NATIONAL BANK OF KAZAKHSTAN

MARKET REVIEW
Enterprise Survey in the Real
Sector of the Economy

1Q2017

CONTENTS

# PRIMARY DEVELOPMENT TRENDS IN KAZAKHSTAN'S REAL SECTOR

In Q1 2017, there was a weakening of negative processes in the economy, which was due to rising prices for oil products and the adaptation of agents to the new economic conditions. The demand for final products has increased, production efficiency indicators have improved, profitability in the mining and manufacturing industries, professional, scientific and technical activities has increased. There was a slowdown in the growth of prices for raw materials.

The negative impact of changes in the Tenge exchange rate to USD, EURO and RR decreased. Performance indicators of enterprises have improved:
– the share of enterprises that did not reduce the volume of production has increased;
– the share of enterprises that did not reduce labor productivity has increased.

At the same time, the deterioration of the price and non-price credit conditions has slowed down.

Primary Trends in the Real Sector	
Market Demand and Prices for Final Products, Raw Materials and Supplies	**Assessment of Business Activity among Enterprises and of Production Efficiency**
The demand for final products increased ⬆	The production output decreased ⬇
Prices of raw materials and supplies are growing ⬇	Investment activity of enterprises worsened ⬇
	Production efficiency indicators improved ⬆
Assessment of the Financial and Economic Standing of Enterprises	
Enterprises' liquidity ratios worsened ⬇	**Influence of the Banking System**
Profitability ratios worsened ⬇	The percentage of enterprises that were rejected a loan has increased ⬇
The percentage of enterprises with arrears increased ⬇	Price and non-price terms and conditions of lending for property, plant and equipment and working capital deteriorated ⬇
The Effect from Changes in the Exchange Rate	
The degree of negative impact of the change in the Tenge exchange rate to USD, EURO and RR is decreasing. ⬆	The gap between an actual and an acceptable interest rate on the tenge loans remained the same ⬆

⬆ - positive change   ⬇ - negative change

DYNAMICS OF THE DEMAND FOR FINAL PRODUCTS

In Q1 2017, the demand in the real sector for final products showed a slight increase; the diffusion index (DI) made up 50.5 as compared to 48.5 in Q4 2016. In Q1 2017, the rates of decline in demand for services slowed down to 48.8, demand for goods increased to 52.3.

In the mining and manufacturing industry the demand for final products increased to 55.1 and 51.8, respectively.

Demand for the finished goods, DI*

Answers of enterprises, %		2016				2017	
		Q1	Q2	Q3	Q4	Q1	Q2 exp.
Increase	1	12.1	26.1	26.7	23.6	17.4	25.9
No changes	2	47.0	48.0	49.9	48.8	49.3	36.9
Decrease	3	40.6	25.8	23.4	27.6	33.3	11.2
Diffusion index, DI=line1+0.5*line2	4	35.8	50.2	51.6	48.0	42.1	57.3
DI, seasonal adjusted	5	42.7	46.5	47.1	48.5	50.5	52.9

Demand for finished goods, DI *
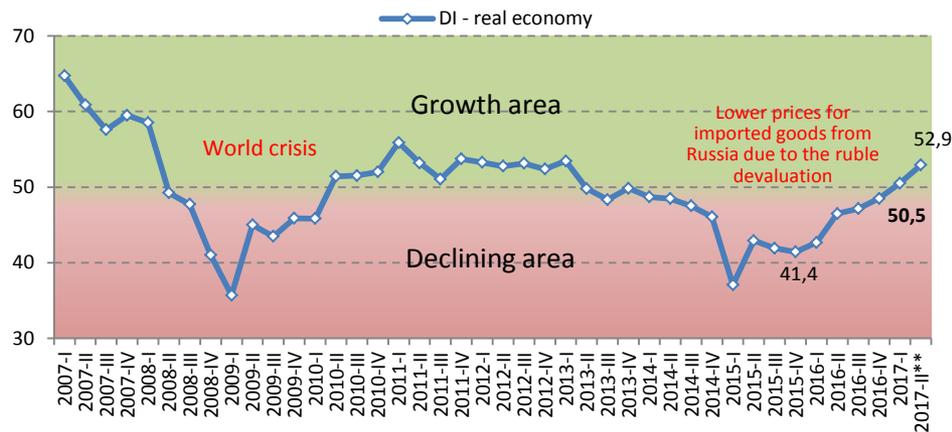
production / production of services
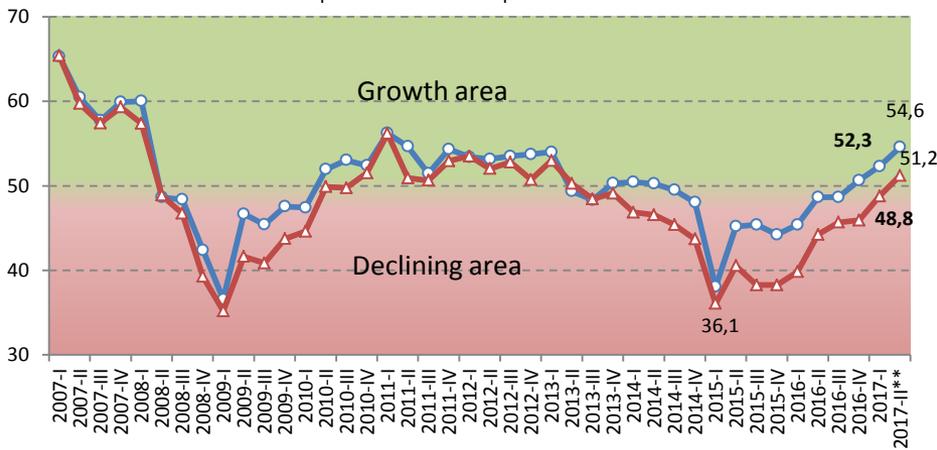
mining / manufacturing
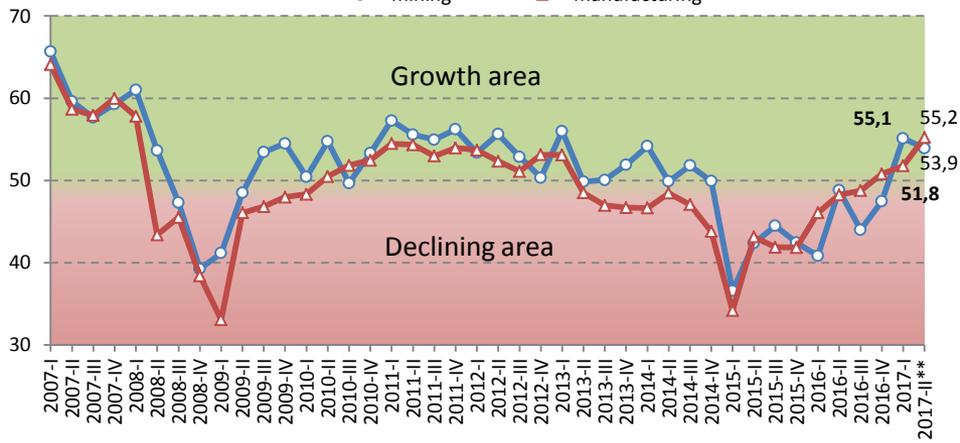
*The higher (the lower) the DI deviates from 50, the higher (the lower) are the rates of growth (decline) in the demand; the level of 50 means the absence of any change
**The Figures show expectations of enterprises regarding the change in the parameter in 2Q2017.

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CHANGE IN PRICES IN THE REAL SECTOR

In Q1 2017, growth rates of prices for final products in the real sector accelerated (DI was 57.9). In the mining and the manufacturing industry prices had increased (DI increased to 54.5 and 59.6, respectively). The tendency of price increase for raw materials and supplies persists (DI=73.9).

In the Q2 2017, the growth in prices of final products, raw materials and supplies is expected to slow down (DI from 57.9 to 57.7 and from 73.9 to 67.4, respectively).

Prices for finished goods, DI*
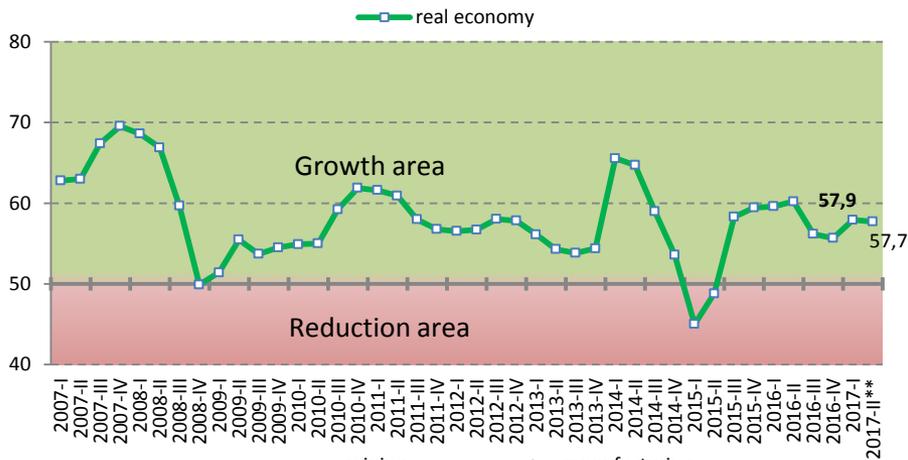
Prices for raw materials, DI*
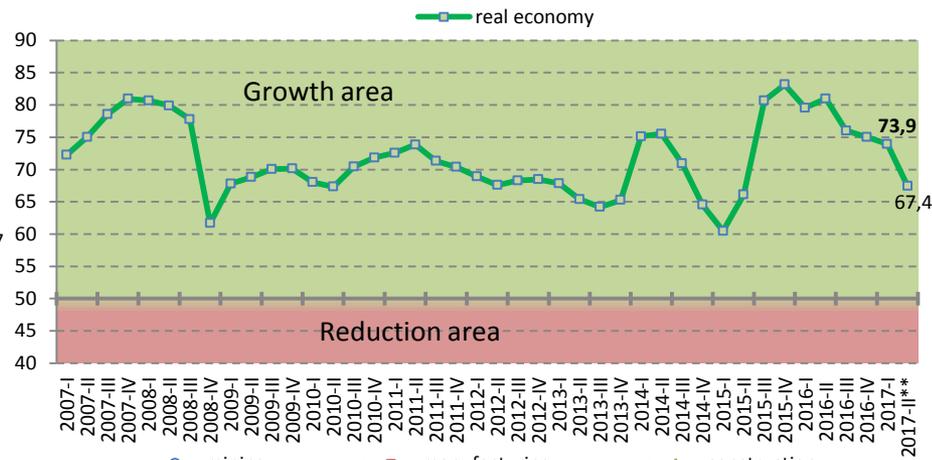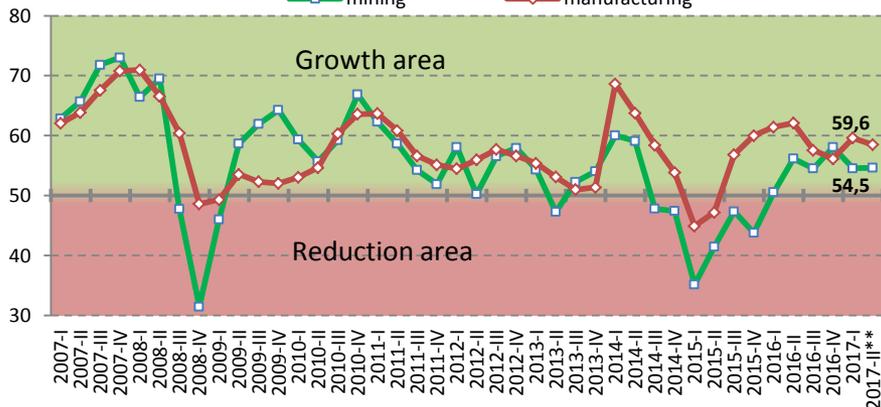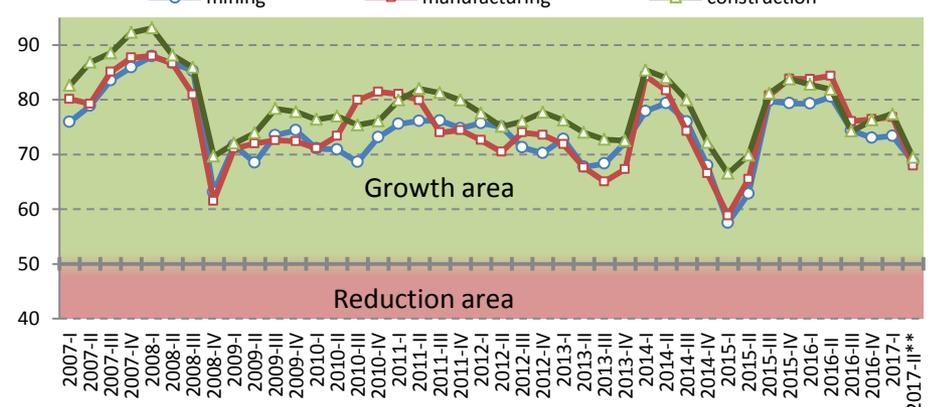
*The higher (the lower) the DI deviates from 50, the higher (the lower) are the rates of growth (decline) in the demand; the level of 50 means the absence of any change

**The Figures show expectations of enterprises regarding the change in the parameter in 1Q2017.

CHANGE IN THE PRODUCTION OUTPUT

In Q1 2017, a significant decrease in the production output was observed (DI = 40.6), which was due to seasonal slowdown in business activity. In Q2 2017, enterprises expect the production output to increase (DI = 57.3).

In Q1 2017, the percentage of enterprises with the capacity utilization more than 90% decreased to 10.8%. The percentage of enterprises with capacity utilization below 50% slightly increased to 38.4%.

Changes in output volume
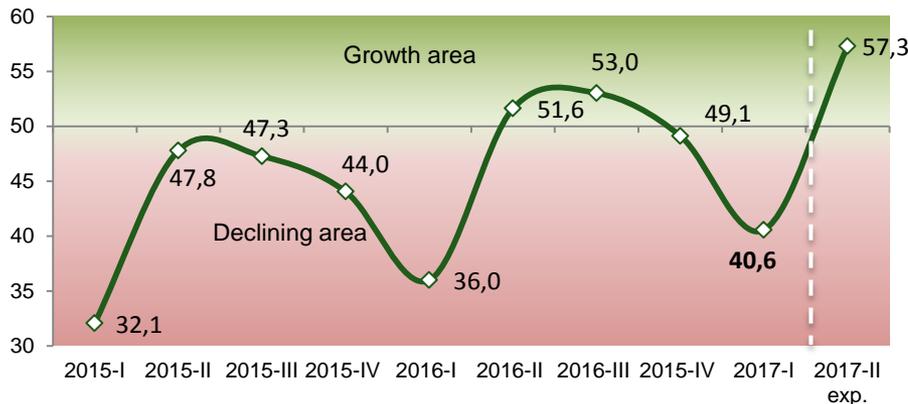
Level of capacity utilization
(short of respondents,%)
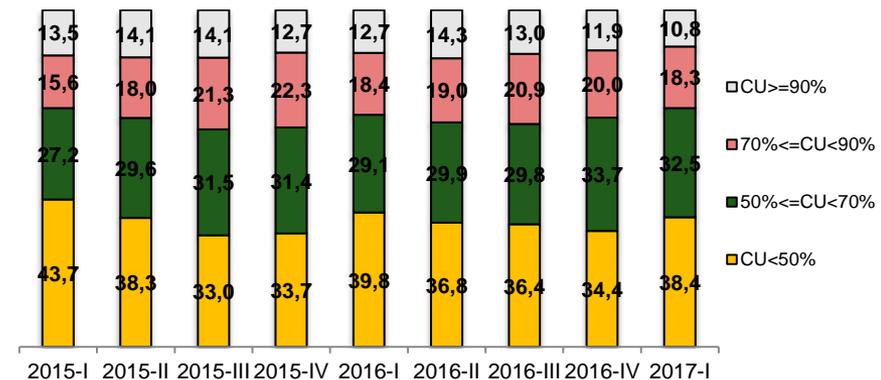
* The higher (the lower) the DI deviates from 50, the higher (the lower) are the rates of growth (decline) in prices; the level of DI=50 means the absence of any change

THE STRUCTURE OF A BALANCE SHEET: ASSETS

In the asset structure of enterprises of the real sector the share of short-term assets increased from 35.9% in Q4 2016 to 36.5% in Q1 2017. In the structure of short-term assets, the share of short-term receivables decreased from 42.3% in Q4 2016 to 40.8% in Q1 2017, and the share of inventories increased from 16.5% in Q4 2016 to 18.0% in Q1 2017.

Turnover of assets and working capital decreased to 12.5% and 34.3%, respectively. The share of working capital within assets increased (to 36.5%).

Structure of assets

	2015-I	2015-II	2015-III	2015-IV	2016-I	2016-II	2016-III	2016-IV	2017-I
Short-term assets	32,4%	32,4%	33,1%	33,2%	34,4%	36,0%	40,5%	35,9%	36,5%
Long-term assets	67,6%	67,6%	66,9%	66,8%	65,6%	64,0%	59,5%	64,1%	63,5%

Structure of short-term assets

	2015-I	2015-II	2015-III	2015-IV	2016-I	2016-II	2016-III	2016-IV	2017-I
Arrearage	22,4%	24,2%	21,8%	20,6%	23,9%	22,1%	16,1%	16,5%	18,0%
Short-term receivables decreased	38,9%	44,3%	44,0%	44,9%	40,2%	43,8%	35,8%	42,3%	40,8%
Other short-term assets	38,7%	31,5%	34,2%	34,5%	35,9%	34,1%	48,1%	41,2%	41,3%

Indicators of assets turnover

| %	2009	2010	2011	2012	2013	2014	2015	2016-I	2016-II	2016-III	2016-IV	2017-I
Assets turnover	14,9	15,8	16,7	17,0	17,5	18,2	14,6	11,3	14,8	12,5	14,0	12,5
Working capital turnover	38,9	40,8	42,0	42,8	44,6	46,6	44,5	32,8	41,0	30,9	38,9	34,3

Percentage of working capital within assets

THE STRUCTURE OF A BALANCE SHEET: LIABILITIES

In the structure of liabilities the share of equity capital slightly increased from 46.2% in Q4 2016 to 46.5% in Q1 2017. The share of fixed liabilities decreased (from 30.2% to 29.2%), and the share of short-term liabilities increased from 23.6% to 24.0%. The situation with arrears slightly improved: the share of enterprises with the overdue accounts payables decreased to 22.5%. Among enterprises which participated in the monitoring, the share of enterprises with the past due on bank loans accounted for 3.2%.

In the structure of current liabilities, the share of short-term accounts payables increased from 50.1% in Q4 2016 to 50.6% in Q1 2017, and the share of bank loans almost remained the same (21,0%). In the structure of non-current liabilities, the share of fixed loans to banks decreased from 55.4% in Q4 2016 to 54.8% in Q1 2017.

Structure of liabilities

Percentage of enterprises with the past due

Structure of current liabilities

Structure of non-current liabilities
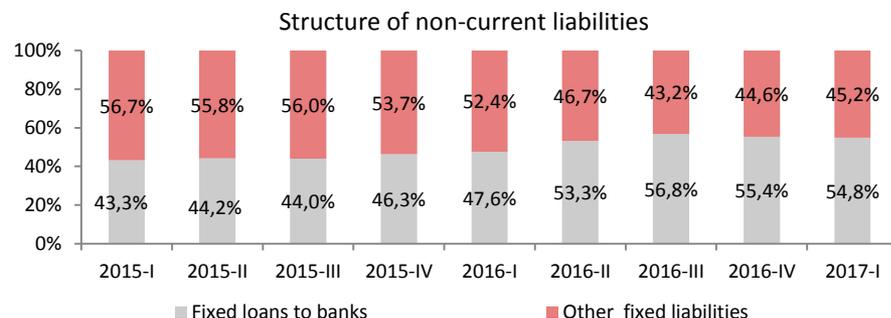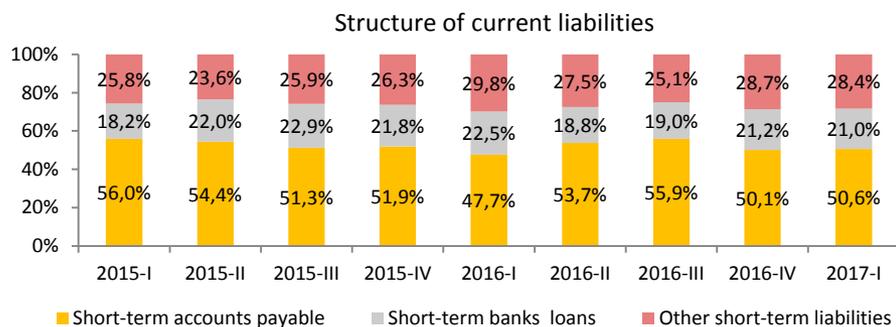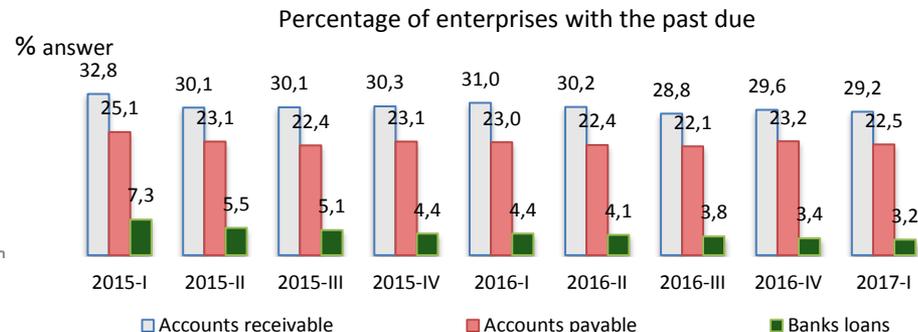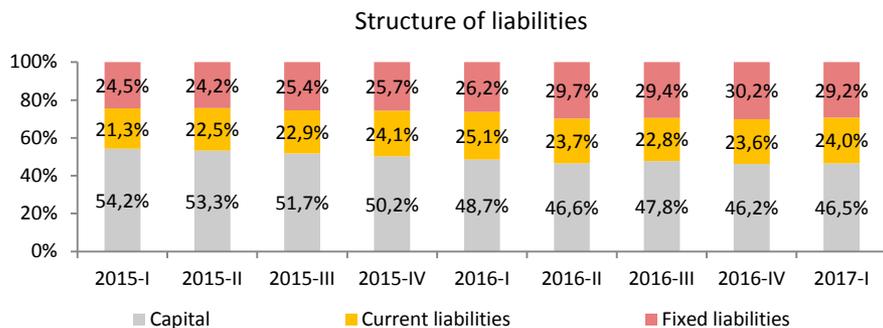
INVESTMENT ACTIVITY

The investment activity of enterprises in Q1 2017 slightly worsened: the share of enterprises, which did not finance their investments, increased to 32.9%. At the same time, the share of enterprises, which used their own funds for these purposes, decreased to 64.1%.

The main funding source for the working capital is still represented by own funds of enterprises (81.3%). The number of enterprises, which use bank loans to replenish their working capital, in Q1 2017 decreased (to 15.7%).

The main factors that limit financing opportunities of enterprises are the shortage of financial resources, insufficient demand for their products and the state of the Kazakhstan's economy.

Funding source for the fixed assets
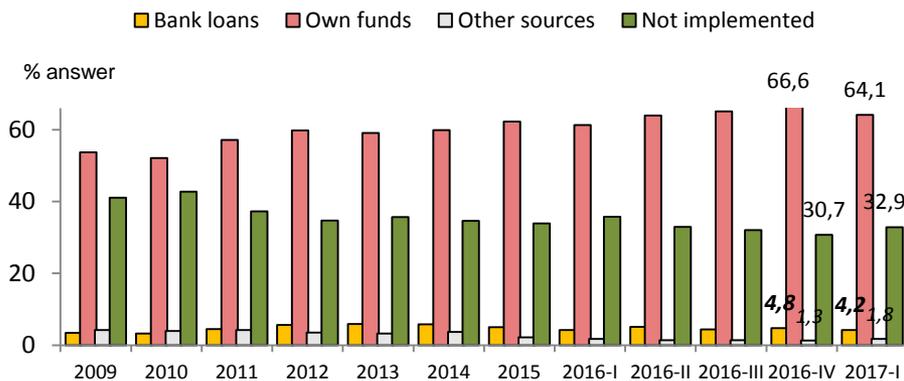
Funding source for the current assets
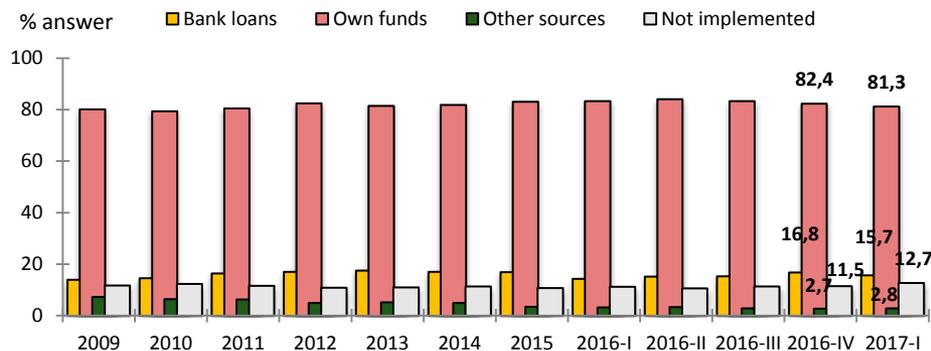
The main factors that limit financing opportunities of enterprises
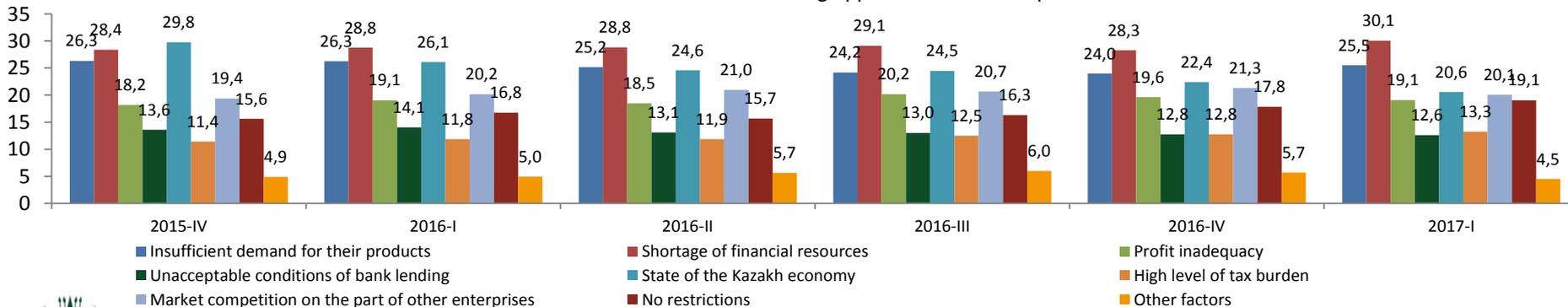
CHANGE IN THE FINANCIAL AND ECONOMIC PERFORMANCE

In Q1 2017, production performance indicators showed growth as a whole. The share of enterprises which did not reduce the production output increased to 70.9%. The percentage of enterprises, which did not reduce the total number of the employees and the labor productivity, also increased to 66.3% and 70.4%, respectively.

In Q1 2017, the current liquidity and overall solvency ratio of enterprises in the real sector remained unchanged (1.5 and 1.9, respectively). The share of low-liquid enterprises (CLR<1) increased to 36.3%.

Indicators of production performance

Legend:
- Percentage of enterprises which did not reduce the labor productivity
- Percentage of enterprises production output
- Percentage of enterprises which did not reduce the total number of employces
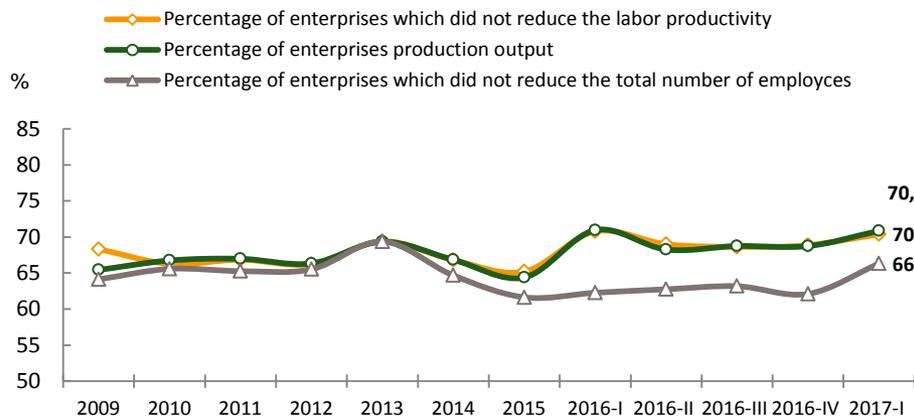
Indicators of liquidity and solvency of enterprises

Legend:
- Current liquidity ratio (CLR)
- Overall solvency ratio
- Percentage enterprises with CLR<1 (rhs)
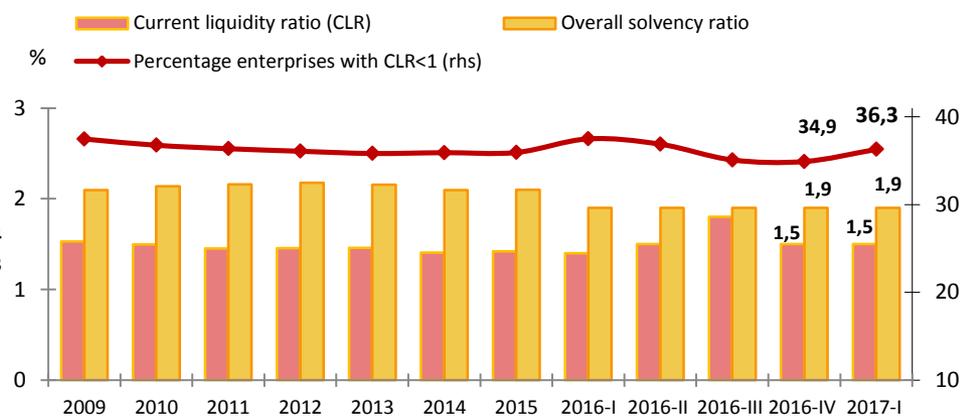
CHANGE IN THE FINANCIAL AND ECONOMIC PERFORMANCE

The return on sales (before taxes) of enterprises in the real sector decreased to 20.7% (36.5% in Q4 2016). The return on sales in the mining industry increased to 58.4% (56.7% in Q4 2016).

In Q1 2017, the share of loss-making and low-profitable enterprises increased to 25.3% (22.5% in Q4 2016), the share of highly profitable enterprises slightly decreased to 36.1% (from 36.3% in Q4 2016). At the same time the share of medium-profitable enterprises decreased to 38.0% (from 41.0% in Q4 2016).

Return on sales, in %
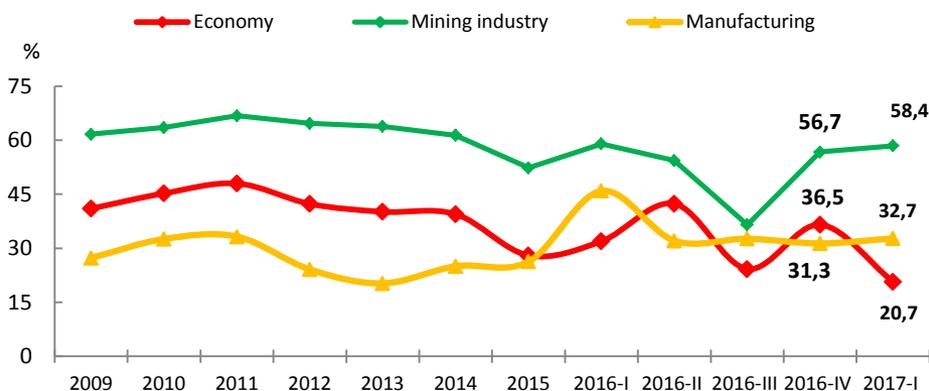
Classification of enterprises in terms of return on sales
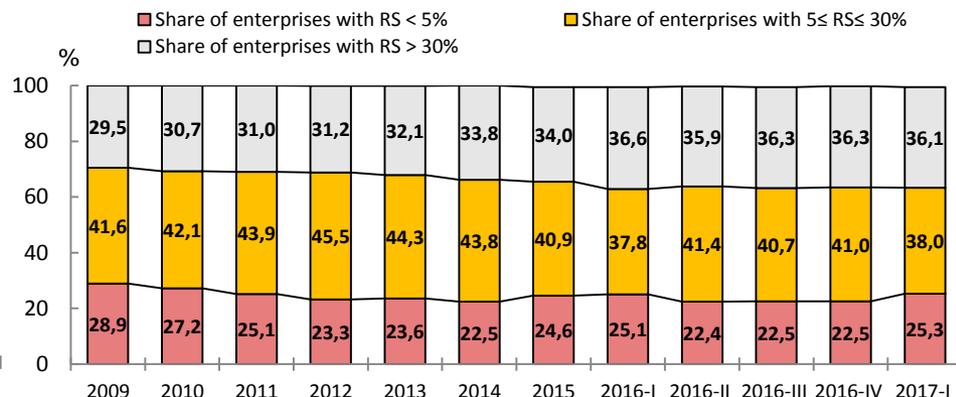
IMPACT ON THE REAL SECTOR OF THE ECONOMY BY THE BANKING SYSTEM

In Q1 2017, the demand of enterprises for bank loans decreased.

In Q1 2017, the share of enterprises, which applied for a bank loan, decreased to 22.1% (from 23.6% in Q4 2016). The share of enterprises, which obtained loans (including next tranche on an earlier credit line) fell to 17.3% (19.9% in Q4 2016). The level of rejected loans increased: the share of enterprises that were rejected a loan increased to 4.8% (from 3.7% in Q4 2016). Moreover, the share of large enterprises, which failed to obtain a loan, also increased to 5.0% (from 3.7% in Q4 2016).

The share of enterprises which intend to get a loan in Q2 2017 increased to 19.4%. The loan demand of enterprises in the manufacturing and mining industry increased (to 26.6% and 11.6%, respectively).

Demand for loans

answers, %

(legend: for economy, mining, manufacturing)
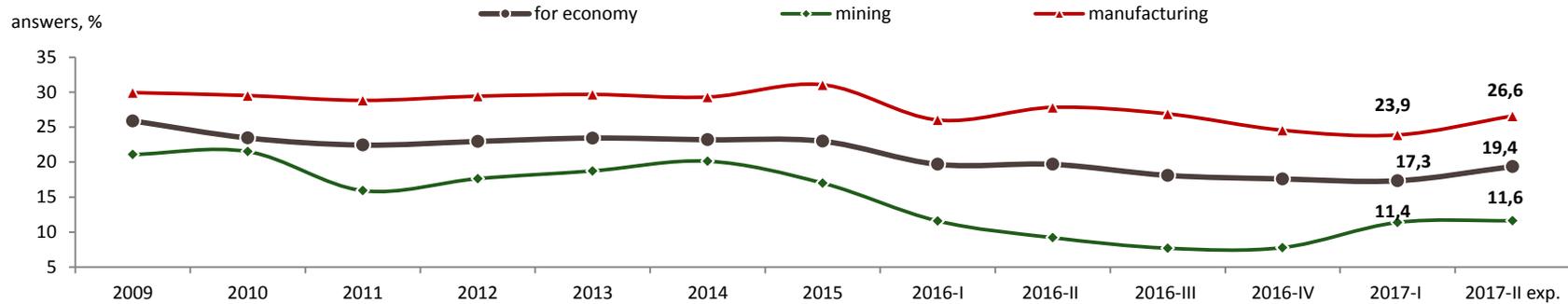
Consideration of applications for lending

answers, %

- share of enterprises that have been denied a loan
- share of enterprises that have received loan
- share of enterprises that applied for a loan

Share of enterprises that have been denied a loan

answers, %

(legend: small and middle, large, economy)
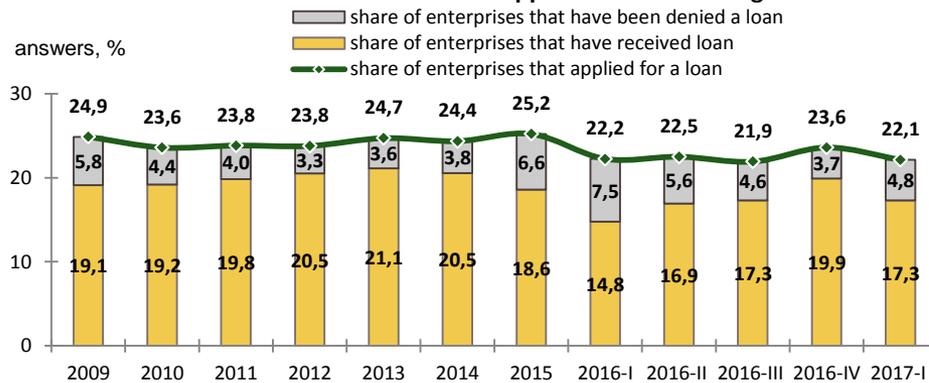
*including the next tranche of the previously opened a line of credit
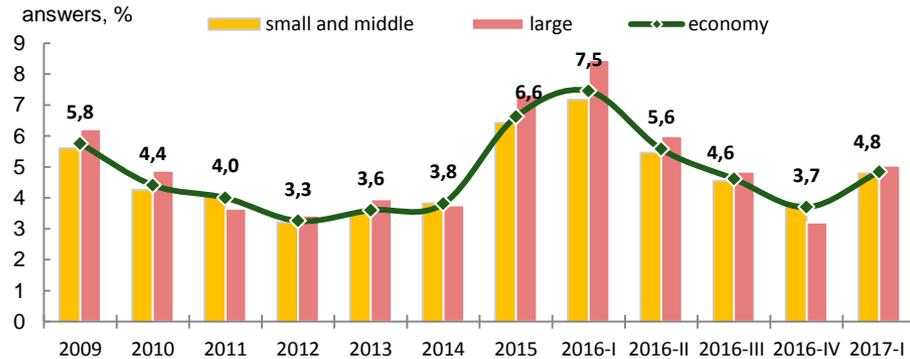
IMPACT ON THE REAL SECTOR OF THE ECONOMY BY THE BANKING SYSTEM

In Q1 2017, price conditions (interest rates on loans, commission fees) and non-price conditions (maximum amount and tenor of a loan, requirements to a borrower's financial standing, collateral requirements) of lending regarding loans for current and fixed assets continued to improve slightly.

The annual average interest rate on loans in the tenge in Q1 2017 decreased slightly to 14.3% (14.4% in Q4 2016). The gap between an actual and an acceptable interest rate on the tenge loans increased: acceptable annual interest rates accounted for 8.0%. An actual loan tenor for loans in the tenge decreased as compared to the previous quarter and was 17 months, and an acceptable loan tenor for enterprises – 27 months.

In Q1 2017 interest rates on foreign currency loans decreased to 8,1% (8.5% in Q4 2016), and interest rates acceptable for enterprises decreased to 3.8%. Actual tenors on foreign currency loans were 22 months, and acceptable tenors – 23 months (in Q4 2016: 24 and 25 months, respectively).

Changes in the conditions of lending
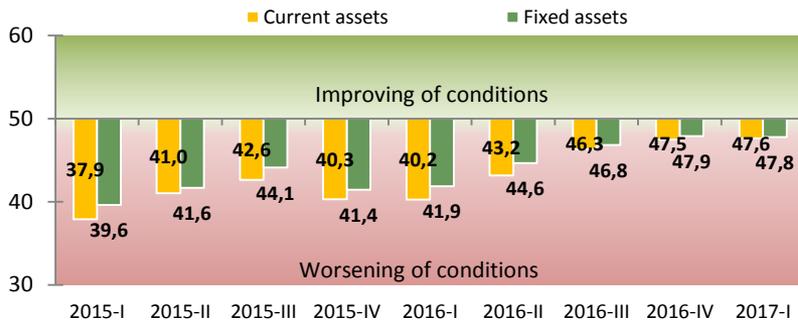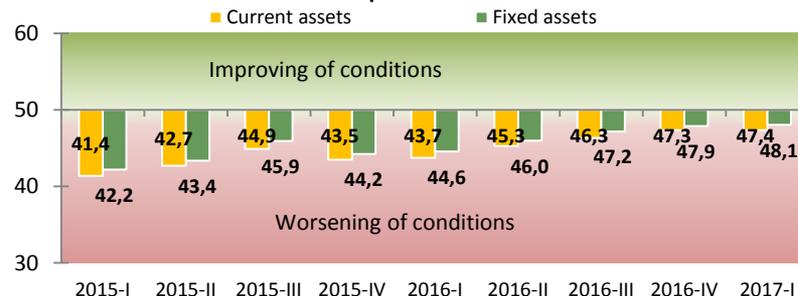
Loan rates and loan terms

* The higher (the lower) the DI deviates from 50, the higher (the lower) are the rates of growth (decline) in the indicator; the level of DI=50 means the absence of any change

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IMPACT ON THE REAL SECTOR OF THE ECONOMY BY THE BANKING SYSTEM

In Q1 2017, debt of enterprises on bank loans increased: DI=46.0. Assets and net worth of enterprises increased as well: the DI of assets and net worth made up 51.9 and 52.5, respectively.

In Q1 2017, the volume of deposits held by enterprises with banks declined (DI=49.8). The decline is noted both on deposits of large enterprises as well as small and medium-sized enterprises: DI = 50.8 and 49.4, respectively. Enterprises in Q2 2017 expect a further decline in deposits (DI= 49.4).

Credit, assets and owned capital
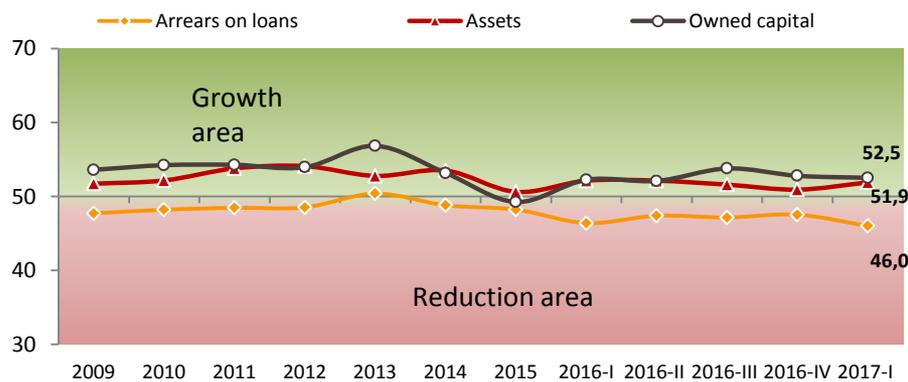
Volume of deposits of enterprises
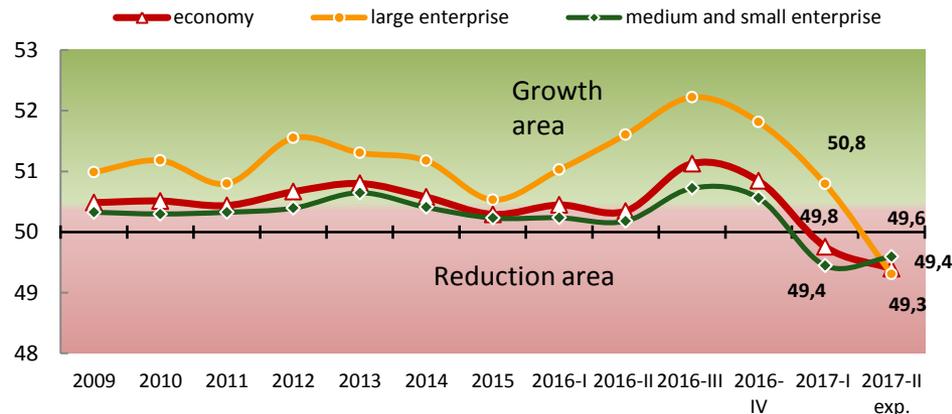
* The higher (the lower) the DI deviates from 50, the higher (the lower) are the rates of growth (decline) in the indicator; the level of DI=50 means the absence of any change

IMPACT OF CHANGES IN THE EXCHANGE RATE

According to the results of the survey of enterprises in the real sector of economy in Q1 2017 the tendency for decreasing of negative impact of exchange rate of tenge to foreign currencies on their activity continued. In general, this was induced by the stabilization of the exchange rate of tenge and gradual adaptation of the economic agents to the free floating exchange rate regime.

In the reported quarter the share of companies indicating negative effect of the change of exchange rate of tenge to USD decreased by 20% compared with the Q1 2016. Furthermore, USD is the second most used currency for transactions with foreign partners (in Q1 2017 share in the basket of currencies accounted for 46%). Russian ruble remains the main currency (53%).

USD/KZT, answer %
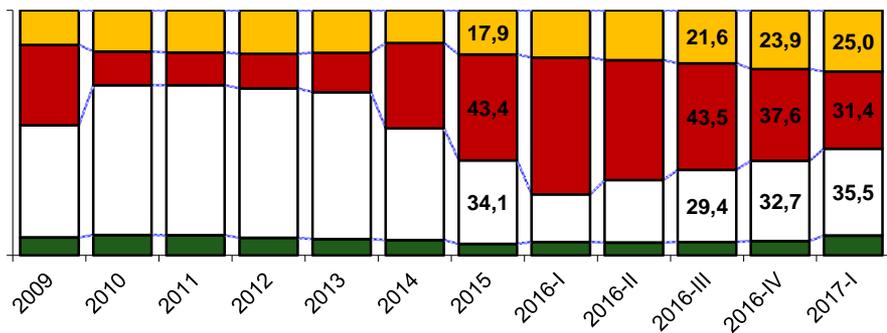
EUR/KZT, answer %
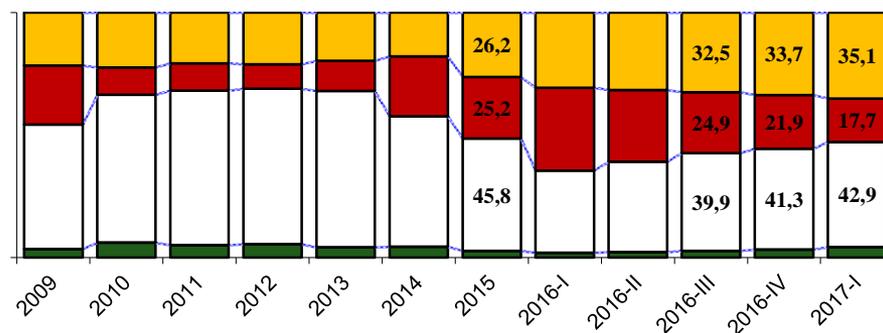
RUB/KZT, answer %
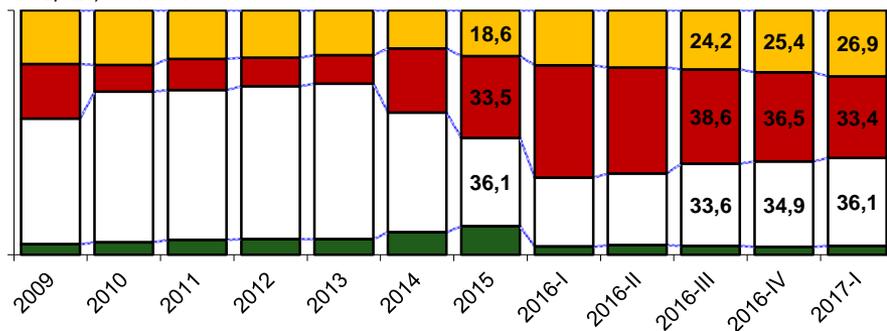
Usage of foreign currency in settlements
(% by currency)

- positive
- negative
- no impact
- I don't know

USD · EUR · CNY · RUR · no settlements · other currency
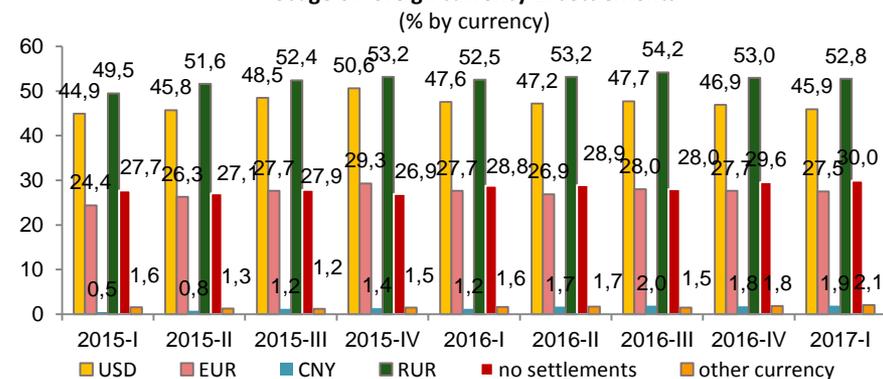
COMPOSITE LEADING INDICATOR*

Commencing from the second half of 2016 composite leading indicator began to recover. According to the results of the survey conducted in 1Q 2017, the positive dynamics of the indicator remains, which implies the continuation of the recovery of economic activity recovery on account of gradual adaptation of the economy to new conditions. Growth of the composite leading indicator is also connected with the improvement of investment activity and business conditions as a result of stabilization of the situation on world commodity markets in 1Q 2017, in the domestic economy and in the economies of the main trading partners.

The survey results reflect the signs of further strengthening of the demand for finished products and services. With the exception of construction and trade sector, where the demand has improved slightly compared to the previous periods but has not yet recovered, the growth in demand has been recorded in all other sectors of the economy.

Respondents pointed to a positive impact on economic activity from the stabilization of the situation in the foreign exchange market. At the same time, according to the results of the survey, the majority of enterprises continue to finance current and fixed assets at their own expense. However, there has been an increase in refusals in the loan applications of enterprises in the real sector in 1Q 2017. These results, in turn, indicate the preservation of relatively tight credit conditions for borrowers.

In 2Q 2017 respondents expect further improvement in the economic situation (CLI amounted to 100.6), as evidenced by increased demand for finished products in all sectors of the economy and lower prices for raw materials.
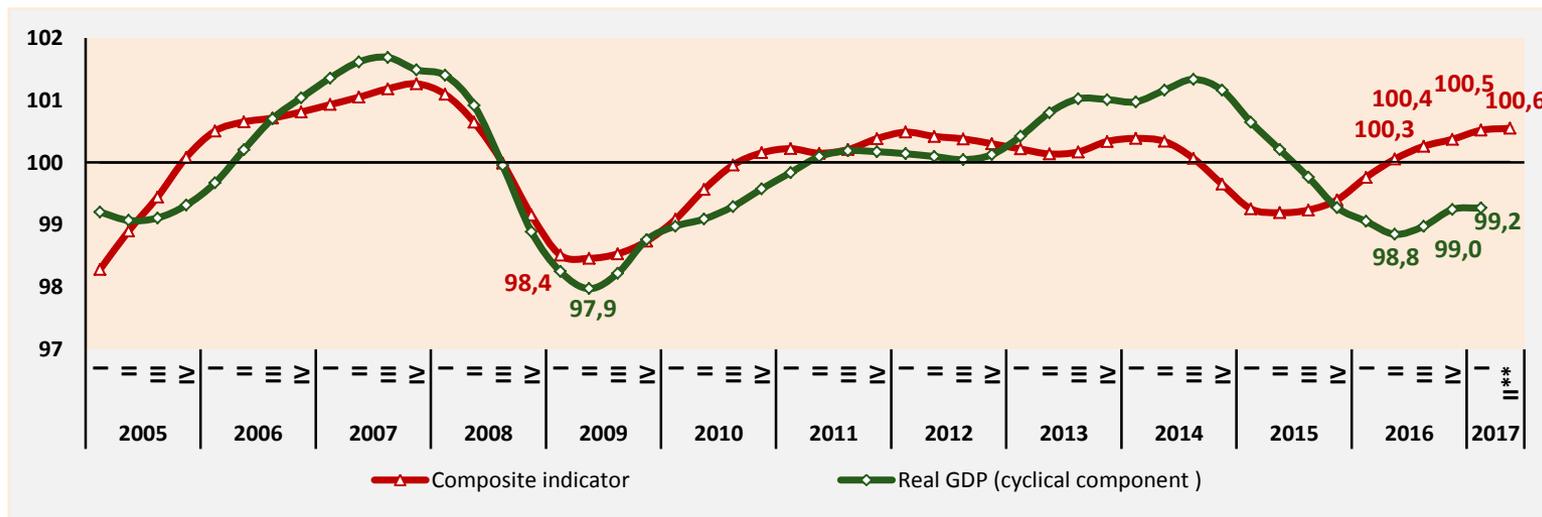
* A composite indicator is used to identify turning points in the business cycle and provides good quality information about the state and directions of trends in the economic activity. A composite indicator reflects a summarized evaluation of opinions of managers of the interviewed enterprises regarding the existing and anticipated situation in their enterprises and possesses the forward-looking feature of the real GDP behavior for 1-2 quarters. Construction of CLI is based on the OECD methodology («OECD System of Composite Leading Indicators, Methodology Guideline», OECD 2012).

** The CLI parameters for 2Q2017 are calculated on the basis of expectations among enterprises in the real sector that participated in the survey.

METHODOLOGICAL COMMENTS

➢ The diffusion index (DI) as reflected in tables and in figures is calculated as a sum of positive responses and a half of "no change" responses. This index is a generalized indicator which characterizes the behavior of the reviewed indicator. If its value is above 50 – this means a positive change, if it is below 50, then the change is negative. In doing so, the further (the higher) the value of the diffusion index deviates from 50, the higher are the rates of change (increase or decrease) of the indicator.

➢ The indicator of "an acceptable interest rate on bank loans" is calculated as the average of interest rates indicated by enterprises participating in the monitoring process as acceptable rates for these enterprises in terms of the existing level of profitability of production.

➢ Numbers reflecting financial ratios are provided as average values calculated based on the whole sample of interviewed enterprises as well as broken down by sector, where necessary, based on estimates of the quarter-end balance sheet numbers received from enterprises. In doing so, the evaluation data as well as the averages calculated on their basis are not aiming at obtaining the absolute precision of their values (since they are not the reporting ones) but rather serve for obtaining updated estimates and for analyzing the trends of the change in the state of the non-financial sector of the economy and its branches.

➢ The composite indicator (CI) possesses the forward-looking feature of the real GDP behavior for 1-2 quarters. The time series of the CI and the real GDP (in terms of prices of the year 2005) are cleared of seasonality and do not contain the trend, i.e. they only include a cyclical component as determined by short-term fluctuations of the economic market environment. For comparability purposes, the resulting cyclical components are standardized, i.e. they are reduced to one (non-dimensional) unit of measurement.

The CI serves to reflect short-term development trends in the real sector of the economy as a whole. It possesses the following features: 1) it has a forward-looking mature; 2) it reflects a cyclical nature in the development of the real sector of the economy; 3) it is quickly designed since it is built on the basis of on-the-spot interviews of enterprises.

Out of indicators built up based on interviews of enterprises, the following leading indicators were included as the CI components:

1) The DI of the change in the demand for final products in economic sectors
2) a group of indicators that reflect the change in prices :
• the DI of the change in prices in the real sector as a whole;
• the DI of the change in prices for raw materials and supplies.
3) a group of indicators that reflect the change in the investment and lending activity:
• the percentage of enterprises which obtained loans to finance their property, plant and equipment (including governmental programs);
• the percentage of enterprises which use other sources apart from own funds and bank loans to finance their property, plant and equipment and working capital;
• the percentage of enterprises which obtained a loan;
• the percentage of enterprises which want to get a loan;
• the level of actual interest rates on loans in the tenge and in foreign currency.
4) the employment rate indicator: the percentage of enterprises where the number of employees decreased
5) the indicator of the impact on activities of enterprises by the change in the exchange rate of the tenge (versus the US Dollar, Euro and Russian ruble)

Research and Statistics Department
National Bank of Kazakhstan