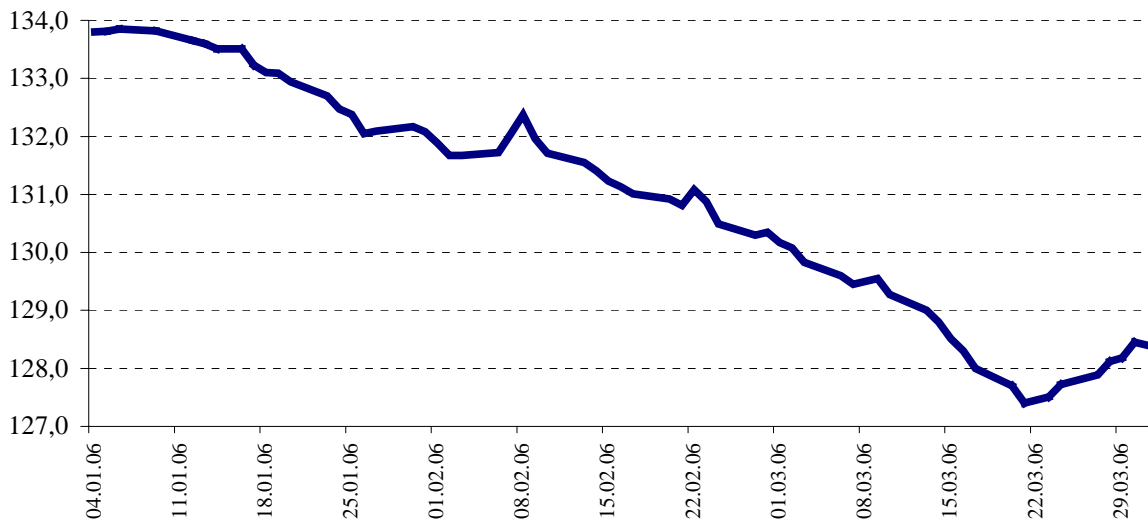
The dynamics of the Russian rouble rate against the Tenge was primarily determined by the policy pursued by the Central Bank of Russia regarding the exchange rate of the Russian rouble against the currencies' basket. For example, during the 1st quarter of 2006 the official exchange rate of the Tenge against that of the Russian rouble strengthened by 0.43% (Graph 17).

In the 1st quarter of 2006 the volume of the stock exchange bargaining at the Kazakhstan's Stock Exchange amounted to USD 6.1 millions and it is 3.1 times as much as that for the similar period of 2005.

In the over-the-counter foreign exchange market the volume of operations for the 1st quarter of 2006 compared with the last year's similar index increased by 3.3. times as much amounting to USD 7.6. billions (Graph 18).

Graph 16

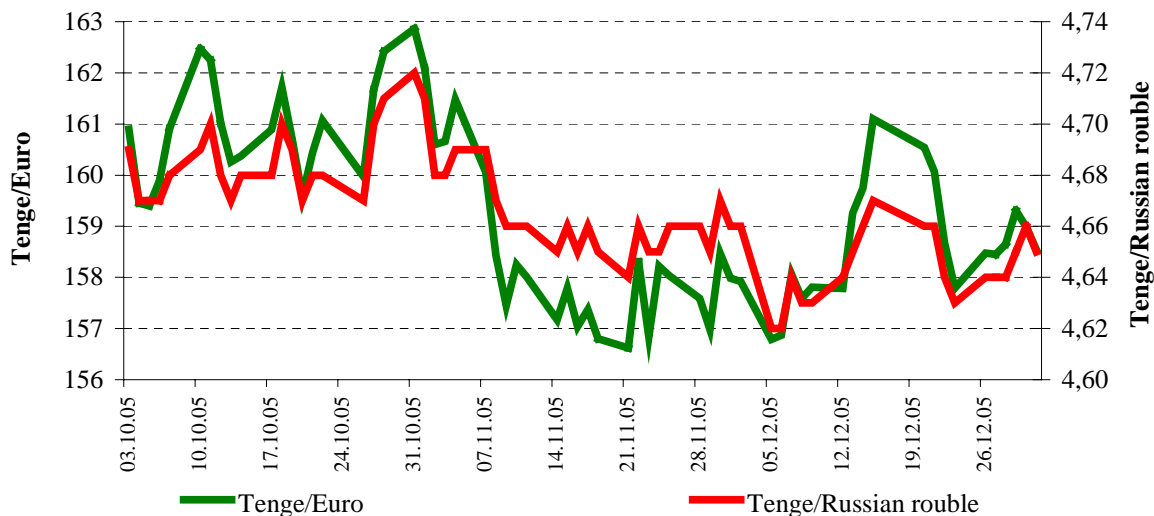
Dynamics of nominal foreign exchange rate of Tenge against US dollar



Source: The National Bank of the Republic of Kazakhstan

Graph 17

Dynamics of official exchange rate of Tenge against Euro and Russian rouble



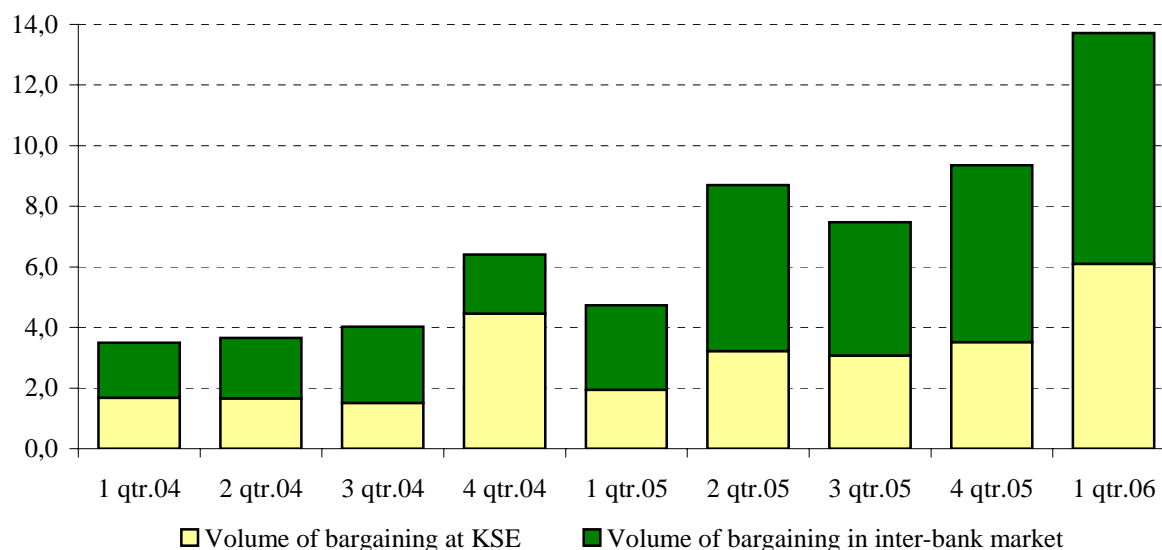
Source: The National Bank of the Republic of Kazakhstan

The considerable supply of foreign exchange over the demand in the domestic foreign exchange market promoted the growth of volumes of interventions of the National Bank compared with those in the previous periods. The coefficient of participation of the National Bank in the Kazakhstan’s Stock Exchange made 50.8%.

The index of the real effective exchange rate (REER) of Tenge as per the outcomes of the 1st quarter of 2006 went up by 5.2%. The real strengthening of the Tenge rate against that of the US dollar and Euro made 6.1% and 5.2%, accordingly and that against the rate of the Russian rouble was devalued in real terms by 1.1% (Graph 19).

Graph 18

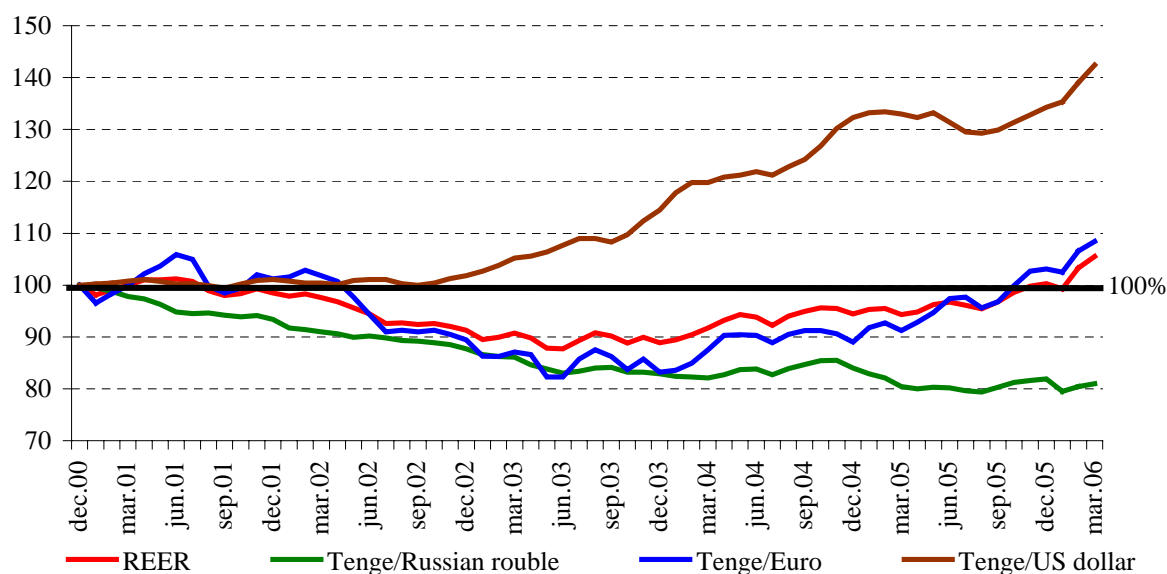
Volume of bargaining in the domestic foreign exchange market, USD billion



Source: The National Bank of the Republic of Kazakhstan

Graph 19

Indices of real foreign exchange rates of Tenge (December 2000 = 100%)



Source: The National Bank of the Republic of Kazakhstan

Rediscout of bills

For the 1st quarter of 2006 11 bills amounting to 2.0 billion Tenge were accepted for discount and the bills amounting to 12.6 billion Tenge were retired. As of April 1, 2006 in the portfolio of the National Bank there were bills amounting to 1.3 billion Tenge.

The volume of operations for rediscount of bills did not substantially affect the level of liquidity in the financial market due to an insignificant volume of these operations.

4. Inflation forecast

a. Estimate of inflation forecast for the 1st quarter of 2006

The actually formed inflation rate in the 1st quarter of 2006 (3.2%) considerably outstripped the forecast for that period (2.3-2.5%).

The actual rate of inflation over the forecast was observed during the entire period. The most substantial deviation was registered in February – actually 1.5% with the forecast 0.7% as well as in March – 0.8% against 0.5%.

In February 2006 the situation in the consumer market was formed under the influence of the appreciation of foodstuffs and paid services to the population. The growth of prices of foodstuffs and paid services to the population during that month was 2.4%, and this is the highest monthly index since December, 1999 and it was primarily conditioned by the appreciation of sugar and fruit and vegetable products. Taking into account that prices of sugar in February of the previous 6 years were exclusively falling down, this appreciation could not be forecast.

Also, the increase of cost of transportation services, mainly motor transport and railway services appeared to be unexpectedly high in the 1st quarter of 2006.

Besides, there is a somewhat underestimation of an influence of a number of factors of long-term nature on the inflation and the same was specific to the year 2005 as well. Among these factors one should single out the increase in the consumer and investment demand that outpaced the increase in the aggregate supply, the rates of growth of wages over the growth of economy, a considerable growth of bank crediting of economy and, respectively, the growth of monetary aggregates, high world prices of oil and other raw material commodities.

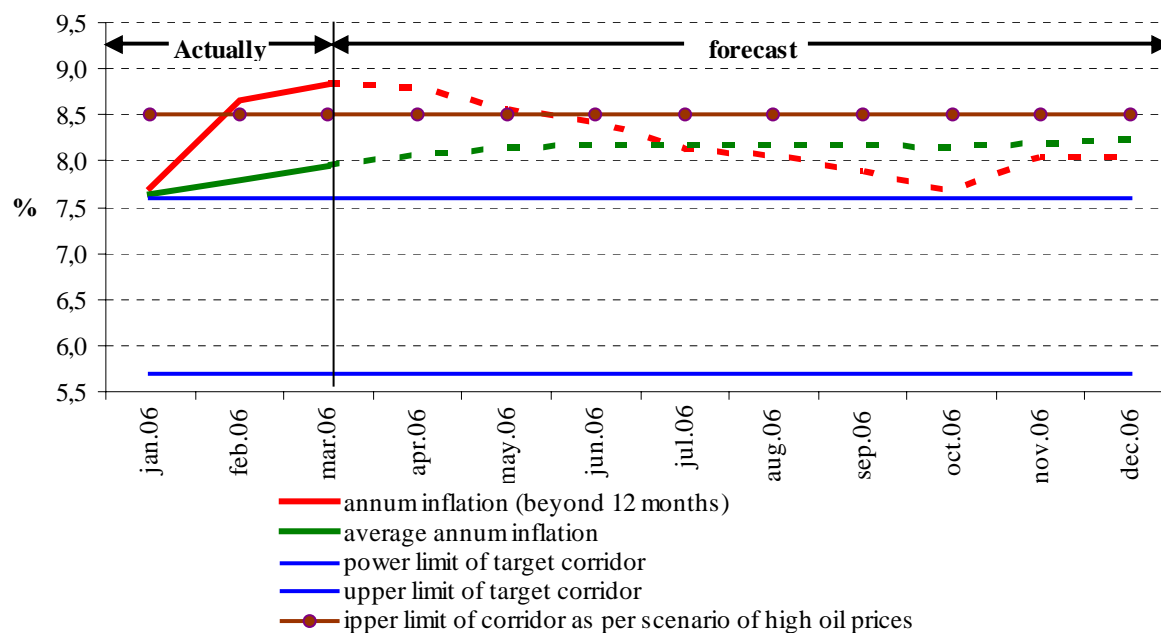
b. Inflation forecast for 2006

It is expected that in 2006 the average annual rate of inflation will make within 5.7-7.3% provided the average world prices of Brent oil in 2006 amount to between USD 45-60 per barrel (Graph 20).

As a result of the situation formed in the world markets for the first months of 2006, however, the average world oil price exceeded USD 60 per barrel. The growth of world oil prices (over USD 65 per barrel) proves the performance of the scenario of high oil prices identified by the Monetary policy guidelines for 2006-2008. The inflation targets in this scenario were identified by the National Bank between 6.9-8.5% as per the average calculations for 2006.

In 2006 the National Bank will continue the implementation of measures for toughening its monetary policy. The deposits of the second tier banks in the National Bank and short-term notes will be the main instruments for regulating the interest rates in the financial market and for sterilization of the surplus liquidity of banks. The National Bank does not restrict the volume of obtainment of deposits but identifies the rates on them. In order to reduce the acuteness of the problem the National Bank of the Republic of Kazakhstan improves the mechanism of calculations of minimum reserve requirements.

Graph 20

Actual situation and inflation forecast in 2005

Source: The National Bank of the Republic of Kazakhstan

Within the scope of implementation of these measures the National Bank continued to fulfill the measures for toughening its monetary policy. For instance, since April 1, 2006 the official refinancing rate was raised up to 8.5% and the rate on deposits obtained was raised up to 3.75%. The possibility of the ongoing raise of these rates is not excluded.

Inflation forecast for the 2nd quarter of 2006

Reduction of inflation rate as against that in the previous quarter is expected in the 2nd quarter of 2006, and at the same time this forecast for this period makes 1.4-1.6% (1.6% in the 2nd quarter of 2005) thus corresponding to 8.4% in annum terms as of the end of July.

The situation in the consumer market at this period is primarily formed under the influence of the seasonality factor, which, in its turn, entails the reduction in prices of some types of foodstuffs.

At the same time, the expectations of the maintenance of inflation at the level of the last year are caused by the current situation in the world markets. Besides, the liquidity in the economy kept at a high level, the active credit policy of the second tier banks, the considerable inflow of foreign exchange in Kazakhstan will impact the formation of consumer prices in the 2nd quarter of 2006 too.

Nevertheless, it is expected that the inflation will be scotched by the measures undertaken by the National Bank in 2005-2006 for toughening its monetary policy and sterilization of the surplus liquidity, in particular for increasing the rates on operations and extending the volume of deposits obtained from the second tier banks and issuing the short-term notes.

Scotching of inflation in the 2nd quarter have to facilitate the measures of the Government of the Republic of Kazakhstan for preventing the growth of prices in the consumer market under conditions of growth of incomes of the population. E.g. the Government of the Republic of Kazakhstan enacted the resolution No.285 dated April 15, 2006 "On Additional Measures for Stabilization of Prices in the Consumer Market".

In pursuance of this resolution the work for the prevention of the unjustified growth of prices of the principal group of goods and services to the population and, first and foremost, prices of foodstuffs, in particular those of meat and fruit and vegetable products will be activated. Besides, the measures for suppressing a price-scheme, disclosing and restraining the unfair competition, abusing of dominating positions by the market subjects will be developed. The measures for providing assistance in setting up a network of wholesale and retail trade markets, developing the trade infrastructure, developing the competitive environment in the commodity markets are undertaken too. Reduction of rates of customs duties and charges on a number of imported foodstuffs and nonfoods has been envisaged as well. For the period from April 15 till October 1 there will be 50% reduction of the railway tariffs at transporting fresh fruit and vegetable, fruit and berry and water-melons perishable products.

Inflation forecast for the 3rd quarter of 2006

As shown by the previous years, the period from July till September is characterized by the lowest rate of inflation during the whole year and it is caused by a seasonal reduction in prices of a number of goods and services.

A certain cooling of inflation will be provided by measures undertaken by the National Bank and the Government in 2005-2006.

The inflation forecast for the 3rd quarter of 2006 makes 0.8%-1.1%. This corresponds to 7.9-8.1% in annum terms.