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 – October 2021'
Nur-Sultan City, November 10, 2021, 09:00 a.m.

Dear Askar Uzakpayevich!

Dear colleagues!

The global economy continues its **recovery** accompanied by **rising inflation** as a result of caused by the pandemic **imbalances in supply and demand**, **high commodity and food prices.**

INFLATION BACKGROUND IN THE GLOBAL ECONOMY REMAINS INCREASED

The **global** inflationary background remains **elevated**. Both **developed countries** and **emerging markets** record updates to **longstanding highs**. This September, inflation in the US rose to a **record 5.4%**, in the **EU** and **Russia** to **4.1%** and **8.1%** in October, respectively. In **China**, rise in producer's prices, which is mostly paid attention to when making decisions on monetary policy, this September made **10.7%.**

According to IMF estimates, with **exhaustion** of the remaining shocks in **the short term** period, inflation in **developed** countries and **emerging** markets will temper by **mid-2022**. With **more prolonged** supply and demand imbalances, supply **disruptions** and rising **commodity and food prices**, the IMF estimates that stabilization of inflation could last until **2024**.

This October, global **food prices** continued to rise, reaching a **10-year high**. **FAO index** for the month increased by **3.9%** and reached **133.2 points** due to growing prices for **vegetable oil, cereal and dairy products.**

The National Bank estimates that inflationary pressure will remain **high throughout 2022** in **emerging markets**, including Kazakhstan, given persisting imbalances and rising inflationary expectations.

MONETARY POLICY WORLDWIDE GETS TOUGHER AGAINST THE BACKGROUND OF THE GROWING INFLATION

Participants of the financial market set **longer inflationary expectations.** Share of options in the United States that set inflation for the next **5 years** above **2%** is over **80%**, **56%** in the **UK**, **41%** in the **Eurozone**. Key rate **futures** and **forwards** are also priced with a greater likelihood of rate hikes in **2022**.

As part of tightening monetary conditions in October-November of this year, **17** countries **raised** their key rates. Since the beginning of this year, the **global monetary policy index** ascended from **4.18%** to **5.10%** this October.

Amid rising **inflationary pressure,** on **November 3, 2021** the **US Fed** announced the **start of the curtailment** of the quantitative easing program by USD **15 billion** monthly.

In these conditions, launch of a **rate hikes cycle** by **developed countries** poses risks of capital **outflow** from emerging markets. In this connection, **EM currencies** are **under pressure** against the background of **USD appreciation** and growing yields on **government securities** in developed countries. This October index of the **EM currency** basket against the USD weakened by **0.8%.**

WITHIN THE EAEU INFLATION SIGNIFICANTLY EXCEEDS THE TARGET

In all the EAEU countries, a **significant excess** of the inflation **target** is also recorded.

In Russia (8.1%), Armenia (9.1%), Belarus (10.2%), the current inflation rate is **more than double** the fixed targets.

In these conditions, Central Banks **respond** to growing inflationary risks by raising key rates.

In the EAEU countries, **stabilization of the inflation** is expected in **2022-2023** but with different dynamics, given current levels and **response measures** from Central Banks.

IN KAZAKHSTAN, CHANGES IN THE LABOR MARKET AFFECT PRICE FORMATION

In Kazakhstan, **business activity index** this October moved to a **positive** zone making **50.1**.

Improvement in business activity has an impact on **demand** for labor, which is **growing faster than supply**, reflected in a **49% surge** of vacancies in the first half of this year.

A number of industries have demonstrated an **increase in wages** and **job cuts** for the fifth month in a row. Employees quit in search of more **comfortable working conditions** and **higher salaries.**

In conditions of rising salaries, service **cost index** has **continued** its **growth** since July 2020 from **49** to **67**. **Recovery** in business activity and **growth in wages**, given a **high share** of wages in the **cost** of services (**50%**), create extra pressure on **inflation**.

ANNUAL INFLATION FOR 10 MONTHS REMAINED AT

8.9%

Monthly inflation in October was **0.7%**. Annual inflation remained at the level of **8.9%**, ceasing its growth for the **first** time in the last 6 months amid a slowdown in **food** prices from **11.5%** to **11.3%**. Along with that, **non-food** inflation continued to accelerate from 7.5% to **7.8%**, inflation of **paid services** - from 6.8% to **6.9%**.

Food inflation amounted to **0.7%** against the background of a seasonal growth in prices for **fresh vegetables** by **5.5%** (a 0.3 p.p. contribution) and eggs (**7.2%**). **Cucumbers** and **tomatoes** have demonstrated the highest growth by **22%**. Increased **egg** prices were caused by a **drop in production of** poultry farms, **higher cost of forages** as well as a probable cancellation of **subsidies** from **2022**.

Non-food inflation for the month amounted to **1%** due to a jump in prices for **diesel fuel** by **16.6%** or **34 KZT**. A significant **increase** in prices for **diesel fuel did not allow to reduce** annual inflation this October.

Inflation of **paid services** stood at **0.5%** amid recovery in business **activity** and higher **costs** in the **service sector.** IAV growth in production of services for 9 months of this year amounted to **2.9%.**

In **October**, number of **regions** with **accelerated** annual inflation fell from 13 to 7 (out of **17**). In **6** regions, annual inflation **eased up** and in **4** regions it **remained** at the level of this September.

Stabilization of the growth of food prices **in regions** is a result of implementation by the Government and the akimats of the Anti-inflationary Response Package designed to **curb non-monetary** inflation factors.

Despite the first signs of price stabilization, the **inflationary background** remains high and stable so far. Based on these factors, this October the National Bank **raised** the base rate by **25 basis points up to 9.75%.**

REDUCING CURRENT ACCOUNT DEFICITS

For 9 months of 2021, **current account deficit** decreased and, according to preliminary data, amounted to **(-) USD 3.0 billion** against the background of an improvement in the trade balance.

Exports of goods soared by **20.4%** to USD **43.1 billion** due to increased exports of **oil** by USD **3.6 billion** as well as **non-ferrous** and **ferrous metals**.

Imports of goods grew by **2.7%** to USD **28.0 billion,** largely driven by an increase in **consumer** goods by USD **1.5 billion.**

Recovery in the oil prices led to a **53.7%** surge in **income payments** to foreign direct investors up to USD **15.7 billion** from USD **10.2 billion** in 9 months 2020.

Continued growth of **consumer imports** restrains improvement in the **payment balance** and, as a result, creates pressure on the **foreign exchange market.**

CONTINUING DEPRECIATION OF TENGE AGAINST THE BACKGROUND OF GROWING OIL PRICES

Despite a **7.5%** increase in oil prices up to USD **84.4** per barrel over the month, the national currency lost **0.3%** of its value down to KZT **427.15** per USD in conditions of recovering **economic activity** and continuing **fiscal impulse.**

Against the background of an increased **demand** from business and households, **import of the Russian goods** in the 2nd quarter of this year accelerated to **36.1%** in annual terms from **2.4%** in the 1st quarter of this year, which led to depreciation of the tenge against the Russian ruble in October to **6.05** tenge per ruble, or by **3.4%.**

Along with that, increase in the base rate keeps **attractive debt instruments in tenge**, as evidenced by the growth in a volume of investments of non-residents in government securities of the Republic of Kazakhstan in October by **75 billion** KZT to **863 billion** KZT. Extra supply of foreign currency from **foreign** investors contributes to improvement of market **liquidity** and partial **satisfaction of demand.**

Stable demand for foreign exchange amid **growing imports**, its **limited** supply and **volatility** in foreign markets will **continue** to bring **pressure** on the KZT exchange rate.

INVESTMENT INCOME OF THE NATIONAL FUND REBOUNDED AFTER MARKET ADJUSTMENT

Assets of the National Fund at the end of October this year amounted to USD **55.1 billion.**

In October, USD **988 million** were sold to ensure allocation of target and guaranteed transfers in the amount of **428 billion** KZT.

Receipts to the National Fund in October amounted to **103 billion** KZT, including USD **163 million** in foreign currency.

Investment income of the National Fund for this October recovered after market adjustment and totaled USD **871 million** mainly due to the growth of **shares** and **gold**. **Thanks to a balanced allocation** of assets of the National Fund, investment income has **recovered** since the beginning of the year and stood at USD **2 billion** or **3.44%.**

NBK GOLD AND FOREIGN EXCHANGE RESERVES HAVE GROWN DUE TO RISING GOLD PRICES

Gold and foreign exchange reserves at the **end of this October** amounted to USD **35.8 billion**, having increased by USD **307 million** over the month.

The gold portfolio grew by USD **1.2 billion** driven by a **3.8%** rise in the gold price up to USD **1,796** per ounce.

Assets in freely convertible currencies **contracted** by USD **854 million** mainly due to a decrease in **balances on correspondent accounts of second-tier banks.**

Total **gross international reserves** made USD **90.9 billion**, having expanded by USD **354 million** over the month.

DIVERSIFICATION OF UAPF PENSION ASSETS CONTRIBUTES TO INVESTMENT INCOME

UAPF pension assets at the end of this October amounted to **13.2 trillion** KZT, having increased from the beginning of the year by **337.3 billion** KZT or **2.6%**.

As of October 31, 2021, **545.5 thousand** requests of contributors for early withdrawal of pension savings in the amount of **2.0 trillion** were satisfied, where housing issues account for

97.1% or **1.95 trillion** KZT.

Size of accrued **investment income** from the beginning of this year was about **1.2 trillion** KZT, where assets of a foreign exchange portfolio account for **14%**.

Following results of 10 months 2021, **9.9% profitability** was obtained with **7.0%** inflation, respectively, a **real profitability** of **2.9%** was ensured for UAPF depositors.

Additionally, this October, in pursuance of an **instruction** of the Head of State, the National Bank **ensured technical readiness** of the National Payment System.

1.Within the **Interbank Payment Card System** (IPCS), an infrastructure for processing card transactions has been created. Currently, work is underway to **integrate** this system with international payment systems - Visa, Mastercard, Union Pay.

2. Currently, platform of the **Instant Payment System** (IPS), designed for real time retail **payments** and money **transfers**, has been upgraded.

Launch of components of the National Payment System will be carried out in a **pilot mode** in **November-December 2021**.

Dear Askar Uzakpayevich, colleagues!

In order to achieve the goal set by the Head of State to **level off the inflation** to **8.5%** in **2021,** during the remaining two months of this year cumulative inflation should not exceed **1.4%.** This task is **achievable**, given that **historically** in November-

December over the past 5 years, cumulative inflation averaged **1.7%.**

Today, the Government and Akimats **focus** their attention on growing prices for food staples. However, one should also pay attention to food products that are **not included in the food staples** but have a **large weight** in the CPI and **tend** to appreciate in the last months of the year.

Adoption of **systemic** and **preventive measures** in order to **eliminate imbalances** in the commodity markets within the Anti-Inflationary Response Package will allow **stabilize** inflation and enter the target corridor **4-6%** in **2022**.

Thank you for attention!