Report of NBK Governor at the meeting of the Government of the Republic of Kazakhstan
'Outcomes of Socio-Economic Development and Performance of Republican Budget for January – September 2021'
Nur-Sultan City, October, 12, 2021

Dear Askar Uzakpayevich!

Dear colleagues!

Following results of 9 months of this year **growth in global** GDP and **business activity** is reported worldwide, which is accompanied by an **increased inflationary** pressure and **expectation of tighter** monetary conditions.

(ECONOMY IN THE WORLD AND IN KAZAKHSTAN CONTINUES RECOVERY)

In the 3rd quarter of this year the global economy has returned to a **pre-pandemic** level and, according to OECD forecasts, will continue to recover in **2021-2022**. Growth of the **global GDP** in 2021 will make **5.7%**, including **5.3%** among countries which are major trading partners of Kazakhstan in the Eurozone, **8.5%** in **China**, and **2.7%** in **Russia**.

After **3 months of decline**, the **Global Composite PMI** in September rose from **52** to **53** due to the **service** sector.

In Kazakhstan, **business activity index** fell by **0.4 points** to **49.8** due to decreased activities in construction and services to **49.3** and **49.1**, in industry the index rose by **1.8 points** to **50.9.**

Reported **rapid recovery** of the global economy was possible due to **fiscal stimuli** and **soft monetary conditions.**

(*AS A RESULT OF INCREASING GLOBAL DEMAND, RAW MATERIALS RISE IN PRICE)*

Rapid growth of demand that followed the global economic recovery is putting **pressure** on **commodity prices**.

Cost of **industrial commodities** this August soared by **38.5%**, mainly due to a **42.6%** surge in prices for base metals in connection with a **high demand** from **China** and **developed countries**. Prices for **agricultural raw materials** for this period grew by **22.7%.**

This **September, FAO Food Price Index** rose to **130.0** because of higher prices for **vegetable oils, cereals, dairy products** and **sugar**. Over the year, FAO index has soared by **32.8%.**

An extra source of increase in producer's prices at the end of September this year was a **further rise in the cost** of dry cargo **transportation**, which, according to the Baltic Dry Index, soared by **5.4 times** in price compared to December 2019, and by **10-fold** versus **May 2020**.

Taking into account **higher commodity prices** and **rising** transportation costs, the OECD estimates their contribution to annual consumer price inflation in the **G20** countries at **1.5 p.p**.

(DEVELOPED COUNTRIES SET TO TOUGHENING OF MONETARY POLICY)

As a result of rising inflationary pressure worldwide, **developed countries** also set to **tighten** monetary policy.

At the meeting on September 22 this year the **Fed** discussed an **earlier** rate hike **as early as in 2022** instead of **2023**. An announced **QE curtailment** is expected in **November** this year.

The **ECB** is reducing a volume of **bond purchases** amid **accelerating inflation** in the **EU** to a **13-year** high of **3.4%,** including in **Germany** to a **28-year** high of **4.1%,** in **France** to a **10-year** high of **2.7%.**

Since the beginning of September this year, **22 countries** have **raised** their key rates, including once again in **Russia** - by **0.25 p.p.** up to **6.75%** against the background of inflation growth to a **maximum** in **5 years** - **7.4%** this September. Central banks of **New Zealand** and **Norway** also made a **25 b.p.** increase.

In this regard, an **expected withdrawal** of stimulus measures by central banks of **developed countries** is an **important stage in transition** to a neutral monetary policy worldwide.

(SIGNIFICANT ADJUSTMENT IS TAKING PLACE IN FINANCIAL MARKETS AGAINST THE BACKGROUND OF A FALLING RISK SENTIMENT)

Against the background of an earlier transition to toughening monetary policy by developed countries, an **adjustment** is taking place in the financial markets.

Market volatility in September was enhanced by fears of a crisis in the Chinese debt market associated with a risk of default by the largest developer **Evergrande Group**, and rising gas prices in Europe and Asia.

Following September, the **USD** appreciated by **1.7%**, while currencies of **emerging markets** depreciated by **2.9%**. **Global** stock **indices** for **developed countries** and **emerging markets** fell by **4.3%** and **4.2%** due to worsening risk appetite. Yields on **10-year US public stock** grew in September by **18 b.p**. due to tension with the public debt ceiling.

As a result, there is an **outflow** of capital from financial markets against the background of a **simultaneous** decline in value of **shares, gold and public stock in developed countries**.

(INFLATION FOR 9 MONTHS OF 2021 ROSE)

Under the pressure of the above-mentioned factors, inflation in **Kazakhstan** continued to accelerate reaching **8.9%** this **September**, despite the seasonal decline in prices for **vegetables** by **8.7%** and **fruits** by **2.4%**.

Food inflation still makes a major contribution as it accelerated over the month from **11.4%** to **11.5%** due to the rise in prices for **meat (1.3%), vegetable oils (0.6%)** and **sugar (1.1%).**

Non-food inflation inched up by **0.2 p.p.** in September from **7.3%** to **7.5%** amid rising prices for **diesel** (**3.8%** for the month), **gas (0.9%)** and **coal (1.9%).**

Further rise in prices for **fuels and lubricants** and a possible rise in prices for **grain** represent a significant risk for inflation **stabilization**.

Deteriorating external inflationary background, especially from countries which are major trading partners, such as the Russian Federation, is an **extra** source of inflationary **pressure**.

In these conditions, **effective** implementation of the **Anti-Inflationary** Response Package designed to **stabilize** non-monetary factors should **restore** the inflation in **2021 to the upper limit** of the **7.5-8.5%** corridor. For its part, the National Bank will **continue** to pursue **disinflationary** monetary policy based on a thorough analysis of external markets and the internal situation.

(THIS SEPTEMBER ANNUAL INFLATION ACCELERATED IN 13 OUT OF 17 REGIONS)

In order to stabilize non-monetary factors this **September** the Government, together with akims, has launched implementation of the **Anti-Inflationary Response** Package.

As a result, cumulative growth in prices for **staple foods fell from maximum 10.4% in August to 9.6%** following results of this September. However, according to results of the first week of October, prices **continued to grow** making **9.9%** since the beginning of this year. Main contribution to rising cost of staple foods was made by a rising cost of **eggs**, **chicken** meat, **cabbage**, **sugar** and **beef**.

In September, prices for **diesel fuel** rose by **3.8%** and in some regions its growth exceeded **10%**. Despite growing output and suspended exports, there is a **shortage of diesel fuel,** which increases **inflationary pressure** and indirectly affects **other goods**.

Over the past month, annual inflation **accelerated** in **13** out of **17** regions. Moreover, **in 6 regions** it **exceeds 9%.**

According to the National Bank, price **stabilization** in **regional markets** and **prevention of shortages of goods** are key factors to curb inflation this year.

(TENGE EXCHANGE RATE INSIGNIFICANTLY FELL IN

SEPTEMBER 2021)

Despite a **tangible** rise in oil prices, growing **demand** in the domestic foreign exchange market puts **pressure** on KZT exchange rate.

For 9 months of 2021, purchases of STBs on the stock exchange expanded by **19%** and reached an average of USD **2.6 billion** monthly against the background of an increase in imports of consumer goods by **25%** for 7 months of 2021. **Fiscal stimulus** and **use of pension savings** are also factors behind increased imports and growing demand for foreign exchange.

During the month, tenge received support from **operations to convert funds of the National Fund** to make transfers to the budget and sale of **subjects of the quasi-public sector.** For 9 months of this year, companies of the quasi-public sector sold USD **2.3 billion** in foreign exchange earnings.

Global enhancement of the USD continues to put pressure on currencies of emerging markets, including **tenge**. As a result, despite a significant increase in oil prices by **7.6%** to **USD 78.52** per barrel, the national currency lost **0.1%** of its value for the month to **KZT 425.75** per USD. As of October 11, the exchange rate is **424.55** KZT/ USD, up by **0.3%** since the beginning of the month.

(ASSETS OF THE NATIONAL FUND SHRANK AS A RESULT OF MARKET ADJUSTMENT)

Key trends in global markets as signals of the US Fed's curtailment of its stimulus program as well as an adjustment in the markets have facilitated a decrease in the country's international reserves.

Assets of the National Fund at the end of September this year amounted to USD **55.0 billion,** having decreased by **USD 1.9 billion** for the month.

In September, USD **913 million** were **sold** to ensure allocation of target and guaranteed transfers in the amount of **392 billion** KZT.

Receipts to the National Fund in September totaled **135 billion** KZT, including USD **259 million** in foreign currency or **110 billion** KZT in equivalent.

Investment income of the National Fund for September 2021 turned out to be **negative** and amounted to **(-) USD 1.20 billion** or **(-) 2.11%** due to an adjustment for all asset classes.

A **simultaneous** decline in prices across all asset classes is **short-term.** As of October 11, **investment income** of the National Fund has **partially recovered** and made USD **250 million** since the beginning of the month. In the long term, **strategic allocation of the National Fund balances risks.**

(IN CONDITIONS OF A FALLING GOLD PRICE, VALUE OF GOLD AND CURRENCY DIMINISHED)

Gold and currency reserves at the end of this September totaled USD **35.6 billion**, down by USD **1.2 billion** since the beginning of the month.

Gold portfolio contracted by USD **0.8 billion** due to a **4.6%** fall in the gold price down to USD **1,731** for an ounce as a result of higher yields on **US treasury bonds** amid signals from the US Fed to roll down its large-scale stimulus program.

Assets in freely convertible currencies **decreased** by USD **0.4 billion** mainly due to **contracting balances on correspondent accounts.**

Gross international reserves totaled USD **90.6 billion.**

(INVESTMENT INCOME SUPPORTS GROWTH OF UAPF PENSION ASSETS)

UAPF pension assets at the end of this September made **13.1 trillion** KZT, up by **194.3 billion** KZT or **1.5%** year-to-date.

As of the reporting date, number of **executed applications** of depositors for early withdrawal of pension savings totaled **491.7** k requests for an amount of **1.9 trillion** KZT, where housing issues account for **97.5%**.

Following results of 9 months of this year, an **8.9% yield** was obtained with 6.2% inflation. Thus, from the beginning of this year, **real profitability** of **2.7%** was provided for UAPF investors.

Dear Colleagues!

Current acceleration of inflation in Kazakhstan is caused equally by both **external** and **internal** factors.

Against the background of an improving **balance** in global commodity markets and recovering **supply chains**, **external factors** are expected to **stabilize by the end of next year.**

In these conditions, key efforts in the medium term should focus to eliminate **imbalances** in certain domestic markets and mitigate **import dependence** as factors of inflationary pressure.

As an example, today Kazakhstan receives **40.8%** of its imports from **Russia**, which is **indicative**, given **acceleration** of inflation in Russia to a record level of **7.4%** in September this year.

An equally important aspect to cut inflationary pressure is to **complete implementation of countercyclical fiscal rule** and **limit a growth pace** of budget expenditures.

Successful implementation of this package of measures will improve coordination of monetary and fiscal policies to achieve the inflation target in the **4-6%** corridor in **2022**.

Thank you for your attention!