

Monetary Policy REPORT

December 2021

NATIONAL BANK OF KAZAKHSTAN

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Monetary Policy Report is a quarterly publication of the National Bank, which contains the analysis of key macroeconomic factors affecting inflation as well as the forecast of macroeconomic parameters in the short- and medium-term horizon.

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PREAMBLE

Global business activity in the world, despite recurrent outbreaks of coronavirus, continues to recover. The industry is growing at a slower pace than services. Industrial production continues to be constrained by supply chain disruptions, skyrocketing energy prices, and material and labor shortages.

The recovery growth of Kazakhstan's trading partners has been largely implemented in 2021. Given higher existing GDP growth rates and expectations of continued supply disruptions, the dynamics of economic activity in trading partner countries in the forecast period has been revised downward. In 2022, the economic activity in Russia and China is expected to slow down to potential levels, while the economic growth in the EU will be building above 4%.

The imbalance between supply and demand observed in the market, problems with global supply chains, as well as a shortage of materials, exacerbate the global inflationary background. In the United States, the consumer spending deflator in October 2021 showed a record value in the last thirty years, accelerating to 5.0% on an annualized basis with a target of 2%. Annual inflation in China accelerated to 1.5% in October 2021. The acceleration is due to persistent supply disruptions and logistical problems, the re-spread of COVID-19 and high increases in energy prices. The growth of consumer prices in Europe in October 2021 showed the highest value in the last 13 years, accelerating to 4.4%. Among the main reasons for the significant rise in prices in the EU, as in many countries of the world, one can single out the active recovery of domestic demand, the global rise in prices for energy resources and food, and a low base of inflation in 2020. Forecasts for inflation in the EU are revised upwards compared to the estimates a quarter earlier, China - decreased.

Inflation in Russia continues to remain at elevated levels, having developed at 8.1% in October 2021 (Upd: 8.4% in November). The heightened dynamics of inflation in Russia is accompanied by an expansion of consumer demand, slower growth in supply, a poor harvest, higher world prices for raw materials, and heightened inflationary expectations. Against the background of the existing significant pro-inflationary pressure in October 2021, the Bank of Russia raised its inflation forecast for the end of 2021 from 5.7-6.2% to 7.4-7.9%. The revision of the short-term inflation forecast was accompanied by an increase in the key rate by 0.75 percentage points. up to 7.5%.

The FAO food price index rose 1.2% month-on-month in November, reaching its highest level since June 2011.

At the same time, certain external factors of inflation are showing signs of some stabilization. In November 2021, the Baltic Dry Index declined from its peak in October. However, it is still 6 times the May 2020 level.

A certain correction is being observed on the world oil market after a long rise in prices. In late November and early December, prices fell to 65-66 USD dollar per barrel due to concerns about the spread of a new strain of coronavirus. Despite the emergence of certain events that affect the growth of volatility in the market, the balance of risks does not shift towards the worsening. At the OPEC + meeting on December 2 this year it was decided to maintain the current parameters of the transaction, providing for a planned increase in production by 400 thousand barrels per day. Taking into account the current situation and forecasts of international organizations, the oil price of 70 USD dollar per barrel was considered as the basic development of the economy in the forecast round "November-December 2021".

Economic activity in Kazakhstan continued to demonstrate positive dynamics. For ten months of 2021, GDP growth in annual terms was 3.5%. The accumulated growth rates of the mining industry since the middle of last year entered the growth zone for the first time. Against the background of the last year's low base, most of the sectors of the economy are showing positive dynamics. At the moment, only agriculture and the provision of other types of services make a negative contribution to GDP. The decline in agriculture is due to the low grain harvest.

The recovery dynamics of consumer demand continues. The positive dynamics of retail trade remains. At the same time, the growth in the turnover of non-food products is accompanied by accelerated growth rates of consumer lending. An additional factor indicating an increase in consumer activity is the positive dynamics of household income. This is facilitated by the high growth rates of real wages of employees in

practically all sectors of the economy, with the exception of transactions with real estate, art, and the provision of other types of services.

There are now signs of a slowdown in **headline inflation.** At the end of November 2021, annual inflation in Kazakhstan slowed down slightly and amounted to 8.7% compared to 8.9% in October of this year. Nevertheless, there is high uncertainty about the stability of the outlined dynamics, including against the background of the emergence of a new strain of coronavirus - omicron.

The decrease in overall inflation was due to a slowdown in the growth of prices for **food products** from 11.3% to 10.9% and paid services from 6.9% to 6.4%. Disinflation for oils and fats, sugar and eggs made a significant contribution to the current slowdown in the growth of the food component in the context of stabilization of monthly dynamics and a high base of the previous year. At the same time, in November 2021, the growth in prices for bakery products and cereals, meat products continued, which is associated with increased costs of producers, a decrease in the gross harvest of grain crops.

In November 2021, the annual **non-food inflation** accelerated from 7.8% to 8.3% as a result of the continued growth in prices for fuels and lubricants and solid fuels. The annual growth in consumer prices for fuels and lubricants amounted to 22.3% (monthly growth - 4.3%): the cost of gasoline increased by 18.4% (2.4%), diesel fuel - by 46.6% (14.6%) . The rise in fuel prices is taking place in the context of rising producer prices.

The annual growth rate of prices for **paid services** in November 2021 slowed down to 6.4%. This is due to a slowdown in the growth of prices for regulated utilities, catering, hairdressing and personal services. At the same time, the growth of rental rates accelerated.

According to the National Bank's estimates, the seasonally adjusted annualized consumer price growth in recent months has slowed down from its peak in June, amounting to 5.6% in November 2021 (in October - 7.1%). Monthly estimates of the annualized core inflation indicate the formation of inflationary processes for the second month in a row within the target band of 4-6%. It is important how the dynamics of sustainable components will anchor in the target corridor in December 2021 and 2022.

Compared to the previous forecasting round, short-term inflation forecasts have not changed significantly. At the end of 2021, inflation is expected to be in the range of 8.5-8.7%. With further effective implementation by the Government and local executive bodies of the Package of Anti-Inflationary Response Measures for 2021-2024, inflation will form close to the lower limit of the forecast range. Accelerating growth in prices for non-food products will be offset by a slowdown in inflation for food. Taking into account the rise in the price of fuels and lubricants, the continuing rise in electricity prices and heightened inflationary expectations, inflation will continue to form at high levels. In the medium term, higher inflation will be observed in the trading partner countries of Kazakhstan compared to previous estimates. This is due to an upward revision of inflation in the trading partner countries of Kazakhstan and a higher dynamics of external food prices. On the other hand, a more restrained trajectory of the output gap will offset the influence of external factors on the medium-term trajectory of inflation. By the end of 2022, in the context of continued effective implementation of the Anti-Inflationary Response Package and the release of a high base in 2021, annual inflation will slow down to 6.0-6.5%.

The trajectory of the output gap has been revised downward compared to the previous forecast round. This is due to the lower forecast dynamics of the components of aggregate demand and economic activity as a whole. Nevertheless, in the forecast period, it is assumed that the upward trajectory of the output gap will continue amid a slight acceleration in GDP growth in 2022. In the medium term, the output gap will be at near-zero levels.

In 2021, given a low base of 2020, the recovery growth of the economy will be 3.7-4.0%. In 2021, the GDP growth rates had not undergone changes compared to previous estimates. In 2022, the GDP growth rates are expected to accelerate to 3.9-4.2%. At the same time, medium-term forecasts have slightly decreased being associated with a downward revision of the dynamics of economic activity in Kazakhstan's trading partner countries and more negative effect of disruptions in global and local supply chains on the country's economy compared to previous estimates. The consumer demand will keep growing due to the expected increase in the people's income and wages and in the consumer lending. Investment demand will be

demonstrating growth due to an overall recovery of the business activity. Due to persisting positive external demand and gradual easing of restrictions on oil production as part of OPEC+ transaction, exports will be demonstrating positive growth rates. Government consumption will show a minor upturn against a feeble rise in the national budget spending. For its part, the increase in imports will be related to the growing consumer and investment demand.

Compared to the previous forecasting round, the risk profile has generally remained unchanged; however, there are still high risks that inflation would deviate from the baseline scenario. There are essential risks that inflationary expectations would remain heightened, prices for certain food products, including bread and bakery, flour and meat, and fuel lubricants as well as a further deterioration of the situation with with supplies and logistics in the environment of new outbreaks of COVID-19.

Based on a detailed analysis of the situation in the external and domestic economy, consistency of the projected inflation dynamics with the actual values as well as updated forecasts of key macroeconomic indicators for the medium term, on December 6, 2021, the Monetary Policy Committee of the National Bank of the Republic of Kazakhstan decided to leave the base rate unchanged at 9.75% per annum with a interest rate band of +/- 1.0 p.p.



I. PROSPECTS OF THE DEVELOPMENT OF THE MACROECONOMIC SITUATION

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1.1. Forecast Assumpstions

The COVID-19 pandemic continues to predetermine a further development of the global economy. High inflation in countries, disruptions in global supply chains, and recurrent coronavirus outbreaks are expected to have some restraining effect in the near term. At the same time, as a result of the ongoing immunization campaign and the fact that countries most likely will not impose the same strict anti-COVID measures as they did last year or earlier this year, no strong drawdown in the global economic growth is expected.

According to the IMF forecasts, in 2021 the global economy's growth rates will be slightly lower than expected and will make up 5.9%. This is partly explained by lower forecasts for some developed countries because of problems with supply chains as well as for a number of Asian countries due to increase in coronavirus incidences. In 2022, the global economy is projected to slow down to 4.9%. The imbalance between supply and demand for many goods, which has arisen against the backdrop of the COVID-19 pandemic, is expected to persist for some time. Production in industries that are more dependent on supplies and component parts will remain under pressure. The service sector will serve as one of the growth drivers. Consumer activity, in turn, will remain hightened given the accumulated big savings and growth in wages. At the same time, demand may be slightly subdued by high prices and a limited choice of goods.

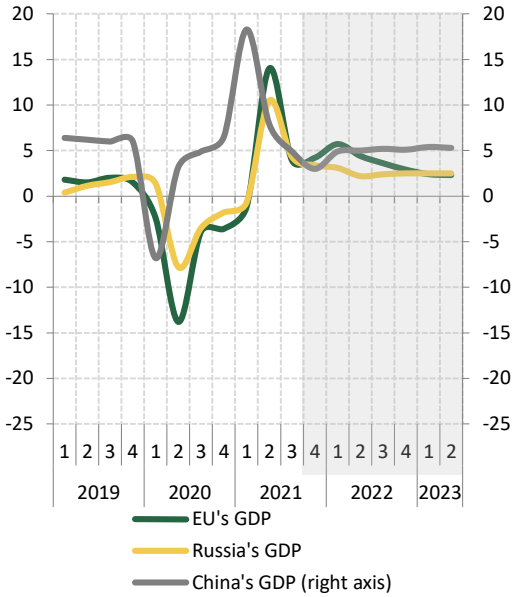
Over the forecast horizon, the pandemic continues to bring some uncertainty factor. The risks of a feebler global economic development are closely linked to inflation risks, which may increase if energy and raw material prices persist for a longer period and problems with suppliy chains remain unresolved. If these risks materialize, developed countries may move to normalization of their monetary policies earlier than expected, which threatens with capital outflow from developing countries, the increase in costs of financial terms and hightened volatility in foreign exchange markets. The risks of weaker development of the Chinese economy due to the current problems faced by the economy also remain relevant for further development.

According to projections of Consensus Ecs., during the forecast period the EU economy will be generally developing at a higher pace compared to earlier projections owing to the improved estimates for France and Italy. Even taking account of the new coronavirus outbreaks that occurred this autumn, Consensus Ecs. raised its forecast for 2021 to 5.0% (YoY) (in August 2021, 4.6% was projected, YoY). In 2022, a strong domestic demand, ongoing improvement of the situation in the labor market, favorable financial environment and a further implementation of the government recovery and resilence facility (RRF) will support high growth rates. The car industry and the construction sector will keep exerting a restraining effect in view of the problems with global supply chains, a shortage of microcircuit chips and high prices of the raw materials used. Thus, according to projections made by Consensus Ecs., in 2022 the economic growth in the EU would account for 4.2% (YoY) (a previous forecast was 4.3%, YoY) (Figure 1).

Lately, the Chinese economy encountered an array of problems related to recurrent outbreaks of coronavirus, disruption with electricity supply, a slowdown in the industrial production rates, the tightening of regulation in certain sectors, as well as to declined investments into real estate due to problems with Evergrande. Under the pressure of the above factors, the growth rates of the Chinese economy in 2021 would be lower than it was projected earlier. Consensus Ecs. lowered its forecast for 2021 from 8.6% (YoY) to 8.0% (YoY). Given the fact that many of the currently existing problems remain unresolved, it is expected that their negative effect may partially carry over to the next year. In this connection, Consensus Ecs. projects that in 2022 the growth rates in China will decrease from 8.0% (YoY) in 2021 to 5.1% (YoY) (in August 2021, the forecast for 2022 was 5.6%, YoY) (Figure 1). A more moderate economic growth rate is expected to be supported by the government through tax abatements, introduction of subsidies and implementation of a number of infrastructure projects. A further recovery in the service sector and retail sales is also expected to exert positive influence on the growth.

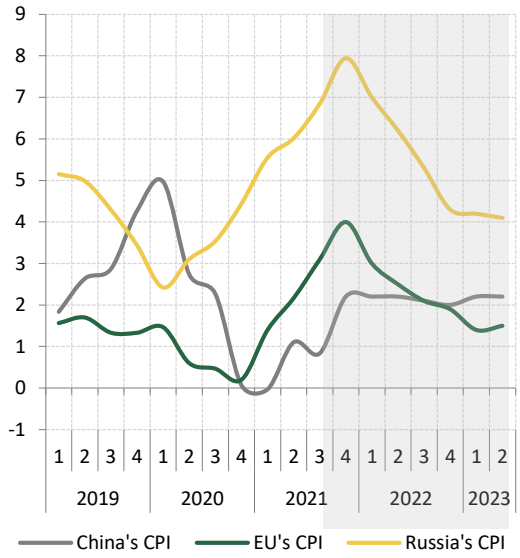
Forecasts about the Russian economy for 2021 are much better. According to projections of Consensus Ecs., the economic growth rates would account for 4.2% (YoY) (a previous forecast was 3.8%, YoY). The improvement in the forecast is largely related to a better environment in the global oil and gas market, easing of OPEC+ requirements on cutting the oil production, a heightened investment and consumer activity in the country. Meantime, the growth rates may be somewhat lower than expected as a result of deteriorating epidemiological situation this autumn as well as in view of a lower grain harvest. According to forecasts, next year the Russian economy will be developing at the level consistent with its potential due to lower energy prices, moderate bank lending and a feebler growth of the consumer activity. Consensus Ecs. projects a 2.6% growth (YoY) (a previous estimate was 2.8%, YoY) (Figure 1).

Figure 1. GDP Growth Rates in China, the EU and Russia in Real Terms, YoY, %



Source: Eurostat, National Bureau of Statistics of China, Rosstat, Consensus Ecs.

Figure 2. Inflation in China, the EU, Russia, YoY, %



Source: Eurostat, National Bureau of Statistics of China, Rosstat, Central Bank of Russia, Consensus Ecs., European Commission

According to the updated IMF forecasts, before the end of 2021, inflation in developed countries is expected to reach the peak followed by comeback to pre-pandemic levels by mid-2022. Inflationary pressure in developing countries will remain because of increased prices of food, oil and imported goods due to depreciation of their currencies.

According to projections of Consensus Ecs., inflationary pressure in the EU is expected to persist at least till the end of this year as a result of growing energy prices (gas, oil, commercial metals). Next year, as the problems with supply chains are resolved and supply in the market expands, inflationary pressure will start to gradually subside. An anticipated decline in oil rpices should also reduce the pressure. Hence, inflation will come back to its pre-pandemic levels by the end of the forecast period (Figure 2).

In China, consumer inflation will remain below the target over the forecast horizon (Figure 2). Due to the increased producer prices, the pass-through effect onto the consumer goods producing industries is expected to become more pronounced in the nearest term. Against this backdrop, inflation may accelerate temporarily. However, there is little likelihood that there will be a dramatic and ongoing rise in prices.

Inflation in Russia, just as in the EU countries, is building above expectations, peaking historical maximums. Based on the current dynamics, inflation forecast for Russia was also raised significantly. According to projections, as the existing temporal factors cease their effect and given a high base of 2020, inflation will be gradually decelerating. Based on expectations, inflation would approximate its target only by the end of the forecast period (Figure 2).

Given higher inflation forecasts for Russia and the EU, it is contemplated that an increased inflationary pressure on consumer prices in Kazakhstan on the part of trading partner countries will persist during the forecast period.

Risks from external monetary conditions also increased. The US Fed may start tightening the monetary policy far in advance than expected due to exacerbation of inflationary processes and anticipations of a feebler economic growth. Now, the market players are contemplating that the policy rate of the US Fed could be raised at least three times before mid-2022.

For many developing countries, including Kazakhstan, this bears the risks of increased volatility in the markets, capital outflow and depreciation of currencies.

Box 1. The World is Exceeding the Target

One of the most striking economic consequences of the COVID-19 pandemic was the general increase in inflationary background. In most countries, inflation has broken through historic highs. As a comparison, in the United States, inflation stood at the current level about 30 years ago, and in the European Union – more than 13 years ago.

In the environment of increased inflationary pressure, inflation had gone above the target in almost all developed and developing countries that moved to inflation targeting (Figures 1, 2). Thus, for example, among developing countries, in October 2021, inflation in Georgia accelerated to 12.8% against the target of 3%. In Brazil and Russia, with a 4% target, inflation reached 10.25% and 8.1%, respectively. Even in developed countries, where inflation had been staying below the targets for a long time, it demonstrates an over-run (Figure 2). At present, among developed countries, consumer inflation in the USA is one of the highest.

Figure 1. Dynamics of Inflation in Developing Countries (YoY)

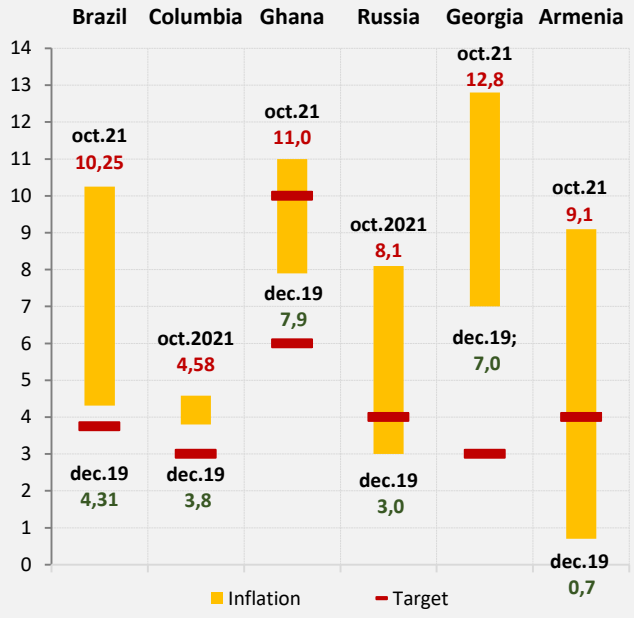
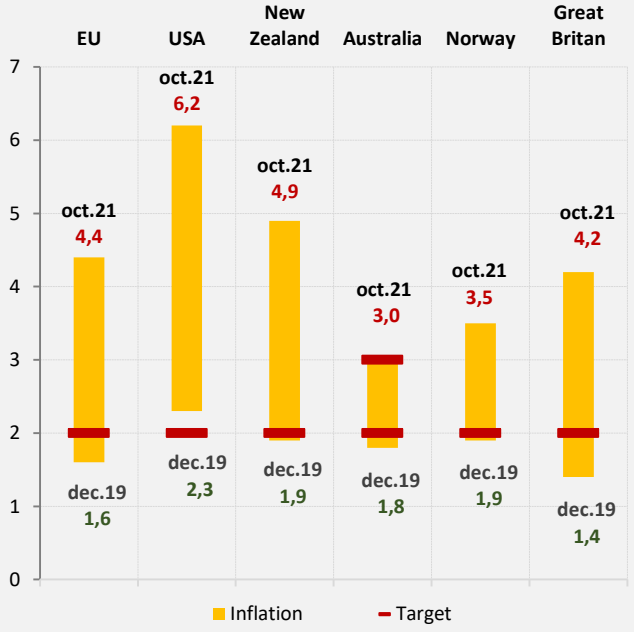


Figure 2. Dynamics of Inflation in Developed Countries (YoY)



Source: Central Banks and National Statistical Authorities

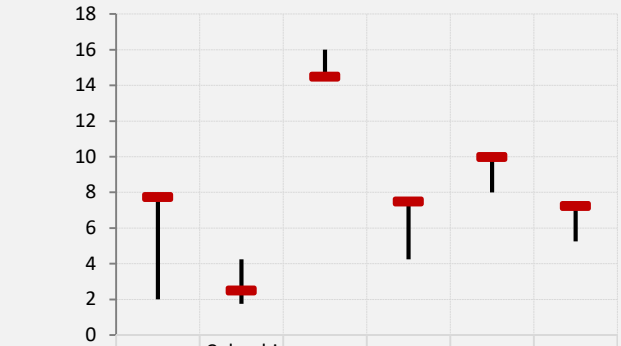
In global terms, the main source of the present spike in prices has been a rapid growth of consumer demand over supply. For this reason, as well as given the increasing problems with supplies, a shortage of materials and personnel, inflationary pressure was ratcheting up. A rise in world food and energy prices made an additional contribution to the inflation growth.

When the inflation structure is looked at in terms of countries, one may note that in the period of strict restrictive measures prices for food, alcohol beverages, utility services and healthcare services were going up in many developed countries. Prices for public catering services and transport were plummeting (an opposite picture was observed during prior crises: food prices were falling while prices for services were growing). As quarantine measures were liberating, the structure of consumer spending began to

change – transport services, car rent, clothes and public catering services started to appreciate in terms of price. Also, prices for energy resources increased given the rise in world prices. Thus, in October 2021, the US prices for this group went up by 30%, YoY (in December 2019 – a 7.3% decline, YoY).

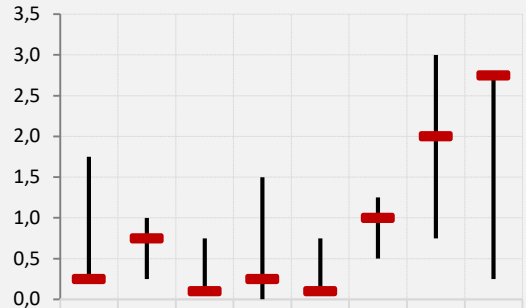
Figure 3. Dynamics of Central Bank Interest Rates in 2019-2021

Developing Countries



	Brazil	Columbia	Ghana	Russia	Georgia	Armenia
Dec.2019	2,00	4,25	16,00	6,25	9,00	5,50
Dec.2020	2,00	1,75	14,50	4,25	8,00	5,25
Oct.2021	7,75	2,50	14,50	7,50	10,00	7,25

Developed Countries



	USA	New Zealand	Australia	Norway	UK	Rep. of Korea	Iceland	Czech Rep.
Dec.2019	1,75	1,00	0,75	1,50	0,75	1,25	3,00	2,00
Dec.2020	0,25	0,25	0,10	0,00	0,10	0,50	0,75	0,25
Oct.2021	0,25	0,75	0,10	0,25	0,10	1,00	2,00	2,75

Source: Central Banks

In 2020, with an aim of supporting the economic activity, central banks of developed and developing countries reduced their policy rates (Figure 3). In 2021, the situation in developing countries was generally similar to that of developed countries; however, a rise in food prices was considerably higher. A more rapid price growth was observed among fruits and vegetables, fish and seafood as well as vegetable oils. Among non-food products, there was a significant increase in prices of clothes and among services – in transport prices.

In view of increasing inflationary pressure worldwide, central banks in developing countries started to increase their policy rates (Figure 3). Several central banks in developed countries also moved to the cycle of increased interest rates. Just to mention a few, the Republic of Korea, Norway, Iceland, the Czech Republic and New Zealand. Al in all, over 35 central banks increased their interest rate as of today.

A futher development of inflationary processes in the world is still causing uncertainty. Nonetheless, the emergence of yet another coronavirus strain and robustness of the existing inflation factors have somewhat worsened the expectations. The US Fed now anticipates that the existing high inflation will be more lentgthy than projected earlier. Hence, the curtailment of stimulative measures will probably accelerate significantly, thus creating additional risks of increased volatility for emerging markets.

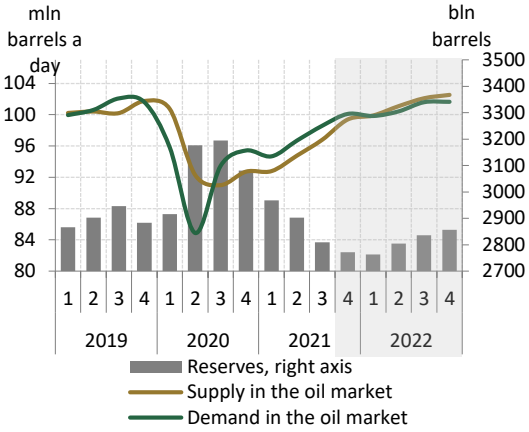
Development prospects of the global oil market remain positive. The EIA expects that the global demand for oil will remain strong, as minimum, until mid-2022. Oil supply, for its part, will be growing at a more moderate pace. The oil shortage will be prevailing in the market. Starting from the second half of 2022, the oil supply will be exceeding its demand since OPEC+ will reduce the volumes to be cut and production in the countries outside of OPEC will keep growing. The earlier oil shortage will overflow into the surplus, whereby prices will be experiencing pressure (Figure 3).

Projections of international organizations regarding the future dynamics of the demand for oil are generally in line with the prior expectations. The organizations agree that in the nearest future the oil market will turn into surplus. The main explanatory factors include recurrent coronavirus outbreaks and a feebler activity in the industrial sector. High oil prices will also retard the growth. Thus, according to estimates of international organizations, in 2021 oil consumption will amount to 96-98 million barrels a day on average. In 2022, according to expectations, the demand for oil would go up to 99-100 million barrels a day (Figure 5).

Forecasts about global oil production also have not undergone considerable changes (Figure 5). In 2021-2022, oil production among countries outside of OPEC is expected to go up in the USA, Canada, Russia, Norway, Brazil and other countries. According to IEA, the US share among other countries outside of OPEC in the expected overall growth in supply my account for about 60%. OPEC+ member countries will continue to ramp up oil production within the framework of the agreement. Given the existing quotas, oil production inx OPEC+ countries should increase by 2 million barrels a day in total by the end of 2021. By September 2022, the rate of oil production should come back to that of the end of 2018 (the basic level for calculation of restrictions). Therefore, restriction on oil production will be lifted completely.

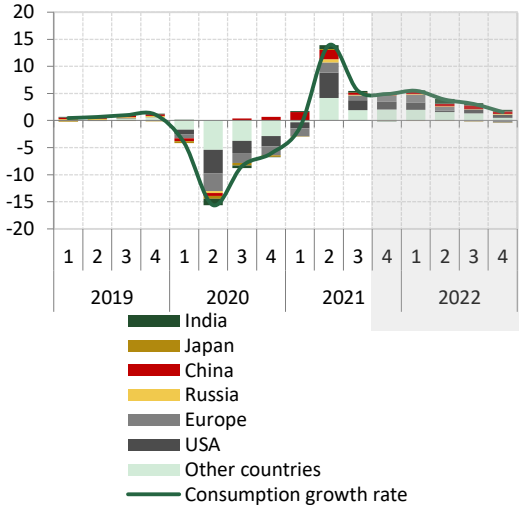
It should be mentioned that the situation in the global oil market improved significantly compared to the previous forecasting round. For the first time since 2018, oil prices exceeded 80 US dollars per barrel. This was nurtured both by a strong demand and the OPEC+ policy of gradual ramp-up in oil production.

Figure 3. Dynamics of the Global Oil Market



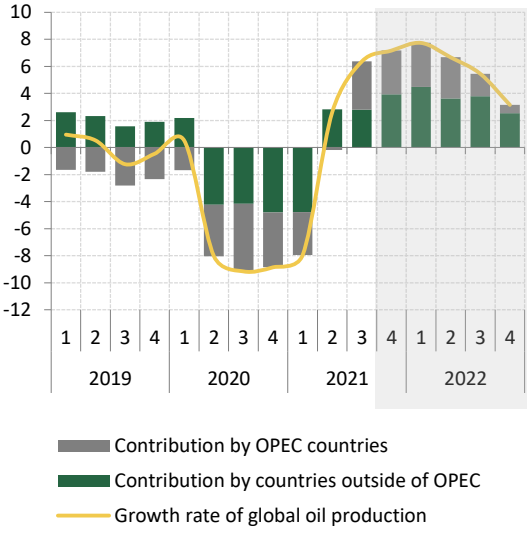
Source: EIA

Figure 4. Global Oil Consumption, YoY



Source: EIA

Figure 5. Global Oil Production, YoY, %



Source: EIA

In turn, the deteriorating epidemiological situation in some countries had not changed the risk balance for worse, and oil prices have responded to such impact at a short length.

Projections of international organizations generally remain positive, even though there is still uncertainty about the COVID-19 pendemic and many oil exporting countries anticipate an increase in production.

Given the existing situation and forecasts of international organizations, the baseline scenario of economic development for the forecast period from the fourth quarter of 2021 to the second quarter of 2023 was raised from 60 to 70 US dollars per barrel.

Under the optimistic scenario, Brent oil price is expected to be 80 US dollars per barrel throughout the entire forecast period.

Under the optimistic scenario, Brent oil price is expected to be 60 US dollars per barrel throughout the entire forecast period.

1.2. Dynamics of the Economic Development under the Baseline Scenario

The current dynamics of economic activity is forming in line with the NBK's optimistic scenario, developed within the framework of the previous forecast quarter. By the end of 2021, GDP growth is projected at a level of 3.7-4.0%.

Assumption forecasts in terms of development factors and the dynamics of GDP components have undergone minor changes, namely, changes affected the dynamics of general government consumption and the domestic demand. The changes are related to the dynamics of government consumption, which were formed below the expectations of the National Bank.

Growth rates of the domestic demand will be slightly higher owing to more rapid rates of growth in gross formation. Implementation of infrastructure projects in the manufacturing industry is under way. A contribution to the growth of investment activity will be made by a gradual mainstreaming of investments in the mining industry and also by high investment activity of the population expressed in the growing investments in residential construction.

Before the end of the year, the post-pandemic household demand is expected to realize, at the same time, the growth rates have been revised slightly downward. Slower growth rates of household consumption are associated with recurrent outbreaks of COVID-19 that exert a constraining effect on a full pledged recovery of the demand and its fast return to pre-pandemic levels. In general, the growth in household consumption will be supported by increased real income of the population due to an ongoing rise in wages in the economy. The consumer lending continues to provide an additional support to the household consumption.

In the second quarter of 2021, the dynamics of exports moved to the growth zone and the upward dynamics is expected to persist until the end of the year, which will be driven by anticipated recovery in the growth rates of oil and gas condensate production in Kazakhstan due to the easing of OPEC+ restrictions on a daily oil extraction. An expanded external demand in light of a gradual recovery of the EU economy will become an additional factor for the growth in exports.

The upturn in imports will be curbing the GDP growth because of the increasing domestic consumer and investment activity of the population and investments in key sectors of the economy.

Medium-term forecasts regarding the GDP growth were revised downward as a result of a more moderate increase in the economic activity in countries-Kazakhstan's trading partners and more negative effect on Kazakhstan's economy on the part of disruptions in global and local supply chains compared to the assessments made a quarter earlier.

Nonetheless, in 2022, the GDP growth rates are expected to accelerate to 3.9-4.2%. The economic growth will be promoted by a gradual improvement in the epidemiological situation and also by a weaker effect of COVID-19 on the economic activity as a result of adaptation of economic agents to new realities. Alongside with that, a gradual easing of restrictions as part of the OPEC+ and anticipated termination of transaction of oil producing countries will facilitate the ramp-up of production of energy resources compared to 2021. It will lead to some acceleration of exports and more active dynamics of investments. In 2022, the positive dynamics of consumer demand will be persisting due to the anticipated growth in real income of the population, in wages and the consumer lending. Growth rates of the government consumption will be modest given a slight increase in the national budget spending with the exclusion of debt service expenses.

The output gap path has been revised downward compared to the previous forecasting round. It is related to the downward revision of the forecast dynamics of the aggregate demand components and the economic activity as a whole. Nonetheless, the upward path of the output gap is supposed to persist over the forecast period given a minor acceleration in the GDP growth rates in 2022. In the medum term, the output gap will be staying aroud zero.

In comparison with the previous forecast round, short-term inflation forecasts have not undergone significant changes. By the end of 2021, inflation is expected to be in the range of 8.5-8.7%. With further effective implementation by the Government and local executive bodies of a Set of anti-inflationary response measures for 2021-2024, inflation will form close to the lower limit of the forecast range.

Some acceleration in the growth of prices for non-food products and services will be offset by a slowdown in the growth of food prices. Nevertheless, given the appreciation of fuel and lubricants in terms of price, the continuing rise in electricity fees and heightened inflationary expectations, inflation will continue to build at high levels.

A projected disinflation of a food component in the short term will be largely asscoaited with the exclusion from calculation of high monthly rise in prices in 2021 and an expected comeback of monthly growth rates to their historical values. Meantime, a persistently high growth rate of prices for some goods and a high level of world prices will be putting pro-inflationary pressure along with persistence of significant risks of acceleration of food inflation.

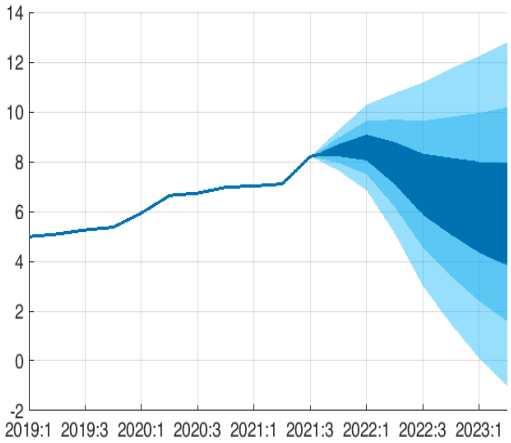
Acceleration of inflationary processes in the non-food markets will be associated with recovery of the people's consumer activity and expectations regarding a rise in import prices in the environment when supply chains are disrupted. The demand-pull pro-inflationary pressure will be associated with the growth in wages, including due to the increase in minimal wages and high rates of consumer loan disbursements.

Over a short-term horizon, a moderate growth in prices for paid services due to persistence of the existing pricing in the market of regulated utility services is anticipated. However, there are risks that electricity fees will be growing further given the expected rise in prices of coal. In addition, due to the recovering consumer demand and the growing prime cost, some increase in prices for non-regulated services is anticipated.

An additional overall pro-inflationary pressure on goods and services in the consumer basket will be put by the recovering consumer activity, high inflationary expectations as well as by the indirect effect from the rise in prices for fuel and lubricants via the increase in the prime cost of goods and services.

In 2022, the annual inflation forecasts had not undergone significant changes. Over the medium-term horizon, external inflationary background will be higher compared to previous assessments.

Figure 6. Inflation, Quarterly Average, YoY, %



Source: NBK's forecast

It is related to an upward revision of inflation in Kazakhstan's trading partner countries and higher dynamics of external food prices. On the other hand, a more modest path of the output gap will be offsetting the effect of external factors on the medium-term inflation path. Inflation is expected to decelerate given the expiry of the high base of 2021 and gradual reduction of external inflationary pressure.

According to the estimates of the National Bank, taking into account the effective implementation of a set of anti-inflationary Response Measures, inflation will slow down to 6.0-6.5% by the end of 2022 (Figure 6). At the same time, the realization of pro-inflationary risks associated with imbalances in certain markets of goods and services, disruptions of global and local supply chains and the persistence of high inflationary expectations may lead to the formation of inflation above the forecast range.

Inflationary processes will be decelerating in the environment of decreasing external inflationary pressure.

Inflation in China is anticipated to go above the target rate significantly, and price growth in the EU will be actively slowing down to the target. Inflation in Russia, however, despite its reduction, will be building slightly above the target by the end of 2022. It is worth mentioning that disinflationary effect from deceleration of inflation dynamics in trading partner countries will be less pronounced compared to the previous assessments.

In the medium term, world food prices are supposed to slightly decline after their rise in the short term. As compared to the previous forecasting round, forecasts regarding the FAO Cereal Index have been revised upward. This was related to the reduced estimates of production in a number of countries as well as to the expected growth in consumption and reduced stocks compared to the 2020-2021 agricultural season. Along with that, over a medium-term horizon, as the situation with the harvest is coming to normal and logistics problems and problems with supply disruptions are easing up, world cereal prices are expected to smoothly decline.

1.3. Alternative Forecast Scenarios

Due to the existing uncertainty associated with the recovery path of the global economy and relation between demand and supply in the global raw

commodity markets, in addition to the baseline scenario the National Bank considered alternative scenarios of oil prices.

As the pessimistic scenario, the National Bank considered the scenario, where **oil prices fall to 60 US dollars per barrel and will remain at this level until the end of the forecast horizon.**

This scenario would be realized if the global epidemiological situation deteriorates due to the emergence of new COVID-19 strains, the world economy would be recovering slowly and enduring imbalances in the oil market appeared.

If the situations evolves under te pessimistic scenario, the recovery path of Kazakhstani exports will be more moderate due to feeble dynamics of external demand for primary products from Kazakhstan. Negative dynamics of revenues of enteprises operating in the mining sector compared to the baseline scenario will result in curtailment of production and investments thus negatively affecting such sectors as construction, transport, trade and other services. The weaker dynamics of people's income and investments would somewhat limit the growth of consumer and investment demand. Therefore, the recovery of Kazakhstan's economy in 2021-2022 will be more modest compared to the baseline scenario**. In 2022, the economic growth will account for 3.6-3.9%.**

Throughout the forecast period, inflation will continue to build above the target band. Despite the disinflationary pressure from the domestic demand, the high dynamics of inflationary processes compared to the baseline scenario will be driven by the weaker real exchange rate of the tenge, possible disruption in the supply of import products and the corresponding rise in inflationary expectations.

If the **optimistic scenario** is realized, the path of oil prices is assumed to be at **80 US dollars per barrel over the forecast horizon.** Such price path, despite the planned increase in oil production by OPEC+, will be due to the confident recovery of the global economy and the growing demand for oil. High prices of hydrocarbons and strong external demand from trading partner countries will lead to higher growth rates of Kazakhstan's economy than under the baseline scenario. **In 2022, the GDP growth will account for 4.1-4.4%.**

If the situation develops in line with the optimistic scenario, inflation will be slowing down faster compared to the baseline scenario. This will be ensured by the stronger dynamics of the tenge exchange rate and lower external inflationary pressure, mainly due to a low inflation path in Russia. During the forecast horizon, inflation will be building near the upper boundary of the target band.

1.4. Risks in the Medium Term

As compared to the previous forecasting round, the risk profile is generally unchanged, while risks of inflation deviation from the baseline scenario remain high.

The persisting or strengthened restrictive measures in the world due to the spread of new COVID-19 strains (for example, omicron) can lead to a slowdown in the global economy and disruptions in the supply of final and intermediate products. Internal factors include the risks of limited supply, growth in production costs and increased demand. The above factors can cause a significant acceleration of inflation in Kazakhstan (Figure 7).

Recovery of the global economy and the effective OPEC+ agreement on cutting oil production determine the prices for Brent crude oil in the range of 70-80 US dollars per barrel. In this regard, the risk of a sharp drop in oil prices to the levels of the beginning of the pandemic remains low.

Nonetheless, this risk is likely to materialize if restrictive measures are introduced due to an increase in the incidence of new COVID-19 strains and the decreased global demand, as well as increased oil supply by OPEC + countries.

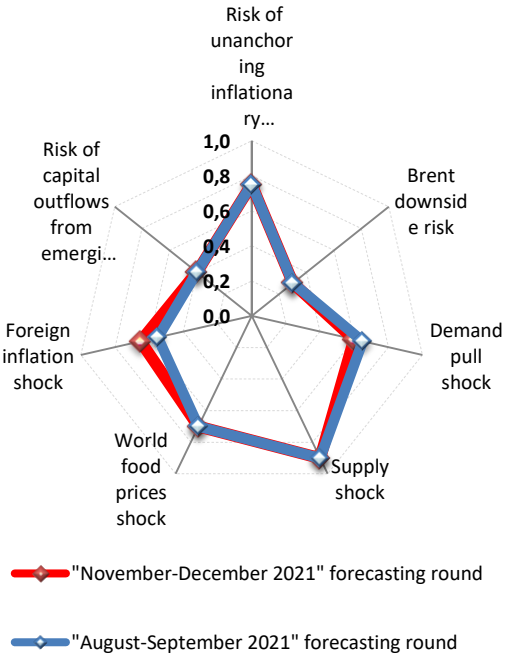
Compared to the previous forecasting round, the risk of importing external inflation from the countries – Kazakhstan's trading partners, increased. Rising energy prices, disruption of supply chains lead to significant inflationary pressures in the world. Despite the fact that these processes are expected to be temporary, the risk that they will continue and may result in inflation boost looks high. In addition, a high growth in real estate prices worldwide, coupled with the recovering demand for services, may be the cause for high inflationary expectations and the further unwinding of the inflationary spiral. The realization of these risks will trigger a rise in prices of imported goods in Kazakhstan, contributing to the general increase in prices.

The risk of importing external food inflation remains significant due to the strong growth in world prices for a wide range of food products (cereals, vegetable oils, meat). A possible decrease in crop output, problems with the labor force because of restrictions on its mobility, hightened demand due to an ambition of many countries to ensure food security, can cause the persistence or intensification of imbalances in the food markets and subsequently lead to increased prices for food in Kazakhstan.

The risk of capital outflow from emerging markets to developed countries remains high. The tightening of monetary policies in developed countries as a consequence of heightened inflationary pressure may result in increased volatility in the global financial markets. This factor can lead to depreciation of currencies in developing countries, including in Kazakhstan.

Among internal factors, the risk of demand-pull inflationary pressure somewhat decreased given that a lower path of the economic recovery of Kazakhstan is anticipated. However, as a result of a more intensive growth of the people's income and consumer lending, this risk remins high. The risk of acceleration of inflation pushed by supply factors is still high due to a low wheat crop in Kazakhstan, a possible growth in the cost of production given rising prices for fuel and lubricants and energy prices.

Figure 7. Risk Map Based on the Expert Judgment



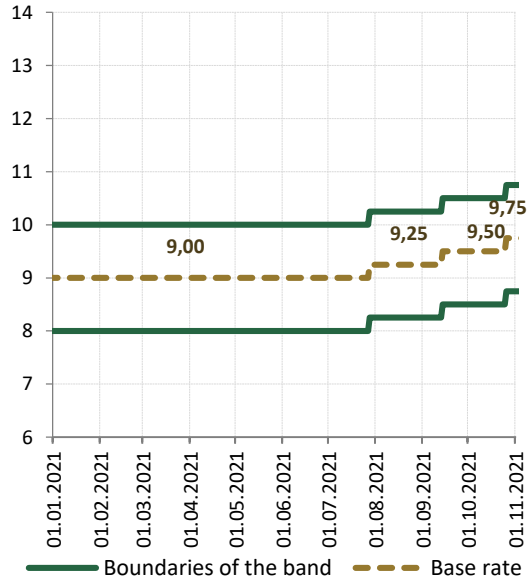
Source: NBK's calculations

Finally, the risk of unanchoring inflationary expectations continues to materialize and will persist in the medium-term in the environment of high food inflation and hike in prices for non-food products and services.

II. MONETARY POLICY

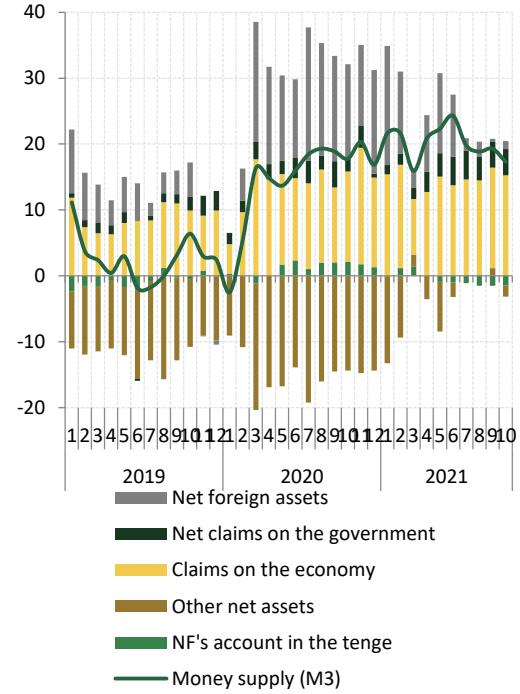


Figure 8. Base Rate Band in 2021, %



Source: NBK

Figure 9. Money Supply, YoY, %



Source: NBK

2.1. Decisions on the Base Rate

From September to December 2021, the National Bank made three decisions on the base rate.

The decision to raise the base rate to 9.5% made on September 13, 2021, was predicated by prevailing inflationary pressure in the economy against acceleration in world food prices and prices of raw commodities, along with the outrunning recovery of global demand over output potential. An additional effect on the price growth was exetrted by internal inter-seasonal shocks, by actively recovering consumer demand and also a rise in prices of electricity, gas and fuel and lubricants.

In September and October 2021, inflation made up 8.9% in annual terms. The National Bank continued to pursue a disinflationary monetary policy with a view to slow down the price growth and to fit inflation into the target band of 4-6% by the end of 2022.

On October 25, 2021, the National Bank made the decision to increase the base rate to 9.75% (Figure 8). Such decision was motivated by persisting inflationary pressure that resulted in inflation rate above the National Bank's forecasts, by rising prices in the global commodity markets, acceleration of inflation in trading partner countries and high inflation expectations.

On December 6, 2021, the National Bank made the decision to set the base rate at 9.75% per annum. The decision on the base rate was made based on the progressing inflationary processes in the economy.

2.2. Money Supply and Money Market

The growth rate of money supply is slowing down but remains high due to the increase mainly in retail lending.

The money multiplier has been stable. Despite its slowdown in October 2021, money supply remains in the two-digit growth zone (Figure 9). Annual increase in the money supply in October accounted for 17.3%, which is comparable with the growth rates in the same period of the last year (17.8%).

The main factor causing the growth in money supply is still the increasing retail lending and growing claims on the Government from the banking sector, primarily because of the volumes of government securities in the banking system portfolio. In October 2021, foreign assets made a minor positive contribution to the money supply dynamics due to the rising price of gold amid investor concerns about escalation of inflation worldwide.

The reserve money slowed down its rates of expansion in annual terms in connection with a gradual release of the high base of 2020 (Figure 10).

The money multiplier (the ratio of money supply and reserve money) since the beginning of this year has been stable due to a comparable growth in the reserve money and in the money supply (Figure 10).

The money market rates are setting between the base rate and the lower boundary of the target band except for the periods when the demand for liquidity heightens. The exposure on the NBK's operations decreased in november. From September 15, 2021, the KASE started to calculate and publish new indicators – TONIA Compounded Index and TONIA Compounded Rate.

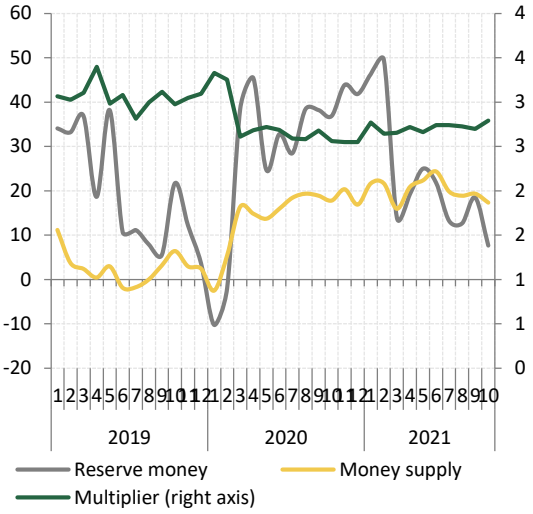
The money market continues to function in the environment of liquidity surplus. At the same time, by the end of November 2021, the balance on operations of the NBK decreased to 3.9 trillion tenge amid of a reduction in the volume of notes and deposit auctions (Figure 11).

Liquidity is mainly withdrawn via the open market operations where the share of deposit auctions is increasing and the share of notes is decreasing, including due to limitation of the 6-month note issuance and termination of one year notes issuance (Figure 12).

The National Bank was providing liquidity via reverse repo operations, and their share decreased in September-November 2021 compared to the summer period.

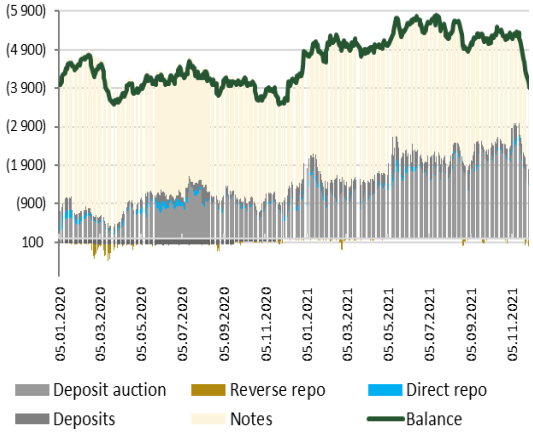
The money market rates went up following the base rate increase in September and October, setting mainly between the lower boundary of the interest rate band and the base rate. During tax periods, given a high demand for the tenge liquidity, TONIA was reaching the upper boundary of the band (Figure 13).

Figure 10. Growth of Monetary Aggregates, YoY, %



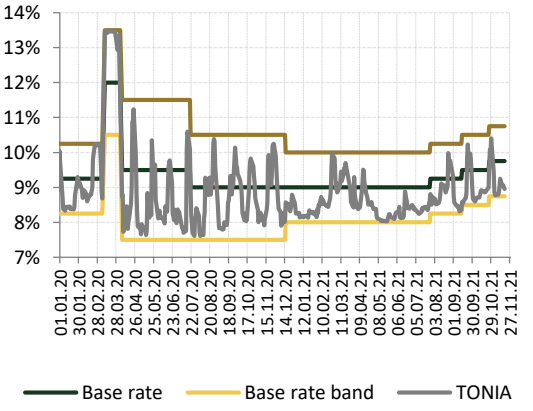
Source: NBK

Figure 11. Exposure on the National Bank's Operations, billion tenge



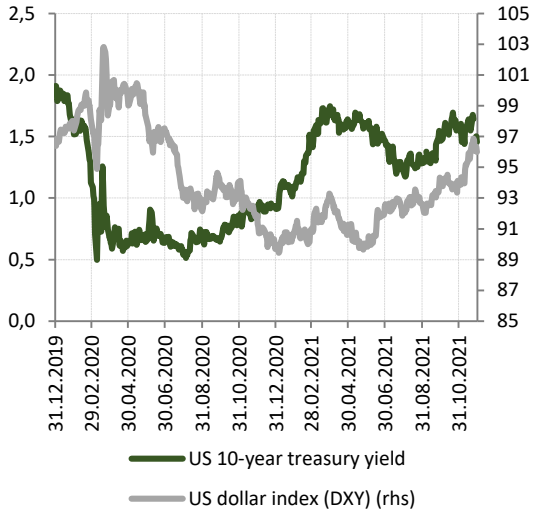
Source: NBK, KASE

Figure 12. Interest Rate Band and TONIA



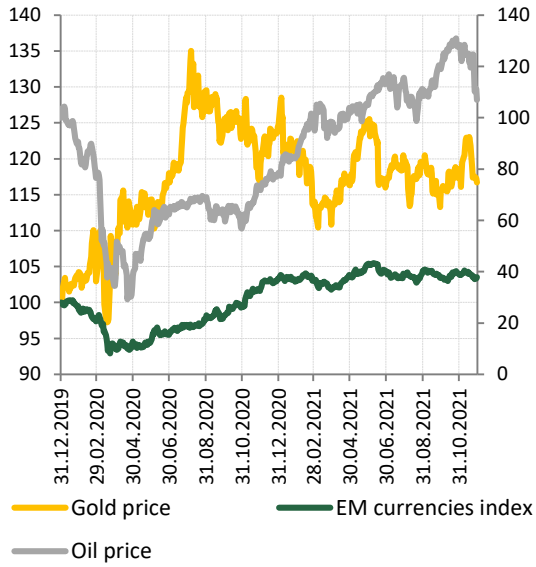
Source: NBK, KASE

Figure 13. Yield on the 10-year US Government Securities, USD Index



Source: Refinitiv

Figure 14. Dynamics of the Emerging Market Currency Index, and of the Cost of Gold (31.12.2019=100) and Oil



Source: Refinitiv

In September of this year, KASE started to calculate and publish new money market indicators – TONIA Compounded Index and TONIA Compounded Rate, which serve as a benchmark in the pricing of financial products and provide an opportunity to diversify the product lines for the financial market players.

2.3. Foreign Exchange Market

The exchange rate of the tenge continues to be formed under the impact of external and internal conditions. Expectations about the tightening of the Fed's monetary policy was conductive to a global appreciation of the US dollar and to the growth in yield on treasury bonds. The upturn of oil quotes in September-October was followed by their reduction by end-November due to the expectation of surplus in the market. Decline in oil prices and appreciation of the US dollar coupled with the growing demand for foreign exchange in the domestic market intensified pressure on the exchange rate of the tenge.

The anticipation that the Fed would tighten its monetary policy led to the growing yields on treasury bonds and a lower risk appetite among investors, resulting in appreciation of the US dollar (Figure 13). Negative sentiment in the global markets at the end of September had intensified due to potential systemic risks because of financial problems of a large Chinese construction company Evergrande Group. During September-November of this year, prices of gold were demonstrating high volatility associated with uncertainty in the markets (Figure 14).

In October, the price of oil was demonstrating its maximums since October 2018, having reached 86.7 US dollars on October 25 of this year, resulting from the growing demand against a limited supply. The increase in demand was driven by a sharp shortage of gas and coal in Europe and Asia on the threshold of the heating season and the increase in international flights. Along with that, from November of this year, oil quotes were decreasing due to projections about an excessive supply in the market of energy carriers and concerns regarding a coordinated use of strategic reserves of oil by certain countries next to the USA (the UK, China, India, Republic of Korea, Japan).

In general, in September-November, Brent oil quotes were moving within the range of 71-86 US dollars per barrel (Figure 14).

Despite a lower risk appetite of foreign investors, the share of non-resident investments into government securities of Kazakhstan continued to grow. Foreign investments into government securities of Kazakhstan at end-October went up to 863 billion tenge (794 billion tenge at end-August).

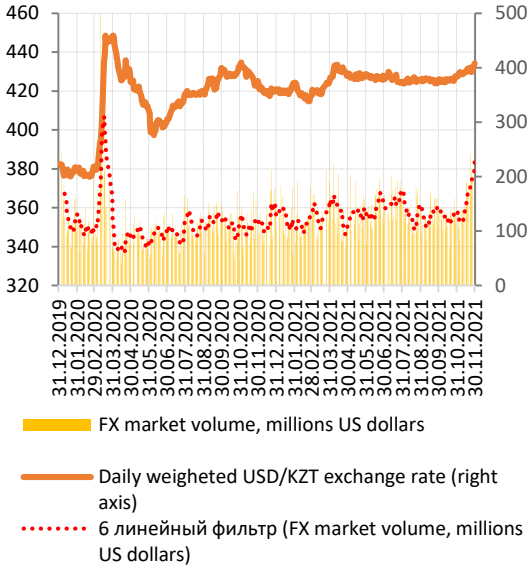
Among internal factors, a high demand for foreign exchange driven by the recovery of economic activity and the growing imports of consumer goods continued to put considerable pressure on the exchanhge rate of the tenge.

In response to a heightened demand, the tenge was supported by operations on conversion of the National Fund's resources to make transfers to the budget and sell export proceeds by entities from the quasi-government sector.

In September-November, being influenced by external and internal conditions, the exchange rate of the tenge was moving within the range of 423,92-434,20 tenge, having depreciated by 2.1% over the period from 425.42 to 434.20 tenge per US dollar (Figure 15).

At the end of November, in order to prevent destabilizing fluctuations of the tenge in the face of a sharp deterioration in external conditions, the National Bank conducted currency interventions in the amount of $ 239 million.

Figure 15. Dynamics of the Exchange Rate of the Tenge and the Trading Volume



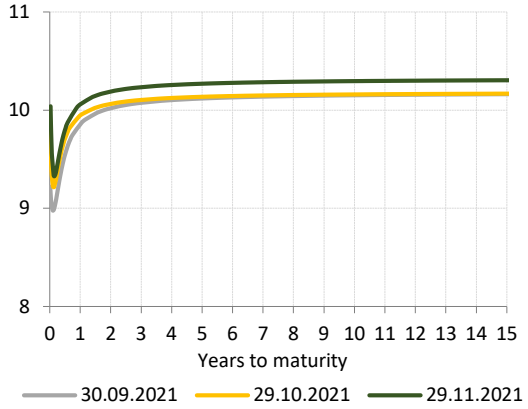
Source: KASE, NBK

2.4. Stock Market

The volume of securities trading in the primary market in September-November of this year went up versus June-August of this year. Given the increase in the base rate, the risk-free yield curve was demonstrating growth over a short-term section. The corporate bond index also increased.

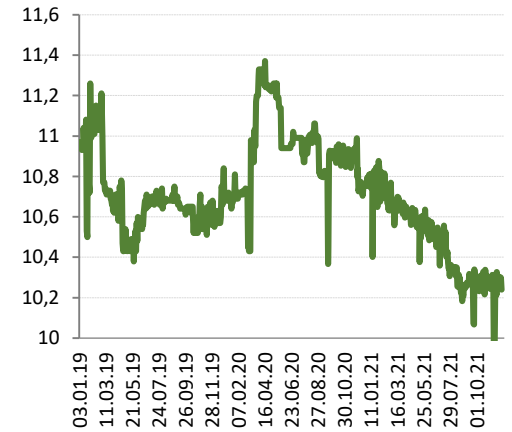
Given the planned issuance of government securities in accordance with the Schedule of the MoF RK for 2021 and borrowing of resources by akimats (local administrations) as part of implementation of the "Employment Road Map for 2020–2021", the volume of securities trading in the primary market in September-November went up to 950.4 billion tenge or by 1.5 times compared to June-August 2021.

Figure 16. Change in the Risk-Free Yield Curve, %



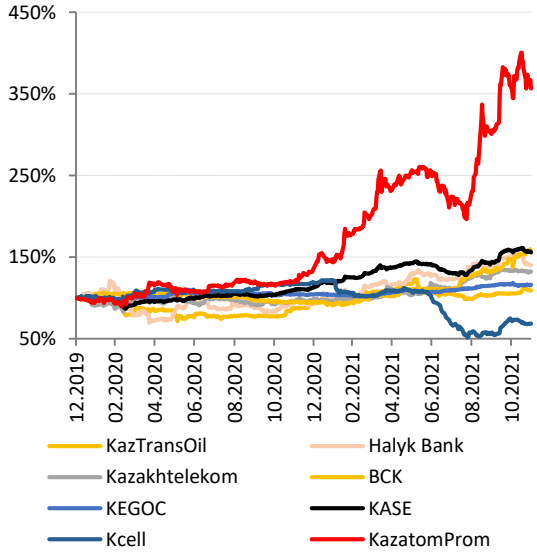
Source: NBK

Figure 17. Yield on Corporate Bonds, %



Source: KASE

Figure 18. KASE Index (Dec.2019=100)



Source: KASE

The MoF RK continued to issue its short-term securities with maturity from 1 to 3 years and yield from 10.16% to 10.48% per annum. Mainly medium-term and long-term government securities were issued with the yield from 10.43% to 10.87% per annum. In order to finance the housing construction and as part of implementation of the "Employment Road Map for 2020–2021" government program, local executive authorities borrowed 165.8 billion tenge during the period from September to November.

The risk-free yield curve at the end of November this year increased throughout the entire segment after previous decisions to raise the base rate (Figure 16).

The volume of placements in the primary market of corporate bonds in September-November amounted to 369.6 billion tenge. The quasi-government sector, the Kazakhstan Sustainability Fund and banks retain their leading positions in terms of placement volumes. The tendency to issue medium- and long-term obligations is persisting among issuers.

The weighted average market rate on placed corporate bonds (excluding those bonds that were placed at a rate below the base rate level) accounted for 12.13% in November (in August – 11.14%). The performance index on corporate bonds at end-November was 10.92% per annum, which is by 0.7 pp higher than at the end of this August (Figure 17).

The KASE Index growth in September-November accounted for 16.1%, having reached the historical maximum on November 18, 2021 – 3 810.7 points (Figure 19). In the reporting period, the leading positions in the KASE index structure belonged to "Kazatomprom" NJSC – 54.8%, "Bank CenterCredit" JSC – 22.6%, "Kcell" JSC – 19.4%.

During the period from August to October of this year, the volume of trades in the equity market amounted to 109.2 billion tenge. The record high volume of trades was observed in September, in connection with a sale of 24% of stock of mobile operator "KCell" JSC by "Kazakhtelecom" JSC to the investor community at open bid.

2.5. Deposit Market

The growth rates of deposits in the banking system continued to slow down. The main contribution to the increase was made by retail and corporate deposits in the tenge.

Overall deposit dollarization at the end of this October keeps decreasing due to a significant reduction in the percentage of foreign currency deposits of the population.

In November 2021, cap rates of the "Kazakhstan Deposit Insurance Fund" JSC increased.

The growth rates of deposit portfolio slowed down to 18.6% YoY in October 2021 (from their peak in July of this year – 26.5%). Deposits in the domestic currency continue to make the main contribution to the deposit base growth whereas the growth rates of foreign currency deposits keep decreasing (Figure 19).

Deposits in the tenge went up by 29.1% in annual terms. Such increase in deposits was driven mainly by the growth in retail deposits (individuals – by 35%, corporate entities – by 23.8%).

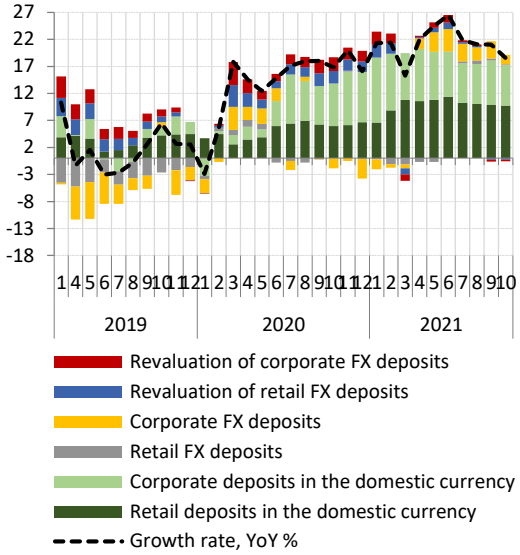
During the reporting period, the upturn of deposits in the national currency has returned to normal as the effect of a partial use of pension savings for improving living conditions weakened.

Foreign currency deposits grew by 3.3% in annual terms due to the increase in the corporate sector deposits (6.6%) against a 0.3% reduction in retail deposits in annual terms.

Overall deposit dollarization decreased to 35.6% in October 2021 from 37%, where it was staying in the second quarter of this year (Figure 20). Dollarization of the corporate sector, despite stabilization compared to peaks in the middle of the year, remains high because of volatility in external markets versus the beginning of the year, accounting for 37.2% at the end of October 2021 (Figure 12). Dollarization of retail deposits has declined since the beginning of the year by 5.1 pp and accounted for 33.9% (it is the minimum since October 2008).

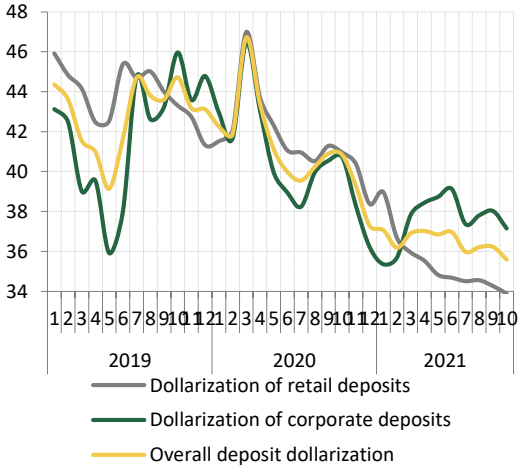
Deposits with maturity of up to 1 month making up 84% (in October 2021) of all corporate time deposits account for the main share in attracted corporate sector deposits. Interest rates on these types of deposits as the most sensitive to the change in monetary conditions

Figure 19. Contribution by Components to the Growth in Deposit Volume, YoY, %



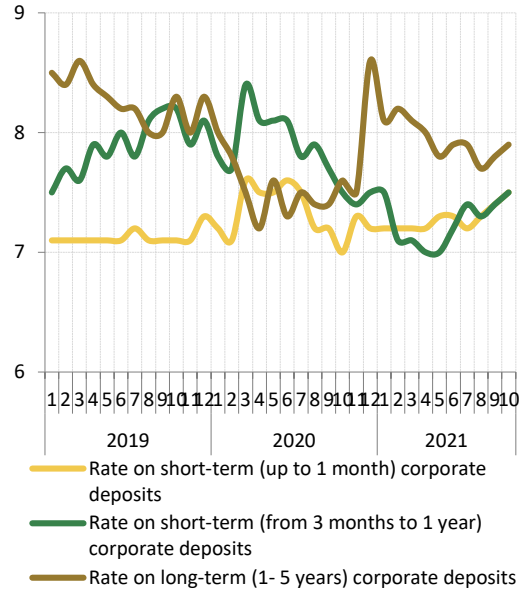
Source: NBK

Figure 20. Deposit Dollarization, %



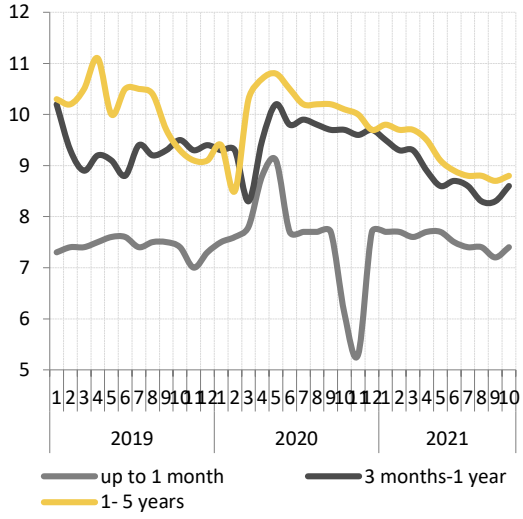
Source: NBK

Figure 21. Interest Rates on Corporate Deposits in the Tenge, %



Source: NBK

Figure 22. Interest Rates on Retail Deposits, %



Source: NBK

were increasing subsequent to the base rate to 7.5% in October compared to 7.2% in July 2021 (7.0% in October 2020). Corporate deposits with maturity from 3 months to 1 year (with the share of 12.2% of time deposits) also increased from 7.4% to 7.5% in October 2021 (7.5% in October 2020). Interest rates on long-term deposits with maturity of 1-5 years (with the share of 2% of time deposits) remained at the level of July, accounting for 7.9% in October 2021 (7.6% in October 2020) (Figure 21).

In the retail sector, where longer deposits compared to the corporate sector are prevailing (the share of deposits with maturity from 3 months to one year is 43.3%, and with maturity from one year to five years – 43.8% in October), interest rates were also growing along with a significant growth of the retail deposits portfolio in the tenge. Interest rates on deposits from 3 months to one year grew from 8.3% in July to 8.6% in October 2021 (9.7% in October 2020), and on deposits with maturity from 1 to 5 years – remained at 8.8% (10.1%). Short-term deposits of up to 1 month (with the share of 7.0%) remained unchanged at 7.4% (6.1%) (Figure 22).

After the NBK's base rate was increased from July 2021, the "Kazakhstan Deposit Insurance Fund" JSC raised interest rates on short-term retail deposits. Interest rates on demand deposits were increased in November 2021.

In general, deposits remain as the most attractive investment instrument for the population. According to the joint survey conducted by the KDIF and banks, about 92% of respondents from 128 localities of the country choose deposits as the main instrument of investment.

2.6. Credit Market

Credits to the economy continue to grow, mainly owing to retail loans in the tenge. Consumer loans made the main contribution to the increase in loans to the population. The costs of credits to the real sector is growing after the increase of the base rate.

In October of this year, the credit portfolio of banks increased by 19.1% in annual terms, amounting to 17.2 trillion tenge.

The main factor for the loan portfolio growth is the lending to the retail sector in the tenge.

Loans to corporate sector in the national currency also retained their positive contribution to the growth in bank loans (Figure 23).

The ramp-up of consumer loans remains as the driver for the retail loan portfolio. Loans provided to the population for consumer purposes have gone up due to the growing household consumption. In October of this year, mortgage loans grew by 39.5% in annual terms owing to the implemented government housing and mortgage programs (Figure 24).

The cost of consumer loans decreased to 19.2% from 19.9% in July 2021 (20.4% in October 2020) given significant volumes of consumer loans. The expansion in the share of market-based mortgage programs on the part of the second-tier banks led to the rise of the weighted average interest rate on mortgage loans from 8.1% to 8.4% (7.9% in October 2020).

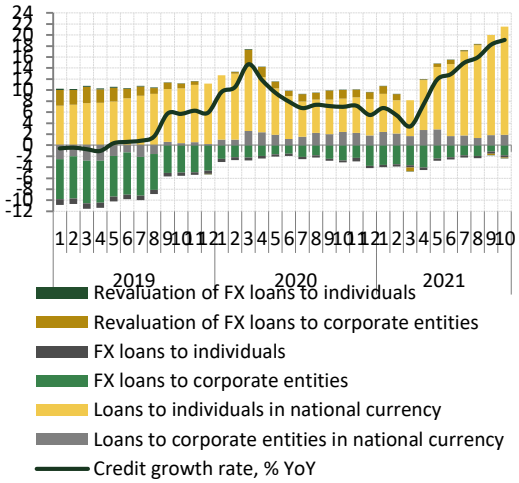
Since the beginning of this year, the volume of new loans provided to the corporate sector entities went up by 16.3% or 1 210.9 billion tenge compared to the same period of the previous year.

However, in view of the comparable volume of repaid loans, since the beginning of this year the loan portfolio has grown far less and accounted for 2.4% only. A positive contribution was made by such sectors as the industry, agriculture, trade and communication. Loans to small business entities have gone up by 29.5% to 3.3 trillion tenge since the beginning of this year.

According to the bank survey on lending for the third quarter of 2021, the demand for loans has grown owing to small business entities and the demand on the part of large businesses has decreased. As for the population, their demand for mortgage loans and car loans decreased against the increasing demand for consumer loans.

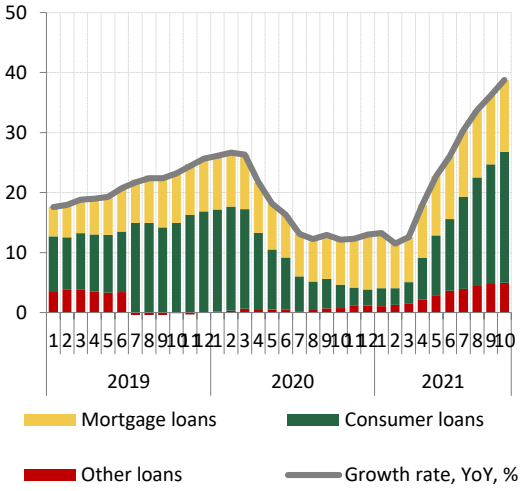
The weighted average interest rate on loans to businesses in the tenge in the short-term segment increased from 11.3% in July to 11.6% in October 2021 (11.6% in October 2020). The cost of long-term loans grew from 13.1% to 13.3% (12.3% in October 2020) (Figure 25).

Figure 23. Credits to the Economy, YoY, %



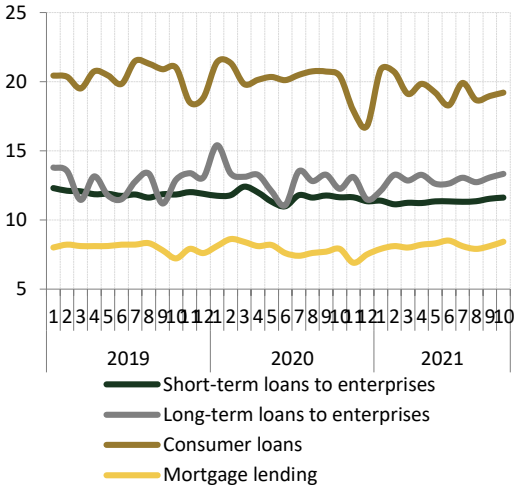
Source: NBK

Figure 24. Contribution by Components to the Annual Growth of Retail Sector Loans, YoY, %



Source: NBK

Figure 25. Rates on Loans in the National Currency, %



Source: NBK



III. MACROECONOMIC CONDITIONS

III. MACROECONOMIC CONDITIONS

3.1. External Sector

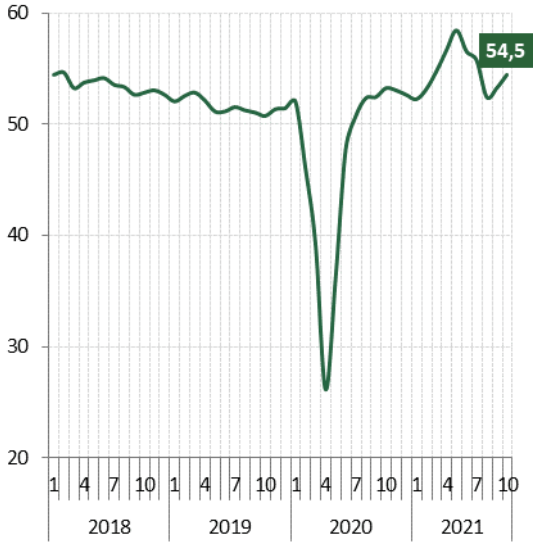
The business activity in the world, despite recurrent coronavirus outbreaks, continues to recover (Figure 26). The Global Composite PMI in October 2021 grew to 54.5 points (in September 2021– 53.3 points). As surveys show, the industry is growing at a slower pace than services. According to producing companies, the industrial production is retarded, as before, by disruptions in supply chains, a hasty growth in energy prices as well as a shortage of materials and labor force.

Imbalance between the demand and supply observed in the market, problems with global supply chains and also a shortage of materials intensify the global inflationary background.

In many developed and developing countries, the consumer inflation is hitting a record high. Thus, inflation in the USA has grown by 6.2% (YoY) for the first time since 1991. In the EU, a spike in prices became the maximum for the last 13 years and in October 2021 made up 4.1% (YoY). Among largest European economies, the highest rise in prices is observed in Spain, Germany, and France. In the structure of inflation, energy carriers and food products demonstrate the highest growth. Among non-food products, new and used cars show a surge in prices that is driven by a shortage of microcircuit chips and disruption in supply chains.

In the global oil market, in spite of the efforts made by the USA and other countries to expand the supply, Brent oil prices are above 80 US dollars per barrel (Figure 27)

Figure 26. Global Composite PMI[1]



Source: Bloomberg

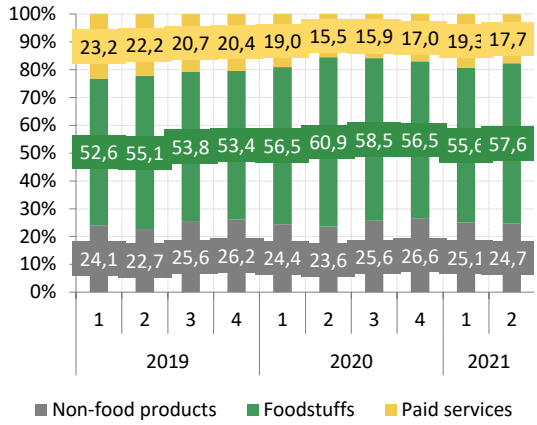
Figure 27. Brent Oil Price, US dollars (monthly average)



Source: U.S. Energy Information Administration (EIA)

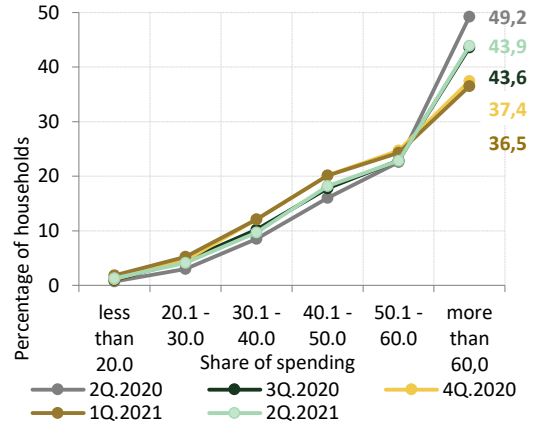
[1] – *an index value of more than 50 means an increase in the indicator, less than 50 means a decrease, and equal to 50 means its invariance*

Figure 28. Structure of Nominal Consumer Spending of Households



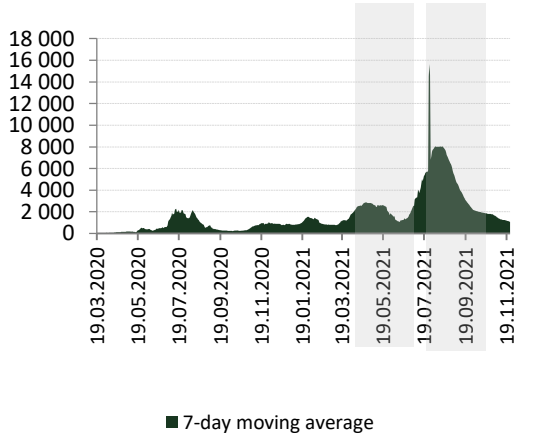
Source: BNS ASPR

Figure 29. Percentage of Household Spending on Food in the Consumer Spending, as %



Source: BNS ASPR

Figure 30. New COVID-19 Cases in Kazakhstan



Source: ourworldindata.org, NBK's calculations

3.2 Development of the Domestic Economy

The consumer demand continues to recover, however, consumer activity has not yet returned to the pre-crisis levels and the dynamics of household demand in the second quarter of 2021 demonstrated moderate growth rates.

A modest growth in the consumer demand is partly associated with unstable epidemiological situation in the country that somehow limits complete recovery of household spending. Thus, at end-March – beginning of April of this year recurrent COVID-19 outbreaks were observed and there were new daily incidences of the infection (Figure 30).

Along with a rise in food prices in the second quarter of 2021, consumer preferences of the populations shifted again. So, within the total spending on consumption, the share of nominal expenditures of the population for food increased, spending on paid services decreased and the share of spending on non-food products slightly reduced (Figure 28). Such tendency is also traced in the increased number of households that use most of their consumer expenditures for food (Figure 29). The share of such households reached the level of the thrird quarter of 2020 when realization of the demand for non-food products and services was limited by the quarantine measures. The present increase in the people's spending on foodstuffs is most likely associated with accelereation of the food inflation.

By the third quarter, the dynamics of retail sales, after their peak in the second quarter of 2021, started to slow down. A sizable growth in the second quarter of 2021 resulted from both the reviving consumer activity of the population and from a low base of the second quarter of 2020, when the turnover contracted by 36.8%. In the third quarter, the turnover demonstrated moderate growth rates. Realization of retail sales was in a certain way limited by a recurring deterioration in the epidemiological situation in mid-July and at the beginning of September when there were on average over 6000 new coronavirus cases in the country every day (Figure 30).

Retail sales of foodstuffs are starting to grow due to the increasing production and imports of food (Figure 31).

The dynamics of turnover of non-food products also shows moderate growth rates that are supported by the increased non-food imports (a 10.6% growth, YoY) and accelerated growth rates of consumer loan disbursements (a 2.1 times growth, YoY).

The positive dynamics of the people's income in Kazakhstan continues to support the growth in consumption of the population. In the structure, income from hired labor, from student scholarships is increasing and income from self-employment demonstrates considerable recovery. Real income of the population from retirement benefits and allowances is decreasing and thereby is making a negative contribution to the buildup in earnings thus worsening the financial standing of the social groups outside the labor force. One of the factors of reduced income from allowances is the statistical base effect associated with the increased payouts in 2020 in connection with the lockdown.

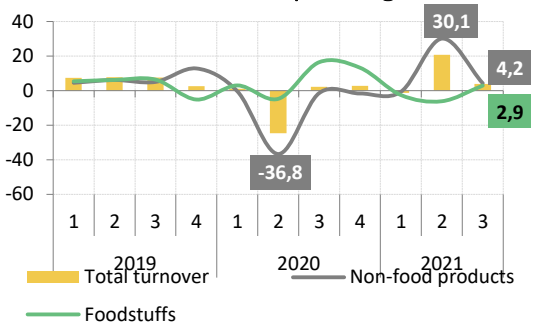
Reduction in income of this group of population was accompanied by the increased poverty rate of the people in Kazakhstan.

In the third quarter of 2021, income retained its positive dynamics and real per capita income of the population increased by 5.8% (Figure 32).

Income of employees keep demonstrating the positive dynamics. In the third quarter, real wages increased by 9.8%. High growth rates of salaries in the public sector (public administration and defense, healthcare and education) are persisting and real wages in the real sector recovered significantly (Figure 32).

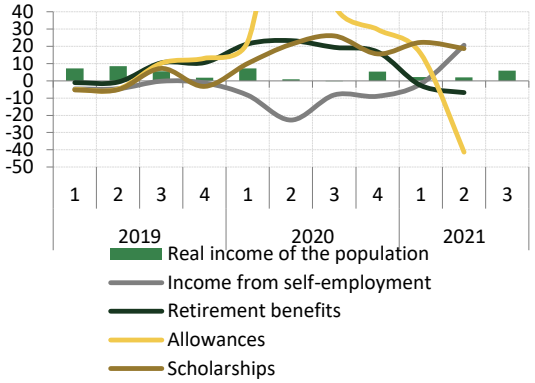
In the environment of increasing fiscal incentives in Kazakhstan's economy over the last three years growth rates of wages in the public sector are outrunning those in the real sector (Figure 33).

Figure 31. Percentage of Household Spending on Food in the Consumer Spending, YoY, %



Source: BNS ASPR, NBK's calculations

Figure 32. Dynamics of Real Income of the Population and its Components, YoY, %



Source: BNS ASPR, NBK's calculations

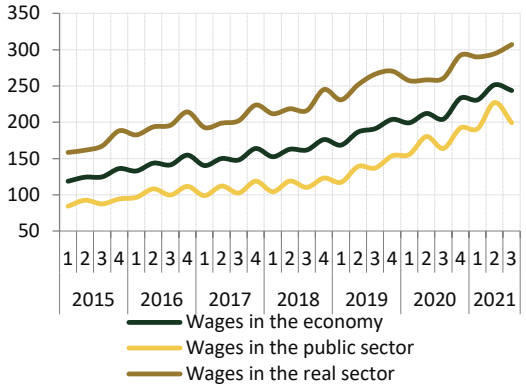
Figure 33. Dynamics of Real Wages in the Real and Public Sectors[2], YoY, %



Source: BNS ASPR, NBK's calculations

[2] Real wages in the real and public sectors are calculated by weighing the growth rates of wages based on the share of a sector in the total payroll fund

Figure 34. Average Monthly Wage, tenge



Source: BNS ASPR, NBK's calculations

This being said, an average wage rate in the public sector is still below the average wages in the real sector of the economy (Figure 34).

Box 2. Has the Real Sector Recovered?

Figure 1. Size of Enterprises by Economic Sectors

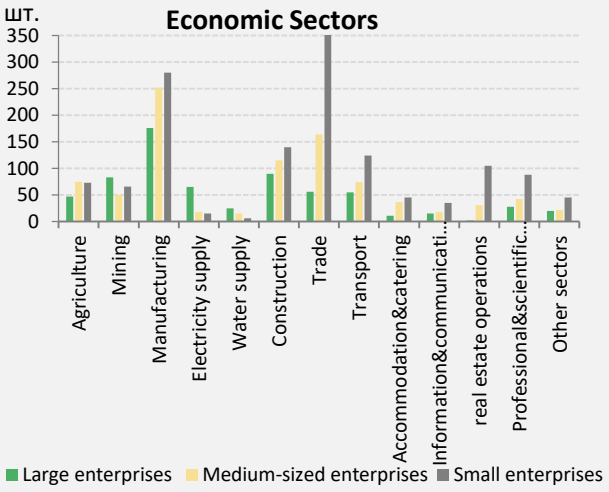
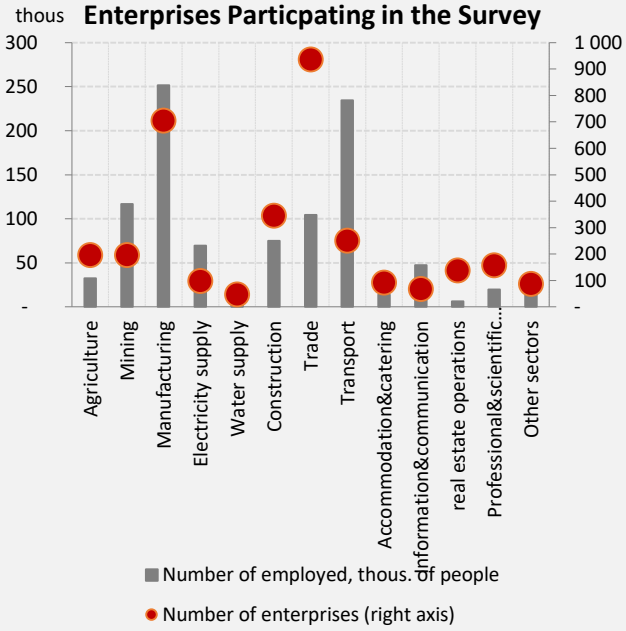


Figure 2. Quantitative Indicators of Enterprises Particpating in the Survey



mining industry, a negative effect was caused

The National Bank, as part of monitoring of the real sector enterprises, conducted a one-time survey among participating enterprises in order to assess the effect of pandemic on their operations. Thus, 3 327 enterprises took part in the survey, including 673 large enterprises, 913 medium-sized enterprises and 1741 small enterprises (Figure 1). In the industry-based breakdown, the maximum number of enterprises was presented in the wholesale and retail trade – 935, and the minimum number – in the water supply industry – 46 enterprises. They represent a number of economic sectors with a total number of workers from 6.4 thousand (real estate operations) to 251.6 thous. individuals (the manufacturing industry) (Figure 2).

The survey results showed that the COVID-19 pandemic and measures taken to prevent its spreading have negatively affected operations of these enterprises in general. This was stated by 66.1% of interviewed enterprises, of which 12.9% suffered the most. At the same time, 32.0% of enterprises noted that the pandemic did not exert any effect on their operations. In terms of sectors, the mostly affected enterprises were those from the sector of trade, the mining industry, construction and accommodation and catering services where the percentage of negative responses accounted for 69%, 69%, 77% and 82%, respectively (affected negatively). In the sectors of accommodation and catering services and trade negative effect was caused by imposition of quarantine restrictions in respect of public catering companies and restaurant business, hotels, and shut down of shopping malls. In the

Figure 3. Question 1 "Did the COVID-19 pandemic and restrictions affect the enterprise's operations?"

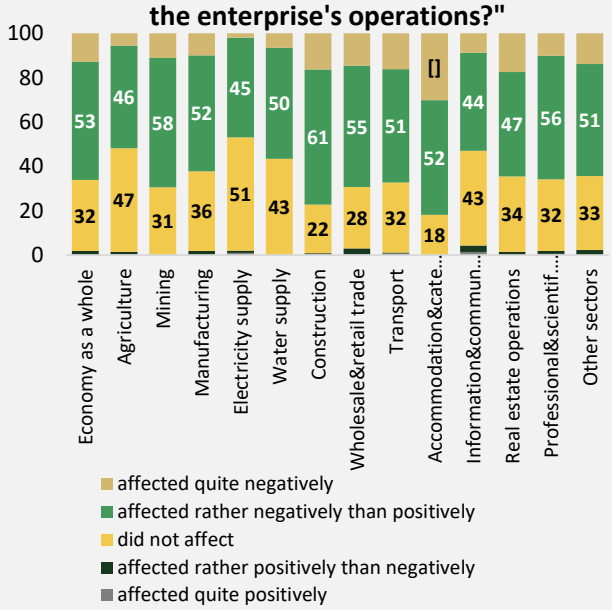
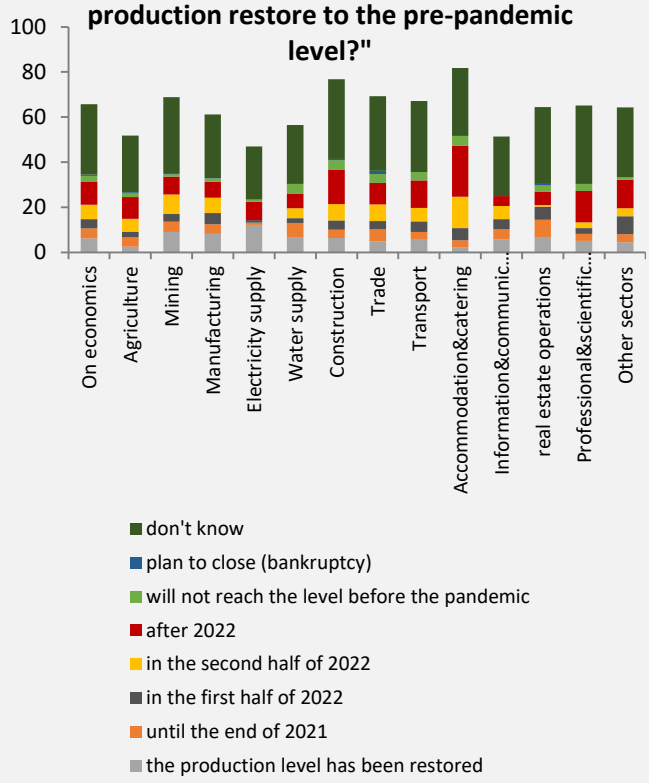


Figure 4. Question 2 "When will production restore to the pre-pandemic level?"



by a sluggish external demand for key export goods and the existence of restrictive measures on crude oil production as part of OPEC+. A number of sectors provided more positive assessments of the situation. So, the lowest perentage of enterprises that noted a negative effect was presented by such sectors as agriculture, and information and communication (52% and 53%, respectively). These sectors were least exposed to imposition of restrictive measures (Figure 3).

It is worth mentioning that in order to mitigate the effects of shocks on the economic activity, in 2020 the Government was undertaking various support measures. One of such measures had been exemption from taxes and other mandatory payments from the payroll fund (personal income tax, social tax, compulsory social health insurance and pension contributions) from April 1 to October 1, 2020, for small- and medium-sized business entities in the most affected economic sectors (retail trade, transport, restaurant business, cinemas, travel business, education, real estate operations, theater and concert business, hair dressers and beauty salons). Large business entities were also exempted from the above taxes and deductions but for a shorter period – from April 1 to July 1, 2020. In addition, concessional lending programs for SMEs and individual entrepreneurs that suffered from imposition of the state of emergency were designed and expanded ("The Economy of Simple Things", "The Employment Roadmap").

This year, the economy is gradually recovering. However, recurring cases of deterioration in the epidemiological situation constrain a faster day-to-day expansion in the consumer demand. This reflects on assessments of further development prospects by enterprises.

Out of enterprises that noted a negative effect of the pandemic, 6.2% of respondents state that the production level has been restored. 4.4% of enterprise plan to recover before the end of this year, and 10.5% – in the next year (4.1% – in the first half of the year, 6.4% – in the second half of the year). 10% of enterprises believe that their production level will be restored to the pre-pandemic performance only after 2022. 2.8% of the interviewed enterprises think that they will not be able to come back to the pre-pandemic level of production, 0.6% are planning to wind up (bankruptcy), and 31.2% do not know when they will recover (Figure 4).

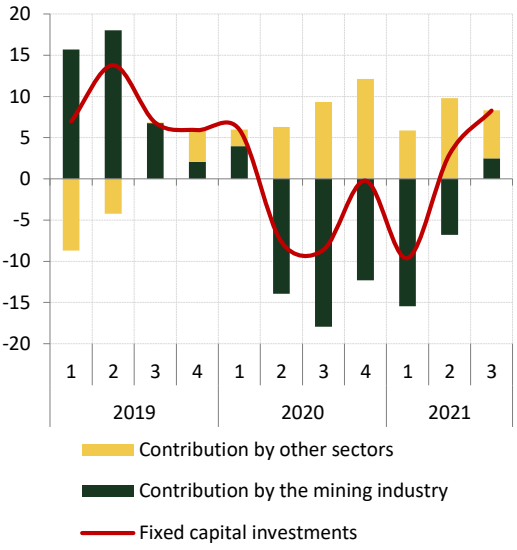
In the third quarter of 2021, the recovering dynamics of the investment activity was progressing. Fixed capital investments increased by 8.3% in real terms (Figure 35).

As for the technology structure of investments, in the third quarter construction and major overhaul works slowed down; since the beginning of the year, a considerable positive contribution of residential construction has been observed in this sector, while construction of non-residential buildings demonstrated some slowdown. In the structure of fixed capital investments, two-digit growth rates are shown by investments into renewal of property, plant and equipment and other types of investments are still in the descent zone. For the first time since suspension of a project at the TCO, namely since mid-2020, investments into the mining industry began to grow. At the same time, growth rates of investments in other sectors of the economy including in the manufacturing industry and construction slightly decreased. In the third quarter of this year, investments in the transport sector, information and communication and electricity supply contracted.

Investment activity of the population expressed in investments into residential construction continues to remain high (Figure 36). The dynamics of investment activity keeps being supported by mortgage programs and measures related to withdrawal of monies by payers from the UAPF's accounts. Owing to such programs, activity in the real estate market has been maintained at high levels this year. The number of purchases/sales exceeded 50 thousand transactions a month in certain periods (Figure 38). However, commissioning of primary housing is not growing at such dynamic pace. A certain shortage in the primary housing market leads to the increase in demand for the secondary housing.

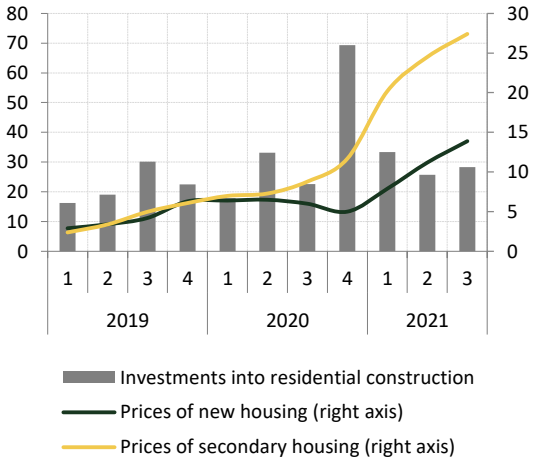
Such situation resulted in a significant gap between prices in the primary and secondary housing market from the second half of the last year. Thus, in the third quarter of 2021, prices in the secondary real estate market continued their growth, which accounted for 27.4%. The rise in prices in the primary market also slightly accelerated due to an increase in the price of construction materials and made up 13.9% (Figure 36).

Figure 35. Fixed Capital Investments, YoY, %



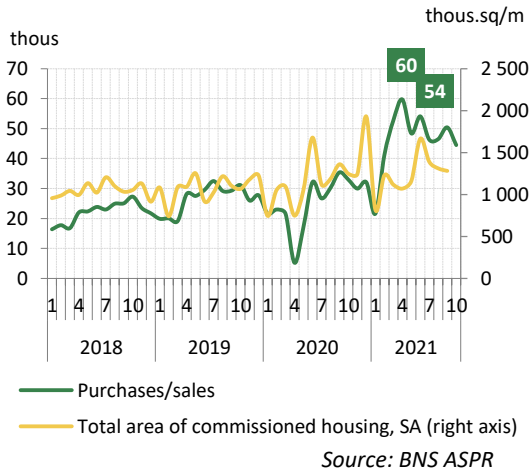
Source: BNS ASPR

Figure 36. Investments into Residential Construction and Prices in the Real Estate Market, YoY, %



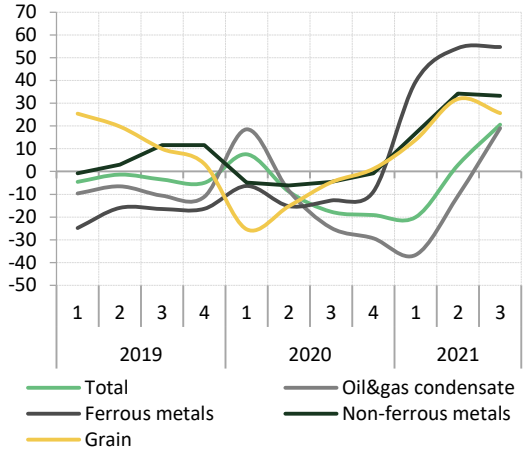
Source: BNS ASPR

Figure 37. Home Purchases/Sales and Commissioned Housing



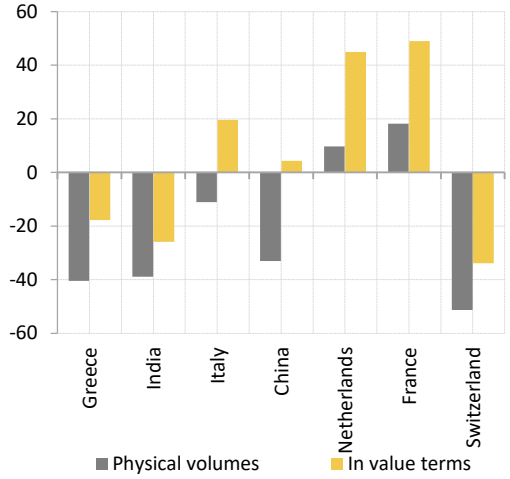
Source: BNS ASPR

Figure 38. Exports by Major Commodity Groups, cumulative, YoY, %



Source: NBK

Figure 39. Oil Exports on a Country-by-Country Basis in January-September 2021, YoY, %



Source: BNS ASPR

Gradual recovery of the global economy is embodied in Kazakhstan's foreign economic activities. According to the preliminary data from the BNS ASPR, in January-September 2021, foreign trade turnover amounted to 72.8 bln US dollars and increased by 12.7% compared to the same period of 2020, with exports growing by 20.6% (43.3 bln US dollars), and imports – by 2.8% (29.5 bln US dollars) .

The main contribution to the growth in total exports was made by oil exports, which increased by 19% in annual terms (Figure 38). On a country-by-country basis, oil exports to Italy, the Netherlands, France and Singapore increased in terms of value.

Given reduction in oil production in January-September 2021 by 3.3% (YoY), oil exports in kind decreased by 9.2% (YoY), namely, to India, Switzerland, Italy, Greece and China. At the same time, exports of oil to Singapore sharply increased (Figure 39).

In the structure of non-ferrous metals exports in value terms, export of copper increased by 38.2% (YoY), of aluminum – by 41.8%, silver – by 40.7%, zinc – by 10.3% and lead – by 10.2%. However, exports in-kind decreased – copper by 11.3% (YoY) and zinc – by 15.4% due to reduced supplies to China. In-kind exports of lead decreased by 37.7%. Alongside with that, exports of aluminum increased by 6% (YoY).

Among cereals, during nine months of 2021, exports of wheat and meslin were growing both in value terms (by 26.7%), and in-kind (by 18.1%). In particular, exports to Turkmenitan, Iran, Afghanistan and China went up.

In the structure of foodstuffs, owing to the increased meat production, exports of meat in-kind went up by 50.2% (by 9.1 thous. tons) as a result of a 2.8 times growth in supplies to Russia.

Exports of wheat decreased by 15.1%, being mainly triggered by the reduced volumes of exports to Afghanistan as a result of unstable situation in the country.

The upturn in imports during nine months of 2021 was driven by a sharp increase of 34.7% (YoY) in imports from China and from the EAEU countries – by 24.2%, including from Russia – by 24.7%, whereas imports from the EU countries showed a 8.9% decline.

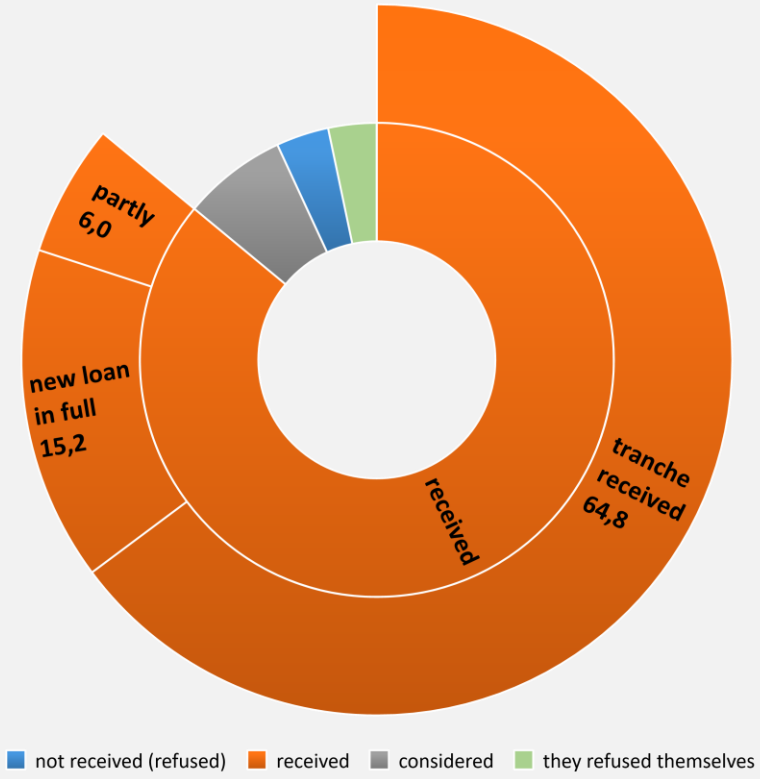
In the structure of foodstuffs, imports of meat in-kind went down by 13.7%. Imports of milk decreased by 22.3%, mainly due to the cut-off in supplies from Iran and Belarus. Along with that, imports of vegetable oils and fats and sugar increased. Among vegetables, imports of onions and carrots increased. Meantime, imports of cucumbers and potatoes decreased.

As for non-food products, given a lower incidence rate of coronavirus in the country, imports of medications decrease due to reduction in supplies from Russia, China and India. At the same time, in the environment of recovering consumer demand, imports of clothes are growing. Imports of cars are going up, including from Russia and Uzbekistan.

Box 3. Assessment of Financial Condition of Enerprises-Bank Borrowers

One third of enterprises have loan debt. Based on the data obtained in the course of a quarterly enterprise monitoring of the National Bank of Kazakhstan, in the third quarter of 2021, 34.5% of enterprises had liabilities on bank loans on their balance sheet, and the percentage of enpterprises with bank loans past due over 90 days accounted for 7.4%. In the third quarter of this year, 17.5% of enterprises applied to banks for loans, of which 15.1% (or 86.0% of the number of applicants) obtained the loan. Most of these enterprises (64.8%) received a regular tranche on the existing credit line, and new loans were originated to 21.2% of enterprises, of which 15.2% (or 71.7% of enterprises applying for a new loan) received the amount they requested, and others received only a part of the requested amount. 4.2% of applying enterprises (or 19.8% of those applied for a new loan) received a larger part of the requested amount, and 1.8% of the applying enterprises (or 8.5% of those to whom a new loan was originated) received less than a half of the requested amount (Figure 1). In the fourth quarter of 2021, 15.0% of enterprises intend to apply for a bank loan, of which 5.3% are already having liabilities on bank loans, and 1.0% even have an ovderdue debt.

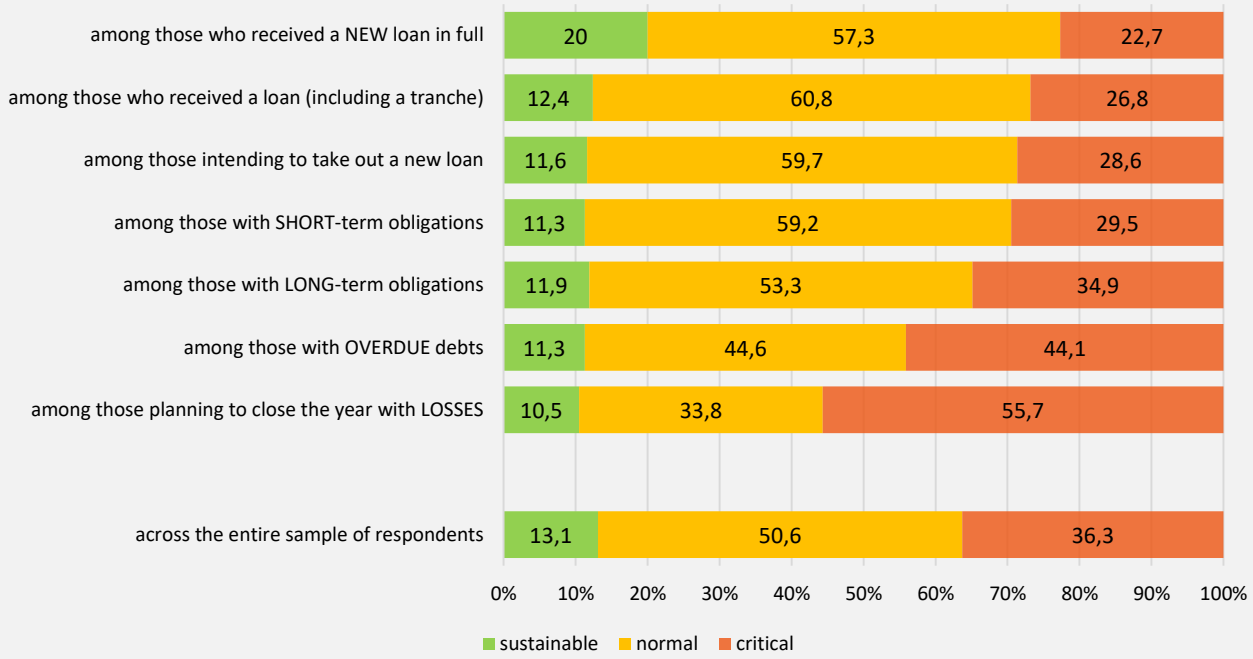
Figure 1. Results of consideration of applications for lending in Q3 2021, %



The level of debt burden is insignificant. The weighted average lelel of debt burden[3] in the economy is 13.5% based on the data of 3326 enterprises participating in the survey. In the sample of enterprises that have liabilities on bank loans the debt burden accounted for 23.1%, whereas among those who were rejected a loan it reaches 25.5% of revenues from realization of their products/services. At the same time, enterprises that intend to apply for a loan in the fourth quarter of 2021 have a debt burden of 22.9%.

The financial position of borowers is generally stable. Results of the enterprise classification by the degree of soundness by using the discriminant analysis[4], which is based on the assessment of financial ratios of enterprises that had steadily participated in the survey over the last 12 quarters indicate that the position among borrowing enterprises (including potential borrowers) is not worse than in the economy as a whole. The share of enterprises with critical financial condition is less than in the sample on the whole (36.3%). Only those enterprises that have a past due loan debt show a worse performance, where the share of enterprises with critical financial condition accounts for 44.1% (Figure 2).

Figure 2. Distribution of Enterprises by the Degree of Soundness by Groups



3 Monthly loan payment/Proceeds from the sale of products

4 The discriminant analysis is performed by using classification function, which includes 3 financial ratios: growth rate of revenue from realization of products per one employee, financial independence ratio and the equity growth rate

3.3 Labor Market

In the third quarter of 2021, the labor market continued to stabilize. The labor force increased by 0.75% in terms of quantity, where the number of the employed population increased and the number of unemployed population decreased. In these circumstances, the unemployment rate remained unchanged and accounted for 4.9% (Figure 40).

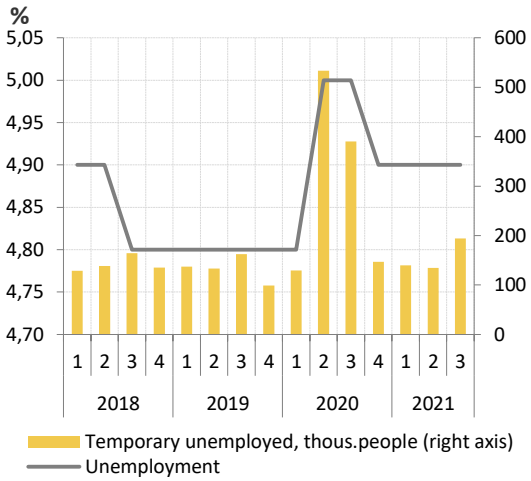
In the third quarter, the numbers of employed population increased due to the ongoing growth of the self-employed population (by 3.3%) and a minor growth of employees in the economy (by 0.5%).

The upturn in employment occurred both owing to the increased number of employees and the self-employed population, in such sectors of the economy as communication, healthcare, administrative and ancillary service activities, trade and accommodation and catering services (Figure 41, Group 1).

The self-employed population increased significantly in the sectors comprising the second group, namely, in real estate operations, construction and other services while the number of employees in these sectors is decreasing. The increase in employment due to the growth in the number of employees was observed in the industry and education, however, against a certain reduction in the number of self-employed in these sectors. The steady downward dynamics is seen in the sectors of the third group (Figure 41, Group 3), where the number of employees has been decreasing for a long time, specifically, in the transport sector, public administration, arts, entertainment and leisure. Stabilization of the situation in the labor market, revival of the economic activity result in a gradual recovery of the growth in labor productivity in the economy.

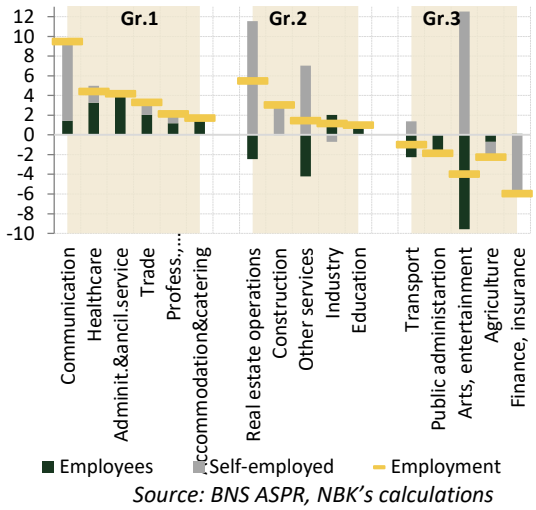
However, given that the epidemiological situation in the country somewhat deteriorated in July and Augut of this year, in the third quarter the number of temporary unemployed population exceeded that of the previous quarters of this year. Additionlly, because of the growing unemployed population, the number of applications to the public employment authorities increased (Figure 42).

Figure 40. Unemployment Rate and Temporary Unemployed Population



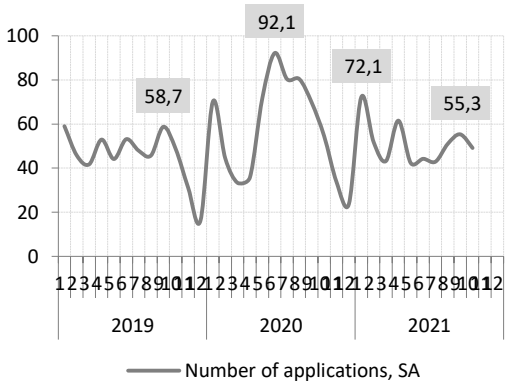
Source: BNS ASPR

Figure 41. Contribution to Employment of the Population by Employees and the Self-Employed by Types of Economic Activities in the Third Quarter of 2021, YoY, %



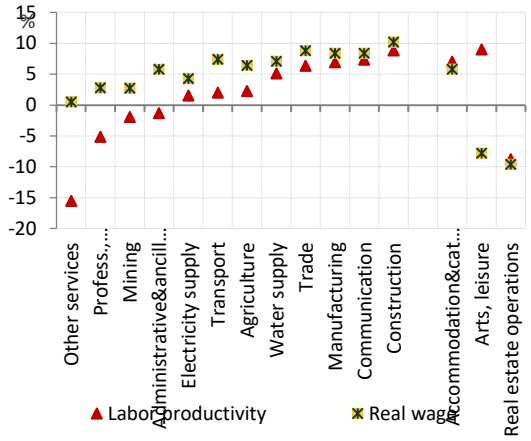
Source: BNS ASPR, NBK's calculations

Figure 42. People Who Applied to the Public Employment Authorities as Job Seekers, thousand individuals



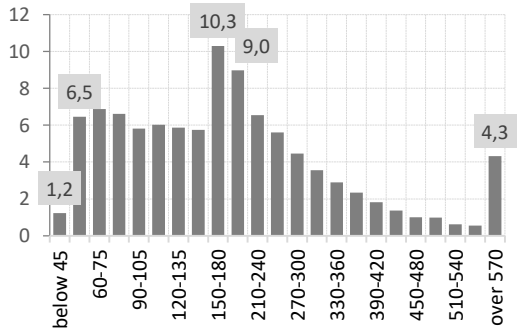
Source: BNS ASPR

Figure 43. Labor Productivity and Real Wages by Types of Economic Activities, 9 months of 2021, YoY, %



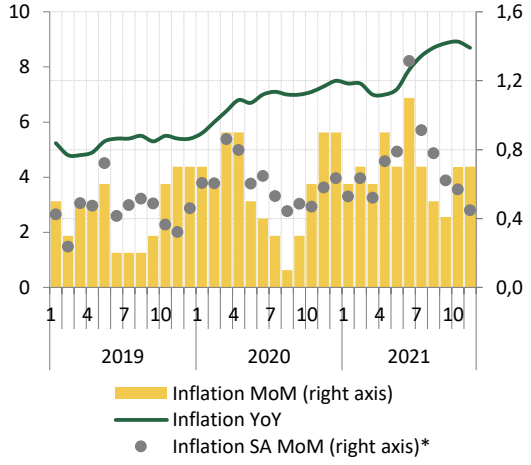
Source: BNS ASPR, NBK's calculations

Figure 44. Distribution of Employee Wages in the Republic of Kazakhstan5



Source: BNS ASPR

Figure 45. Inflation Dynamics, %



Source: BNS ASPR, NBK's calculations

**- Seasonal adjustment was performed by using the X-12-ARIMA method from 2011 until present*

[5]*Distribution of the number of employees who worked a full month by the amounts of accrued wages for April 2021*

The labor productivity is growing in many sectors of the economy except the mining industry, real estate operations, administrative and ancillary service activities and other services (Figure 43). Despite the growing labor productivity in Kazakhstan's economy, in many sectors of the economy the increase in real wages is outrunning the growth rates of labor productivity, except for accommodation and catering services, arts, entertainment and leisure, and real estate operations. A rise in wages not supported by a similar growth in labor productivity in many sectors of the economy retains pro-inflationary risks on the part of producers.

In order to support the low-wage employees, from 2022 the minimum wage is expected to be raised from 42.5 thous. tenge to 60 thous. tenge. According to the structure and distribution of employees based on wages, 7.7% of employees in the country this year had wages less than 60 thous. tenge (Figure 44).

The raise of minimum wage from the next year will directly target this group of employees. In the industry-based breakdown, a large number of employees with wages below 60 thous. tenge are concentrated in the public sector: education – 49.7%, healthcare – 10.8% and public administration and defense – 9.8%. As for those employees whose average monthly wage exceeds 60 thous. tenge, the raise of minimum wage will have an indirect relation to them through reduction of taxable base and, hence, some increase in their net income.

The largest number of employees in terms of wage is concentrated in the group with a wage from 150 to 180 thous. tenge, accounting for 10.3% of the total number of employees. In 2021, modal and median wages of Kazakhstanis conform to this group and made up 173 249 and 157 863 tenge, respectively. As compared to 2020, modal and median wages grew by 2.0% and 10.9%, respectively.

3.4. Inflation

As at the end of November 2021, annual inflation decelerated to 8.7%, staying above the target rate of 4-6% (Figure 45). The rise in prices of non-food products (8.3% YoY) was offset by disinflationary processes in the food market and the market of paid services where the annual inflation rate decelerated to 10.9% and 6.4%, respectively.

The annual growth in food prices after a lengthy acceleration started to decelerate and accounted for 10.9% at end-November (Figure 46). A considerable contribution the present deceleration of food inflation was made by disinflation of oils and fats, sugar and confectionery as well as dairy products and eggs owing to stabilization of monthly dynamics and a high base of the previous year.

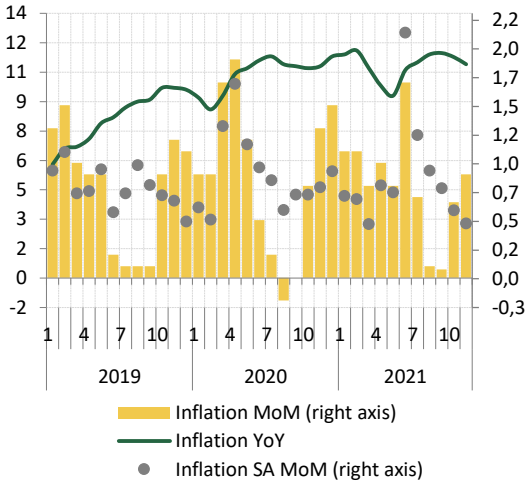
In November 2021, the annual rise in prices of bread and bakery and cereals reached 8.5%. At the same time, producer prices in October 2021 increased by 15.9% in annual terms because of a high growth in cereals prices of 14.7% YoY. This is associated with persistently high world prices and reduction in the domestic crop of cereals and pulses (in October 2021, the volumes of plant production decreased by 26.9% YoY). Hence, a further increase in consumer prices following the producer prices is possible. Along with that, the diminishing of yield, especially of forage crops, may put pro-inflationary pressure also on such branches as meat, dairy products and eggs (Figure 47).

In November 2021, the rise in prices of meat production accounted for 10.7% compared to the same period of the previous year, including the increase in prices of lamb meat and poultry by 15.3% and 17.2%, respectively. Appreciation of meat products in terms of price is associated with higher costs of raising cattle. Thus, in October 2021, prices of forage crops went up by 24.2% compared to the same period of the previous year, diesel feul in November 2021 increased by 46.6% in terms of price. Therefore, the growth of meat producer prices accounted for 9%, including poultry – 14.1%.

In November 2021, growth rates of prices for vegetables in annual terms remained high – 24.6% (beetroots – a 78.6% increase, cabbage – 39.8%, carrots – 32.8%, potatoes – 23.7%). A moderate rise in prices of fruits by 4.3% due to a declined price of oranges and apples is exerting disinflationary effect in the market of fruit and vegetable prduction.

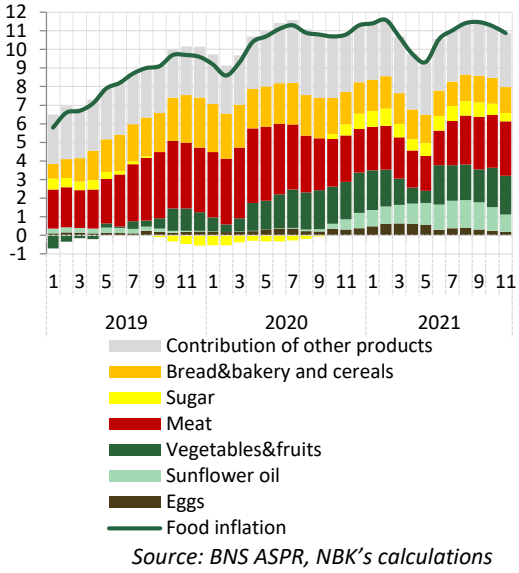
In November 2021, the price of sugar increased by 0.8%. However, given a high base of the previous year, annual inflation decelerated to 18.2%. According to BNS ASPR, during January-September 2021, realization of sugar in the domestic market decreased by 4.2%. At the same time, the domestic production increased by 3.4 times and imports went down by 41.7%.

Figure 46. Dynamics of Food Inflation, %



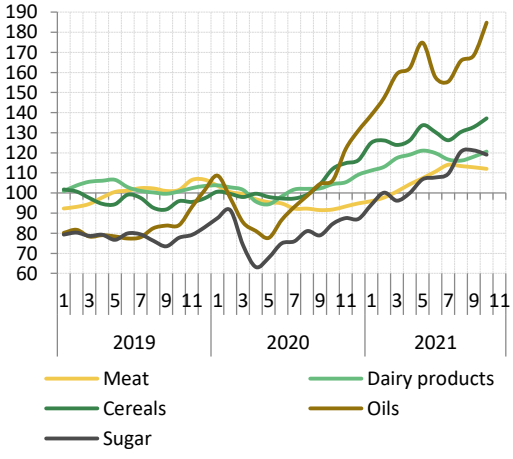
Source: BNS ASPR, NBK's calculations

Figure 47. Contribution of Particular Products to the Food Inflation, YoY, %



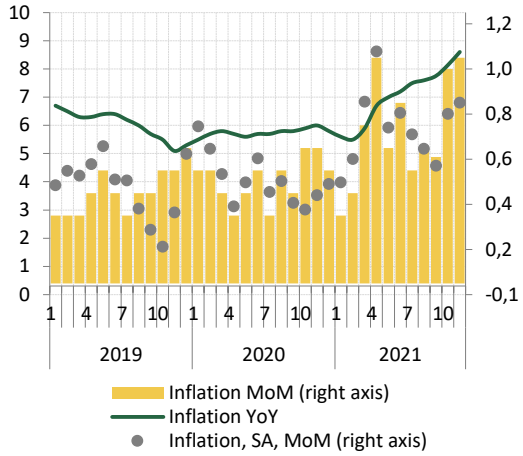
Source: BNS ASPR, NBK's calculations

Figure 48. World Food Price Indices, 2014-2016=100



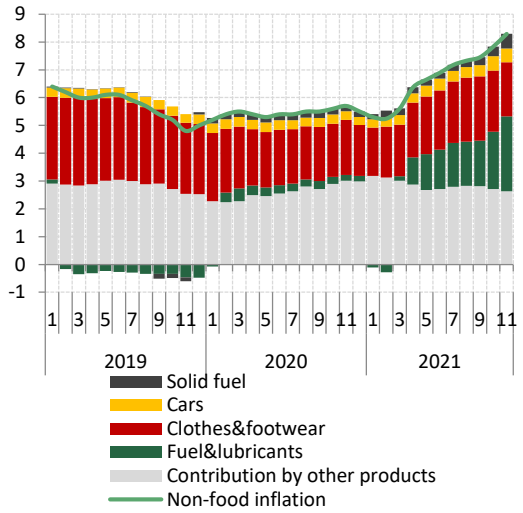
Source: UN FAO

Figure 49. Dynamics of Non-Food Inflation, %



Source: BNS ASPR, NBK's calculations

Figure 50. Contributions by Non-Food Products, YoY, %



Source: BNS ASPR, NBK's calculations

An additional pro-inflationary pressure on the domestic pricing of foodstuffs is put by persistently high food prices in the global market (Figure 48). In October 2021, the annual rise in world prices of vegetable oils accounted for 73.6%, sugar – 40.6%, cereals – 22.4%, meat – 22.1%, and dairy products – 15.5%. This, in turn, may lead to a higher cost of imported food products as well as growth in the domestic producer prices given the increase in differential between external and domestic prices.

Non-food inflation in October accelerated to 8.3% in annual terms as a result of an ongoing rise in prices for fuel and lubricants, especially for diesel fuel, as well as for solid fuel and cars (Figure 49).

The contribution of solid fuel, cars, fuel and lubricants, clothes and footwear to the annual non-food inflation in November 2021, according to the National Bank's estimate, made up 5.7 pp. Meantime, contribution of other categories of goods to non-food inflation over the recent months has not demonstrated significant change (Figure 50).

In November 2021, the annual growth in consumer prices of fuel and lubricants accelerated to 22.3%, where the price of gasoline went up by 18.4% and of diesel fuel – by 46.6%. Appreciation of fuel in terms of price occurs due to the growing producer prices (gasoline – by 23.7% YoY, diesel – by 7.3% YoY in October of this year).

An additional pressure on the cost of diesel fuel is put by high exports, which in January-September 2021 showed a four-fold increase versus the corresponding period of the last year. Therefore, the domestic market has run up a deficit of the raw commodity (in January-September 2021 versus the corresponding period of the last year, realization in the domestic market decreased by 3.6%).

It is worth mentioning that the growing cost of fuel and lubricants puts an additional upward pressure on the dynamics of inflationary processes that is manifested both directly and indirectly through the increase in prices of goods and services where fuel and lubricants are used in production and logistics.

In November 2021, prices of coal have increased by 3.7% over the month, with their growth in annual terms accelerating to 9.3%. The increase in consumer prices is caused by the rise in producer prices (by 6% YoY in October of this year) due to the growth in prices of electricity, fuel and lubricants, the raising of wages as well

as a higher cost of PPE servicing. The rising world prices also put an additional pressure on the dometic prices. Given a high differential between external and domestic prices, a further growth of prices in Kazakhstan is very likely. Taking into account the fact that a major portion of energy in Kazakhstan is generated by coal combustion, a rise in prices of coal may cause the growth in electricity fees, which will be putting a significant pressure on producer prices.

The annual growth in prices for cars in November 2021 accounted for 12.9%. The increase in prices was caused by a high growth of import prices and producer prices – by 11.2% and by 10.5%, respectively.

Deceleration of annual growth rates of prices for **paid services** in November 2021 to 6.4% is related to

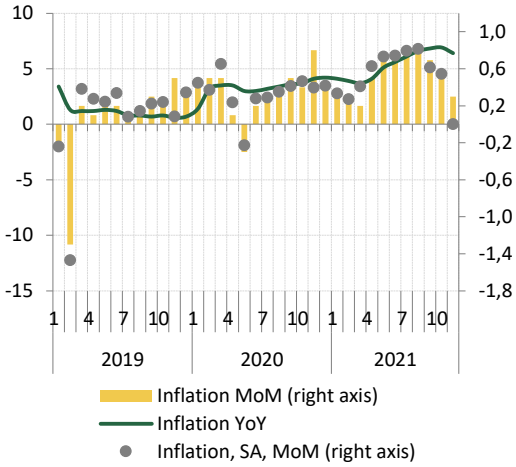
disinflation of regulated services (3.1%) (Figure 51). However, the prices of housing rent continued to grow – to 19.8%, gas – to 12.3% and education services – to 8.2% (Figure 52).

In November 2021, due to the growing real estate prices as well as an increased demand for rental housing from university students because of a limited number of rooms in student dormitories driven by quarantine restrictions, the rental cost of housing went up by 19.8% compared to the same period of the previous year (see Box 4 for more details). The rise in prices of construction materials and home renovation services could be additional factors for the price growth. In November 2021, due to the comeback to the on-site training amd increased costs of educational institutions (utility payments, wages and other administrative expenses), the cost of education services increased by 8.2 in annual terms.

The upward trend in consumer prices of gas is persisting. So, in November 2021 compared to the same period, the price of gas went up by 12.3%, including gas transported by power distribution networks – by 5.5%. The rise in gas prices is associated with the increase in cap rates of wholesale realization of commercial-grade gas in the domestic market[6].

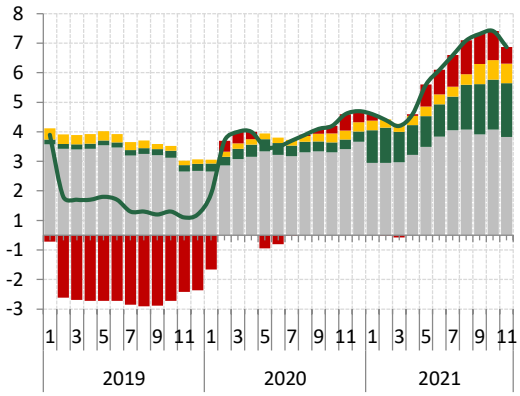
Tariffs also increased in certain markets of non-regulated services in the environment of recovering demand. Thus, in October 2021, the cost of communication services in annual terms accelerated to 3.3%, of public catering

Figure 51. Dynamics of Service Inflation, %



Source: BNS ASPR, NBK's calculations

Figure 52. Contributions to the Paid Services Inflation, YoY, %



Source: BNS ASPR, NBK's calculations

[6] *Order of the Minister of Energy of the Republic of Kazakhstan dated June 3, 2021, No. 188*

services – to 8%, and services related to renovation of residential premises – to 9.1%.

At the same time, in November of this year, annual growth rates of fees for regulated services slowed down to 3.1% due to disinflation of water supply – to 1.3%, waste water disposal – to 1.7% and deflation of thermal power (a 4% decline).

Box 4. Analysis of the Property Lease Market

Figure 1. Price Index of Housing Rent in Kazakhstan, YoY

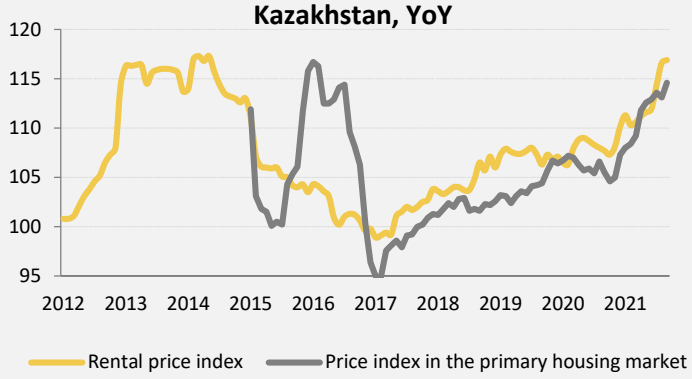
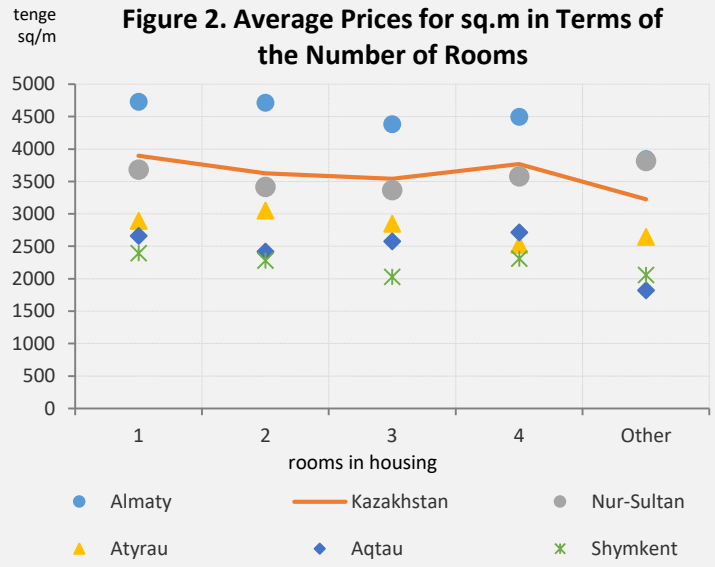


Table 1. Prices in the Rental Market Across Cities

	"Krisha" PeriodicaL			BNS ASPR	
	Max.price of a sq/m	Min.price of a sq/m	Average price of a sq/m	Price of a sq/m in October 2021	Change versus Oct.2020, %
Almaty	16 667	1 000	**4 627**	**3 157**	135.0
Nur-Sultan	12 245	1 215	**3 514**	**3 443**	118.0
Aktau	10 000	857	**2 507**	**2 359**	115.2
Atyrau	10 000	1 154	**2 933**	**2 171**	122.9
Shymkent	80 000	824	**2 236**	**2 111**	133.7
Total	16 667	805	**3 372**	**1 888**	117.0

Source: BNS ASPR, Krisha.kz

Figure 2. Average Prices for sq.m in Terms of the Number of Rooms



The progression of COVID-19 pandemic triggered the rise in prices of many goods and services. The housing market has not been an exception. From 2020, in view of a high demand and low supply, many countries observed almost a two-digit growth in housing prices. Following the rise of housing prices, cost of rent also increased considerably. However, its growth rates appeared to be slower than those of housing prices. Fo example, in the USA, in the second quarter of 2021 housing prices grew by 11.1% (YoY), whereas the rental price increased by 2.3% (YoY). In large European countries (Germany, France, the UK), the price of housing went up from 4.3% to 8.4% (YoY), and the price of rent by 1-2% (YoY) only. A higher growth in rental price is observed in the Eastern European countries (Slovenia, Estonia, Latvia, Romania), where the price growth in October 2021 ranged from 3% to 12% in annual terms.

The rise in rental payment was probably also caused by the lifting of quarantine restrictions and resumption of operations by public facilities. Hence, the demand for real estate is increasing in the cities versus the suburban areas. Also, in connection with work resumption at educational institutions, there is a heightened demand for rental housing from consumers of younger age. In addition, flight resumptions gave a boost to the growth in the demand for real estate in metropolitan cities, coastal and resort areas.

In turn, progressive recovery of the economic activity, getting out of the teleworkibg and online learning regimes also revived activity in the real estate market in Kazakhstan. Since the beginning of 2021, prices in the real estate market – both purchase/sale and rent – have demonstrated a sizable spike.

The peak of price growth in the rental market occurred in August, when the demand for rental property increased due to the fact that university students transferred from online learning to on-site learning. At the same time, although the trend in the real estate market is generally

similar to the overall global dynamics, rental prices in Kazakhstan are growing at the same pace as prices in the primary real estate market.

At present, the upward dynamics of prices is still persisting.

High prices of supply in the rental market may be traced based on the data from Krisha.kz web site. As of November 8, 2021, there were 9480 publications of announcements about rent of apartments in Kazakhstan. In the structure of announcements, the city of Almaty accounts for 32.4% of all announcements, Nur-Sultan – 22.6%, Aktau – 11.4%, Shymkent – 6.1%, Atyrau – 4.6%, and in other towns – 22.9% of announcements.

The prices are growing in all cities and towns. In particular, a sizable growth is observed in large cities of Nur-Sultan, Almaty and Shymkent, given a high positive internal migration balance (during 9 months of 2021: Almaty +21 718 people, Nur-Sultan– +22 346 people, Shymkent – +9 568 people) driven by a concentration of out-of-town students and the labor force. Across the country, the most expensive square meters of rent, according to the BNS, are in large cities as well as Aktau and Atyrau. This trend is also confirmed by the data from Krisha.kz. Given the specifics of data collection from a web site (segment of data at one date), incomplete regional coverage as well as the use of average data of all types of residential buildings (the CPI does not include very expensive consumer goods and services), there are differences in the level of prices in Almaty and across the country on average (Table 1).

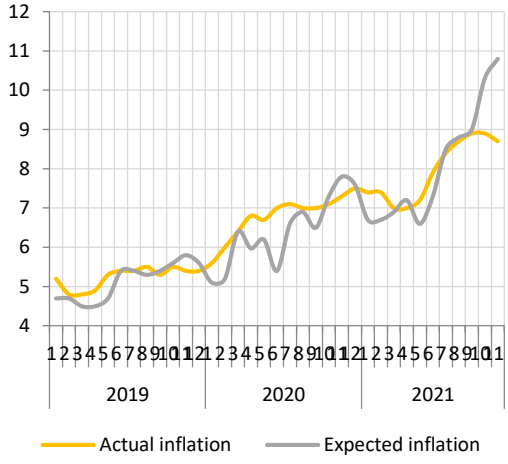
According to Krisha.kz, the highest prices of square meter have one-room appartments and four-room apartments, which is indicative of a high demand on the part of population. However, on a region-by-region basis, such trend is slightly different, for example, in Almaty the cost of one square meter of rented one- and two-room apartments is virtually equal, in Nur-Sultan the cost of square meters in one-room apartments is higher and in Atyrau the cost of one square meter in two- and three-room apartments is higher. The difference in preferences of the population on a region-by-region basis may be related to demographic specifics (a household size), and positive balance of internal migration.

As at the end of October of this year, deceleration in prices in the real estate market and rental market is not yet observed. In some regions, where the prices remained stable throughout the year, by October 2021 price are accelerating (Uralsk, Kostanai).

Recurrent outbreaks of coronavirus and the associated restrictive measures create uncertainty about a further development of the rental market.

Inflationary expectations of the population in September-October remained heightened. A quantitative assessment of inflation one year ahead in October 2021 accounted for 10.3% (Figure 53). The largest share of respondents expects that prices would accelerate in the next 12 months – 33% of respondents (23% in October of the previous year), which has become a historical maximum.

Figure 53. Inflation and Expected Inflation, YoY, %

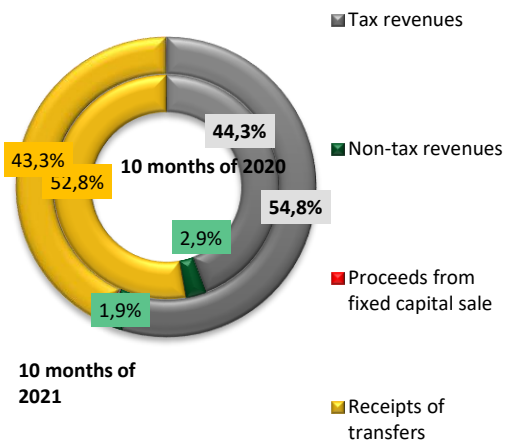


Source: CS MNE, FusionLab

Perception of inflation has been high over the recent months. In July-October of this year, the majority of interviewed people continued to observe a rapid price growth over this year. In October of this year, the majority of households kept noting an especially high rise in food prices, particularly for meat and poultry, bread and bakery, vegetable oil, fruit and vegetable production.

The increased cost of fuel and lubricants, utility services, clothes and footwear were also mentioned. Consumer sentiment in October has not virtually changed, and assessments regarding the prospects of the country's development somewhat improved. At the same time,

Figure 54. Structure of the National Budget Revenues



Source: MoF RK

both the existing and future financial standing is expected to deteriorate. Based on that, respondents began to economize on food more often.

However, the share of interviewed individuals with a loan, including a consumer loan, increased (from 30% in July of this year to 33% in October of this year).

3.5 Fiscal Policy

Aa at the end of ten months of 2021, overall and non-oil budget deficit had been at a lower level compared to the same period of the previous year. This year, both the revenue side and the expenditure side of the budget were demonstrating growth. At the same time, the budget spending for acquisition of financial assets decreased.

During January-October 2021, the national budget deficit amounted to 2.2 trillion tenge, having contracted by 1.1% compared to the corresponding period of 2020 (during 9 months of 2021 – 2.8% of GDP). In January-October 2021, official transfers worth 4 292 billion tenge were received to the revenue side of the budget, where the guaranteed transfer from the NF RK amounted to 2 424 billion tenge, earmarked transfer equaled 1 398 billion tenge, and transfers from the subordinate government authorities – 470 billion tenge.

The non-oil budget deficit (budget deficit excluding transfers from the National Fund and export customs duties for crude oil), according to the National Bank's estimate, during January-September 2021 amounted to 6.1 trillion tenge (during 9 months of 2021– 11.5% of GDP), which is by 4.8% less than in the corresponding period of 2020 (Figure 54).

At present, the law on the national budget for 2022-2024 has been drafted. A three-year national budget plan will be aimed at implementation of the nationwide areas of focus to overcome the consequnces of coronacrisis. The social focus of the budget policy is expected to be preserved (in 2022, the spending on the social sphere will account for 50.8% of the total volume, and in 2024 – 59.8%). It will be secured by the indexation of social benefits, increase in wages to teachers and medical personnel and by construction of public amenities. As part of support of the real sector development, an allocation of resources is

planned in order to go on with implementation of such government programs as the “Nurly Zhol”, “Nurly Zher”, for development of the agro-industrial complex, GPIID, “Roadmap of Business-2025”.

During January-October 2021, national budget revenues increased by 9.9% compared to 2020 and amounted to 9.9 trillion tenge (the share in budget revenues accounted for 54.8%). The growth in revenues was mainly caused by the increase in tax revenues (by 36.1%) due to gradual easing of quarantine restrictions and recovery of the economic activity. The tax hike was observed in wholesale and retail trade, in the manufacturing and mining industry. However,

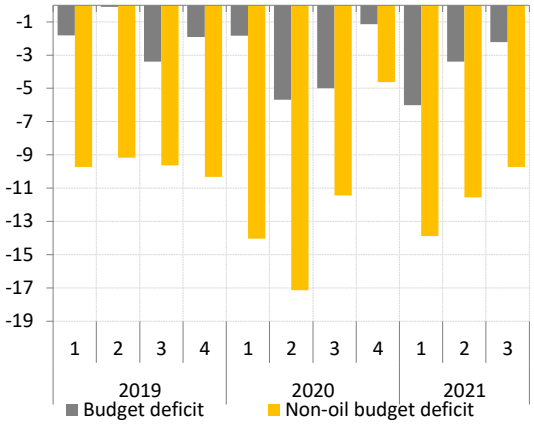
during ten months of 2021, the receipts of official transfers decreased by 9.9% (the share in budget revenues accounted for 43.3%) due to a 12.0% reduction in transfers from the National Fund.

A 30.6% drop in non-tax revenues is driven by the decresed receipts of dividends on government’s stake in the national ownership (NWF “Samruk-Kazyna” JSC).

At the same time, revenues from administrative penalties, fines and sanctions imposed by the government authorities are growing. A 3.9 times rise in proceeds from fixed capital sale is related to the increased sales of tangible assets from the state stockpiles through an auction (a sale of diesel fuel from the state stockpiles to “Petrofan” LLP and “Information and Accounting Center” JSC (Figure 55).

During January-October 2021, the national budget expenditures equaled 11.8 trillion tenge, having increased by 9.0% compared to the corresponding period of 2020. The main contribution to the growth in the national budget expenditures was made by the sector of education – an increase by 55.6% (the share – 8,8%), healthcare – by 27.0% (the share – 13,8%) and debt service – by 29.2% (the share – 7.7%). Alongside with that, expenditures for social welfare and social security grew by 0.6% (the share – 27.4%).

Figure 55. Overall and Non-Oil Deficit of the National Budget, as % of GDP



Source: MoF RK

Core inflation means the inflation, which excludes transitory erratic price changes subject to certain factors of administrative, event-related and seasonal nature. The base rate is the National Bank's key monetary policy instrument that enables to regulate nominal interbank interest rates in the money market. By setting the base rate level, the National Bank determines a target value of the targeted interbank short-term money market rate in order to achieve the goal of ensuring the price stability in the medium term.

Gross Fixed Capital Formation is the growth in non-financial assets, which have been used in the process of production for a long time. Gross fixed capital formation includes the following components: a) acquisition, less retirement, of new and existing fixed assets; b) costs for major improvements of tangible produced assets; c) costs for improvement of non-produced tangible assets; d) expenses in connection with the transfer of title for non-incurred costs.

Gross Domestic Product (GDP) is an indicator that reflects the market value of all final goods and services produced during a year in all sectors of the economy within the territory of the country for consumption, exports and saving, irrespective of the national identity of the used production factors.

Reserve Money includes cash issued into circulation by the National Bank, other than cash at the cash departments of the National Bank, transferrable and other deposits of banks, transferrable deposits of non-bank financial organizations and current accounts of government and non-government non-financial organizations in the tenge at the National Bank.

Money Supply (M3) is determined on the basis of consolidation of balance sheet accounts of the National Bank and banks. It consists of cash in circulation and transferable and other deposits of non-bank corporate entities – residents and the population in the domestic and foreign currency.

Dollarization of the Economy means the situation where a foreign currency (largely – the US dollar) starts to be used for transactions within a country or in certain sectors of its economy, pushing out the domestic currency from the domestic money turnover, and acting as the means of saving, measure of value and the legal tender.

Inflation is an increase in the overall price level of goods and services. In Kazakhstan, inflation is measured by the consumer price index.

Consumer Price Index is the change in the overall price level of goods and services purchased by the population for consumption. The consumer basket of Kazakhstan used for calculation of inflation reflects the structure of household spending and contains goods and services, which represent the largest portion in the consumption of population. The CPI is calculated as the ratio of the cost of a fixed set of goods and services in current prices and its cost in the prices of the previous (base) period. The index is calculated by the Committee on Statistics of the Ministry of National Economy of the Republic of Kazakhstan.

Inflation Targeting is a monetary policy regime, which is oriented at achieving a target inflation rate.

Minimum Reserve Requirements (MRRs) mean the mandatory share of bank's liabilities that a bank is to keep in the form of cash in its cash department and monies on correspondent accounts with the National Bank in the domestic currency (reserve assets). The volume of reserved liabilities of banks is regulated by the MRR ratios.

Reverse REPO is the purchase of a security with the commitment to sell it after a specific period of time and at a specific price. The National Bank conducts reverse repo operations with a view to

provide the tenge liquidity to banks against the pledge of securities in accordance with the National Bank's list of collateral. Open Market Operations are regular operations of the National Bank in the form of auctions for liquidity provision or withdrawal in the money market with a view to set interest rates around the base rate.

Standing Facilities refer to monetary policy instruments for adjustment of volumes of liquidity, which resulted from the open market operations. Standing facilities are provided as part of bilateral arrangements where the National Bank is one party to the transaction. Such operations are conducted at the initiative of banks.

Transferrable Deposits refer to all deposits, which: 1) can be converted into cash at face value at any moment in time without any penalties and restrictions; 2) are freely transferable through a check, draft or endorsement orders; and 3) are widely used for making payments. Transferrable deposits represent a part of the narrow money. Other deposits primarily include savings and time deposits that only can be withdrawn on expiration of a certain period of time, or can have different restrictions which make them less convenient for use in the ordinary commercial transactions and, mainly, meet the requirements established for saving vehicles. In addition, other deposits also include non-transferable deposits and deposits denominated in foreign currency.

Potential Output. Reflects the level of output in the economy that can be reached subject to full utilization of inputs and full employment. It reflects the volume of production, which can be manufactured and realized without creating prerequisites for the change in the price growth rates.

Consumer Basket means a sample of goods and services, which characterizes the standard level and the structure of monthly (annual) consumption of an individual or a family. Such sample is used to calculate the minimum subsistence level, based on the cost of the consumer basket in current prices. The consumer basket also serves as a comparative basis for estimated and real consumption levels and also as the basis to determine the purchasing capacity of currencies.

Interest Rate Channel of the Monetary Policy Transmission Mechanism is the transmission mechanism channel, which describes the impact of the central bank on the economy through the interest rate regulation.

Direct Repo is the sale of a security with the commitment to repurchase it after a specific period of time and at a specific price. The National Bank conducts direct repos with a view to withdraw excess liquidity in the tenge.

Free Floating Exchange Rate. According to the IMF's current classification, under the floating exchange rate framework a central bank does not establish any pegs including operating ones for the level or the change in the exchange rate, allowing the exchange rate to be determined by the market factors. In doing so, the central bank reserves the opportunity to periodically influence the domestic foreign exchange market in order to smooth out the volatility of the domestic currency exchange rate or to prevent its dramatic movements as well as to ensure the financial system stability.

Output Gap is the deviation in GDP expressed as a percentage of a potential output. Expresses the difference between an actual GDP and potential GDP for a certain time interval. Serves as an indicator, which reflects the effectiveness of resources utilized in the country. If an actual output exceeds the potential one (a positive gap), other things remaining equal, the trend of acceleration in the price growth rates would be anticipated because of the overheating of the economy.

Real Exchange Rate refers to a relative price of a commodity produced in two countries: the proportion of commodity exchange between countries. The real exchange rate depends on the nominal rate, on relation between exchange rates of currencies, and prices of goods in the domestic currencies.

TONIA Rate represents a weighted average interest rate on one-day repo opening transactions made on the stock exchange with government securities in the automatic repo sector.

Monetary Policy Transmission Mechanism is the process, by which monetary policy instruments influence final macroeconomic indicators such as the economic growth, inflation. Narrow Reserve Money is the reserve money excluding other deposits of banks at the National Bank.



LIST OF KEY ABBREVIATIONS

bp – basis point
BNS ASPR – Bureau of National Statistics of the Agency for Strategic Planning and Reforms
GDP – Gross domestic product
GPIID - Government Program for Industrial and Innovation Development
EM – emerging markets
EU – European Union
ECB – European Central Bank
CPI – consumer price index
KASE– Kazakhstan Stock Exchange
KSF – "Kazakhstan Sustainability Fund" JSC
NBK – National Bank of the Republic of Kazakhstan
NoF RK – National Fund of the Republic of Kazakhstan
OPEC – Organization of the Petroleum Exporting Countries
Rosstat – the Russian Federal State Statistics Service
REER – real effective exchange rate
IMF – International Monetary Fund
bln – billion
mln – million
MNE – Ministry of National Economy of the Republic of Kazakhstan
MoF RK – Ministry of Finance of the Republic of Kazakhstan
MED – Ministry of Economic Development of the Russian Federation
trln – trillion
thous.– thousand
TCO – Tengizchevroil
CB RF – Central Bank of the Russian Federation
FAO – Food and Agriculture Organization of the United Nations
Fed – Federal Reserve System

