



SAVING GRACE

Kazakhstan 2017 | ECONOMY | VIP INTERVIEW

TBY talks to Daniyar Akishev, Governor of National Bank of Kazakhstan (NBK), on challenges in the national economy, de-dollarization, and the sectors most likely to grow in the coming years.

How would you characterize the changes that have occurred in Kazakhstan's economy in the last decade?

BIOGRAPHY

Daniyar Akishev was born in Almaty on May 25, 1976. In 1996, he graduated with honours from the Kazakh State Academy of Management majoring in Economics (specializing in Organisation of Banking System). He started his career in 1995 as a specialist at the Central Asian Stock Exchange. During 1996–2003, he occupied different positions at the Research & Statistics Department of the National Bank of Kazakhstan, and during 2003–2007, he headed that department. In August 2007, by presidential decree, he was appointed a Deputy Governor of the National Bank of Kazakhstan. From August 2014 to August 2015, he was the head of the Social and Economic Monitoring Department of the Executive Office of the President of the Republic of Kazakhstan, and from August to November 2015 he served as Acting Aid to the President of the Republic of Kazakhstan.

There have been several stages of development in the Kazakhstani economy. Due to the high investment activity of domestic and foreign capital and the consistent implementation of socio-economic reforms in the first half of the 2000s, the economy of Kazakhstan grew rapidly during that period (real GDP growth for 2000–2006 was 10.3% on average). However, such rapid growth strengthened the raw material orientation of the economy and increased its vulnerability to external shocks. During the 2008 crisis, growth slowed to 1.2% in 2009 and spread across all sectors, which was accompanied by a drop in domestic demand and falling investment. The main drivers of economic growth during this period were government measures to stabilize the economy and support the financial sector. The macroeconomic situation in 2010–13 gradually began to stabilize as a result of the recovery of the global economy and growing demand for Kazakhstan's basic export goods. From 2014 to the present, Kazakhstan's economy experienced significant shocks from falling oil prices, reduced

exports, and a depreciation of the national currency.

The situation was further exacerbated by geopolitical crises and the slowing economies of Kazakhstan's main trading partners, in particular Russia, the EU, and China. In 1Q2016, real annual GDP contracted by 0.1% for the first time after the 2009 crisis. However, the measures taken by the government within the framework of anti-crisis programs to stimulate and diversify the economy partially offset the impact of shocks, maintaining employment and contributing to the development of non-oil sectors. According to preliminary statements from the Ministry of National Economy, in 2016 the economy grew by 1%. Such sectors as construction industry, agriculture, manufacturing, transport had a significant contribution to the positive dynamics of the GDP. In addition, growth of investment in fixed capital financed by both the government and the private sector remains high. The dynamics of domestic consumption indicate a gradual adaptation of the population and businesses to the new economic conditions. In general, we can talk about a transition to a gradual recovery of the economy, however this trend is unstable and depends largely on the stability of the external economic environment.

How is the situation with the de-dollarization of the economy progressing?

In January 2016, our statistics showed the share of FX-denominated deposits of individuals amounted to 80%: no one trusted the tenge and people were converting their savings to dollars. In that situation, monetary policy became ineffective and credit channels and the state securities market did not work, meaning no one knew the tenge price. At that point, NBK started providing concrete measures to restore confidence in the tenge. First, we increased the recommended interest rate for tenge deposits from 10-14% and reduced the recommended interest rate on FX-denominated deposits from 3-2%. After some confidence was restored in the oil market as prices gradually increased, the tenge started to appreciate. Between January 2016 and January 2017, the tenge appreciated by 16%. People see tenge deposits as a more appropriate instrument to save money. Overall the share of FX-denominated deposits was 70% in January 2016 and at the end of 2016 it was 55%, so tenge deposits grew by KZT3.3 trillion over the last year while FX-denominated deposits decreased by KZT1.1trillion which is roughly equivalent to USD3.2 billion. We analyzed the experiences of other countries and found that many countries that had a high level of dollarization took many years to achieve the same results. For example, in Turkey changes in the deposits dollarization of 10 percentage points were seen only within five years. My task is to bring this value back to the historical levels of 40% dollar-denominated deposits.

What can you tell us about the consolidation talks in the banking sector?

GDP volume in dollar terms in 2014 was roughly USD221 billion, which fell to around USD133 billion in 2016. This represents a dramatic decline of more than USD80 billion in just two years. Therefore, room for business activity has decreased significantly, which is why we talk about this consolidation, not only in the financial sector but also in construction, mining, and other sectors. The situation has changed and business models

that were successful last decade no longer work. The period of easy money has ended, so there is a need to find additional capital injections for the banks to provide liquidity. If a company does not have funds, it needs to consider some options to merge its assets and the distribution of the market to achieve some effect of optimizing and reducing cost through optimizing management and others. Consolidation of the banking sector is therefore inevitable. However, I would like to mitigate the risks as some players might start an aggressive policy of attracting deposits of individuals' assets to try to save their institutions on the market. This is why I recommended being more careful in terms of asset allocation and providing more safeguards in such conditions.

What is your forecast for the domestic economy over the medium term and in which sectors of the economy do you see the biggest growth and development potential?

The NBK estimates growth of the Kazakhstani economy in 2017 to be 1.5-2%, with oil prices set at USD40 per barrel. The positive - but still quite weak - trend in 2017-18 reveals the slow adaptation of the economy to the new economic reality. The economy will operate below its potential level until 1Q2018, reflecting deflationary pressures from domestic demand side. External demand is expected to be in the positive zone with respect to its potential by mid-2018, primarily due to the acceleration of economic activity in Europe and Russia, which will have a positive impact on the exports of Kazakhstan. In addition to the oil sector, there are industries whose contribution to GDP dynamics remained stable over the past few years. Among sectors with significant potential are agriculture and agro-industrial complex, in particular the development of animal husbandry, food production, and light and textile industries. In addition, our geographic location creates opportunities to improve transport and logistics infrastructure and develop our transit potential. Projects in these areas will attract foreign investments, particularly those of strategic partners such as China, Russia, India, Iran, and others. Currently, the government is actively involved in the development of potential sectors of the economy through financing the enterprises of the real sector at the expense of budgetary funds, supporting small and medium-sized businesses.

What are your expectations for 2017 and what will the main focus of the NBK be?

The main objective of NBK's monetary policy is to ensure price stability. In 2017 we set the inflation target range at 6-8%. The main tasks are to overhaul the monetary policy instruments, as well as to create the pleasant conditions for lending recovery. Key measures will be taken to strengthen the role of the base rate. Moreover, the question about the clarification of the target rate in the money market will be considered. In order to adequately reflect the cost of money in the economy, the official refinancing rate will be equalized to the base rate. In addition, reserve requirements mechanism will be improved. NBK plans to continue working on the formation of the risk-free yield curve, which is an indicator of market expectations on interest rates. NBK will continue to issue its own securities - NBK notes - with various maturities. If necessary, it will use its own portfolio of government securities for the purchase and sale of government

bonds on the secondary market. Along with short-term notes and the auction for the purchase of securities with reverse sale (credit auction), NBK plans to introduce deposit auctions as part of open market operations. We are also highly focused on communication. We will continue to work on the disclosure of information on monetary policy directions, publishing decisions about the base rate and other instruments, also explaining the rationale behind the decisions. In addition, NBK will continue to publish forecasts of the main macroeconomic variables and analytical and statistical information, as well as the results of conducted research.