

National Bank
National Bank
of the Republic of Kazakhstan

Inflation Report
for the Fourth Quarter of 2011

Table of Contents

Table of Contents	2
Basic Terms and Definitions	3
List of Figures and Tables	5
Summary	7
Evaluation of the Inflation Forecasts for the 4 th Quarter of 2011 and for 2011 as a Whole	8
Inflation Forecast for 2012	8
1. Inflationary Processes	10
1.1. Consumer Prices	10
1.2. Core Inflation	11
1.3. Prices in the Real Sector of the Economy	13
1.3.1. <i>Prices in the Industry</i>	13
1.3.2. <i>Prices in Agriculture</i>	14
1.3.3. <i>Enterprise Monitoring</i>	15
2. Inflation Factors	17
2.1. Aggregate Demand	17
2.1.1. <i>Individual Consumption and Investment Demand</i>	17
2.1.2. <i>Government Consumption</i>	19
2.1.3. <i>External Sector</i>	21
2.2. Production	25
2.3. Labor Market	26
2.3.1. <i>Employment and Unemployment</i>	26
2.3.2. <i>Wages and Productivity</i>	28
3. Money Supply	30
3.1. Monetary Aggregates	30
3.1.1. <i>Reserve Money</i>	30
3.1.2. <i>Money Supply</i>	31
3.1.3. <i>Cash in Circulation</i>	32
3.2. Financial Market	32
3.2.1. <i>Deposits of Residents</i>	32
3.2.2. <i>Credits to the Economy</i>	35
3.2.3. <i>Bank Assets and Liabilities</i>	37
3.2.4. <i>Financial Market Rates</i>	40
4. Monetary Policy Instruments and Operations	42
4.1. Interventions in the Domestic Foreign Exchange Market	44
4.2. Minimum Reserve Requirements	45
4.3. Open Market Operations	46
4.4. Standing Facilities	47

Basic Terms and Definitions

In Section 1. Inflationary Processes

Inflation in the Republic of Kazakhstan is calculated based on the consumer price index (CPI) that characterizes changes in the overall prices for goods and services purchased by the population for personal consumption in the cities of Astana and Almaty, in all regional centers and in a selected number of towns and district centers. The consumer basket for calculation of inflation reflects the structure of household expenditures and contains 508 goods and services which represent the largest portion in the consumption of population.

Core inflation – is the inflation that excludes short-term uneven price changes under the influence of certain factors of an administrative, circumstantial, and seasonal nature.

Since 2004 the Agency of Statistics of the Republic of Kazakhstan has been calculating core inflation using five different methods:

- core inflation-1: inflation that does not take into account the rise in prices for vegetables, fruit, gasoline, and coal;
- core inflation-2: inflation that does not take into account the rise in prices for vegetables, fruit, regulated services, and energy resources;
- core inflation-3: does not take into account the five largest and five smallest price hikes;
- core inflation-4: trimmed mean – in the calculation of CPI the components with the cumulative weight of less than 8% and more than 92% are excluded, i.e. the goods and services whose prices have changed (increased or decreased) most of all are not taken into account;
- core inflation-5: median CPI – in the calculation of CPI all price changes are intercepted except for the one which is in the middle of the series ranged by the change in prices, i.e. static median. Median CPI will be equal to the change in the price of the first component which cumulative weight is equal to or exceeds 50%.

Inflationary expectations among enterprises in the real sector are surveyed within framework of **Enterprise Monitoring**, which has been performed by the National Bank since 2002. These surveys are characterized by qualitative estimates by the managers of the enterprises surveyed of the enterprises' production activity ("will rise," "will fall," "will remain unchanged"), including demand and prices for finished products and for the raw materials and supplies used in the previous quarter and the coming quarter.

The diffusion index is derived as the sum of "will rise" responses and half of the "remain unchanged" responses. This index is a generalized indicator that characterizes the trends in the change of a reviewed indicator. An index value above 50 means a positive change in the indicator, and the value below 50 means a negative change.

In Section 2. Inflation Factors

Proceeds to the budget include revenues (tax proceeds, non-tax proceeds, proceeds from disposal of capital assets), repayment of budget credits, and proceeds from disposal of the national financial assets.

Budget expenditures are the expenses (both current and capital expenditures), budget credits, and acquisition of financial assets.

In Section 3. Money Supply

Base Money (reserve money) includes cash issued by the National Bank excluding cash in till of the National Bank (currency outside the National Bank), transferable and other bank deposits, transferable deposits of non-bank financial institutions, and current accounts of public and private non-financial institutions in Tenge with the National Bank.

Narrow money refers to base money not including other bank deposits with the National Bank.

The M1 Monetary Aggregate is calculated as the sum of cash in circulation and transferable deposits held by non-bank legal entities and the public in Tenge.

The M2 Monetary Aggregate is equal to the M1 monetary aggregate plus other deposits in Tenge and transferable deposits of non-bank legal entities and the public in foreign currency.

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 legal entities – residents and households – residents in the domestic and foreign currency.

Transferable 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. Transferable 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 mechanisms. In addition, other deposits also include non-transferable deposits and deposits denominated in foreign currency.

The KazPrime Index represents the average weighted rate of interest on interbank deposits with the banks that are the parties to the Agreement on Formation of the KazPrime Index of Kazakhstan Interbank Deposits with Banks. Each quotation includes the rate for the attraction and placement of funds to the deposit of one of the parties to the Agreement, as well as the volumes of attracted and placed funds. The minimum quotation amount is KZT 150 mln. The maximum spread between quotations is one hundred basis point (1.00% per annum). The standard term for an interbank deposit was three months at the time when the project was launched.

In Section 4. Monetary Policy Instruments and Operations

The National Bank's **participation coefficient** in currency auctions on the Kazakhstan Stock Exchange (KASE) is calculated as the ratio of the National Bank's net participation (purchase minus sale of foreign currency) to the net volume of trading on the KASE.

The balance of the National Bank's operations in the money market is calculated as a sum of the change in the volume of short-term notes in circulation, deposit and correspondent account balances with the National Bank, and net operations on purchase and sale of government securities.

List of Figures and Tables

Figures

- Figure 1. Actual and forecasted inflation in 2011
- Figure 2. Dynamics of quarterly inflation and its components
- Figure 3. Dynamics of annual inflation and its components
- Figure 4. Dynamics of quarterly inflation and core inflation
- Figure 5. Dynamics of annual inflation and core inflation
- Figure 6. Dynamics of the producer price index
- Figure 7. Dynamics of the agricultural price index
- Figure 8. Diffusion indices for changes in the demand and prices
- Figure 9. Contribution of components of aggregate demand to growth in GDP
- Figure 10. Dynamics of personal spending and income
- Figure 11. Dynamics of spending on investments in fixed capital
- Figure 12. State budget execution
- Figure 13. Dynamics of world prices for metals
- Figure 14. Dynamics of world prices for oil (Brent), and wheat (Canada)
- Figure 15. Current account balance
- Figure 16. Indices of real exchange rates of the Tenge
- Figure 17. Dynamics of the nominal exchange rate of the Tenge versus the U.S. dollar
- Figure 18. Dynamics of the official exchange rate of the Tenge versus the Euro and the Russian ruble
- Figure 19. Contribution of key sectors of the economy to growth in real GDP
- Figure 20. Структура экономически активного населения
- Figure 21. Actual unemployment rate
- Figure 22. Dynamics of labor productivity and real wages
- Figure 23. Dynamics of monetary aggregates
- Figure 24. Dynamics of money multiplier and its components
- Figure 25. Dynamics of deposits and their interest rates
- Figure 26. Dynamics of the change in deposits of legal entities
- Figure 27. Dynamics of the change in deposits of individuals
- Figure 28. Dynamics of credits to the economy and their interest rates
- Figure 29. Dynamics of credits to legal entities
- Figure 30. Dynamics of credits to the population
- Figure 31. Dynamics of bank assets
- Figure 32. Structure of bank assets
- Figure 33. Dynamics of bank liabilities
- Figure 34. Structure of bank liabilities
- Figure 35. Dynamics of the KazPrime index
- Figure 36. Dynamics of rates on REPO operations
- Figure 37. Balance of the National Bank's operations in the domestic market
- Figure 38. Boundaries of the National Bank's interest rates band
- Figure 39. Balances of bank correspondent accounts with the National Bank
- Figure 40. Volume of trading in the domestic exchange market
- Figure 41. Coefficient of the National Bank's participation in the Kazakhstan Stock Exchange
- Figure 42. Compliance with minimum reserve requirements
- Figure 43. Volume of placed short-term notes and their yield
- Figure 44. Short-term notes in circulation
- Figure 45. Volume of deposits and interest rates on deposits attracted by the National Bank

Figure 46. Volume of outstanding liabilities of the National Bank on deposits attracted from banks

Figure 47. Volume of the National Bank's refinancing operations

Figure 48. Volume of outstanding liabilities on the National Bank's refinancing operations

Tables

Table 1. Change in price indices and terms of trade

Table 2. Dynamics of changes in the National Bank's assets and liabilities

Table 3. Dynamics of changes in the money supply

Table 4. Dynamics of changes in deposits of residents

Summary

At end-2011, according to the official data provided by the Agency of Statistics of the Republic of Kazakhstan, annual inflation was at 7.4% (in 2010 – 7.8%), i.e. it remained within the boundaries of the target band of 6-8% established by the National Bank for 2011.

The buildup of the inflationary processes in Kazakhstan in 2011 occurred against minimum impact on the part of monetary factors. So, the growth in the money supply in 2011 accounted for 15.0%, reserve money expanded by 10.3%.

The main factors for the inflation growth in 2011 were associated with unstable situation in the global commodity markets, persistent trend of price growth including for the major items of the Kazakhstani exports.

A significant role in the inflation growth was played by the expansion of aggregate demand in the economy as a result of steady growth in the income of the population, particularly the thirty percent increase in retirement benefit payouts and student fellowships from January 1, 2011 as well as the increase in wages to the public sector employees by 30% from July 1, 2011.

High growth rates of the Kazakh economy in 2011 were also conducive to persisting inflationary pressure. At the end of 9 months the country's real GDP growth accounted for 7.2%; with the positive dynamics in virtually all sectors, agriculture, communication and trade should be mentioned specifically.

The inflation buildup in 2011 occurred amidst significant increase in the price of foodstuffs by 9.1% during the period (in 2010 – by 10.1%); there was a notable increase in prices for meat and meat products – by 23.2% as well as cereals – by 43.3%.

The National Bank has been taking actions pursuant to the Monetary Policy Guidelines for 2011 aimed at achieving the main goal of ensuring the price stability, as well as accomplishing its top priority mission – ensuring stability of the Tenge exchange rate and stability of the country's financial sector.

Given some acceleration of inflation at the beginning of 2011 as well as with a view to influence the inflationary expectations, the National Bank made the decision to increase the official refinancing rate to 7.5% from March 9, 2011. Hereafter during 2011 the official refinancing rate as well as interest rates on bank deposits with the National Bank remained unchanged.

From May 31, 2011 the minimum reserve requirements on the bank domestic liabilities were increased to 2.5% and on other bank liabilities – to 4.5% (previously – 1.5% and 2.5%, respectively).

As part of its effort to ensure the domestic currency stability, the National Bank monitors the situation with the exchange rate of the Tenge on an ongoing basis. On February 28, 2011 the transition to the managed floating exchange rate regime of the Tenge was accomplished and since then the situation in the domestic foreign exchange market has been stable.

At the same time unstable situation in the global stock markets was impacting the foreign currency market players in Kazakhstan. This was accompanied by some volatility of the exchange rate of the Tenge versus the US Dollar. Alongside with that, some appreciation of the Tenge versus the US Dollar was observed in the first half of 2011 and some depreciation of the Tenge – in the second half of the year.

The National Bank regulates short-term money market liquidity by issuing short-term notes and taking deposits from banks. The volumes of these operations in the 4th quarter of 2011 decreased as compared to the previous quarters of the year and demonstrated an overall

decrease during the year versus the respective indicators for 2010: the issue of short-term notes decreased by 10.0%, and the volume of deposits taken from banks – by 22.0%.

The National Bank also provides refinancing loans to support current liquidity of banks, with their demand remaining limited.

Evaluation of the Inflation Forecasts for the 4th Quarter of 2011 and for 2011 as a Whole

The actual inflation rate (1.1%) in the 4th quarter of 2011 was lower than the forecast (1.5-1.7%) published in the previous issue of the Inflation Report. The inflation has been lower than the forecast throughout the 4th quarter of 2011.

In the 4th quarter of 2011 there was an even price growth in all group of goods. In their structure, the increased prices for meat products, eggs, education services and utility services should be pointed out. When analyzing the dynamics of the past years, one may note that the growth in prices for such goods and services is typical for such period of the year.

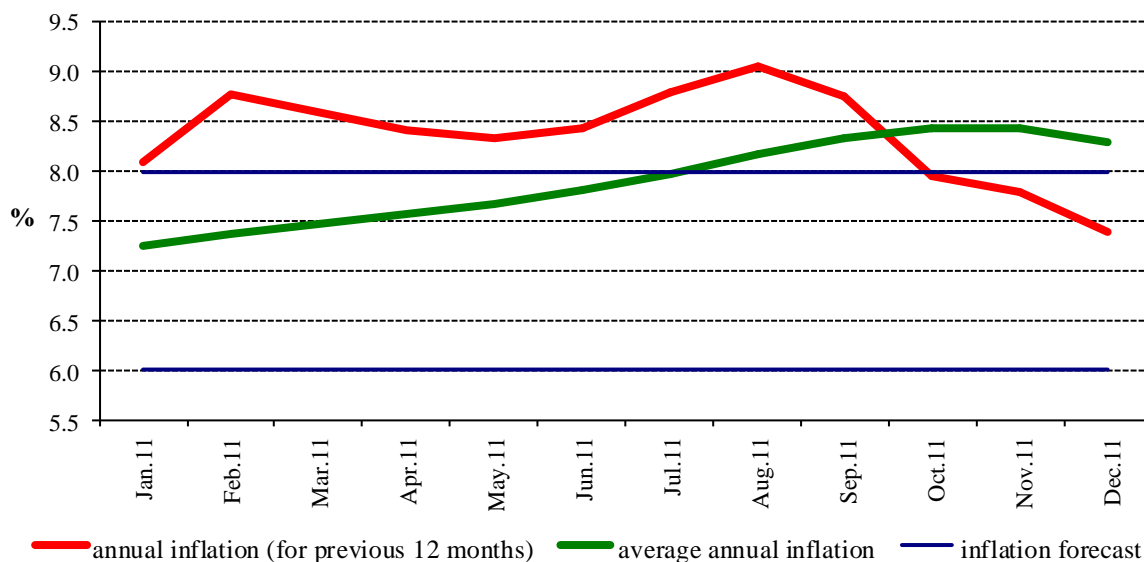
As a whole in 2011, the buildup of inflation process in Kazakhstan was influenced by the increase in prices for foodstuffs and paid services to the population. The growth rates of prices for non-food items were moderate in 2011.

The highest growth rates were observed in prices for such goods and services as cereals (buckwheat, millet), meat and meat products, fuel and lubricants, education and communication services.

The actual annual inflation rate at end-2011 (7.4%) was within the target band of 6-8% established by the National Bank (Figure 1).

Figure 1

Actual and forecasted inflation in 2011



Source: National Bank of the Republic of Kazakhstan

Inflation Forecast for 2012

In 2012 the situation in the consumer market will remain generally stable. Alongside with that the inflationary processes will be building up amidst the growing aggregate demand in the economy. The production growth in the real economy, a stable growth in the cash income of the population, decreased unemployment, and gradual recovery of the lending

activity in the banking sector will be conducive to that fact. Moreover, a low level of competition in certain markets of goods and services will have a negative impact on the buildup of inflationary processes.

Despite the remaining minimal impact of monetary factors on the inflation, price stability in the Kazakh consumer market will still represent the key focus of the monetary policy of the National Bank and will be ensured by the joint efforts of the National Bank and the Government. The target band of the National Bank for inflation is 6-8% at end-2012.

The National Bank, while possessing all necessary instruments, will achieve this goal with appropriate monetary policy measures. Monetary policy of the National Bank will be adequate to the evolving macroeconomic conditions. Money supply in the economy will remain at the level consistent with the growth of the economy.

The interest rate policy of the National Bank will be aimed at maintaining the market rates in the money market of short-term instruments within National Bank's interest rate band.

Measures of the National Bank in the area of foreign exchange policy will be aimed at preventing dramatic fluctuations of the real exchange rate of the domestic currency, which may have a negative impact on the competitiveness of the domestic output in the ever-changing global competitive environment. The National Bank will seek to further reduce its participation in the foreign exchange market with a view to enhance the flexibility of the Tenge exchange rate.

The Inflation Forecast for the First Quarter of 2012 is 2.0-2.2% (in the 1st quarter of 2011 the actual inflation was 3.7%). Generally, this level corresponds to the inflation trends of January-March, which were typical of the past years. Such expectations are associated mainly with the fact that the inflation in the nearest future will be building up under the impact of the seasonality factor.

At end-March 2012 the annual inflation is expected to be within 5.6-5.8%.

The Inflation Forecast for the Second Quarter of 2012 is 1.4-1.6% (in the 2nd quarter of 2011 the actual inflation was at 1.3%), which corresponds to the annual inflation of 5.9-6.1% at end-June 2011.

In April-June 2012 a decrease in prices for certain foodstuffs such as eggs, dairy products, fruits and vegetables, meat products, and education services, is expected.

1. Inflationary Processes

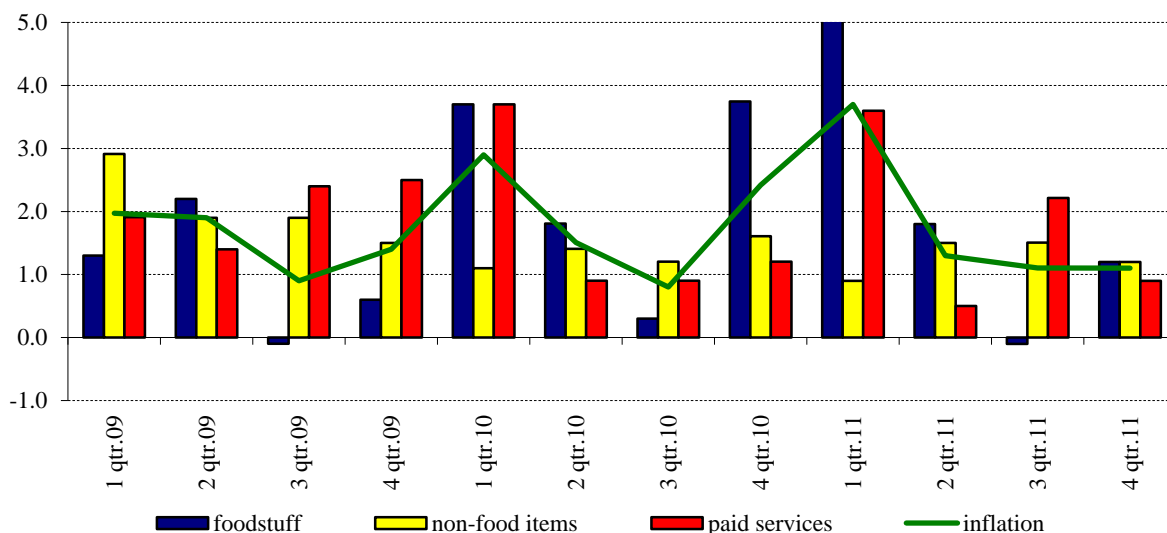
1.1. Consumer Prices

In the 4th quarter of 2011 the inflation was building up mainly under the impact of the price growth for foodstuff and non-food items. As a whole, the inflation in the 4th quarter of 2011 was at the level of the 3rd quarter of 2011 i.e. it made up 1.1% for the quarter. At the same time, the inflation remains relatively low as compared to the 4th quarter of 2010 (in the 4th quarter of 2010 – 2.4%).

The unchanged inflation rate in the 3rd quarter of 2011 versus the previous quarter was accounted for by the increased prices for foodstuffs by 1.2%, non-food items – by 1.2% and the rise in tariffs for paid services by 0.9% (Figure 2).

Figure 2

Dynamics of quarterly inflation and its components (as % of the previous year)



Source: Agency of Statistics of the Republic of Kazakhstan

In the 4th quarter of 2011 in the structure of foodstuff a significant increase was demonstrated in the prices for eggs by 10.1%, meat and meat products – by 6.1% including beef – by 8.5%, horse meat – by 7.5%, lamb – by 6.9%, and pork – by 5.3%. In the 4th quarter of 2011 prices for dairy products increased by 3.0%, mainly because of the growth in price for cottage cheese – by 6.1% and kefir – by 3.3%. During the reviewed period prices for sugar dropped significantly by 23.6%, which appeared to be a favorable factor for the producers of confectionery products. Also, prices of cereals decreased by 9.9%, price of wheat – by 5.3%, rice – by 3.7% and fruits and vegetables – by 3.6%.

In the 4th quarter of 2011 in the group of non-food items prices of clothes and footwear increased by 1.4%, domestic goods – by 1.0%, medications – by 1.1%. After significant growth in prices for fuel and lubricants during the three quarters of 2011, in the 4th quarter of 2011 their price growth was minor. So, the price of gasoline increased by 1.1% and of diesel fuel – by 0.6%.

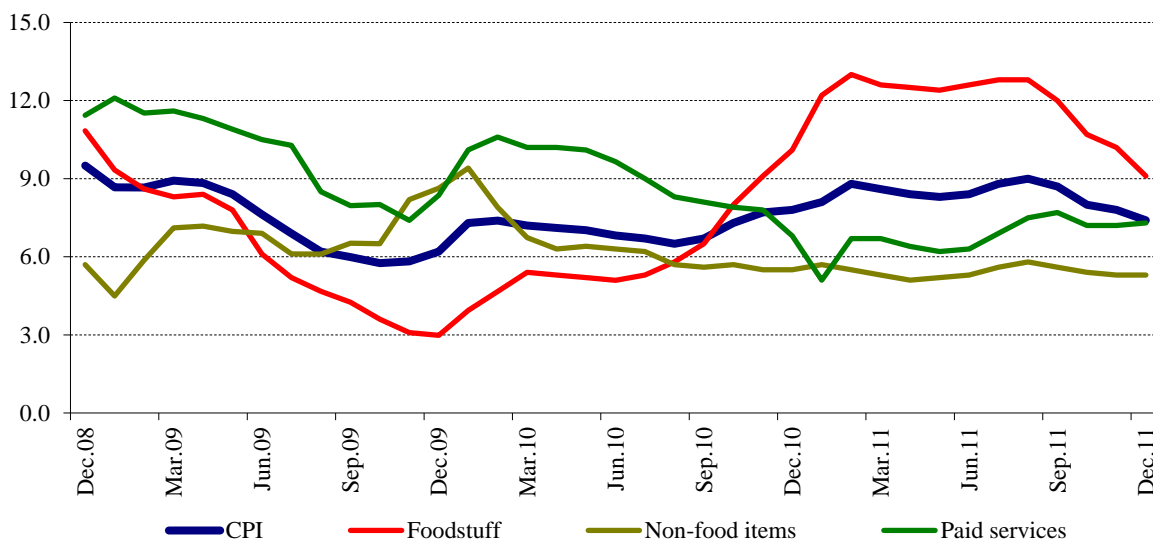
The slowdown in the growth of tariffs in the group of paid services is also worth mentioning. Utility services increased by 1.1% (in the 3rd quarter of 2011 – by 1.5%),

including collection of waste – by 9.3% (by 2.8%), solid fuel – by 5.9% (by 1.2%), housing costs – by 2.6% (by 0.0%).

At end-December 2011 the annual inflation accounted for 7.4% (in December 2010 – 7.8%). In 2011 annual inflation was building up mainly because of the increasing foodstuff prices. Foodstuff prices increased by 9.1% (by 10.1%), prices of non-food items – by 5.3% (by 5.5%), prices of paid services – by 7.3% (by 6.8%) (Figure 3).

Figure 3

**Dynamics of annual inflation and its components
(as % of the respective month of the previous year)**



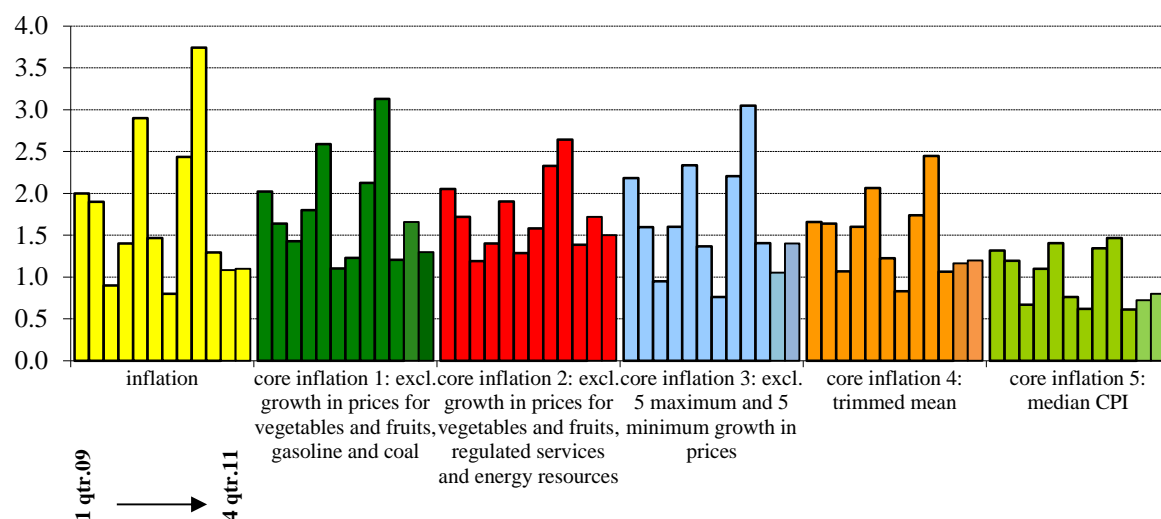
Source: Agency of Statistics of the Republic of Kazakhstan

1.2. Core Inflation

In the 4th quarter of 2011 as compared to the respective quarter of 2010, all core inflation indicators were at a lower level. In doing so, core inflation-1 and core inflation-2 only demonstrated lower growth rates as compared to the previous quarter (Figure 4).

Figure 4

Dynamics of quarterly inflation and core inflation (as % of the previous period)



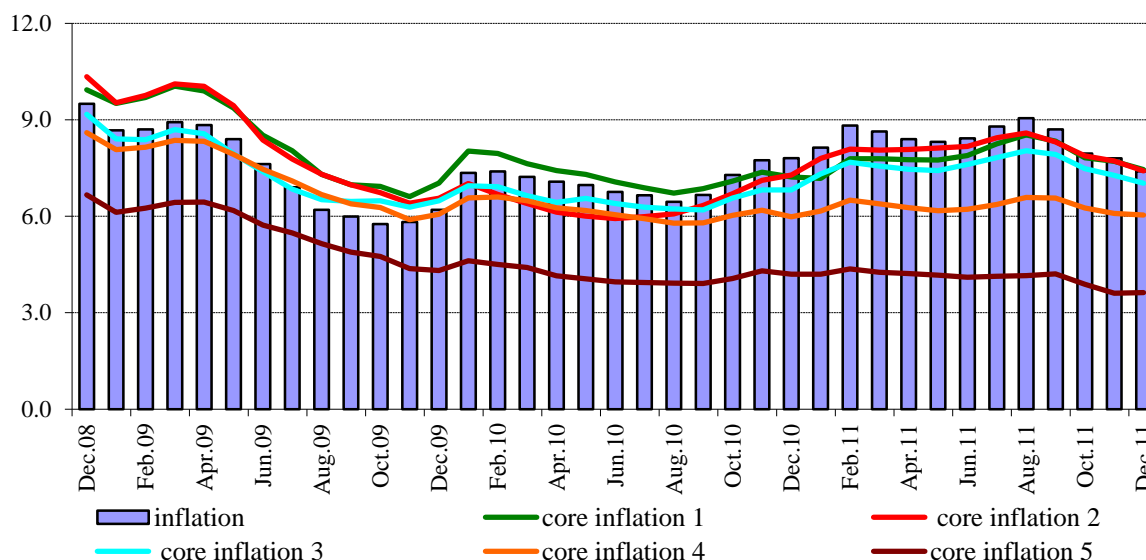
Source: Agency of Statistics of the Republic of Kazakhstan

In October-December 2011 core inflation indicators in annual terms demonstrated a downward trend. Alongside with that, at end-December 2011 core inflation-1 and core inflation-2 indicators were somewhat higher than the headline inflation whereas other core inflation indicators had demonstrated lower rates.

In December 2011 all core inflation indicators in annual terms were at a higher level as compared to their values in December 2010, except for core inflation-5. This speaks for the remaining inflationary background in the economy, with insignificant impact of monetary factors on the inflation (Figure 5).

Figure 5

**Dynamics of annual inflation and core inflation
(as % of the respective quarter of the previous year)**



Source: Agency of Statistics of the Republic of Kazakhstan

1.3. Prices in the Real Sector of the Economy

1.3.1. Prices in the Industry

In the 4th quarter of 2011 the producer prices have decreased by 0.3% (in the 4th quarter of 2010 – the growth by 9.3%). The cost of output depreciated by 0.2%, at the same time in its composition the price of interim consumption products decreased by 0.1%, the price of production means increased by 0.6%, and the price of consumer goods decreased by 1.3%. The prices for production services increased by 0.5%.

In October-December 2011 the producer prices in the mining industry increased. After their growth in the 1st quarter of 2011 by 16.1%, and in the 2nd quarter of 2011 – by 9.6% and the decrease in prices in the 3rd quarter of 2011 by 1.0%, in the 4th quarter of 2011 prices increased by 0.9% (in the 4th quarter of 2010 the growth accounted for 11.1%).

In the 4th quarter of 2011 the cost of energy resources, after its decrease in the previous quarter by 1.2%, increased by 0.6% (in the 4th quarter of 2010 – the growth by 10.2%). In the composition of energy resources, the cost of oil extraction increased by 0.7% (in the 4th quarter of 2010 – the growth by 13.0%), and the cost of gas condensate remained unchanged (the decrease by 4.9%).

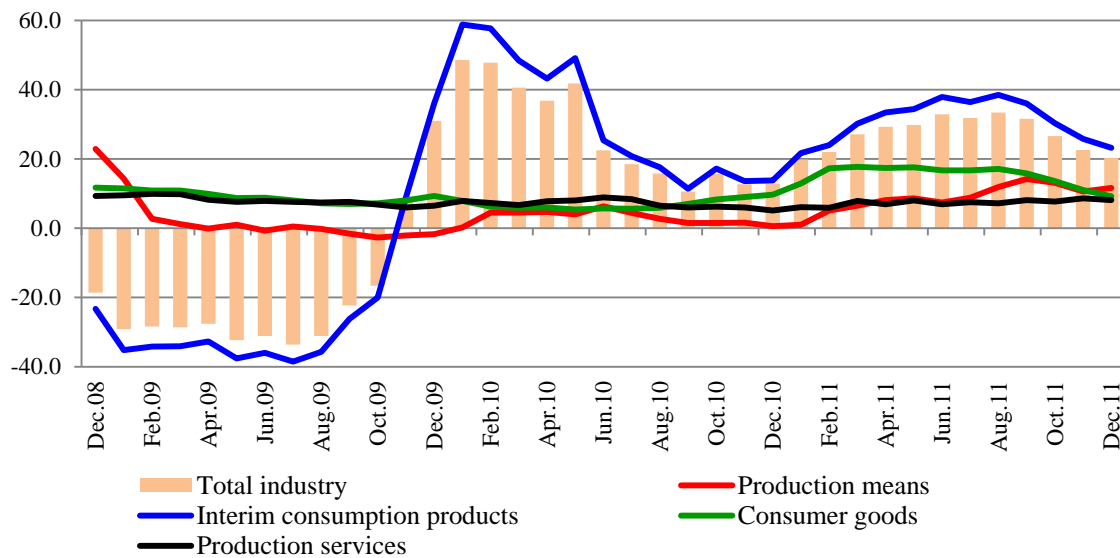
Prices in the manufacturing industry, after their growth in the 3rd quarter of 2011 by 1.4%, decreased by 3.0% in the reporting period (in the 4th quarter of 2010 – the growth by 7.2%). Prices in the metallurgical industry decreased by 6.4%, the cost of foodstuff production depreciated by 4.7%, and the oil refined products increased in price by 0.9%.

The prices for electric energy, gas and vapor supply and air conditioning in the 4th quarter of 2011 didn't change and remained at the level of the previous quarter (in the 4th quarter of 2010 the decrease in prices accounted for 0.4%).

In December 2011 the price growth in the industrial production in annual terms (December 2011 versus December 2010) was 20.3% (Figure 6).

Figure 6

**Dynamics of the producer price index
(as % of the respective month of the previous year)**



Source: Agency of Statistics of the Republic of Kazakhstan

The cost of output increased by 21.3% in annual terms, including the interim consumption products – by 23.2%, consumer goods – by 9.2%, production means – by 11.6%. The cost of production services increased by 8.1%.

1.3.2. Prices in Agriculture

In the 4th quarter of 2011 prices for agricultural production realized across all channels decreased by 8.6% (in the 4th quarter of 2010 – the growth by 21.2%). The dynamics of prices in agriculture was impacted by the decrease in the price for plant production.

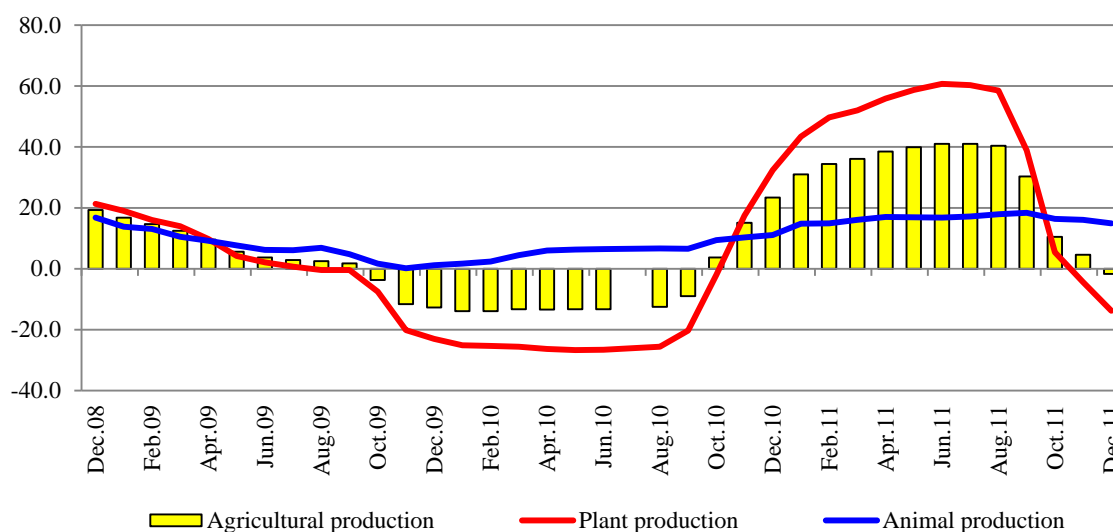
During October-December 2011 the cost of plant production depreciated by 18.8% (in the 4th quarter of 2010 – the growth by 30.7%), alongside with that in the composition of plant production prices for grain cultures decreased by 20.1%, the price of vegetables decreased by 11.3%, and of potatoes – by 16.2%.

In the 4th quarter of 2011 the price of animal products increased by 5.0% whereas in the 1st quarter of 2011 the growth reached 7.7%, in the 2nd quarter of 2011 the decrease by 0.8% was observed and in the 3rd quarter of 2011 the growth was demonstrated again – by 2.6% (in the 4th quarter of 2010 the growth reached 8.0%). During October-December 2011 prices for meat and poultry increased by 3.2%, the price for unpasteurized milk increased by 7.6%, and the price of eggs increased by 10.9%.

At end-December 2011, prices for agricultural products decreased by 1.7% in annual terms. Alongside with that, the price of plant production decreased by 13.8%, and the price of animal products grew up by 14.9% (Figure 7).

Figure 7

**Dynamics of the agricultural price index
(as % of the respective month of the previous year)**



Source: Agency of Statistics of the Republic of Kazakhstan

1.3.3. Enterprise Monitoring

In the 4th quarter of 2011 the growth rates in the demand for final products of enterprises continued to decline in the real sector of the economy as a whole. This is evidenced by the diffusion index of the change in the demand for final products which went down to 52.8 (from 54.5 in the 3rd quarter of 2011). The indicator decreased because of a notable increase in the share of enterprises with the decreased demand for their products to 19.6% (from 16.3% in the 3rd quarter of 2011).

The lowest growth rates in the demand were observed in such sectors as construction (50.2), in the manufacturing industry and trade (both – 51.2). The highest growth in the demand is noted by enterprises in the sector of “production and distribution of electric energy, gas and water” where the diffusion index went up to 66. The demand was growing at a more moderate rate in the manufacturing industry and the sector of “transport and communication” (the diffusion index was about 56).

In the 1st quarter of 2012 as compared to the 4th quarter of 2011 the overall demand in the real sector of the economy is not expected to change: the diffusion index of the change in the demand was 50.4. The growth in the demand is expected in the agricultural sector and the sector of “production and distribution of electric energy, gas and water”, and the decrease – in trade, manufacturing industry and in the sector of “hotels and restaurants”; a slowdown in the growth rate of demand in the rest of the sectors is anticipated.

The growth rates of prices for final products of enterprises in the 4th quarter of 2011 continued to decrease: the diffusion index of the change in prices for final products went down to 56.1 (from 58.2 in the 3rd quarter of 2011) due to the decreased number of enterprises that noted the increase in prices to 19.6% (from 24.9% in the 3rd quarter of 2011).

The decreased rates of growth in prices for final products are observed in all sectors of the economy, except agriculture where increased growth rates were observed. The highest decrease in the growth rates of prices occurred in the manufacturing industry where the prices remained unchanged versus the 3rd quarter of 2011 (the diffusion index was 50.0). The highest growth in prices was observed in trade.

In the 1st quarter of 2012 a notable growth in prices is expected in the real sector of the economy as a whole: the diffusion index of the change in prices for final products was 59.4. The increase in the growth of prices is anticipated by enterprises in all industries, with the highest increase in the price growth rates being anticipated in the manufacturing industry, trade and in the sector of “hotels and restaurants”.

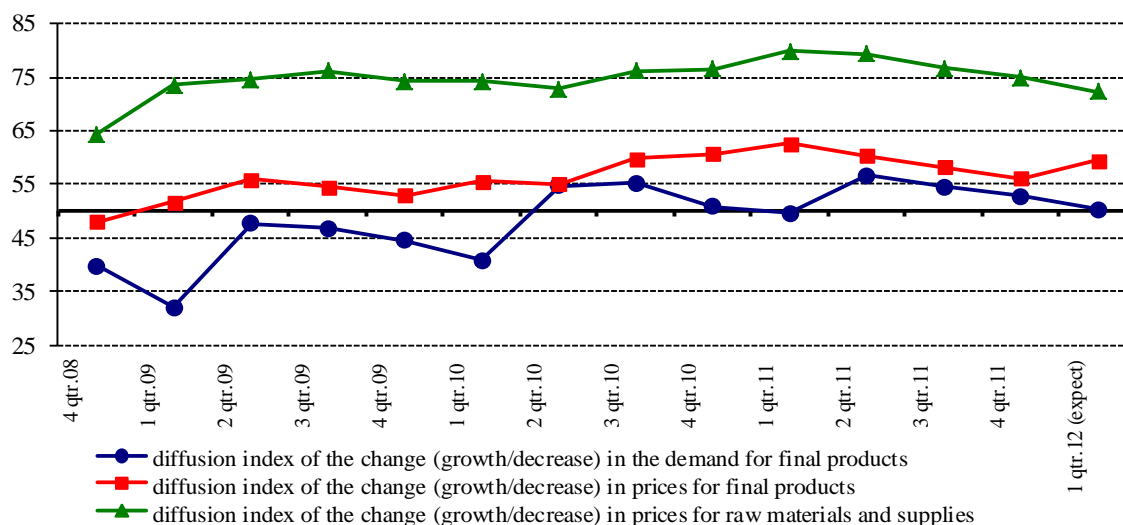
In the 4th quarter of 2011, despite the slowdown in the growth rates, prices for raw materials and supplies remain high: the diffusion index of the change in prices for raw materials and supplies was 75.0 (in the 3rd quarter – 76.8). A minor increase in the price growth rates was noted in such sectors as “production and distribution of electric energy, gas and water” and in the “manufacturing industry”, and the decrease – in all other sectors. In the sample as a whole, the number of enterprises that noted the growth in prices for raw materials and supplies amounted to 52.4%, and only 2.4% of enterprises noted the decrease in prices.

For the 1st quarter of 2012 the diffusion index of the change in prices for raw materials and supplies fell down to 72.4 indicating a notable decrease in the price growth. The indicator decreased due to a notable decrease in the percentage of enterprises that anticipate the price growth.

Thus, judging from the dynamics of the relevant diffusion indices, anticipations of the enterprises about the 1st quarter of 2012 are associated with the unchanged demand for final products, some slowdown in the growth of prices for raw materials and supplies and a notable growth in prices for final products (Figure 8).

Figure 8

Diffusion indices of the change in demand and prices



Source: National Bank of the Republic of Kazakhstan

2. Inflation Factors

2.1. Aggregate Demand

In the 3rd quarter of 2011 the GDP based on the final consumption method as compared to the respective period of 2010 increased in real terms, according to estimate, by 7.1% (the growth in the 3rd quarter of 2010 was estimated at 2.5% and in the 2nd quarter of 2011 – 7.9%).

The GDP growth in the 3rd quarter of 2011 was driven by the increased spending on final consumption stipulated by increased household spending on current consumption and government current consumption as well as the growth in gross formation and decreased net exports.

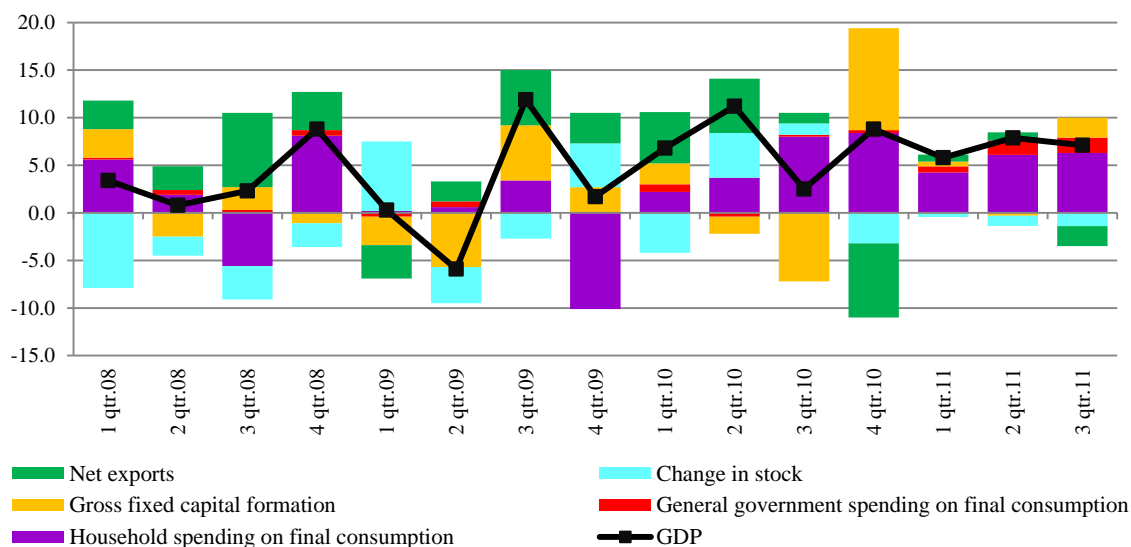
In total, according to estimate, spending on final consumption increased by 12.0% (the 2nd quarter of 2011 – the growth by 12.1%), gross formation increased by 3.8% (the decrease by 7.9%) and net exports decreased by 19.1% (the growth by 6.5%).

As a result, household and government spending on consumption made positive contribution to the growth of GDP formation of (+)6.3% and (+)1.6%, respectively, and gross formation increased the GDP by (+)0.7%.

Alongside with that, in the composition of gross formation fixed capital formation accounted for (+)2.1% and changes in stock – for (–)1.4%. In its turn, net exports made negative contribution to the GDP growth of (–)2.1% (Figure 9).

Figure 9

Contribution of components of aggregate demand to the growth in GDP, %



Source: Information of the Agency of Statistics of the Republic of Kazakhstan, estimates by the National Bank of the Republic of Kazakhstan

2.1.1. Individual Consumption and Investment Demand

Household spending on final consumption in the 3rd quarter of 2011 increased versus the respective period of 2010 by 9.6% (in the 2nd quarter of 2011 – the growth by 10.1%).

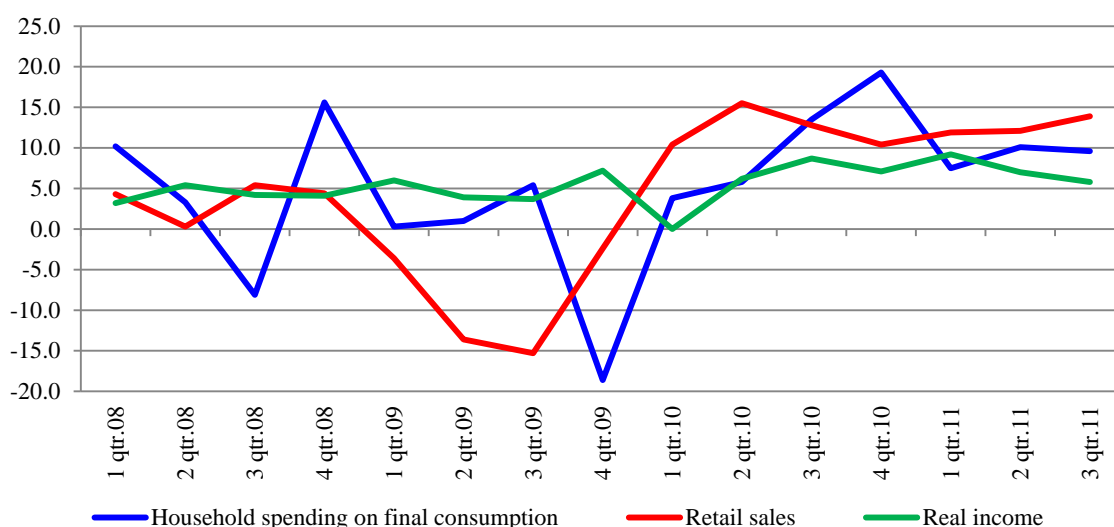
The growth rate of per capita income in nominal terms in the 3rd quarter of 2011 slightly slowed down to 15.2% (in the 2nd quarter of 2011 – the growth by 16.0%) and in real

terms – to 5.8% (the growth by 7.0%). However, such slowdown in the growth rates of per capita income didn't have a significant impact on retail sales whose growth rate accelerated from 12.1% to 13.9% versus the 2nd quarter of 2011.

A high growth rate of the retail sales had a significant impact on the improvement of one of the key GDP components by the final consumption method, namely the growth in the household spending on final consumption, which increased by 9.6% (in the 2nd quarter of 2011 – the growth by 10.1%) (Figure 10).

Figure 10

Dynamics of personal spending and income
(as % of the respective period of the previous year)



Source: Information of the Agency of Statistics of the Republic of Kazakhstan, estimates by the National Bank of the Republic of Kazakhstan

In the 3rd quarter of 2011 the population had more preference to buying in the markets and from individual entrepreneurs where selling volumes increased by 16.7% in nominal terms, whereas sales in the shopping centers increased by 2.8% only.

It should be noted that if in the 1st quarter of 2011 the increase in the cash income of the population (the increase of the amounts of retirement benefits, allowances) served as the driver for the growth in retail sales, in the 2nd quarter of 2011 the growth in credits to the population was conducive to it, and in the 3rd quarter of 2011 the slowdown in the growth rates of lending was offset by the 30% increase in wages to the public sector employees from July 1.

After the decline in the lending activity in the 1st quarter of 2011 by 0.2%, lending increased by 4.7% in the second quarter, and in the third quarter its growth rate slowed down to 2.3%. Alongside with that the growth of consumer lending slowed down in the 3rd quarter of 2011 to 2.7% (the 2nd quarter of 2011 – the growth by 8.0%).

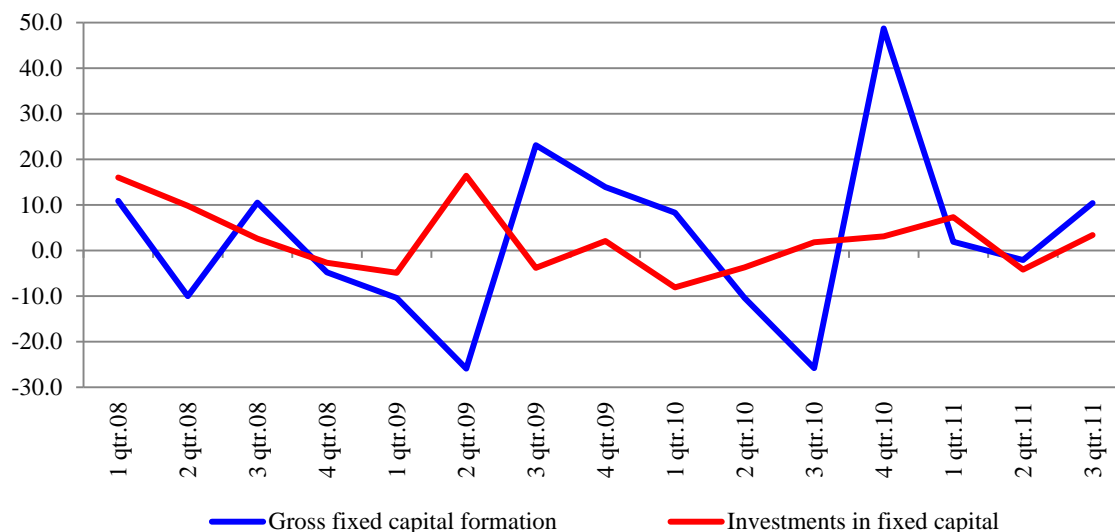
The volume of spending on gross formation, after its decline in the 2nd quarter of 2011 by 7.9%, increased by 3.8% in the 3rd quarter of 2011, thus making positive contribution to the growth in the GDP formation of (+)0.7%.

In the structure of gross formation, gross fixed capital formation increased by 10.4%, making positive contribution to the GDP growth of (+)2.1%, at the same time the second component, i.e. the change in stock, made negative impact thus reducing the GDP growth by (-)1.4%.

The growth in the investment activity of enterprises was conducive to the increase in gross formation in the 3rd quarter of 2011, resulting in the increased volume of investments in fixed capital over the quarter by 3.4% (the 2nd quarter of 2011 – the decrease by 4.2%) (Figure 11).

Figure 11

**Dynamics of spending on investments in fixed capital
(as % of the respective period of the previous year)**



Source: Information of the Agency of Statistics of the Republic of Kazakhstan, estimates by the National Bank of the Republic of Kazakhstan

2.1.2. Government Consumption

Spending on final consumption by the general government in the third quarter of 2011 as compared to the respective period of 2010 increased by 23.9% (in the 2nd quarter of 2011 – the growth by 18.7%).

In total, in the 3rd quarter of 2011 the state budget spending was financed in the amount of KZT 2386.2 bln. or 13.1% of GDP (increased by 2.1 times versus the 3rd quarter of 2010).

Current state budget expenditures totaled to KZT 1.0 trln. which is by 20.8% greater than in the 3rd quarter of 2010. Within the current expenditures the following items demonstrated significant increase as compared to the respective quarter of 2010: costs related to current transfers abroad (by 2.6 times), interest payments on domestic loans (40.4%), other current costs (30.1%), wages (30.0%), current transfers to legal entities (25.7%), current transfers to individuals (25.5%) and employer contributions (25.2%). There were no costs related to other current transfers in the 3rd quarter of 2011, just like in the 2nd quarter of 2011.

In the 3rd quarter of 2011 capital state budget expenditures increased by 12.8% as compared to the respective period of 2010, mainly because of the increase in expenditures on the acquisition of fixed capital and acquisition of land and intangible assets. Expenditures related to capital transfers abroad and domestic transfers didn't change during the 3rd quarter of 2011.

Budget credits in the 3rd quarter of 2011 increased as compared to the 3rd quarter of 2010 by 3.1 times, expenditures on financial asset acquisitions decreased by 37.6%.

During July-September 2011 state budget revenues amounted to KZT 1466.6 bln. or 8.1% of GDP, which is by 13.5% greater than in July-September 2010. In the structure of the state budget revenues two items are still prevailing: tax revenues – 71.5% (in the 3rd quarter of 2010 – 74.1%), and official transfers – 26.2% (21.9%). High percentage of official transfers was secured by the receipt of the guaranteed transfer from the National Fund of the Republic of Kazakhstan to the republican budget in the amount of KZT 360.0 bln.

As a whole, in the third quarter of 2011 tax revenues increased by 38.1% as compared to the third quarter of 2010. The growth was ensured by the increased revenues in absolute terms from corporate income tax, value-added tax and revenues from the use of natural and other resources by KZT 58.4, 79.1 and 23.3 bln., respectively.

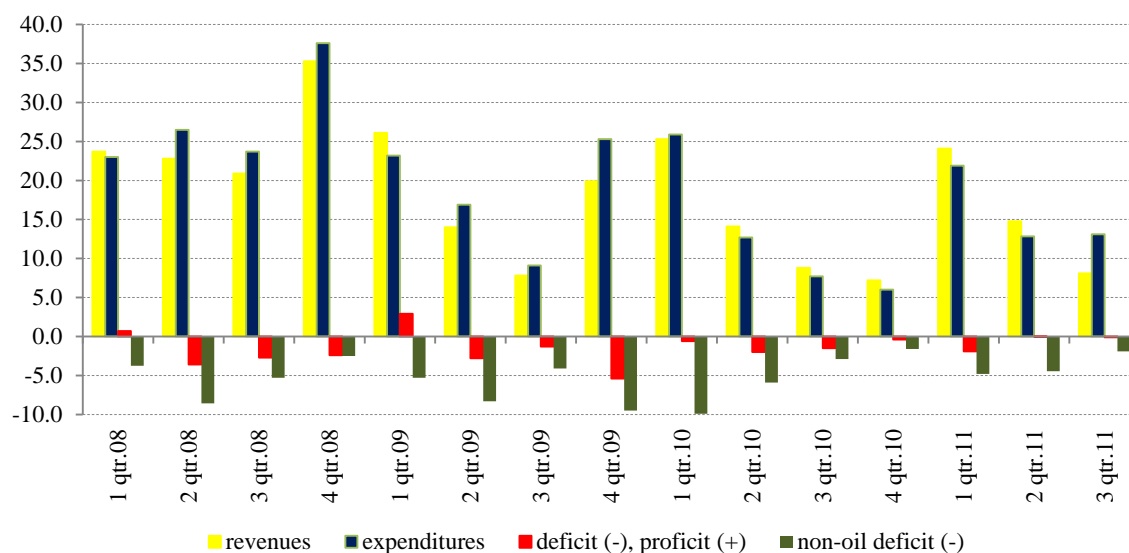
In the 3rd quarter of 2011 as compared to the 3rd quarter of 2010 the volume of received transfers increased by 71.4%, non-tax revenues – by 25.9% whereas revenues from fixed capital sales decreased by 54.0%.

Since the expenditures were in excess of revenues to the state budget in the third quarter of 2011, the deficit of KZT14.4 bln. showed up whereas in the respective quarter of 2010 the deficit was KZT 243.3 bln. (1.7% of GDP) (Figure 12). It should be noted that without the guaranteed transfer of KZT 360.0 bln. to the republican budget from the National Fund, the 3rd quarter of 2011 would have ended with the non-oil deficit of KZT 345.6 bln..

During the 3rd quarter of 2011 the Ministry of Finance borrowed KZT 196.4 bln., mainly by issuing government issue-grade securities. During the same period debentures were also extinguished on securities issued earlier in the amount of KZT 72.7 bln. As a result, account balances of the Government of the Republic of Kazakhstan with the National Bank increased by KZT 109.4 bln.

Figure 12

State budget execution, KZT bln.



Source: Ministry of Finance of the Republic of Kazakhstan, estimates by the National Bank of the Republic of Kazakhstan

The government's domestic debt for the 3rd quarter of 2011 increased to KZT 1916.9 bln. (10.5% of GDP), i.e. by 17.2% higher than in the 3rd quarter of 2010 (8.0% of GDP). The growth was secured by the issue of government long-term treasury obligations (MEUKAM), government long-term saving treasury obligations (MEUZHKA) and government medium-term treasury obligations (MEOKAM).

The Government's external debt in the third quarter of 2011 increased by 16.7% as compared to the third quarter of 2010 (3.5% of GDP) and amounted to KZT 595.7 bln. (3.3% of GDP).

2.1.3. External Sector

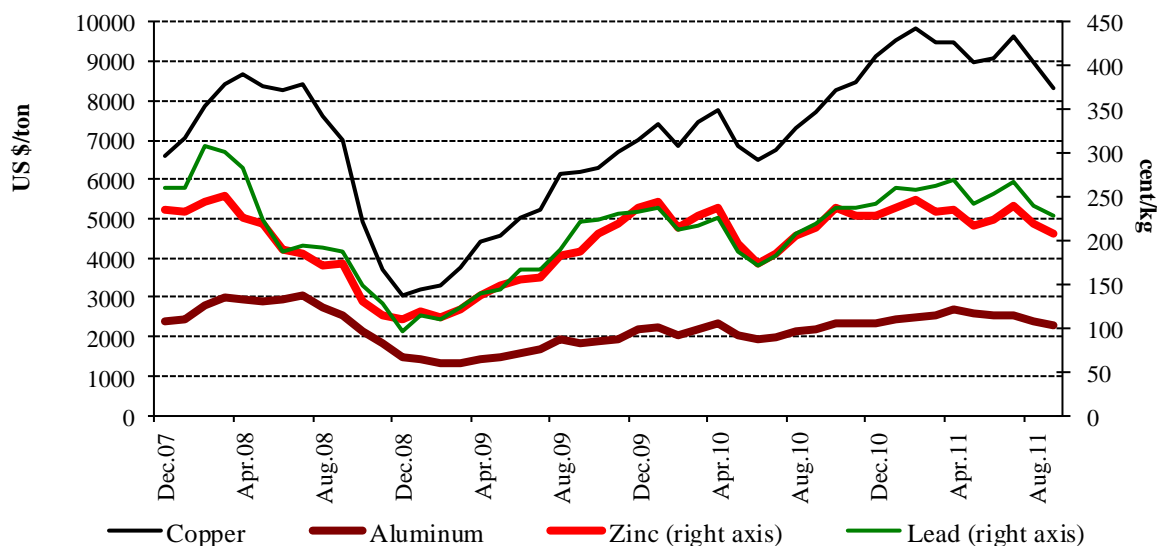
– World prices

In the 3rd quarter of 2011 the situation in the global commodity markets remained unstable, which was accompanied by volatility of prices for certain commodities.

World prices for metals in July-September 2011 demonstrated a downward trend, which was accompanied by gradual decline in the world prices for metals. Prices for copper in the third quarter of 2011 decreased and were at US\$ 8983.7 per ton on average for the period. Prices for aluminum during the 3rd quarter of 2011 decreased by 8.1% and amounted to US\$ 2399.0 per ton. In July-September 2011 world prices for lead decreased by 3.8% amounting to 245.5 cents per kg on average for the period. Prices for zinc decreased by 1.3% at an average price of 222.4 cents per kg for the period (Figure 13).

Figure 13

Dynamics of world prices for metals

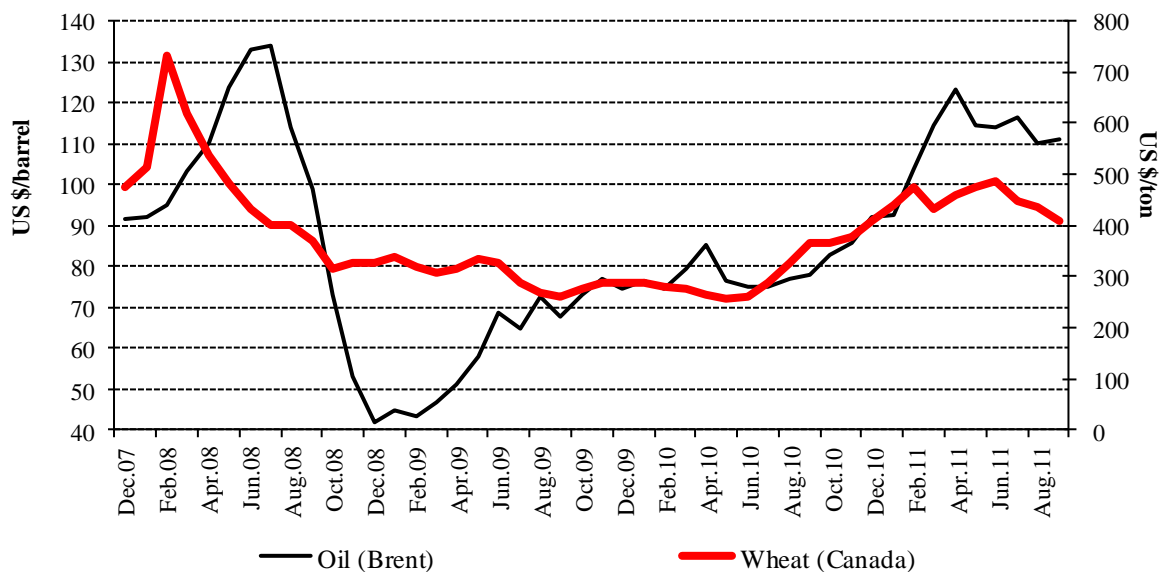


Source: World Bank

In the 3rd quarter of 2011 as compared to the 2nd quarter of 2011, world prices for oil (Brent) decreased by 3.9% and amounted to US\$ 112.5 per barrel on average for the period (Figure 14).

World prices for wheat were gradually decreasing throughout the third quarter of 2011. In the 3rd quarter of 2011 as a whole the world price for wheat (Canada) decreased by 9.4% and was on average at US\$ 429.8 per ton (Figure 14).

Figure 14

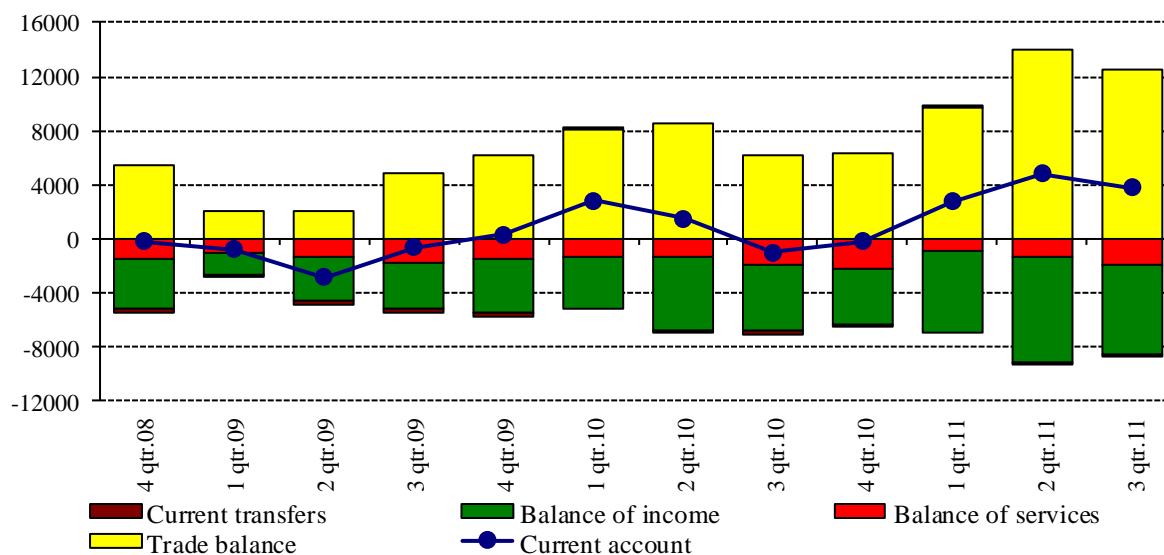
Dynamics of world prices for oil (Brent) and wheat (Canada)

Source: World Bank

– Balance of Payments

At the end of the third quarter of 2011 the current account balance was in surplus of US\$ 3.8 bln. or 7.7,% of GDP for the respective period (Figure 15).

Figure 15

Current account balance, US\$ mln.

Source: National Bank of the Republic of Kazakhstan

Proceeds from the export of goods in the 3rd quarter of 2011 increased by 60.0% and expenditures on commodity imports – by 28.2% as compared to the 3rd quarter of 2010. A positive trade balance increased over 2 times and amounted to US\$ 12.5bln. In the 3rd quarter of 2011 the deficit in the balance of services increased by 1.0% to US\$ 1.9 bln., and the

deficit in the income balance increased by 35.1% and amounted to US\$ 6.7 bln. Net payouts to non-resident on current transfers amounted to US\$ 79.6 mln.

The net outflow of resources on financial account operations in the 3rd quarter of 2011 amounted to US\$ 2.3 bln. (in the 3rd quarter of 2010 – net outflow of US\$ 5.2 bln.). Foreign assets of residents (except for reserve assets) increased by US\$ 3.8 bln., which exceeds the indicator for the respective period of 2010 by 16.3%. Foreign liabilities of residents also increased by US\$ 1.5 bln. (the reduction by US\$ 1.9 bln. in the 3rd quarter of 2010.).

As a result, the negative balance of payments for the 3rd quarter of 2011 amounted to US\$ 1.6 bln. (in the 3rd quarter of 2010 – a positive balance of US\$ 22.8 mln.).

– Terms of Trade and Real Effective Exchange Rate

In the 3rd quarter of 2011 the aggregate terms of trade index was by 39.1% higher than the respective indicator for the 3rd quarter of 2010. Alongside with that, the terms of trade with the Euro zone countries improved by 30.8%, and with Russia – by 30.1% (Table 1).

Table 1

Change in price indices and terms of trade (as % of the respective period of the previous year)

	3 qtr.10	4 qtr.10	1 qtr.11	2 qtr.11	3 qtr.11
Export prices	16.2	18.7	41.1	49.5	55.0
Import prices	2.8	10.3	6.1	17.4	11.6
Terms of trade	16.5	8.0	32.9	29.3	39.1
including:					
The Eurozone countries					
Export prices	18.1	18.2	25.6	47.5	53.3
Import prices	14.0	27.7	6.0	20.3	15.0
Terms of trade	3.7	-8.1	18.8	23.3	30.8
Russia					
Export prices	8.9	9.4	38.2	39.2	53.2
Import prices	7.8	9.2	18.8	27.0	14.3
Terms of trade	1.0	0.3	16.9	10.1	30.1

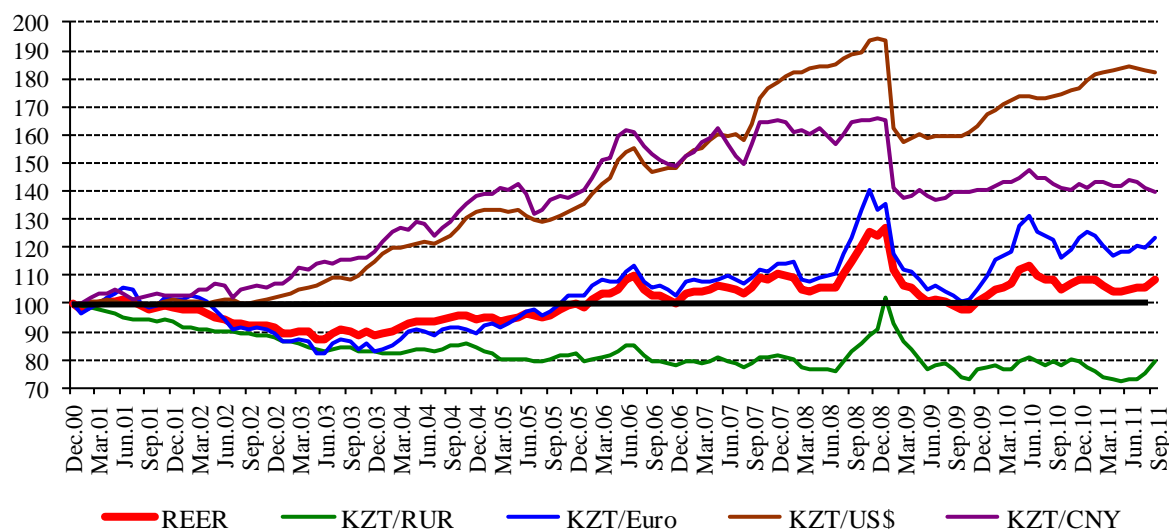
Source: National Bank of the Republic of Kazakhstan

Despite a relatively stable nominal exchange rate, the index of the real effective exchange rate of the Tenge appreciated by 2.0% at the end of the 3rd quarter of 2011 as compared to the previous period. Alongside with that, the Tenge has appreciated versus the CIS currencies basket by 3.7%, and by 1.4% - versus the basket of other currencies.

During the 3rd quarter of 2011 the Tenge depreciated in real terms against the US Dollar by 0.2% as compared to the previous period, against the Euro – appreciated by 2.7% and against the Russian ruble – appreciated by 4.2% (Figure 16).

Figure 16

Indices of real exchange rates of the Tenge (December 2000 = 100%)



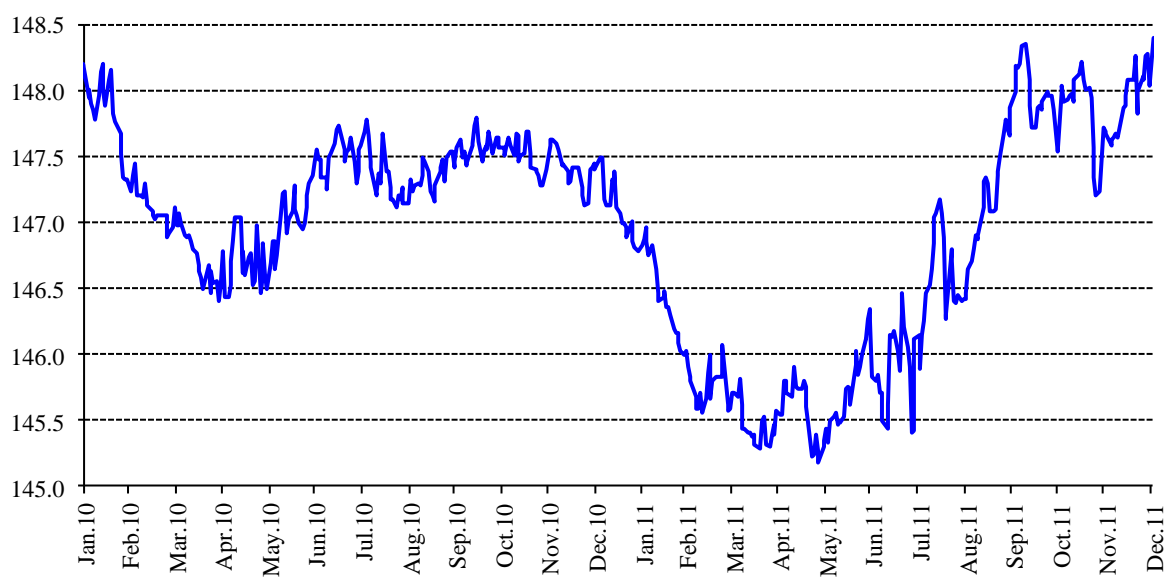
Source: National Bank of the Republic of Kazakhstan

– Nominal Exchange Rate of the Tenge

The average weighted exchange rate of the Tenge for the 4th quarter of 2011 at the stock exchange was KZT 147.94/1US\$. The stock exchange rate at end-period was KZT 148.40/1US\$. Since the beginning of the year the Tenge has depreciated against the US Dollar in nominal terms by 0.6% (Figure 17).

Figure 17

Dynamics of the nominal exchange rate of the Tenge against the U.S. Dollar



Source: National Bank of the Republic of Kazakhstan

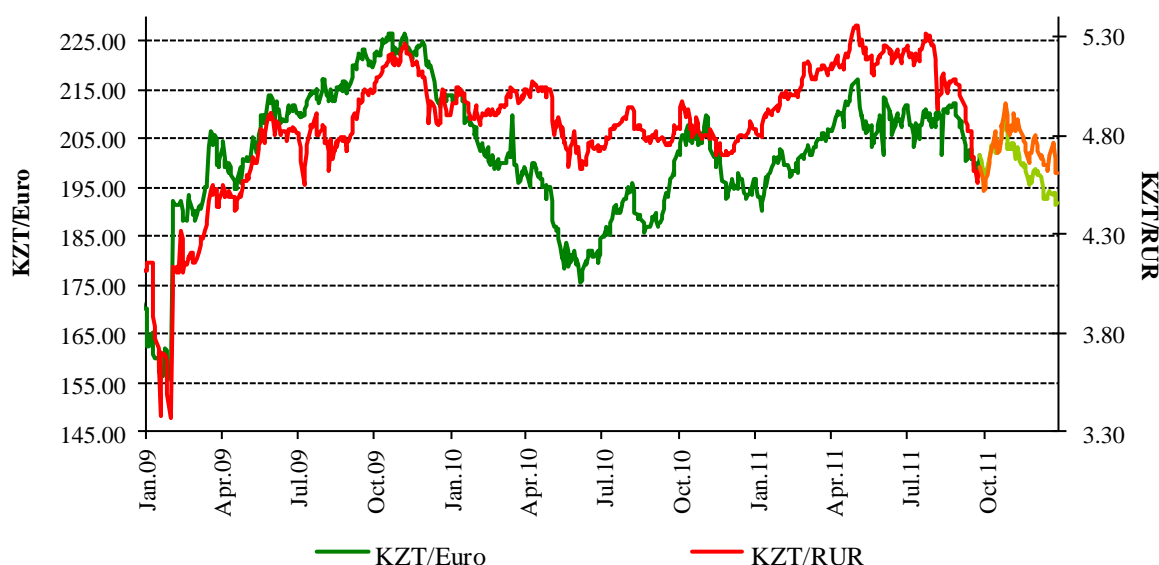
In October and November the exchange rate of the Tenge appreciated versus the US Dollar by 0.1% and in December it depreciated by 0.5%.

Since the transaction volumes in the Euro and the Russian ruble remain insignificant in the stock exchange segment of the domestic foreign exchange market, the exchange rate of the Tenge versus those currencies is calculated based on the cross-rate to the US Dollar. So, the dynamics of the exchange rate of the Tenge versus the Euro and the Russian ruble were driven by the dynamics of the exchange rate of the Tenge versus the US Dollar, the status of the common European currency in the international financial market and the policy implemented by the Central Bank of Russia in respect of the exchange rate of the Russian ruble against the currency basket.

As a whole, during the 4th quarter of 2011 the official exchange rate of the Tenge versus the Euro appreciated by 5.1% and versus the Russian ruble – by 0.6% (Figure 18).

Figure 18

Dynamics of the official exchange rate of the Tenge against the Euro and the Russian ruble



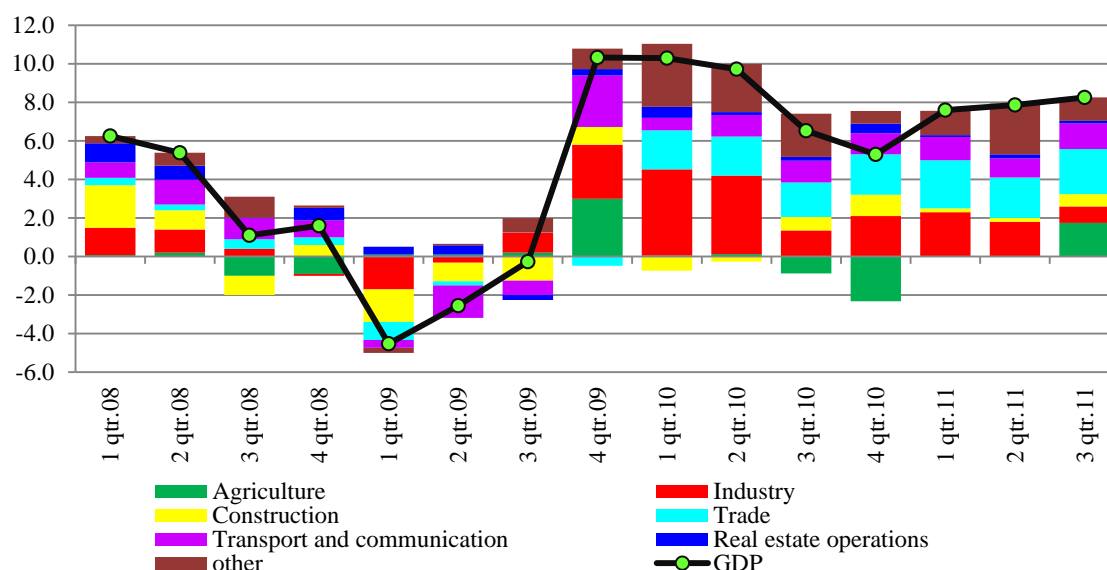
Source: National Bank of the Republic of Kazakhstan

2.2. Production

The volume of GDP output in the third quarter of 2011 amounted to KZT 7226.0 bln. in current prices. Being positively influenced by the growth in production in virtually all sectors of the economy, except financial and insurance activities, the GDP in real terms increased, according to estimates, by 8.3% versus the 3rd quarter of 2010 (in the 2nd quarter of 2011 the growth amounted, according to estimates, to 7.9%) (Figure 19).

Figure 19

**Contribution of key sectors of the economy to growth in real GDP
(as % of the respective period of the previous year)**



Source: Information of the Agency of Statistics of the Republic of Kazakhstan, estimates by the National Bank of the Republic of Kazakhstan

In the production of commodities' segment all key components demonstrated growth. Significant growth was noted in the agricultural sector stipulated by the record crop of grain cultures, also the accelerated growth rates in the construction sector and the slowdown in the industry were observed.

According to estimate, in the 3rd quarter of 2011 the index of physical volume in the industry increased by 3.5% (the 2nd quarter of 2011 – the growth by 5.3%), in agriculture – by 14.3% (1.2%), in construction – by 4.3% (1.1%), which on aggregate resulted in positive contribution to the GDP formation of 3.2%.

In the production of services the decline in financial and insurance activities by 7.2% was fully neutralized by high growth in all other components, which resulted in positive contribution to the GDP formation at the level of 3.7%.

In the 3rd quarter of 2011 the decrease in the volume of financial intermediation services indirectly measured which are used with a negative sign in the total volume of GDP, contributed positively to the GDP formation in the amount of 0.2%.

In its turn, the growth in the index of physical volume of net taxes on products and imports by 14.4% had a significant positive impact on the GDP growth formation of (+)1.1% (in the 2nd quarter of 2011 (-)0.04%).

2.3. Labor Market

2.3.1. Employment and Unemployment

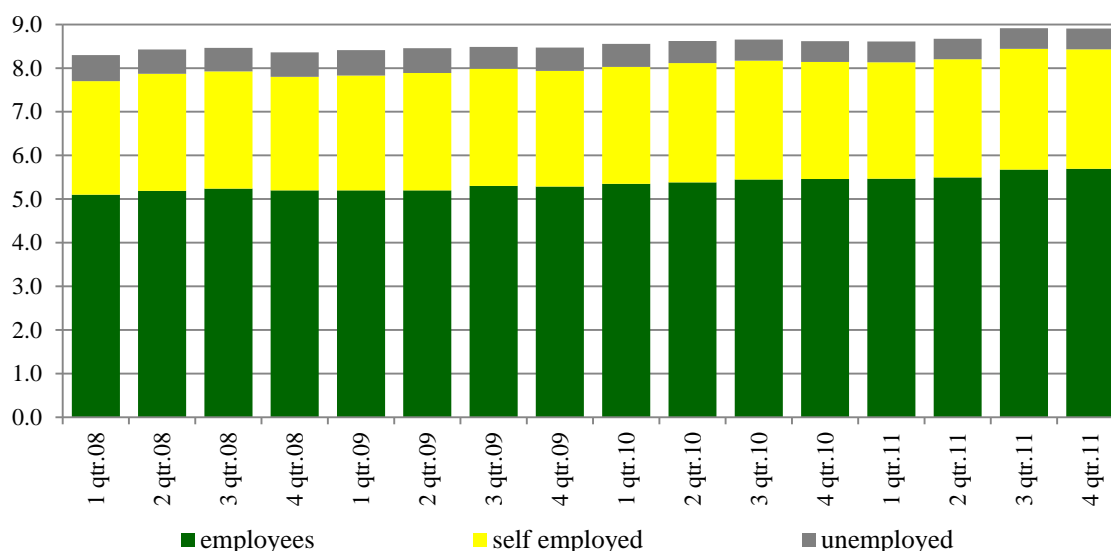
In the 4th quarter of 2011 the number of people employed in the economy, according to tentative estimates, was 8.4 mln., having decreased by 0.2% versus the previous period (the growth versus the 4th quarter of 2010 accounted for 3.5%). At the same time, the number of employees reached 5.7 mln. having increased by 0.4% versus the 3rd quarter of 2011, the number of self-employed – 2.7 mln. people (the decrease by 1.3%).

In the structure of employees, 4.7 mln. individuals (81.8% of all employees) were working in public and non-public institutions, for natural persons – 0.7 mln. individuals (12.2%), at farms – 0.3 mln. individuals (5.7%).

In the 4th quarter of 2011 the number of the unemployed amounted to 477,300 individuals which exceeds the number of the unemployed in the previous reporting period by 1.1% and by 0.5% in the respective period of the previous year (Figure 20).

Figure 20

The structure of economically active population, mln. individuals



Source: Agency of Statistics of the Republic of Kazakhstan

In October-November 2011 the following sectoral changes in the structural composition of employees were observed.

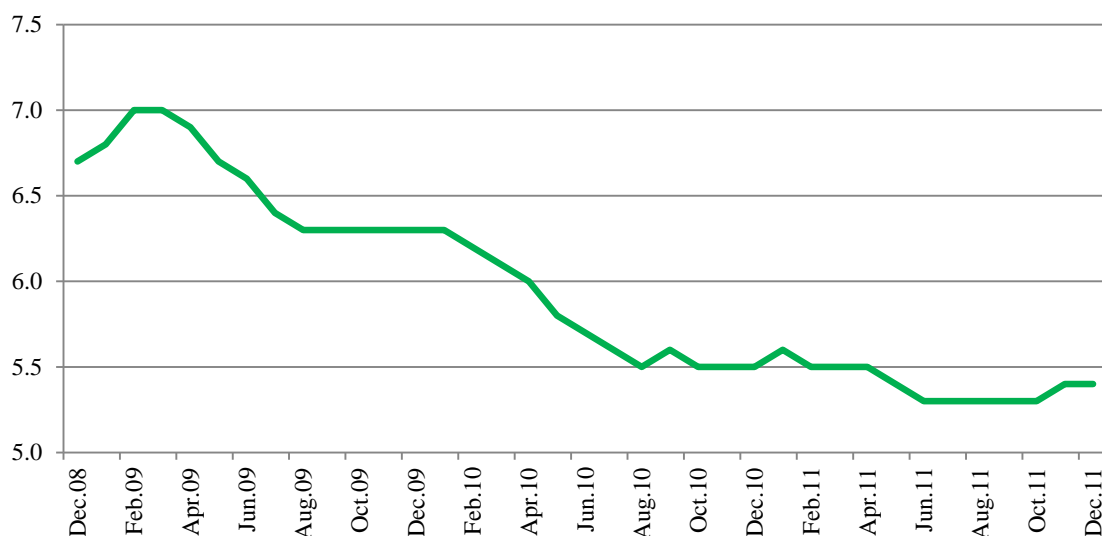
The main sectors that contributed to the growth in the employment rates, as compared to the respective months of 2010, were the following: education; public healthcare and social services; arts, entertainment and recreation; the industry; accommodation and catering services; wholesale and retail trade, repair of cars and motorcycles.

The decrease in the number of the employed was observed in the sectors such as: agriculture, forestry and fishery; general government and defense; mandatory social welfare; real estate operations; water supply; sewage system, control over waste collection and distribution.

The decrease in the number of the employed in some sectors was not fully compensated by their growth in other sectors, whereby the unemployment rate in the 4th quarter of 2011, according to preliminary information, increased from 5.3% in the 3rd quarter of 2011 to 5.4% in the 4th quarter of 2011 (Figure 21).

It should be mentioned in this respect that the Employment Program-2020 which started to be implemented from the 2nd quarter of 2011 had certain impact on the decrease in the unemployment rate and increase of employment among the population.

Figure 21

Actual unemployment rate, %

Source: Agency of Statistics of the Republic of Kazakhstan

2.3.2. Wages and Productivity

In the 3rd quarter of 2011 as compared to the 3rd quarter of 2010 average monthly wages increased in nominal terms by 15.9% (in the 2nd quarter of 2011 – the growth by 9.8%) and by 6.4% - in real terms (the growth – by 1.3%).

As compared to the 2nd quarter of 2011 nominal wages increased by 9.2% and real wages - by 8.0%.

The acceleration of the wage growth rates in the 3rd quarter of 2011 was caused by the 30% rise in wages to the public sector employees from July 1, 2011. As a result, the highest growth in wages in the 3rd quarter of 2011 was observed in July when the wages increased versus the previous quarter by 5.3% in nominal terms and by 4.8% in real terms.

At the end of the 3rd quarter, i.e. in September 2011 as compared to September 2010 the highest increase in nominal wages occurred in the following sectors: education – by 29.8%; public healthcare and social services – by 29.5%; arts, entertainment and recreation – by 28.3%; agriculture, forestry and fishery – by 25.6%; professional, scientific and technical activities – by 24.4%.

The highest wages in money terms were observed in September 2011 in the professional, scientific and technical activities (KZT 181,500) and the lowest – in such sectors as water supply; sewage system, control over waste collection and distribution (KZT 54,600).

Despite a significant GDP growth in the 3rd quarter of 2011 (according to the National Bank's estimate - by 8.3%), the increase in the number of the employed coupled with the wage growth caused the slowdown in the growth rate of the labor productivity index to 4.0% (at the National Bank's estimate), whereas a quarter before the growth in the index reached 6.1% (in the 3rd quarter of 2010 – the growth by 2.4%) (Figure 22).

Figure 22

Dynamics of labor productivity and real wages
 (as % of the respective period of the previous year)



Source: Agency of Statistics of the Republic of Kazakhstan, estimates by the National Bank of the Republic of Kazakhstan

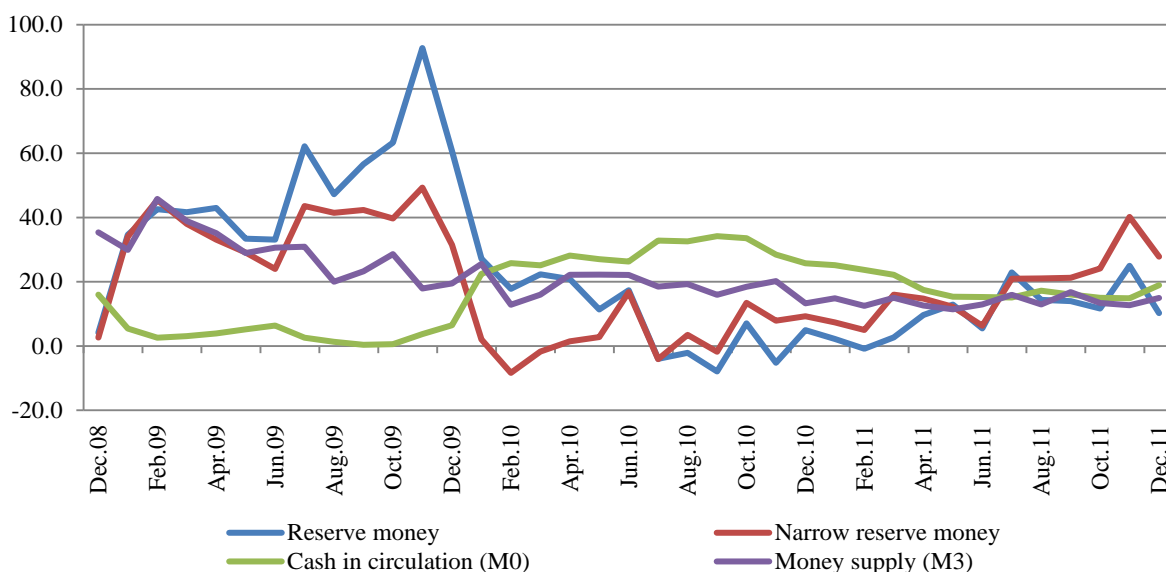
3. Money Supply

3.1. Monetary Aggregates

In the 4th quarter of 2011 the annual dynamics of monetary aggregates demonstrated moderate growth rates (Figure 23).

Figure 23

Dynamics of monetary aggregates
(as % of the respective month of the previous year)



Source: National Bank of the Republic of Kazakhstan

3.1.1. Reserve Money

In the 4th quarter of 2011 reserve money contracted by 1.6% and amounted to KZT 2836.1 bln. at end-December 2011. Narrow reserve money expanded by 4.5% to KZT 2739.3 bln.

During 2011 (December 2011 versus December 2010) reserve money expanded by 10.3%.

During 2011 net international reserves of the National Bank increased by 3.8% and amounted to US\$ 28.8 bln. The growth in the foreign currency balances with correspondent accounts of banks at the National Bank and foreign currency proceeds to the Government's accounts with the National Bank were partially neutralized by foreign exchange sales in the domestic foreign exchange market, operations on the servicing of the Government's external debt and replenishment of assets of the National Fund from gold and foreign currency reserve accounts. As a result, during 2011 net currency reserves (NCR) decreased by 0.2%, and assets denominated in gold increased by 36.0% as a result of transactions and the growth of price for gold in the global markets.

In 2011 net domestic assets of the National Bank increased (Table 2), mainly because of the decrease in liabilities to banks on short-term notes.

Table 2

Dynamics of changes in assets and liabilities of the National Bank
(as % of the respective period of the previous year)

	1 qtr.11	2 qtr.11	3 qtr.11	4 qtr.11
Net international reserves	30.3	30.5	17.0	3.8
Net domestic assets	-384.4	-104.9	6.0	55.8
Net claims on the Government	-0.3	-56.2	-70.6	33.1
Claims on the economy	-352.7	-192.5	30.6	128.9
Other net domestic assets	-34.9	-52.1	-13.5	-9.8
Reserve money	2.7	5.5	14.0	10.3
Narrow reserve money	16.0	6.3	21.2	27.8

Source: National Bank of the Republic of Kazakhstan

3.1.2. Money Supply

During the 4th quarter of 2011 money supply decreased by 0.7% to KZT 9751.1 bln.

During 2011 its growth accounted for 15.0% as a result of increase in both net foreign assets and domestic assets of the banking system (Table 3).

Table 3

Dynamics of changes in money supply
(as % of the respective period of the previous year)

	1 qtr.11	2 qtr.11	3 qtr.11	4 qtr.11
Net foreign assets	50.3	48.5	21.2	16.7
Domestic assets	-8.5	-7.8	17.8	18.0
Claims on the Government	284.7	17.6	-54.5	86.7
Claims on the economy	1.4	4.9	10.2	14.0
Other net domestic assets	-11.1	-21.4	-6.8	-11.7
Money supply	15.0	12.9	16.8	15.0
Cash in circulation	22.1	15.3	16.0	18.9
Deposits of residents	14.1	12.6	16.9	14.3

Source: National Bank of the Republic of Kazakhstan

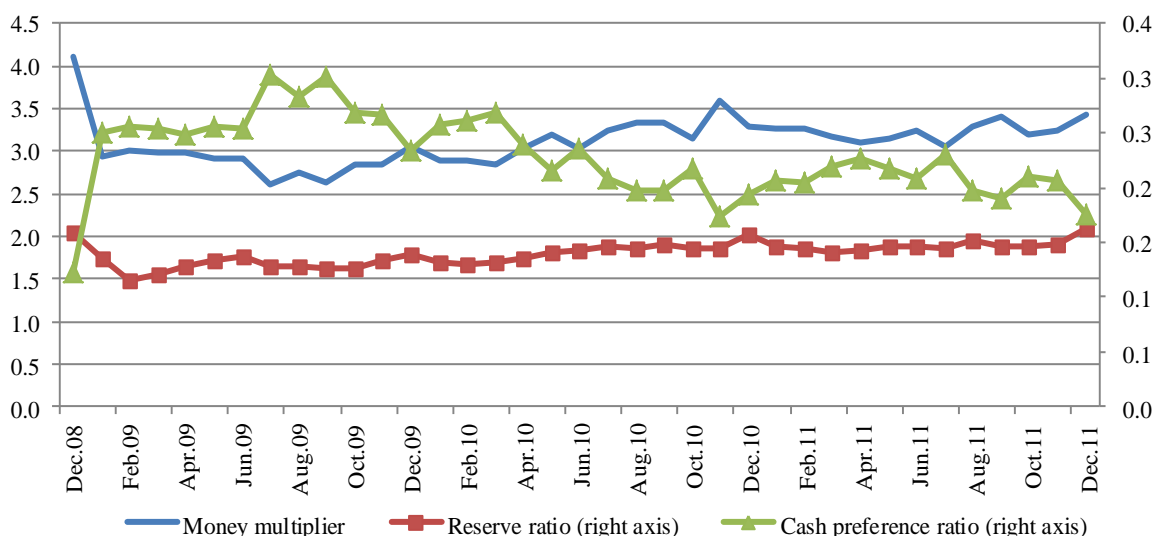
In the structure of net foreign assets of the banking system in 2011 net foreign assets of banks and of the National Bank increased. The growth in net foreign assets of banks was stipulated by the decreased claims of non-residents on banks and increased claims on residents.

During the reviewed period in the structure of the main components of money supply outstripping growth rates of cash in circulation as compared to the growth rates of residents' deposits in the banking system were noted. As a result, the share of deposits of residents in the structure of money supply decreased from 86.5% in December 2010 to 86.0% in December 2011.

The money multiplier grew from 3.30 in December 2010 to 3.44 in December 2011 as a result of outstripping growth rates of money supply as compared to the rates of expansion of the reserve money. Also, the reason for that was the decreased reserve ratio alongside with some increase in cash preference ratio (Figure 24).

Figure 24

Dynamics of money multiplier and its components



Source: National Bank of the Republic of Kazakhstan

3.1.3. Cash in Circulation

The volume of cash in circulation grew during the 4th quarter of 2011 by 8.3% to KZT 1365.7 bln.

During 2011 cash in circulation increased by 18.9%. Cash payouts from the bank cashier departments increased by 20.9% to KZT 1.5 trln., and the receipts to the bank cashier departments also increased by 20.9% to KZT 1.3 trln.

The growth of cash in 2011 was associated with the growth in payouts of wages, retirement benefits and allowances and as a result of the growth in payouts to support ATMs. Also, the increased payouts on demand deposits and checking accounts of individuals were conducive to the growth of cash in circulation. The effect of these factors was not neutralized by the growth in proceeds from the sale of goods, services and delivered works and the increased proceeds from foreign exchange sales observed in 2011.

3.2. Financial Market

3.2.1. Deposits of Residents

At end-December 2011 deposits of residents amounted to KZT 8385.4 bln., having decreased by 2.0% during the 4th quarter of 2011. Deposits of legal entities decreased by 5.5%, and deposits of individuals increased by 6.0%. Deposits in the domestic currency increased by 0.2% to KZT 5755.7 bln. and foreign currency deposits decreased by 6.6% amounting to KZT 2629.7 bln.

In 2011 the deposit base was characterized by the predominant growth of savings in the domestic currency as well as significant increase, since June 2011, of foreign currency deposits of the population. Alongside with that, the decrease in foreign currency deposits of legal entities has largely compensated the inflow of foreign currency to the deposit accounts of the population. As a result, since the beginning of the year deposits in the domestic currency have increased by 20.5%, and foreign currency deposits increased by 2.8% only.

The decrease in the volume of foreign currency holdings in the 4th quarter of 2011 caused by the currency outflow from the accounts of legal entities in November-December

2011 led to a minor decrease in the degree of deposit dollarization, which resulted in the decrease of the percentage of foreign currency deposits to 31.4% in December 2011 versus 32.9% in September 2011.

Thus, despite volatility in the foreign currency segment of the deposit market associated with the foreign currency inflow to deposits of the population from June 2011 and the foreign currency outflow from accounts of legal entities at the end of the year, stable growth in the Tenge deposits continued to serve as a main source for the bank resource base growth during 2011 (Table 4).

Table 4

**Dynamics of changes in residents' deposits
(as % to December of the previous year)**

	Dec. 2008	Dec. 2009	Dec. 2010	Dec. 2011
Deposits of residents	39.1	21.5	11.6	14.3
<i>of individuals</i>	<i>2.8</i>	<i>28.5</i>	<i>15.9</i>	<i>24.1</i>
<i>of non-bank legal entities</i>	<i>60.2</i>	<i>18.9</i>	<i>9.8</i>	<i>10.2</i>
Deposits in the Tenge	32.0	5.9	29.1	20.5
Deposits in foreign currency	54.0	50.0	-11.0	2.8

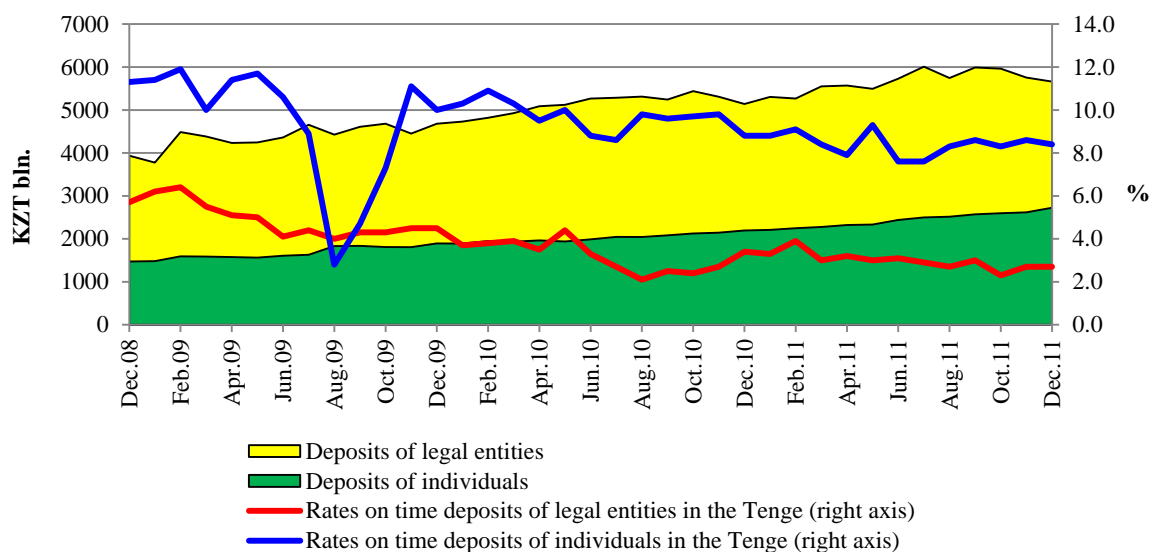
Source: National Bank of the Republic of Kazakhstan

In the 4th quarter of 2011 the interest rates on deposits generally remained at the level of the previous quarter although there was a minor growth in the yield on deposits – both on foreign currency deposits of legal entities and individuals.

In December 2011 the average weighted interest rate on the Tenge time deposits of non-bank legal entities was 2.7% (in December 2010 – 3.4%), and on deposits of individuals – 8.4% (8.8%) (Figure 25).

Figure 25

Dynamics of deposits and their interest rates



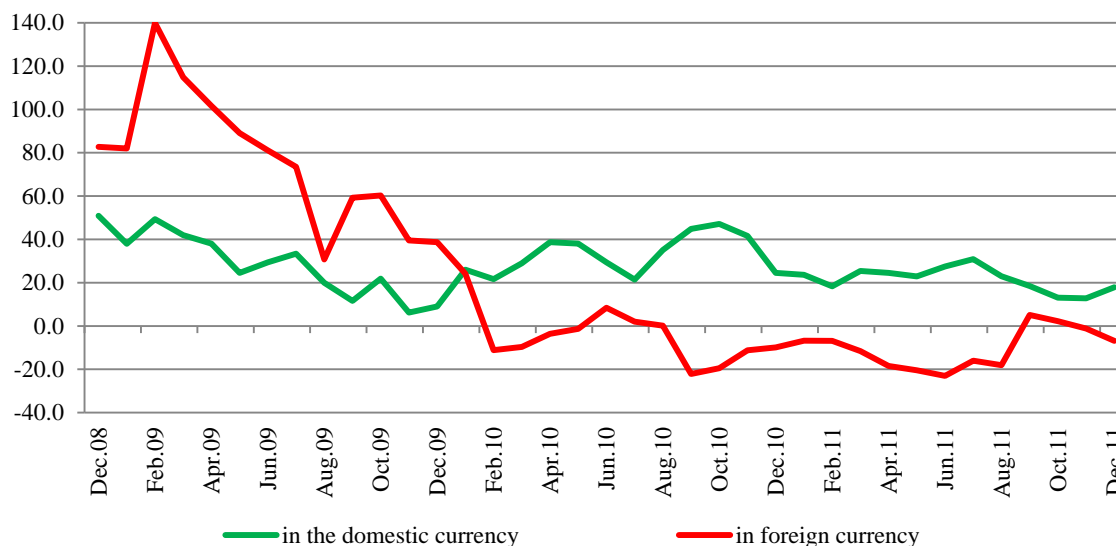
Source: National Bank of the Republic of Kazakhstan

During the 4th quarter of 2011 volume of deposits of legal entities decreased by 5.5% to KZT 5661.2 bln., with the annual growth (December 2011 versus December 2010)

accounting for 10.2%. Deposits of legal entities in the domestic currency increased in annual terms by 17.9% and foreign currency deposits decreased by 6.9% (Figure 26).

Figure 26

**Dynamics of the change in deposits of legal entities
(as % of the respective period of the previous year)**

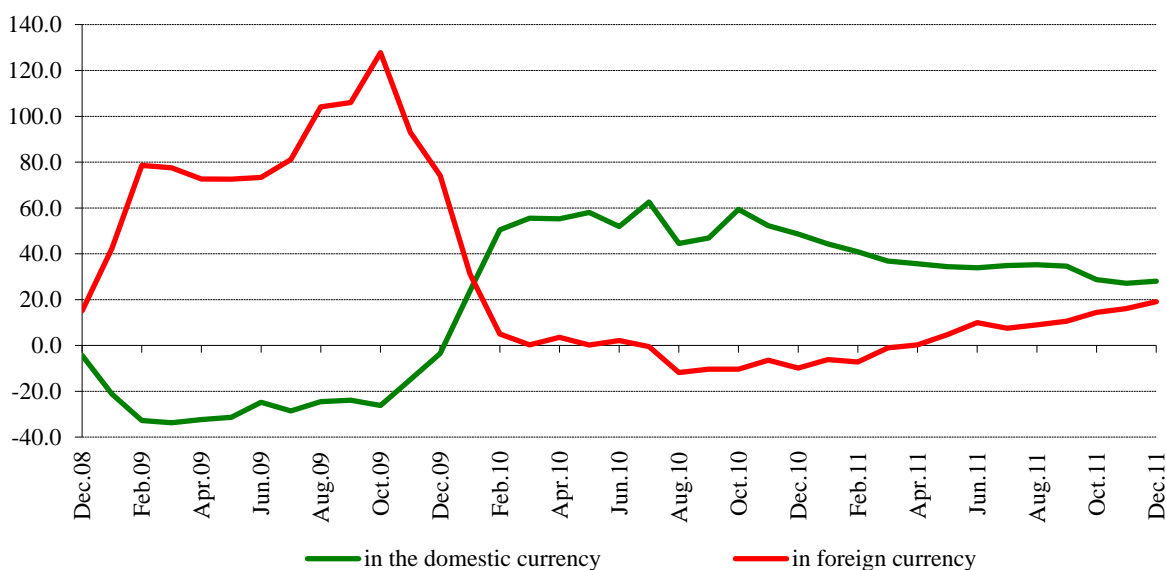


Source: National Bank of the Republic of Kazakhstan

During the 4th quarter of 2011 the volume of deposits of individuals increased by 6.0% and has increased by 24.1% to KZT 2724.2 bln. Deposits of individuals in the domestic currency in annual terms increased by 28.0%, and deposits in foreign currency increased by 19.1% (Figure 27).

Figure 27

**Dynamics of the change in deposits of individuals
(as % of the respective period of the previous year)**



Source: National Bank of the Republic of Kazakhstan

3.2.2. Credits to the Economy

During the 4th quarter of 2011 bank credits to the economy increased by 4.3% to KZT 8781.4 bln. Credits to legal entities increased by 4.5%, and credits to the population – by 3.7%.

During 2011 as a whole the lending volume increased by 15.7%, where credits to legal entities increased by 17.5% and credits to individuals – by 10.9%.

The average weighted rate on credits provided to legal entities in December 2011 decreased from 10.8% to 9.8% versus September 2011 (December 2010 – 11.9%); this was caused by the decrease in the cost of borrowing for legal entities both in the domestic currency and in foreign currency in the 4th quarter of 2011.

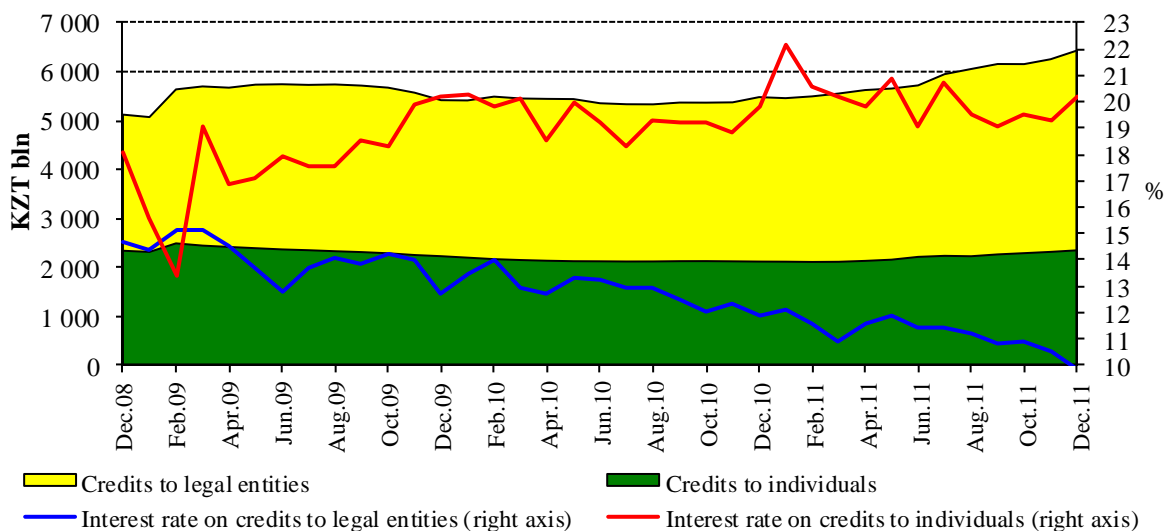
The average weighted rate on credits to individuals in December 2011 increased from 19.1% to 20.2% versus September 2011 (December 2010 – 19.8%). In general, in the 4th quarter of 2011 the growth of rates on foreign currency loans and their slight decrease on the loans in the domestic currency was observed (Figure 28).

In the structure of credits by objects of financing the major volume of debt fell on credits provided for the purchase of working capital (27.7%), for new construction and reconstruction (15.6%), as well as for other purposes (24.1%).

In a sectoral breakdown, the highest debt on bank credits to the economy falls on other sectors (non-production sphere and individual entrepreneurship) – 44.0%, trade – 20.8%, construction – 14.9%, and industry – 12.0%.

Figure 28

Dynamics of credits to the economy and their interest rates



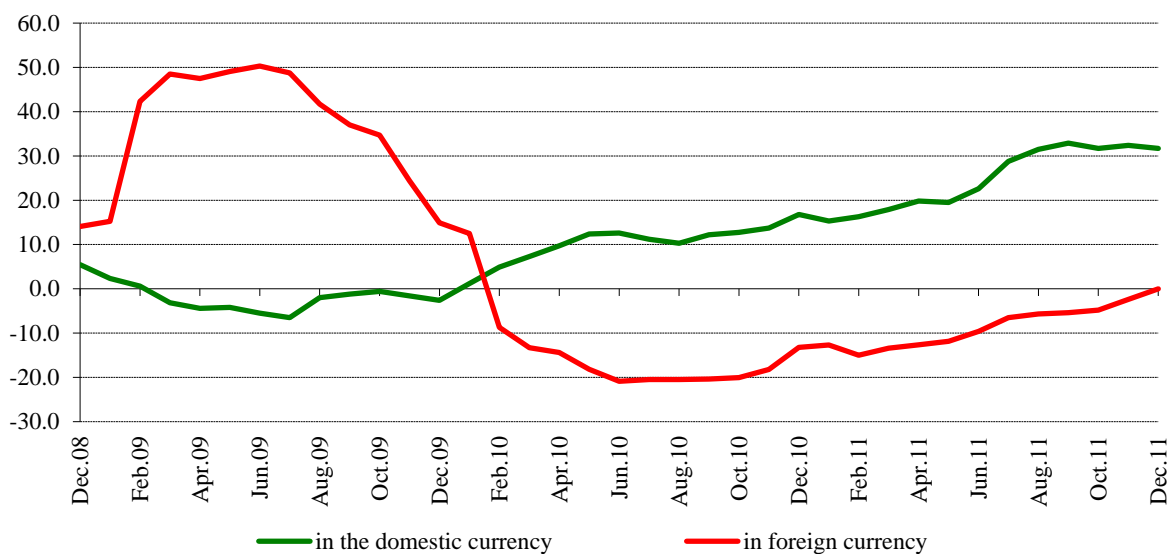
Source: National Bank of the Republic of Kazakhstan

In December 2011 as compared to December 2010, the volume of credits to legal entities increased by 17.5%. There were changes in the structure of credits by their terms. The share of medium- and long-term credits in the total volume of credits to legal entities accounted for 75.0% at end-December 2011 (in December 2010 – 78.8%).

Credits to legal entities in the domestic currency increased by 31.7% in annual terms, and foreign currency credits remained unchanged (Figure 29).

Figure 29

**Dynamics of credits to legal entities
(as % of the respective period of the previous year)**



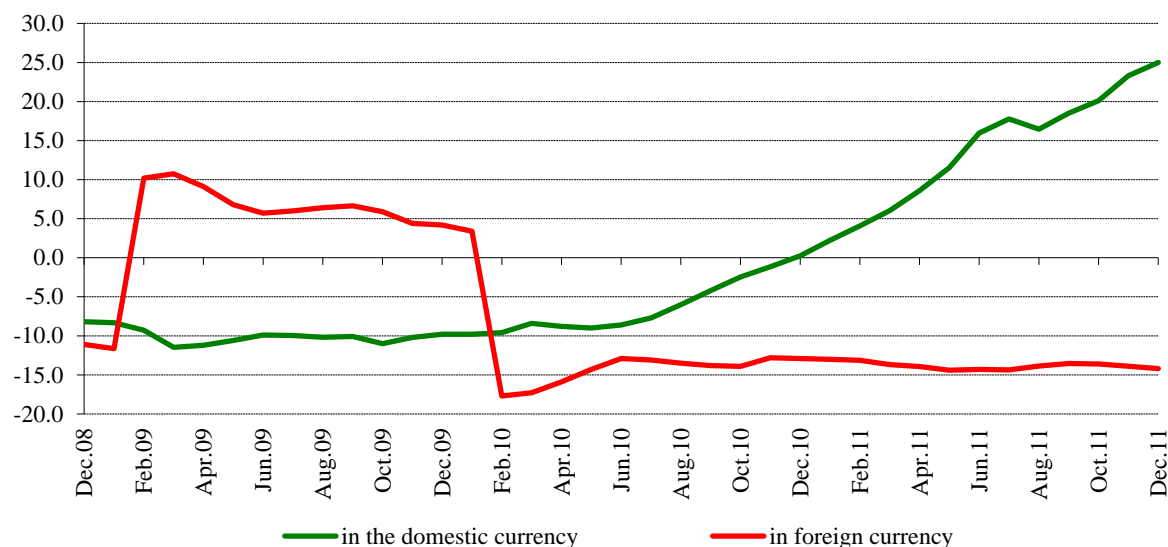
Source: National Bank of the Republic of Kazakhstan

The volume of credits to individuals increased by 10.9% in December 2011 as compared to the respective period of 2010. The share of medium- and long-term credits in the total volume of credits to individuals at end-December 2011 remained virtually unchanged and accounted for 96.2% (in December 2010 – 96.3%).

In the structure of credits to the population, credits in the domestic currency demonstrated the increase by 25.0%, and credits in foreign currency – the decrease by 14.2% (Figure 30).

Figure 30

**Dynamics of credits to the population
(as % of the respective period of the previous year)**



Source: National Bank of the Republic of Kazakhstan

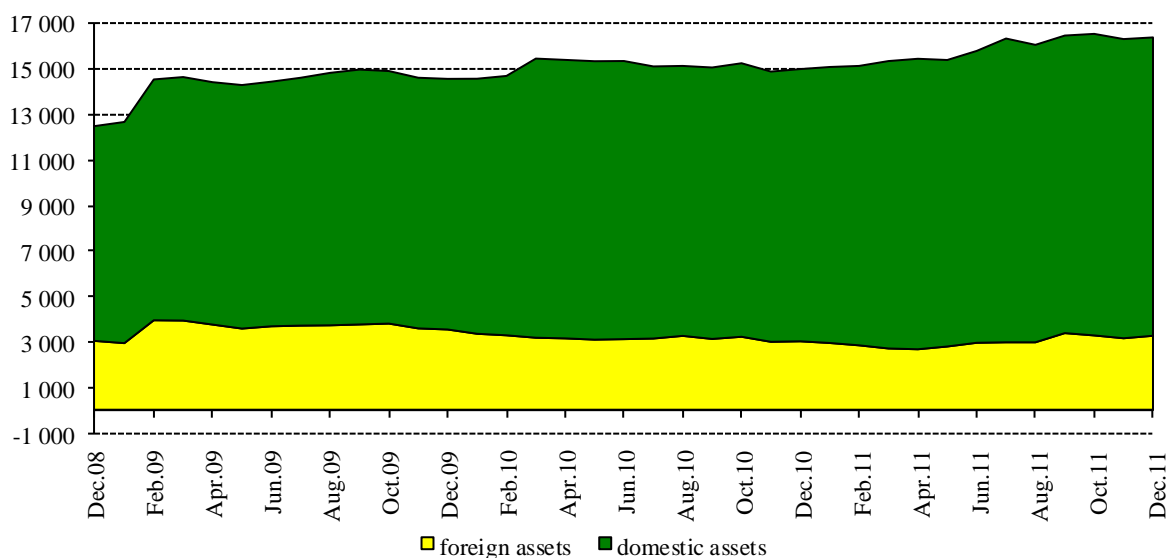
3.2.3. Bank Assets and Liabilities

– Assets

In the 4th quarter of 2011 the amount of bank assets calculated under the Monetary Survey decreased by 0.5% to KZT 16.4 trln. Bank assets increased in annual terms (December 2011 versus December 2010) by 9.3% (Figure 31).

Figure 31

Dynamics of bank assets, KZT bln.



Source: National Bank of the Republic of Kazakhstan

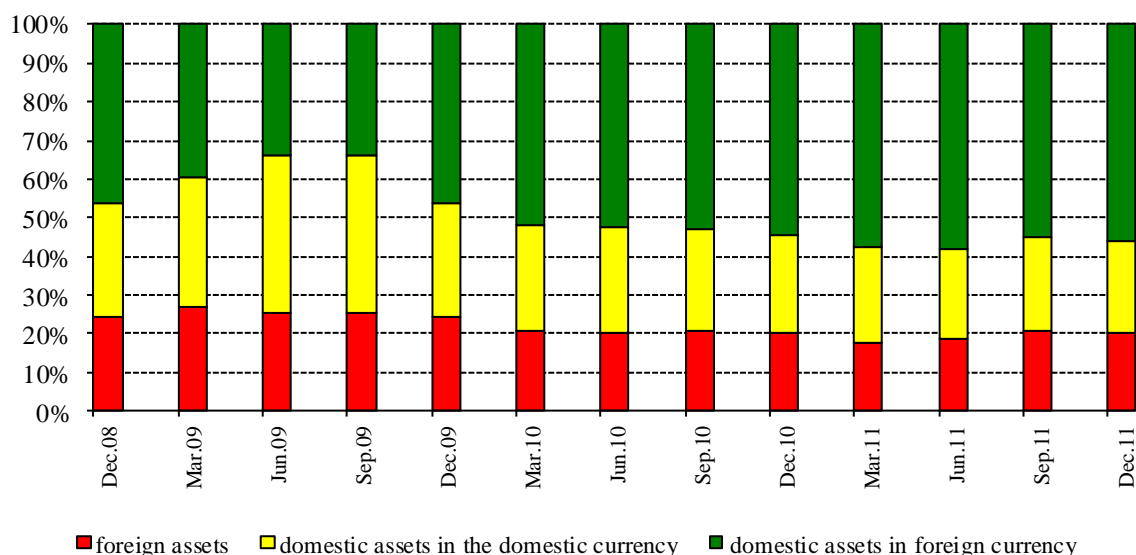
Foreign assets of banks in December 2011 accounted for 20.0% of the total volume of assets or US\$ 22.1 bln. As compared to December 2010, they increased by 5.9% and as compared to September 2011 they decreased by 3.7%.

In the structure of foreign assets in December 2011, credits to non-residents accounted for 49.9% (in September 2011 – 48.2%), deposits placed with non-residents – 29.0% (in September 2011 – 32.2%), securities of non-residents – 4.8% (in September 2011 – 4.2%), and other accounts receivable – 16.2% (in September 2011 – 15.4%).

Domestic assets in December 2011 accounted for 80.0% or KZT 13.1 trln., where domestic assets in the domestic currency accounted for 69.9% or KZT 9.2 trln. and domestic assets in foreign currency – 30.1% or KZT 3.9 trln. During October-December 2011, domestic assets increased by 0.3%, where assets in the domestic currency increased by 0.8%, and assets in foreign currency decreased by 1.0% (Figure 32).

Figure 32

Structure of bank assets, %



Source: National Bank of the Republic of Kazakhstan

In October-December 2011 the quality of bank assets was slightly deteriorating. The share of standard assets decreased from 47.7% to 45.9%, share of doubtful assets increased from 35.5% to 37.0%, and share of bad assets increased from 16.8% to 17.1%.

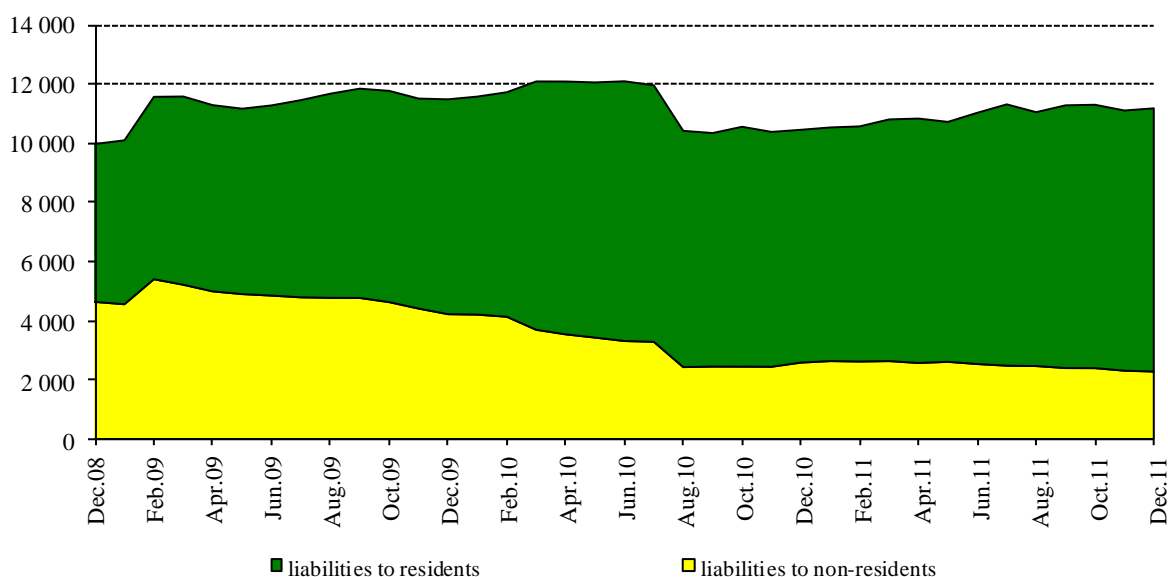
In the structure of doubtful assets a certain migration of assets towards concentration of assets of category 1, 3 and 5 is observed. In the structure of doubtful assets the share of assets of category 1 decreased from 30.2% to 30.0%, of category 2 increased from 9.9% to 12.4%, category 3 – increased from 22.8% to 23.2%, category 4 – decreased from 8.2% to 7.6%, and category 5 – decreased from 28.9% to 26.8%. Such changes in the structure of doubtful assets indicate a remaining threat of deterioration in the quality of bank assets.

As a whole, under the Monetary Survey for the 4th quarter of 2011, bank assets demonstrated a slight growth. Despite the overall mitigation of the level of credit risk as a result of an improved financial condition of the corporate sector and households, low asset quality still represents weak aspects of the Kazakh banking system. The slowdown in the growth rates of lending in the 4th quarter of 2011 to 4.3% versus 6.2% in a prior quarter was not conducive to the improvement in asset quality since the process of replacing bad loans by new ones is virtually non-existent. Banks still adhere to a conservative policy to a greater extent and prefer to lend to the best-quality borrowers.

– Liabilities

In the 4th quarter of 2011 total bank liabilities calculated under the Monetary Survey decreased by 0.9% and accounted to KZT 11.2 trln. at end-September (Figure 33).

Figure 33

Dynamics of bank liabilities, KZT bln.

Source: National Bank of the Republic of Kazakhstan

In December 2011 as compared to September 2011, bank liabilities to non-residents decreased by 4.9% to KZT 2.3 trln. (US\$ 15.4 bln.). Bank liabilities decreased by 13.8% versus the respective month of 2010. At end-December 2011 bank liabilities to non-residents accounted for 20.4% of the total volume of bank liabilities.

In the structure of bank liabilities to non-residents, the share of liabilities on deposits of non-residents increased from 6.3% in September 2011 to 6.8% in December 2011, the share of liabilities on securities increased from 71.8% to 72.9%, and credits from non-residents decreased from 19.1% to 17.9, respectively.

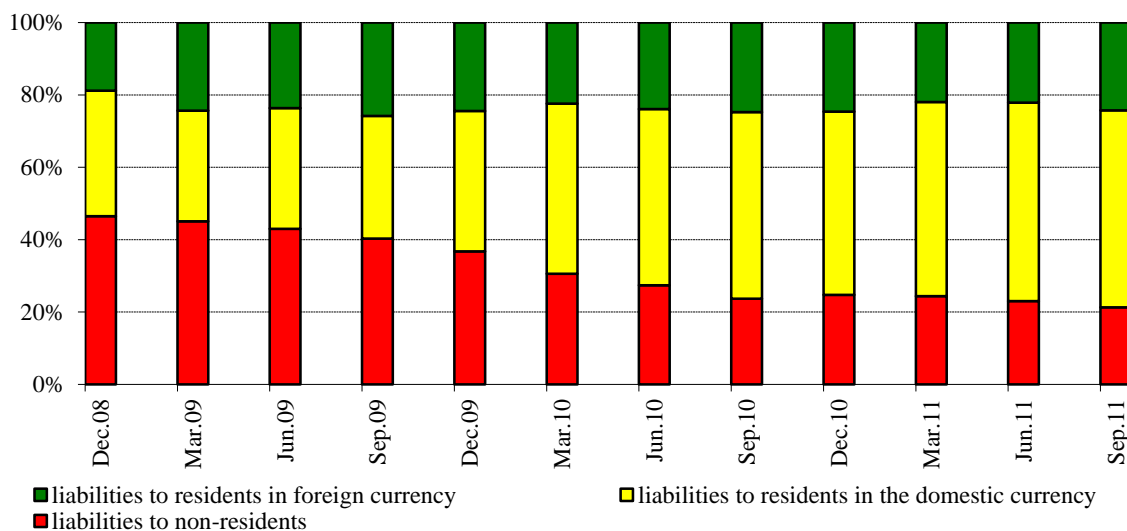
During October-November 2011 liabilities to residents increased by 0.2% to KZT 8.9 trln. (US\$ 60.0 bln.), where liabilities in the domestic currency increased by 2.1% to KZT 6.3 trln., and foreign currency liabilities decreased by 4.2% to KZT 2.6 trln. (Figure 34).

Thus, in the 4th quarter of 2011 there was a multi-directional trend in respect of bank liabilities: both the growth in liabilities to residents and the decrease in liabilities to non-residents. The growth in liabilities to residents was secured by the increase in the domestic currency component. The decrease in liabilities to non-residents occurred as a result of the decrease in credits to non-residents.

Therefore, one may state that during the fourth quarter of 2011 the process of replacing the external funding by the domestic funding sources was continuing.

Figure 34

Structure of bank liabilities, %



Source: National Bank of the Republic of Kazakhstan

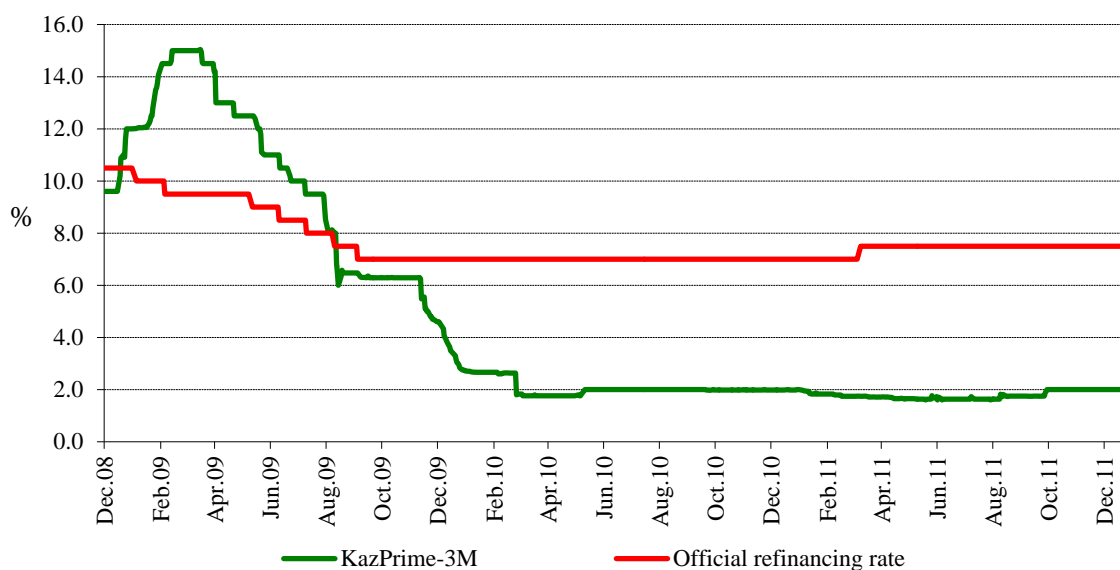
3.2.4. Financial Market Rates

In the 4th quarter of 2011 the growth of interest rates was observed in the interbank market.

The KazPrime index increased from 1.72% on average during the 3rd quarter of 2011 to 2.00% on average during the 4th quarter of 2011. At the same time, at end-December the index remained unchanged as compared to end-September – 2.00% (Figure 35).

Figure 35

Dynamics of the KazPrime index and the official refinancing rate, %



Source: Kazakhstan Stock Exchange, National Bank of the Republic of Kazakhstan

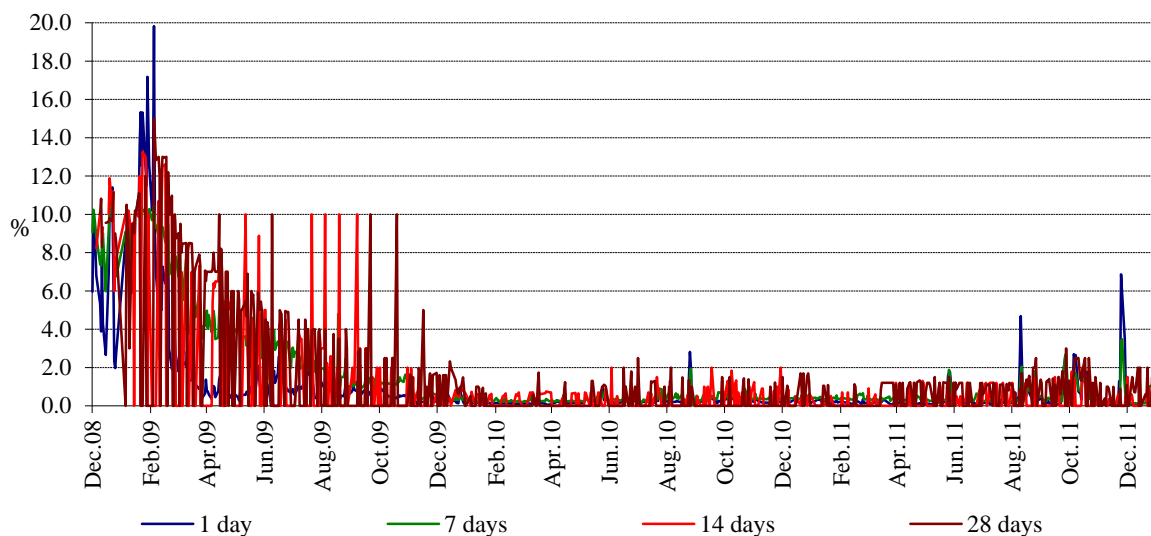
The average weighted rate on 1-day operations in the sector of the automatic REPO in the 3rd quarter of 2011 increased and made up 1.37% (in the 3rd quarter – 0.74%). Its maximum level was 6.89% and minimum – 0.03%.

Rate fluctuations on 7-day REPO operations in the 4th quarter of 2011 were within the range of 0.10% - 3.48% (the average weighted rate was 0.45%), on 14-day REPO operations – between 0.15% and 2.00% (the average weighted rate was 1.23%), and on 28-day REPO operations – between 0.39% and 2.50% (the average weighted rate was 1.67%) (Figure 36).

In the 4th quarter of 2011 the transaction volumes in the sector of automatic REPO decreased by 25.1% as compared to the previous quarter.

Figure 36

Dynamics of rates on REPO operations, %



Source: Kazakhstan Stock Exchange

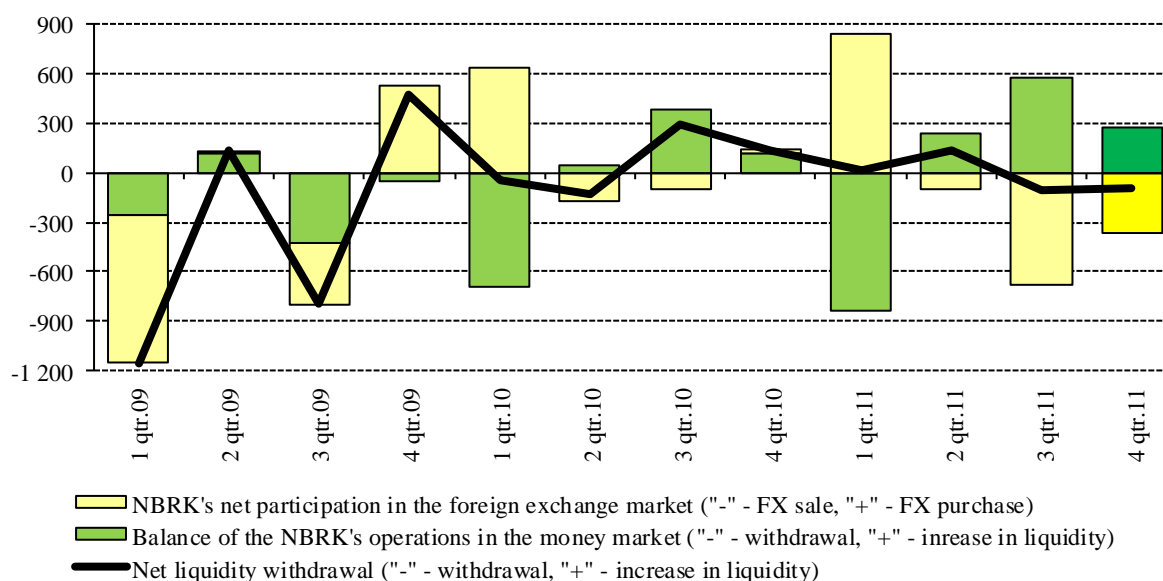
4. Monetary Policy Instruments and Operations

In the 4th quarter of 2011 the situation in the financial market remained stable, banks had sufficient Tenge liquidity.

During the 4th quarter of 2011 the National Bank's operations in the financial market resulted in the withdrawal of the Tenge liquidity, which occurred mainly because of the net sale of foreign exchange by the National Bank in the domestic foreign exchange market (Figure 37).

Figure 37

Balance of the National Bank's operations in the domestic market, KZT bln

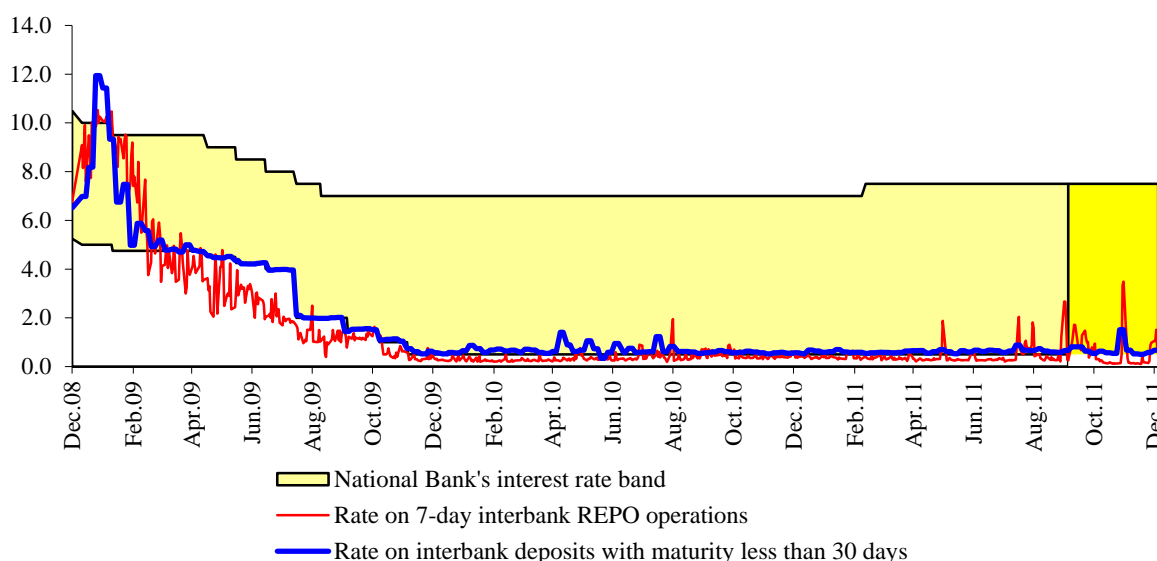


Source: National Bank of the Republic of Kazakhstan

In the 4th quarter of 2011 the National Bank's rate band remained unchanged. The official refinancing rate was maintained at 7.5%, rates on deposits attracted from banks also haven't changed: the rate on 7-day deposits is 0.5%, and on one month deposits – 1.0%.

In the 4th quarter of 2011 the situation in the money market was characterized by the interest rate volatility. In October 2011 interest rates slightly increased and in November they started to gradually decrease. In the 4th quarter of 2011 on average, the level of rates was closer to the lower boundary of the National Bank's rate band. The average weighted rate on interbank deposits with maturity less than 30 days decreased from 0.66% in the 3rd quarter of 2011 to 0.57% in the 4th quarter of 2011. The average weighted rate on interbank 7-day REPO operations hasn't changed and was 0.45% in the 4th quarter of 2011 (Figure 38).

Figure 38

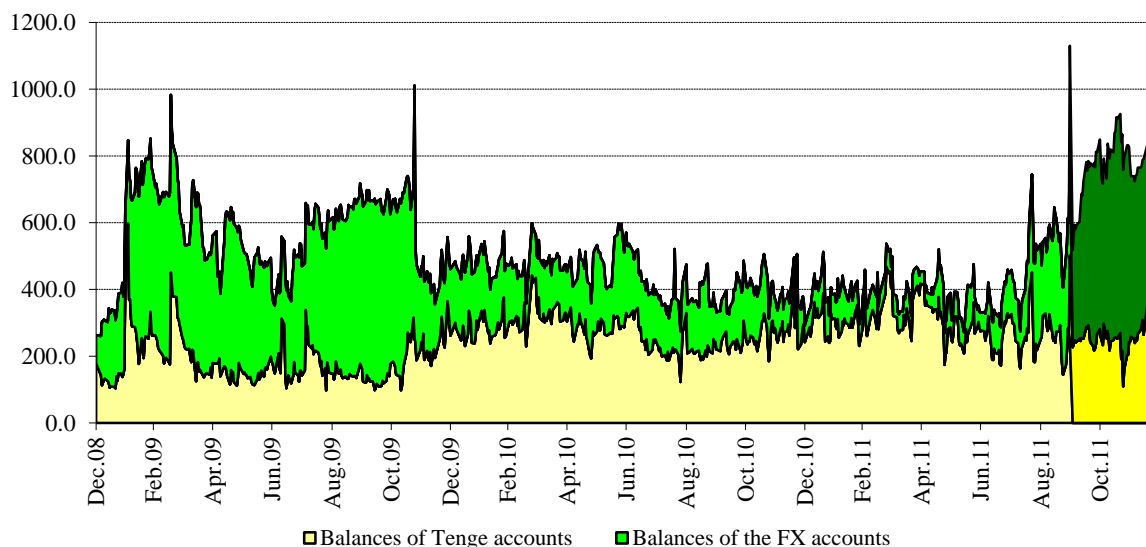
Boundaries of the National Bank's interest rates band, %

Source: National Bank of the Republic of Kazakhstan

In October-December 2011 the dynamics in correspondent account balances of banks with the National Bank was multi-directional. In October-November 2011 correspondent account balances of banks in foreign currency were gradually increasing and in December 2011 they decreased. As a whole, their volume at end-December 2011 decreased by 10.8% as compared to that at end-September 2011.

Correspondent account balances of banks in the domestic currency in the 4th quarter of 2011 were also volatile; their growth was interchanging with their decrease and vice versa during the entire period. So, in October-November 2011 they were gradually decreasing and in December their upward trend outlined. As a result, their volume increased by 39.9% at end-December 2011 as compared to end-September 2011 (Figure 39).

Figure 39

Balances of correspondent accounts with the National Bank, KZT bln.

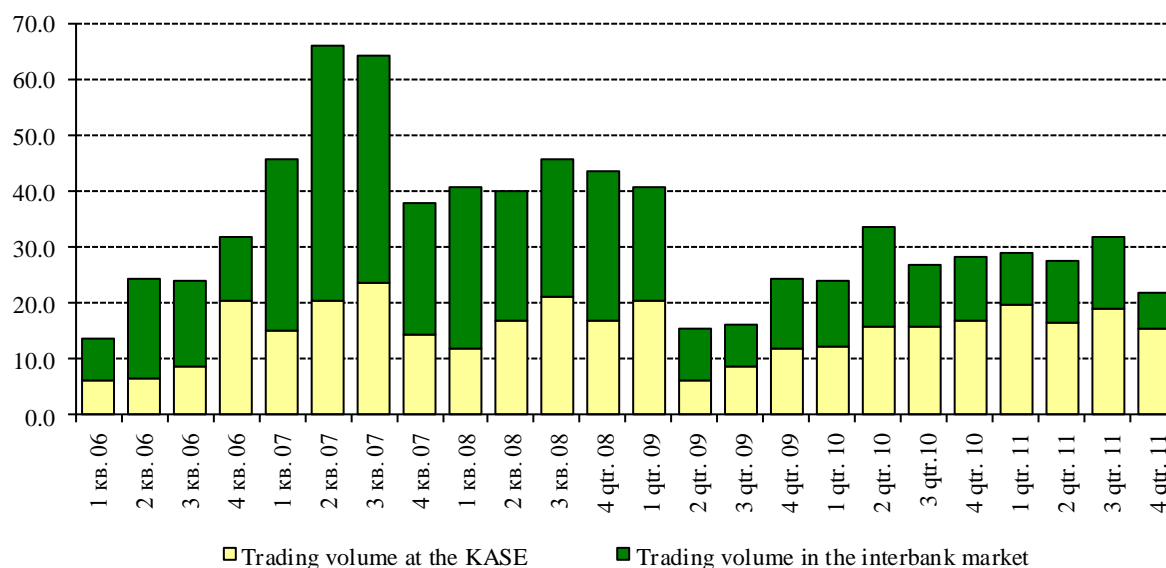
Source: National Bank of the Republic of Kazakhstan

4.1. Interventions in the Domestic Foreign Exchange Market

In the 4th quarter of 2011 the total trading volume in the FX segment of the Kazakhstan Stock Exchange and in the interbank foreign exchange market amounted to US\$ 21.7 bln., having decreased by 31.8% as compared to the 3rd quarter of 2011.

The volume of trades in the Dollar position at the Kazakhstan Stock Exchange decreased by 19.2% as compared to the 3rd quarter of 2011 and amounted to US\$ 15.5 bln. (net trades at the Kazakhstan Stock Exchange made up 81% of gross trades). In the off-exchange foreign currency market the volume of transactions during the 4th quarter of 2011 decreased by 50.9% as compared to the previous quarter and amounted to US\$ 6.2 bln. (Figure 40).

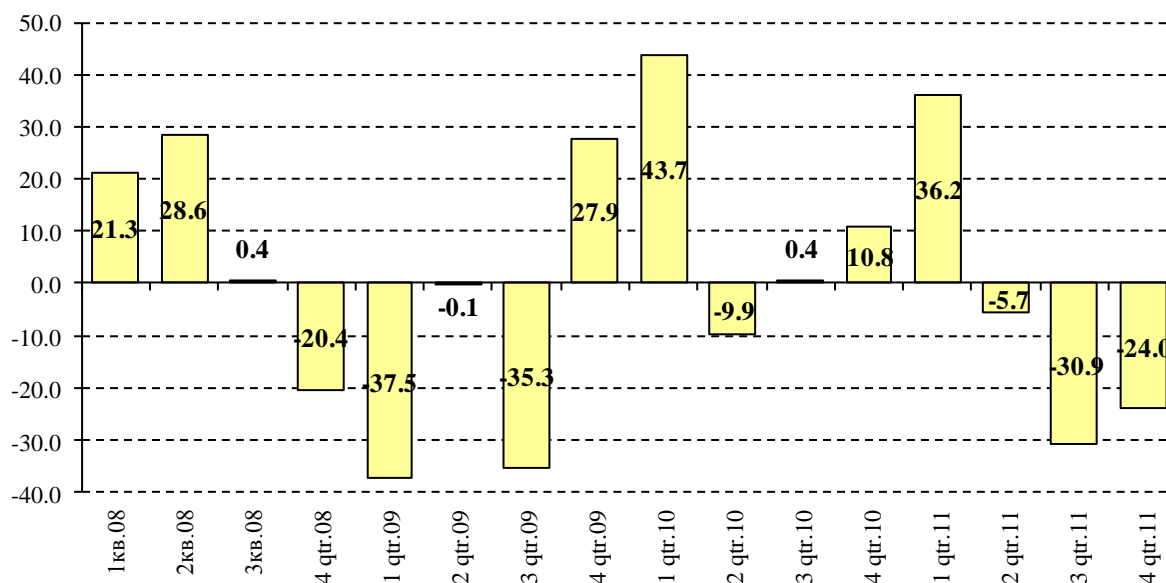
Figure 40

Volume of trading in the domestic exchange market, US\$ bln.

Source: National Bank of the Republic of Kazakhstan

At the end of the 4th quarter of 2011 the National Bank's participation coefficient in the Kazakhstan Stock Exchange made up (-)24,0% (in the 3rd quarter of 2011 it was (-)30,87%) (Figure 41). Thus, in the 4th quarter of 2011 the National Bank was primarily the seller of foreign exchange in the domestic foreign exchange market.

Figure 41

Coefficient of the National Bank's participation at the Kazakhstan Stock Exchange, %

Source: National Bank of the Republic of Kazakhstan

4.2. Minimum Reserve Requirements

In the environment of persisting inflationary pressure, with a view to tighten monetary policy, amendments were made to the Resolution of the National Bank's Managing Board #54 "On Establishing Ratios of Minimum Reserve Requirements". The decision to change the

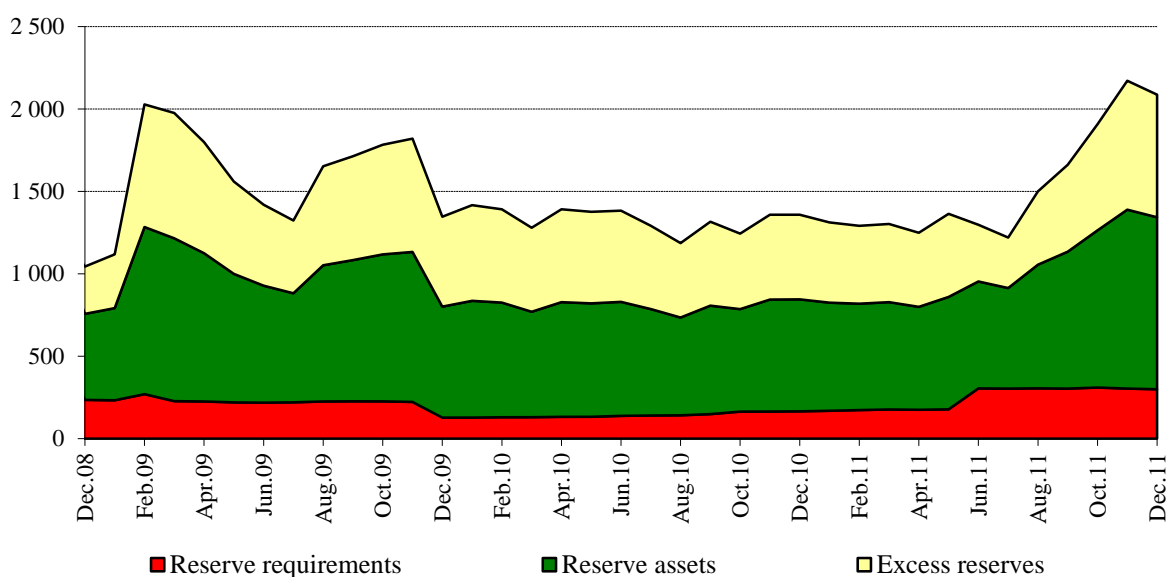
ratios of minimum reserve requirements (MRR) was made at the meeting of the National Bank's Managing Board that took place on April 29, 2011). The MRR ratio for the domestic liabilities was established at 2.5%, and for other liabilities – at 4.5%.

Pursuant to the existing legislation, new MRR ratios became effective as of May 31, 2011. As a result of the change in minimum reserve requirements, from June 2011 to August 2011 a reduction in excessive bank liquidity was observed. The increase in excessive liquidity has been observed since August 2011.

On average during October-December 2011 reserve assets exceeded the required reserving volume by 3.4 times (in the 3rd quarter of 2011 – by 2.3 times on average, in the 3rd quarter of 2010 – by 4.4 times on average) (Figure 42).

Figure 42

Compliance with minimum reserve requirements, KZT bln.



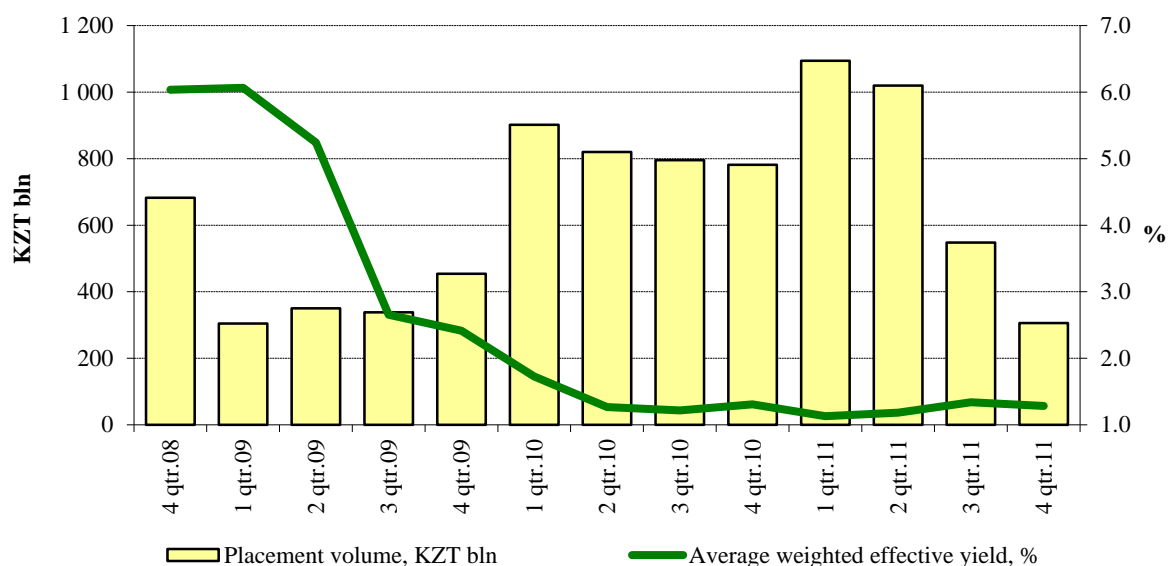
Source: National Bank of the Republic of Kazakhstan

4.3. Open Market Operations

In the 4th quarter of 2011 the demand of banks for short-term notes of the National Bank reduced. This was accompanied both by low emission volumes and the decreased volume of short-term notes in the bank portfolios. The minimum demand for such instruments was noted in October-November 2011.

The volume of short-term notes issued in the 4th quarter of 2011 as compared to the 3rd quarter of 2011 decreased by 44.1% and amounted to KZT 305.9 bln. The highest volume of issued short-term notes was in December (over 78% of the total volume issued during the 4th quarter of 2011). The average weighted yield on issued notes decreased from 1.34% in the 3rd quarter of 2011 to 1.28% in the 4th quarter of 2011 (Figure 43).

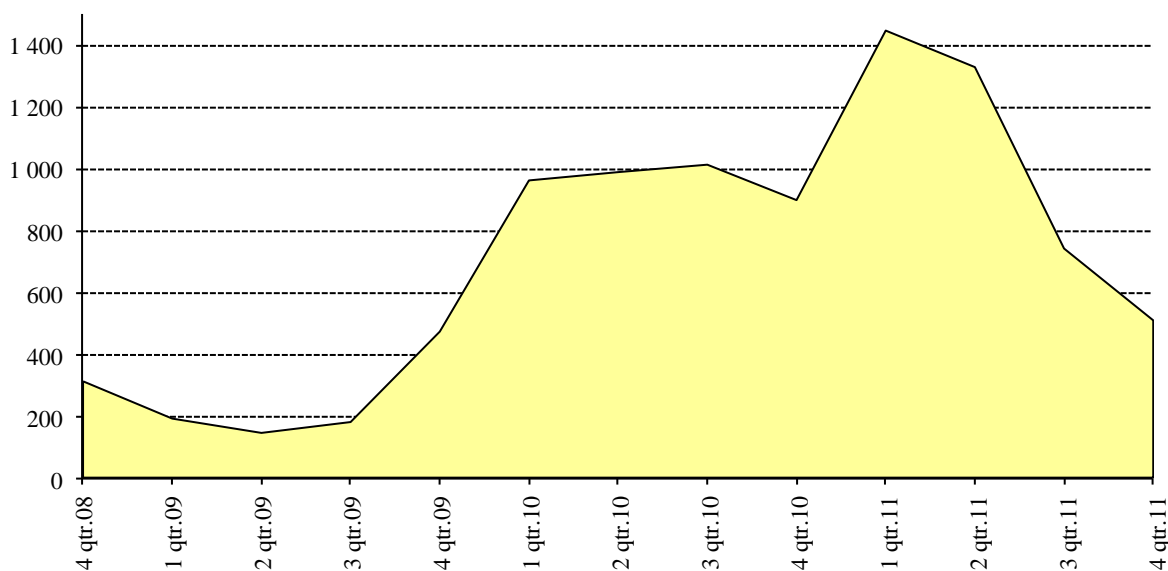
Figure 43

Volume of placed short-term notes and their yield (for the period)

Source: National Bank of the Republic of Kazakhstan

At end-December 2011 the volume of short-term notes in circulation amounted to KZT 509.8 bln., which is by 1.8 time less than the volume at end-December 2010 (Figure 44).

Figure 44

Short-term notes in circulation, KZT bln. (at end-period)

Source: National Bank of the Republic of Kazakhstan

4.4. Standing Facilities

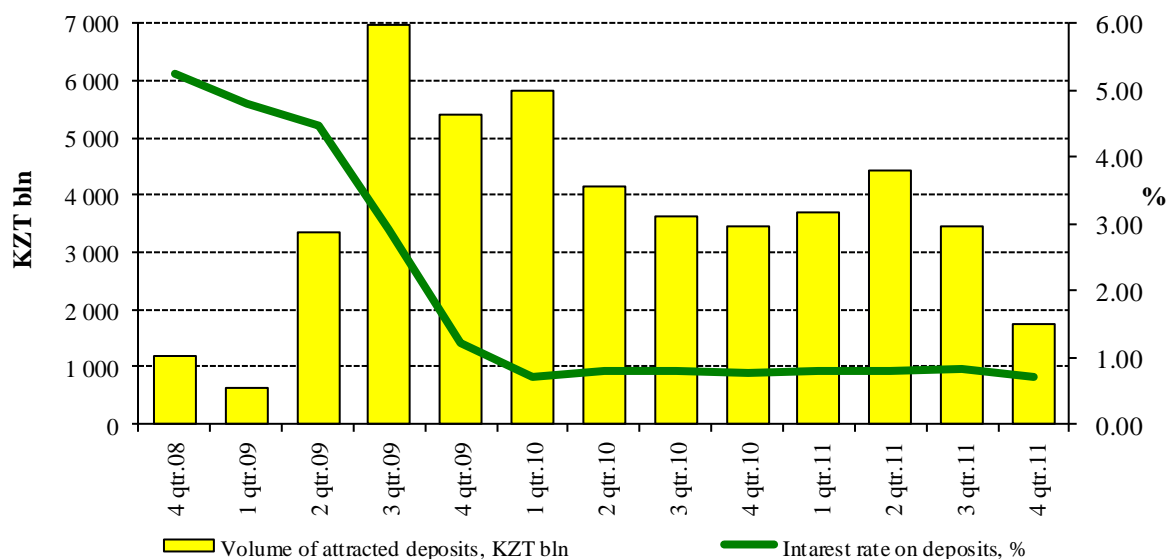
In the 4th quarter of 2011 the volume of deposits attracted from banks decreased as compared to the previous quarter. At the same time, the maximum volume of attracted deposits was noted in November whereas in October and December the volumes were not high. As a whole, during October-December 2011 deposits worth KZT 1745.3 bln. were

attracted, which is two times less than the amount in the 3rd quarter of 2011 and the 4th quarter of 2010.

The average interest rate on deposits decreased from 0.81% in the 3rd quarter of 2011 to 0.71% in the 4th quarter of 2011 (Figure 45).

Figure 45

Volume and interest rates on deposits attracted by the National Bank (for the period)

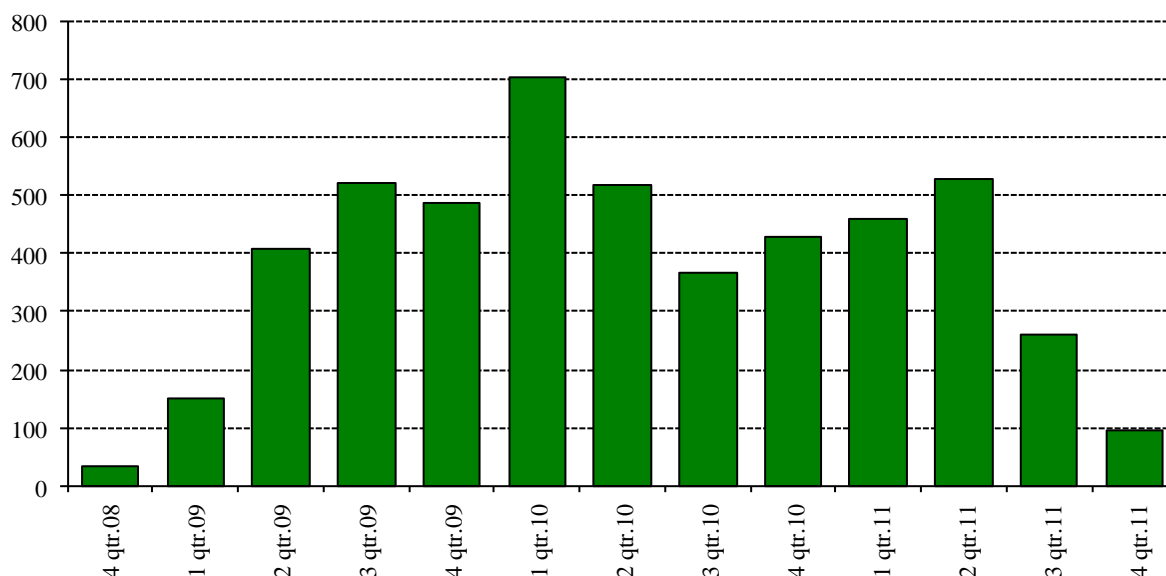


Source: National Bank of the Republic of Kazakhstan

The decrease in the volumes of attracted deposits was accompanied by the decrease in the volume of the National Bank's outstanding liabilities on such deposits. In December 2011 the volume of outstanding balances on deposits of banks with the National Bank amounted to KZT 94.1 bln., which is by 4.6 times less than the volume of December 2010 (Figure 46).

Figure 46

Volume of outstanding liabilities of the National Bank on deposits attracted from banks, KZT bln. (at end-period)

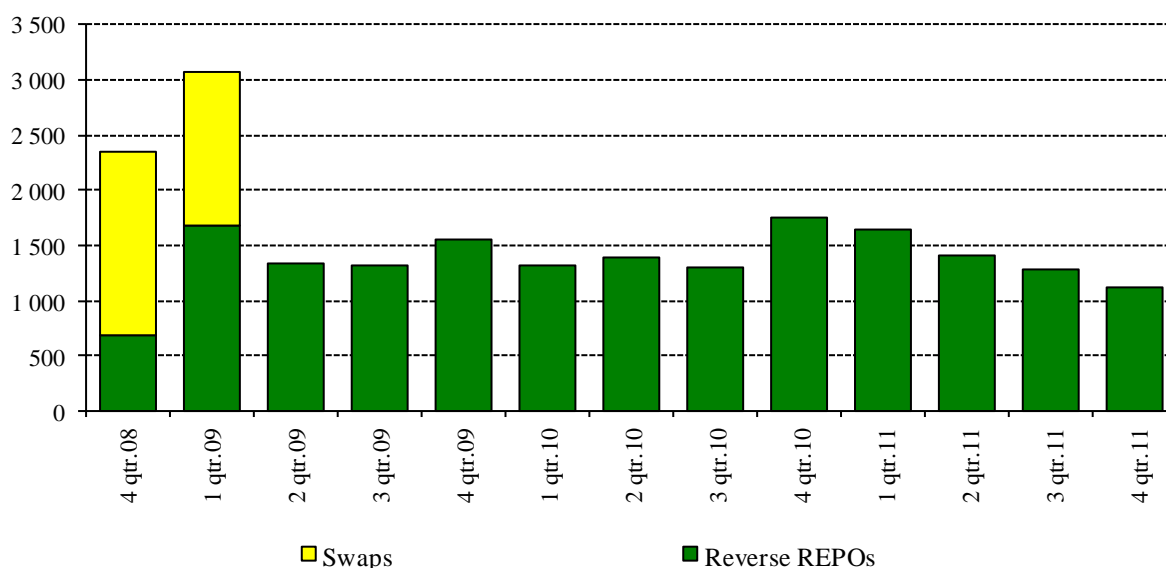


Source: National Bank of the Republic of Kazakhstan

In addition to sterilization operations, in the 3rd quarter of 2011 the National Bank continued to provide refinancing loans to the banking sector through reverse REPO operations. Total volume of reverse REPO operations in October-December 2011 amounted to KZT 1114.9 bln. The volumes of these operations decreased by 13.3% as compared to the previous quarter (Figure 47).

Figure 47

Volume of the National Bank's refinancing operations, KZT billion (for the period)

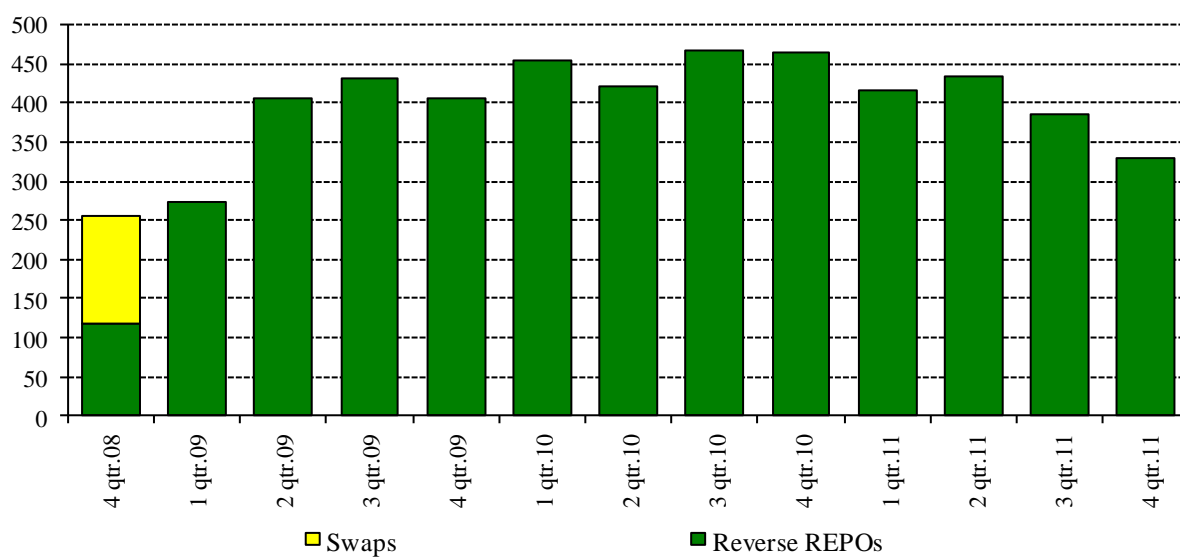


Source: National Bank of the Republic of Kazakhstan

At end-December 2011 the outstanding debt on reverse REPO operations also decreased and amounted to KZT 329.2 bln. (Figure 48).

Figure 48

Volume of outstanding liabilities on refinancing operations of the National Bank , KZT bln. (at end-period)



Source: National Bank of the Republic of Kazakhstan