

National Bank
National Bank
of the Republic of Kazakhstan

Inflation Report
for the First Quarter 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 First Quarter 2011	7
Inflation Forecast for 2011.....	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>	14
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>	20
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. Execution of the state budget
- 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 against the U.S. dollar
- figure 18. Dynamics of the official exchange rate of the Tenge against the Euro and the Russian ruble
- figure 19. Contribution of key sectors of the economy to growth in real GDP
- figure 20. Structure of the economically active population
- 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 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 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

In Q1 2011 the inflation was at 3.7% (in Q1 2010 – 2.9%), at end-March 2011 the annual inflation was at 8.6% (in December 2010 – 7.8%).

The buildup of the inflationary processes in Kazakhstan in January-March 2011 occurred against the minimal impact of monetary factors. So, the growth in money supply was 4.4% in Q1 2011, and the reserve money expanded by 9.2%.

The main factors for the growth of inflation in January-March 2011 were an instable situation in the global commodity markets accompanied by the growth in prices including for the major items of the Kazakhstan's exports, stable growth in the personal income, buildup of inflationary expectations due to the increased amount of pensions and benefits allocated from the budget from January 1, 2011.

In addition, the increased business activity in the economy is also conducive to sustained inflationary pressure. In 2010 the Kazakh economy had demonstrated quite high rates of growth. So, the real GDP growth in 2010 was 7%. Alongside with that the growth in production was observed almost in all sectors including mining and manufacturing industries, trade, transport, communications and construction.

At the same time, the anti-inflationary policy implemented in 2011 through concerted actions of the Government, National Bank and local executive authorities will help ensuring a stable situation in the consumer market and keeping the inflation within the established target band of 6-8% at end-2011.

The National Bank takes actions in accordance with the Monetary Policy Guidelines for 2011 that are aimed at ensuring the price stability, stability of the exchange rate of the Tenge and stability of the country's financial sector.

Against the backdrop of some acceleration of inflation in Q1 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. Interest rates on bank deposits with the National Bank remained at the existing minimum level: 0.5% for 7-day deposits and 1.0% – for 1-month deposits.

For the purposes of ensuring stability of the domestic currency, the National Bank is continuously monitoring the situation with the exchange rate of the Tenge. Given stabilization of the situation in the foreign exchange market and lower devaluation expectations of the population, the National Bank decided to repeal the exchange rate band of the Tenge and move to the managed floating exchange rate regime of the Tenge from February 28, 2011.

The transition to the managed floating exchange rate regime doesn't disengage the National Bank from its obligations of ensuring stability of the domestic currency. The National Bank will keep implementing the policy aimed at ensuring stability of the domestic currency and maintaining a favorable competitive environment for the domestic producers.

The National Bank regulates short-term liquidity in the money market by issuing short-term notes and taking deposits from banks. The National Bank provides refinancing loans to support current liquidity of banks.

The mechanism of minimum reserve requirements as well as their ratios didn't change in Q1 2011. Minimum reserve requirements for banks were 1.5% on domestic liabilities and 2.5% - on other liabilities.

Evaluation of the Inflation Forecasts for the First Quarter 2011

The actual inflation rate in Q1 2011 (3.7%) was higher than the forecast (2.5-2.7%) which was published in the previous issue of the Inflation Report. The inflation rate in

January and February was significantly higher than the projected level whereas in March it appeared to be lower than expected.

The main increase in prices in Q1 2011 was for foodstuffs. In their structure the increased prices for cereals, meat and dairy products, fruits and vegetables and sugar should be emphasized. When analyzing the dynamics of the past years, one may note that the increase in prices for fruits and vegetables, meat and dairy products is common for such period since it is caused by the seasonality factor. The growth in prices for sugar as well as cereals occurred in view of unstable situation in the global commodity markets caused by adverse weather conditions in a number of countries in 2010.

According to the estimate, the inflation in Q1 2011, excluding increased prices for foodstuffs, was 2.2% instead of actual 3.7%.

The impact of non-food items on inflation in January-March 2011, due to a moderate price growth for these items, remained insignificant. The impact on the part of paid services increased in February 2011 because of significant growth of prices and tariffs for utilities (cold and hot water supply, sewage, electricity).

The actual annual inflation rate at end-March 2011 (8.6%) was higher than the forecast (7.2-7.4%) which was published in the previous issue of the Inflation Report.

Inflation Forecast for 2011

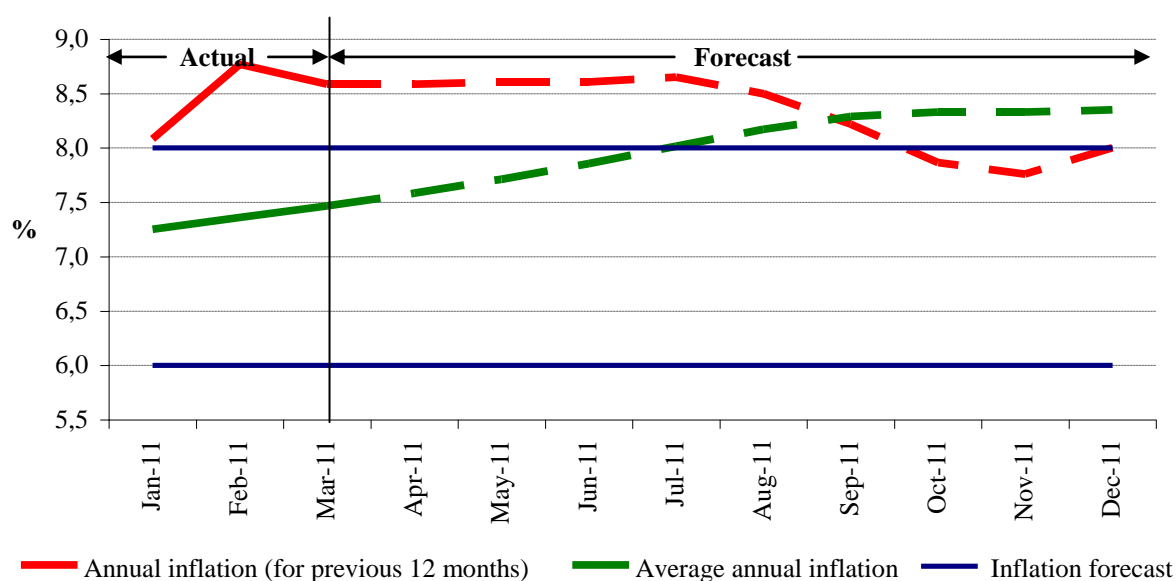
Under the Monetary Policy Guidelines of the Republic of Kazakhstan for 2011, the main objective of the National Bank was to keep the inflation within 6-8% (figure 1).

The inflationary processes in 2011 will be building up against the imbalance of aggregate demand and supply. Some escalation in the inflationary pressure is anticipated due to the increase of wages, benefits and other welfare payments from the budget in July 2011. Furthermore, in 2011 the situation in the global commodity markets will apparently remain unstable, thus putting some upward pressure on the inflation within Kazakhstan.

The monetary policy will be adequate to the developing macroeconomic conditions. Money supply in the economy will remain at the level corresponding to the growth of the economy.

figure 1

Actual and forecasted inflation in 2011



Source: National Bank of the Republic of Kazakhstan

The inflation forecast for Q2 2011 is 1.4-1.6% (in Q2 2010 actual inflation was 1.4%). Generally, this level is in line with the inflation trends of April-June that were typical in past years. These expectations are associated with the fact that the inflation buildup in the nearest term will be primarily affected by the seasonality factor. The decrease in prices for some items of goods and services (eggs, meat, dairy products, and lubricants) is expected. Some slowdown in the price growth rates for fruits and vegetables, meat products, and public utilities services is possible.

At end-June 2011 the annual inflation is expected to be at 8.5-8.7%.

The inflation forecast for Q3 2011 is 0.5-0.7% (in Q3 2010 actual inflation was at 0.8%), which corresponds to the annual inflation of 8.1-8.3% at end-September 2011.

In July-September 2011 the decrease in prices is expected for certain foodstuffs such as eggs, dairy and meat products, fruits and vegetables, certain public utilities services. At the same time, the buildup of inflationary expectations is possible because of scheduled increase of budget payouts in July 2011. Furthermore, the remaining stable growth of world oil prices in the long run will put pressure on the pricing for fuel and lubricants inside the country. Given that these commodities are used in the production of certain types of goods and services, this may be conducive to the growth in the costs of production and therefore in the final cost of goods and services.

1. Inflationary Processes

1.1. Consumer Prices

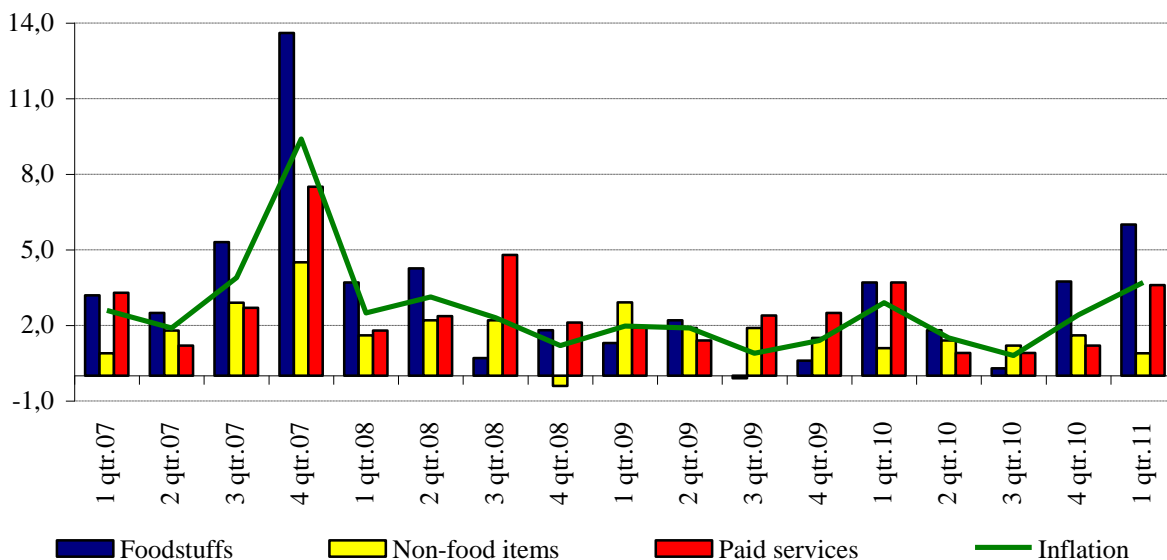
In Q1 2011 a trend for the increased inflationary pressure in the economy remained. During the period inflation was growing at a higher rate as compared to Q1 2010. In January-March 2011 inflation was at 3.7% (in Q4 2010 – 2.4%).

Accelerated inflation rates in Q1 2011 were caused by the seasonality factor due to the increase in prices for certain food items and certain services provided to the population including regulated services (cold and hot water supply, electric energy, and communication services).

Foodstuffs increased in price by 6.0%, non-food items – by 0.9% and paid services – by 3.6% (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

The major rise in prices in Q1 2010 was in such goods and services as cereals – by 38.6%, fruits and vegetables – by 16.4%, sugar – by 12.0%, wheat flour – by 7.7%, meat and meat products – by 6.9%, oils and fats – by 6.0%, dairy products – by 4.3%. Rice has fallen in price by 1.9%.

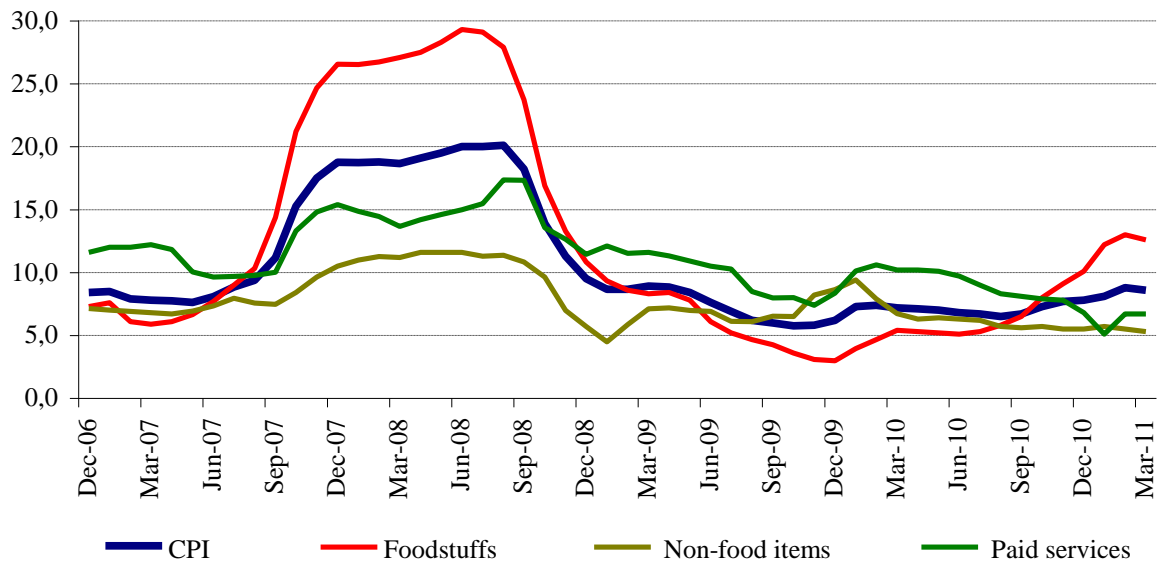
In the group of non-food items the major increase occurred in the prices for gasoline by 2.6%, for diesel fuel – by 2.4%, for medications – by 1.2%.

In the group of paid services, utility payments decreased by 3.5%. Alongside with that the fee for electricity increased by 9.4%, cold water – by 4.5%, district heating – by 3.6%, hot water – by 3.1%. Prices for communications services increased by 9.7%, including telephone and facsimile services – by 11.7%, legal services – by 4.4%.

At end-March 2011 the annual inflation was 8.6% (in December 2010 – 7.8%). The price of foodstuffs increased by 12.6% (10.1%), non-food items – by 5.3% (5.5%), paid services – by 6.7% (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

In annual terms, the biggest growth in prices was for fruits and vegetables, oils and fats, tobacco, sugar, meat and dairy products, bread and bakery and cereal products, diesel fuel and gasoline, liquefied gas, medications, detergents and cleansers, electricity, cold and hot water, sewage, educational services, out-patient services, and transportation services.

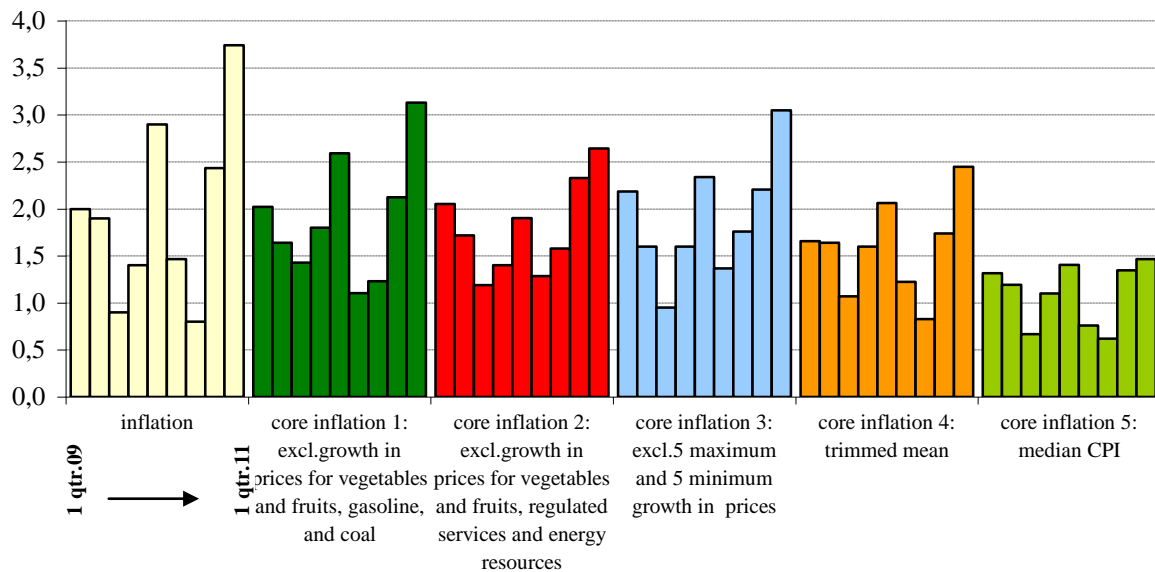
1.2. Core Inflation

Core inflation in Q1 2011 alike the headline inflation demonstrated higher growth rates, both as compared to the prior quarter and as compared to the respective quarter of 2010 (figure 4). This dynamics was primarily caused by higher growth rates of prices for virtually all foodstuffs which are included in the calculation of the consumer price index.

In January-March 2011 indicators of the core inflation demonstrated a multi-directional dynamics in annual terms. Core inflation-1 in January-February 2011 was accelerating while in March 2011 it had stabilized. Other indicators of core inflation, after some acceleration in January-February 2011, started to gradually slow down in March 2011. At the same time, all core inflation indicators were at a lower level at end-March 2011 as compared to the headline inflation.

figure 4

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

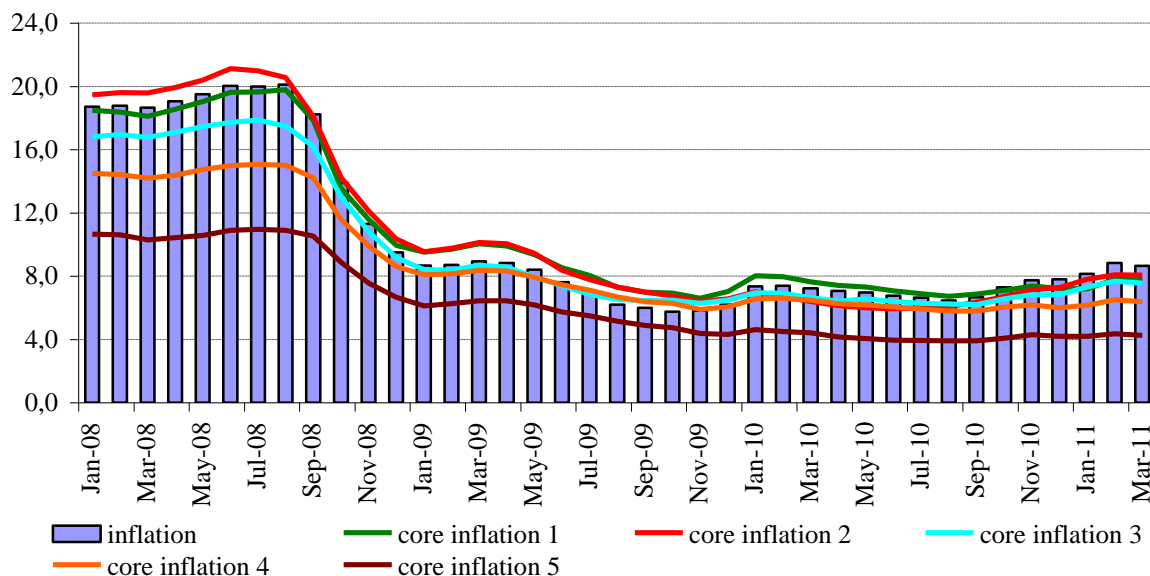


Source: Agency of Statistics of the Republic of Kazakhstan

In March 2011 all core inflation indicators in annual terms were higher as compared to December 2010. This is indicative of persisting inflationary background in the economy, while the impact of monetary factors on inflation is insignificant (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 Q1 2011 the producer prices have increased by 12.7% (in Q1 2010 – by 0.1%). The cost of output appreciated by 13.5%, at the same time the price of production means within its composition increased by 5.4%, the price of consumer goods – by 8.0%, and interim consumption products – by 14.3%. The price of production services increased by 4.7%.

In January-March 2011 the growth rate of producer prices in the mining industry accelerated significantly. After their growth by 11.1% in Q4 2010, in Q1 2011 the prices increased by 16.1% (in Q1 2010 – the decrease by 1.5%).

The cost of energy resources in Q1 2011 increased by 16.0% (in Q1 2010 – the decrease by 1.6%). In the composition of energy resources, the cost of oil production increased by 16.3% (in Q1 2010 – the decrease by 3.1%), the cost of gas condensate increased by 20.2% (the decrease by 4.9%).

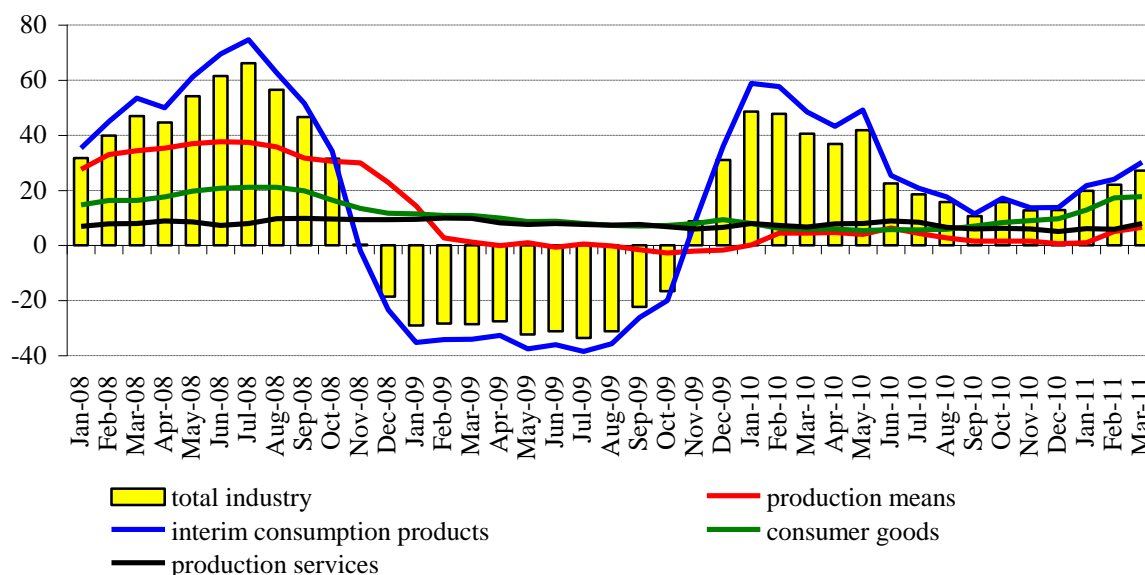
The growth rate of prices in the manufacturing industry in Q1 2011 slowed down from 7.2% to 6.2% as compared to the previous quarter (in Q1 2010 – the growth by 1.1%). Prices in the metallurgical industry increased by 7.9%, prices in the foodstuff production increased by 9.0%, refined products increased in price by 4.4%.

There was an increase in prices in the production and distribution of electric energy, gas and water in Q1 2011, which amounted to 10.9% (in Q1 2010 – the growth by 13.4%).

In March 2011 the growth of prices in the industrial production in annual terms (March 2011 to March 2010) accounted for 27.1% (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 28.6% in annual terms, including the interim consumption products – by 30.2%, consumer goods – by 17.7%, production means – by 6.5%. The cost of production services increased by 7.9%.

1.3.2. Prices in Agriculture

In Q1 2011 prices for agricultural production realized across all channels increased by 9.7% (in Q1 2010 – the decrease by 0.5%). The dynamics of prices in agriculture was impacted by appreciation of output in the plant production to a greater extent and in stock-breeding – to a smaller extent.

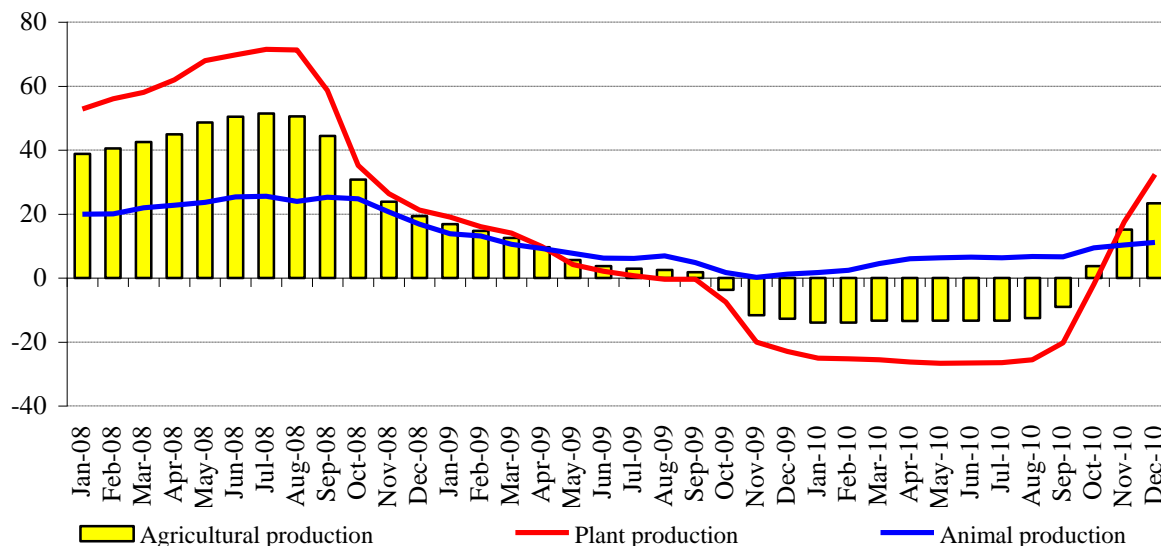
During January-March 2011 the price of plant production increased by 11.0% (in Q1 2010 – the decrease by 3.3%), where the prices for grain cultures increased by 11.4%, vegetables increased in price by 14.6%, and potatoes - by 17.4%.

The cost of animal products appreciated by 7.7% in Q1 2011, whereas in Q4 2010 the growth amounted to 8.0%, and in Q1 2010 the prices grew by 3.1% only. During January-March 2011 prices for meat and poultry increased by 6.9%, the cost of unpasteurized milk increased by 14.6%, and the price of eggs increased by 0.3%.

At end-March 2011, prices for agricultural products increased by 36.1% in annual terms. The cost of plant production increased by 52.0%, and animal products increased in price by 16.1% (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 Q1 2011 the demand for final products of enterprises slightly decreased: this is evidenced by the diffusion index of the demand for final products which was 49.6 (in Q4 2010 – 50.9). The decrease in the indicator occurred due to the fact that the percentage of enterprises with the increased demand for their final products decreased to 21.8% (in Q4 2010 – 23.7%).

The decrease occurred in all sectors other than “production and distribution of electricity, gas and water”, “transport and communications” and “mining industry”, where the demand increased although with lower rates as compared to the previous quarter. The highest decrease in the demand was noted in the hotel and restaurant business.

In Q2 2011 a notable growth in the demand for final products is expected in the economy as a whole: the diffusion index of the change in the demand went up to 60.0.

Alongside with that, 27.6% of interviewed enterprises anticipate that the demand for final products will rise, and only 7.7% anticipate that it will fall. The highest growth in the demand is expected in the “manufacturing industry”, and enterprises in the sector of “production and distribution of electricity, gas and water” expect that the indicator will fall.

The growth rates of prices for final products of enterprises in Q1 2011 somewhat increased as compared to the previous quarter: the diffusion index of the change in prices for final products has risen to 62.8 (in Q4 2010 – 60.7) due to the increased number of enterprises which noted the price growth to 30.5% (in Q4 2010 – 25.9%).

The growth in prices for final products is noted by all sectors except agriculture where the indicator decreased insignificantly (to 49.6). The highest increase in the growth rates occurred in such industries as “production and distribution of electricity, gas and water”, “trade”, “manufacturing industry” and “mining industry”. The slowdown in the indicator was observed in the “transport and communications” and “mining industry”.

In Q2 2011 some slowdown in the price growth rates is anticipated; that is evidenced by the diffusion index of the change in prices for final products which was 59.6. The maximum decrease in the price growth rates is anticipated in such industries as “production and distribution of electricity, gas and water”, “mining industry” and “real estate operations, rent and services provided to enterprises”. At the same time, an increase in the growth rates of prices for final products is anticipated in agriculture and construction.

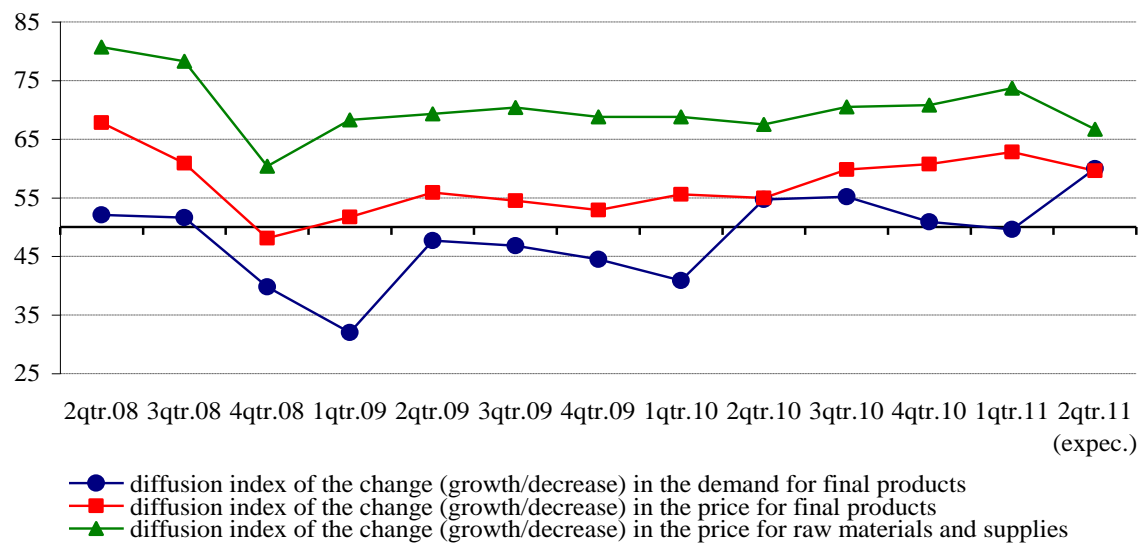
In Q1 2011 there was a notable increase in the growth rates of prices for raw materials and supplies as compared to the previous quarter; they still remain at a high level in the economy as a whole: the diffusion index of the change in the price for raw materials and supplies was 73.7 (in Q4 2010 – 70.8). The increased rates of price growth were observed in all industries except “agriculture, hunting and forestry” and “transport and communications”. In the sample as a whole a number of enterprises that noted the increase in prices for raw materials and supplies increased as compared to the previous quarter amounting to 55.9% (in Q4 2010 – 50.1%). The number of enterprises with decreased prices for raw materials and supplies accounted for 1% only.

In Q2 2011 the diffusion index of the change in the price for raw materials and supplies has fallen to 66.7 indicating the slowdown in the growth of prices. At the same time the number of respondents anticipating the price growth reduced significantly – to 42.4% (in Q4 2010 – 55.9%) (figure 8).

Thus, judging from the dynamics of the relevant diffusion indices, anticipations of the enterprises about Q2 2011 are associated with a slowdown in the growth rates of prices for raw materials and supplies and for final products and a notable growth in the demand for final products.

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

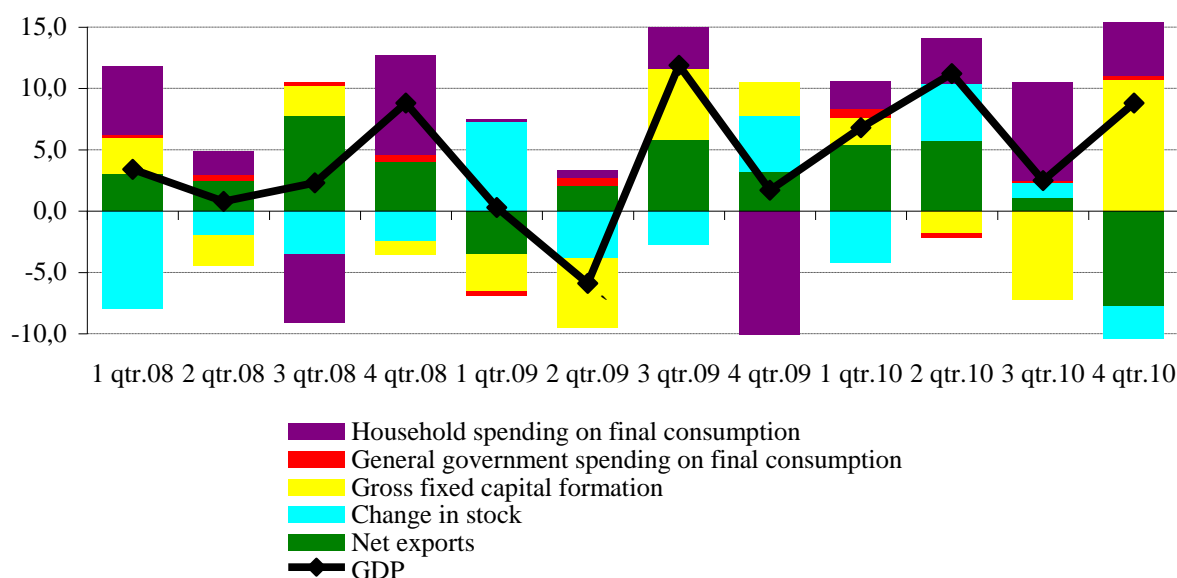
In Q4 2010 the GDP based on the final consumption method as compared to the respective period of 2009 increased in real terms, according to the estimate, by 8.8% (in the previous quarter - by 2.5%).

Despite the significant fall in one of the key GDP components (gross fixed capital formation) – net exports, the growth in gross formation and increase in spending on final consumption were the reason for the GDP growth, with significant acceleration of its rate. Gross formation increased by 20.2%, spending on final consumption grew up by 16.8%, and net exports decreased by 88.0%, because of the growth in imports and decrease in exports.

Net exports' contribution to the GDP growth was negative and accounted for (-)5.9%, gross fixed capital formation (+)10.7%, households consumption (+)8.4%, change in stock (-)3.2% (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

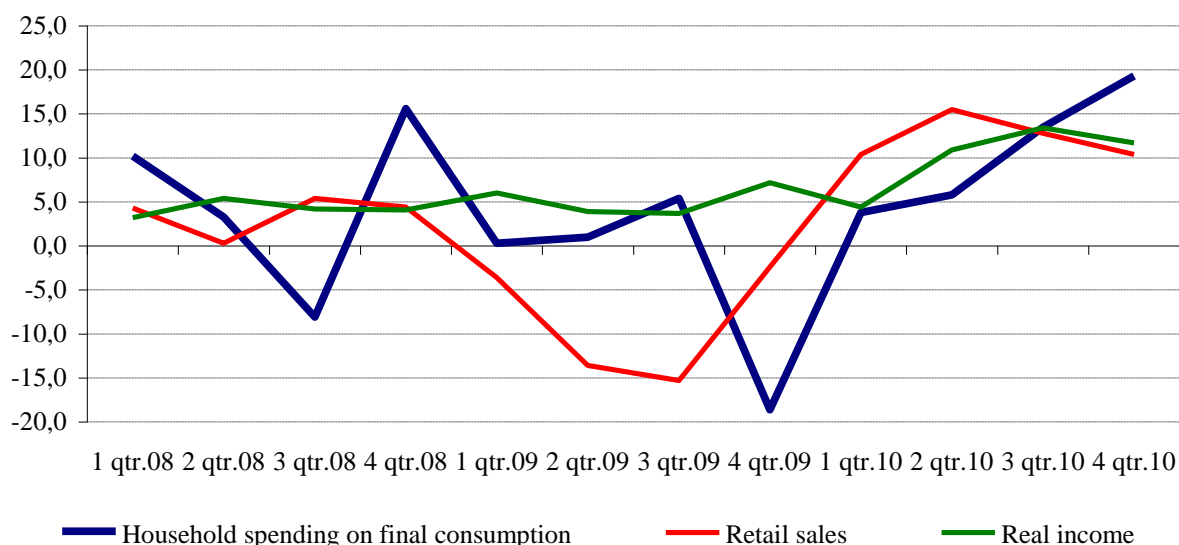
2.1.1. Individual Consumption and Investment Demand

Household spending on final consumption in Q4 2010 increased versus the respective period of 2009 by 19.3% (in Q3 2010 – the growth by 13.5%).

The slowdown of in the growth rate of per capita income in real terms to 11.7% (in Q3 2010 – the growth by 13.4%) also affected retail sales, whose rate slowed down to 10.4% (in Q3 2010 – the growth by 12.8%). Nonetheless, a fairly high growth rate in the retail sales had a significant impact on the improvement of one of the key GDP components by the aggregate demand method, namely the growth in the household spending on final consumption, which also benefited from a low comparative base, since in Q4 2009 the household spending on final consumption decreased by 18.6% (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

During the entire 2009 the population had more preference to buying in the markets whereas sales in the shops and shopping malls, whose percentage in the total volume of retail sales is significant and accounts for 55%, decreased.

In 2010 the growth in the business activity and recovery of the Kazakh economy, stabilization of the situation in the banking sector, overcoming of negative consequences of the crisis in the global economy as well as the increase in the amounts of social welfare payments, retirement benefits, scholarships and wages were the basis for the change in the consuming behavior pattern of the population. As a result, the volumes of sales increased both in the markets and in the shops, deferred demand began to realize and retail sales increased by 12.3% at the end of 2010.

The total volume of spending on gross capital formation, after its significant decline in Q3 2010 by 25.0%, in Q4 2010 increased by 20.2% as compared to the respective period of 2009, thus making positive contribution to the GDP growth of (+)7.5%.

In the structure of gross formation the gross fixed capital formation increased significantly, which, after its decline in the prior quarter by 25.8% increased by 48.7% in Q4 2010 thus contributing positively to the GDP growth of (+)10.7%.

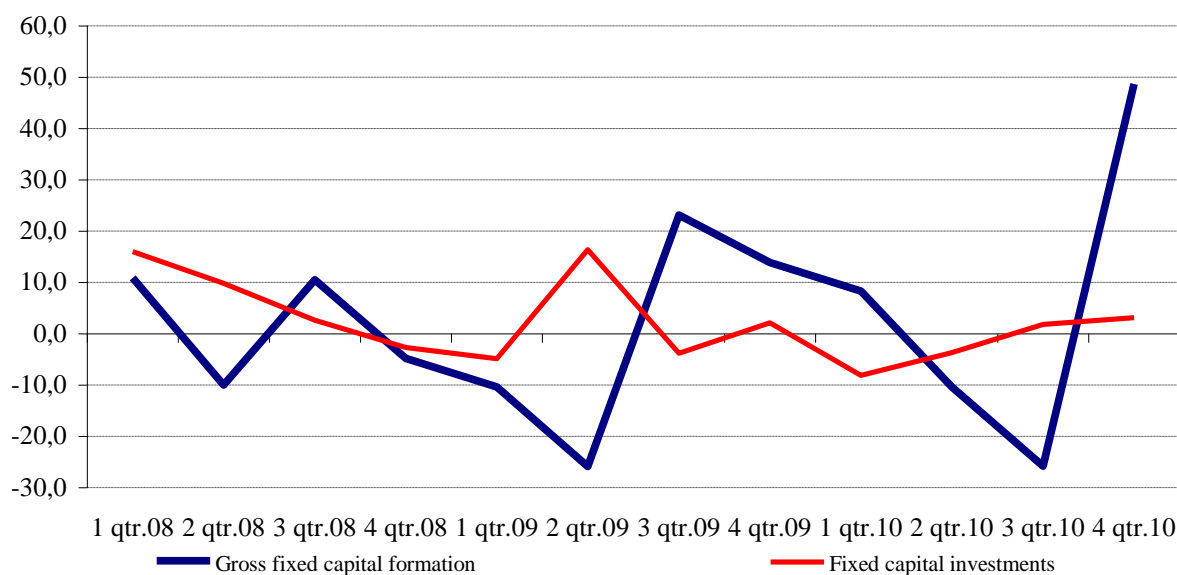
Such growth was ensured by the investment activity of enterprises which improved in Q4 2010 and resulted in a 3.1% increase of fixed capital investments (Q3 2010 – the growth by 1.8%) (figure 11).

In its turn, the second component of gross formation, namely the change in stock, decreased by 21.2% in comparable prices, thus making negative contribution to the GDP growth of (-) 3.2%.

However, such negative contribution was fully neutralized by significant positive effect of the first component, thus resulting in the growth of gross formation as a whole.

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 Q4 2010 as compared to the respective period of 2009, increased by 3.5% (in Q3 2010 – the growth by 2.7%).

In general, during Q4 2010 the state budget spending was financed in the amount of KZT1 280.6 bln. or 6.0% of GDP. As compared to Q4 2009, the increase accounted for 23.6%.

Current state budget expenditures totaled KZT914.9 bln., which is by 24.3% greater than in Q4 2009. Within the current expenditures, the expenditures for interest payments on domestic loans, for current transfers to legal entities as well as for service purchases and other current expenditures, increased the most. Capital expenditures of the state budget in Q4 2010 increased by 21.7% as compared to the respective period of 2009, mainly because of the growth in the item “Buildup of fixed capital” in absolute terms. The highest increase in percentage, as compared to the respective quarter of 2009, was demonstrated by purchases of land and intangible assets and capital transfers abroad, by 4.1 and 2.2 times, respectively.

During October-December 2010, state budget revenues amounted to KZT1543.0 bln. or 7.2% of GDP, which is by 23.6% greater than in October-December 2009. Two items still prevail in the structure of the state budget revenues: tax revenues – 73.8% out of the total revenues (in Q4 2009 – 71.5%) and official transfers – 21.1% (20.4%). A high percentage of official transfers was secured by the receipt of the guaranteed transfer of KZT275.0 bln. from the National Fund of the Republic of Kazakhstan to the republican budget.

As a whole, in Q4 2010 tax revenues increased by 45.0% as compared to Q4 2009. The increase was due to the increased revenues from value added tax and revenues from the use of natural and other resources 65.3% and 47.8%, respectively.

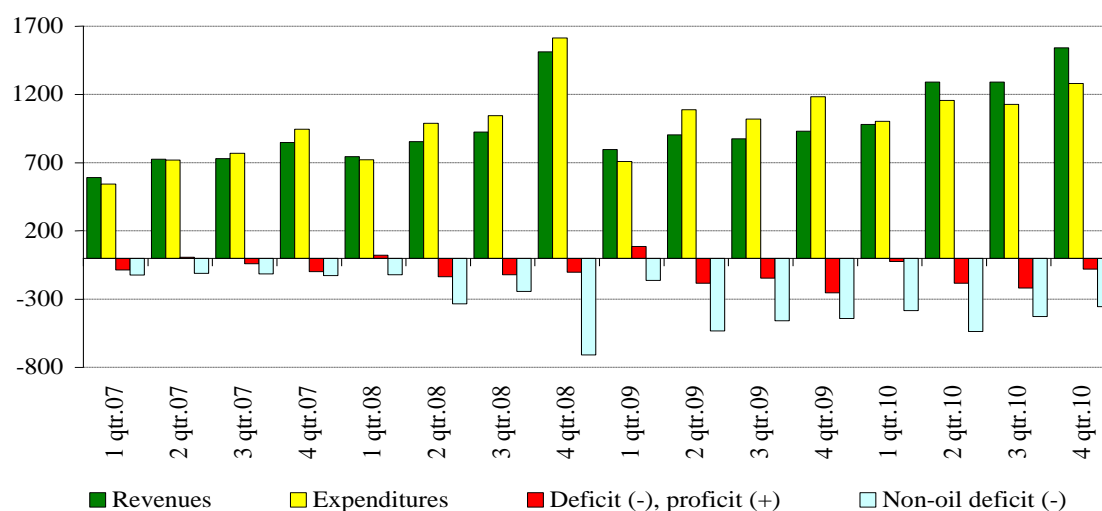
In Q4 2010 as compared to Q4 2009, revenues from the fixed capital sales increased by 2.2 times, whereas the volume of non-tax revenues decreased by 30.3%.

Since the expenditures were in excess of revenues to the state budget in Q4 2010, the deficit of KZT79.8 bln. showed up whereas in the respective quarter of 2009 the deficit

amounted to KZT252.5 bln. (figure 12). It should be noted that without the guaranteed transfer of KZT 275.0 bln. to the republican budget from the National Fund, Q4 2010 would have ended with the non-oil deficit of KZT354.8 bln.

figure 12

Execution of the state budget, % of GDP



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

In Q4 2010 the Ministry of Finance borrowed KZT144.4 bln., mainly by issuing government issue-grade securities. During the same period debentures were also extinguished on securities issued earlier for the amount of KZT70.0 bln. As a result, account balances of the Government of the Republic of Kazakhstan with the National Bank decreased by KZT5.4 bln.

Government domestic debt for Q4 2010 increased to KZT1669.1 bln. (7.8% of GDP), i.e. by 29.5% as compared to Q4 2009 (8.1% of GDP). The growth was secured by the issue of government long-term treasury obligations (MEUKAM), government long-term indexed treasury obligations (MUIKAM), and government long-term saving treasury obligations (MEUZHKAM).

The Government's external debt in Q4 2010 increased by 68.0% as compared to Q4 2009 (1.6% of GDP) and amounted to KZT552.9 bln. (2.6% of GDP).

2.1.3. External Sector

– World Prices

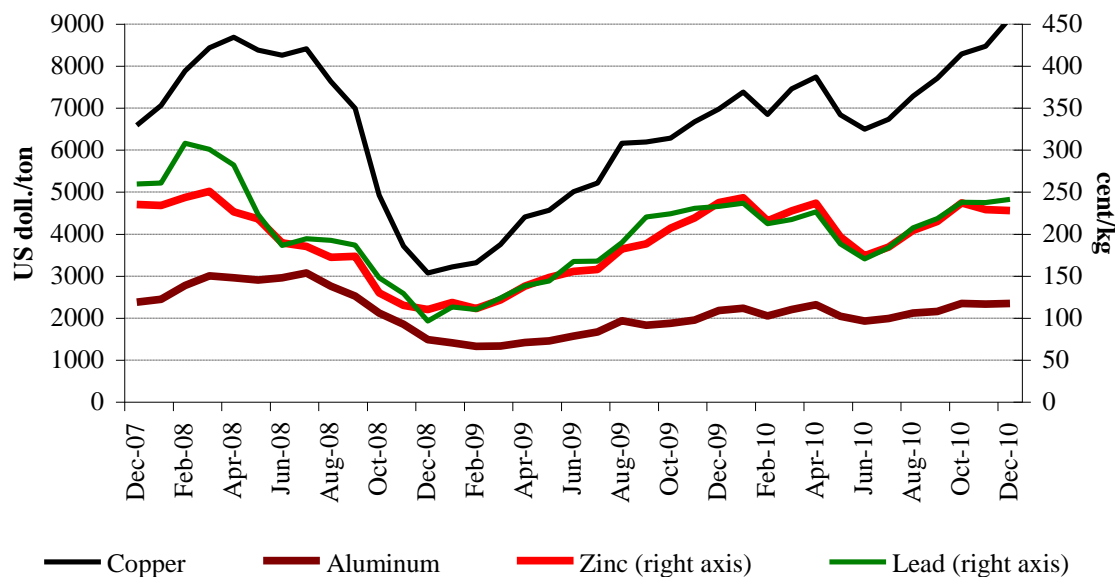
In Q4 2010 the situation in the global commodity markets remained unstable, which was accompanied by volatility of prices for certain commodities.

World prices for metals in October-December 2010 demonstrated a multidirectional trend. Some metals increased in price whereas the prices for some others decreased or remained stable. Prices for copper in Q4 2010 had a steady upward trend. On the overall, during the period they had grown by 19.2% and were at US\$8636.3 per ton on average during the period. Prices for aluminum were volatile: the growth was interchanging with the fall in prices. On the overall, in October-December 2010 they increased by 12.1% and amounted to US\$2343.7 per ton. World prices for lead in Q4 2010 increased by 17.6% and amounted to 239 cents per gram on the average during the period. Prices for zinc were decreasing during

the entire period, however, they increased by 15.0% as compared to Q3 2010, with the average price for the period being 231.5 cents per a kilo (figure 13).

figure 13

Dynamics of world prices for metals

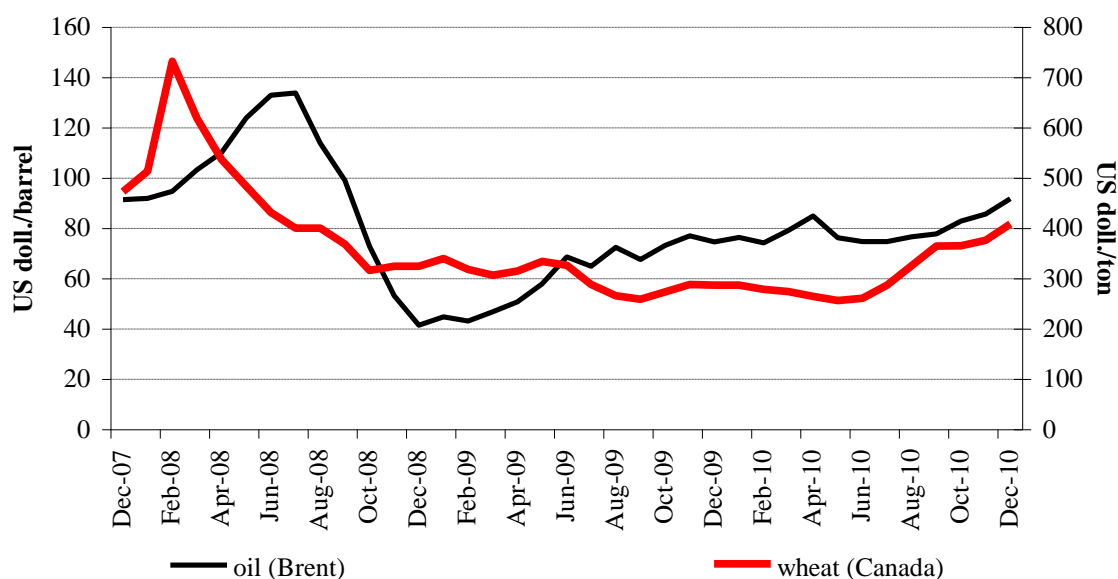


Source: World Bank

In Q4 2010 an upward trend for oil prices in the global market continued. As a whole, during Q4 2010 as compared to Q3 2010, oil prices (Brent) increased by 13.6% and were at US\$86.79 per barrel on average for the period (figure 14).

A similar situation was observed with the world prices for wheat. As a whole, during Q4 2010 the world price for wheat (Canada) increased by 17.6% and was on average at US\$383.6 per ton (figure 14).

figure 14

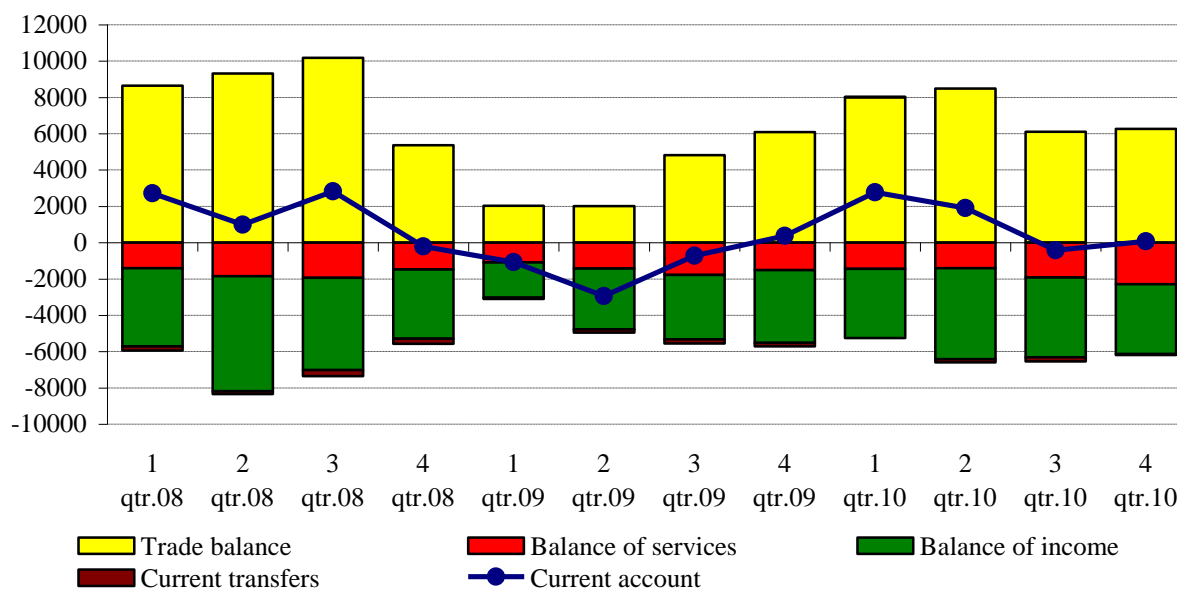
Dynamics of world prices for oil (Brent) and wheat (Canada)

Source: World Bank

– Balance of Payments

In Q4 2010 the current account balance was in surplus of US\$67.9 bln. (figure 15).

figure 15

Current account balance, US\$ mln.

Source: National Bank of the Republic of Kazakhstan

Proceeds from the exports of goods in Q4 2010 increased by 14.6%, and expenditures on commodity imports – by 23.6% as compared to Q4 2009. A positive trade balance increased by 2.9% and amounted to US\$6.3 bln., the deficit in the balance of services as compared to Q4 2009 increased by 51.5% to US\$2.3 bln., and the deficit in the income

balance decreased by 4.1% and amounted to US\$3.8 bln. Net payments to non-residents on current transfers amounted to US\$57.8 mln., which is by 70.4% less than in Q4 2009.

The net outflow of resources on financial account operations was US\$20.6 mln. in Q4 2010 (in Q4 2009 there was a net inflow of US\$ 1.2 bln.). Foreign assets of residents (except for reserve assets) increased by US\$12.3 bln., which is by 7.7 higher than in the respective period of 2009. Foreign liabilities of residents also increased by US\$12.3 bln. (growth by US\$ 2.8 bln. in Q4 2009).

As a result, the positive balance of payments for Q4 2010 amounted to US\$363.8 mln. (in Q4 2009 – US\$2.2 bln.).

– Terms of Trade and the Real Effective Exchange Rate

In Q4 2010 the aggregate terms of trade index was by 11.7% higher than the respective indicator for Q4 2009. Alongside with that, the terms of trade with the Euro zone countries deteriorated by 5.7%, and with Russia – improved by 1.9% (table 1).

table 1

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

	1 qtr.09	2 qtr.09	3 qtr.09	4 qtr.09	1 qtr.10	2 qtr.10	3 qtr.10	4 qtr.10
Export prices	-47.0	-52.5	-44.9	-16.6	48.2	60.1	17.3	18.9
Import prices	-1.2	-15.8	-18.2	-3.4	9.4	12.9	4.0	7.0
Terms of trade	-45.8	-42.4	-34.4	-11.3	22.6	42.7	16.1	11.7
including:								
the Euro zone countries								
Export prices	-54.2	-56.5	-49.9	-18.0	66.0	59.9	17.9	17.9
Import prices	17.7	0.1	12.8	32.5	22.4	31.0	14.1	24.5
Terms of trade	-57.8	-57.9	-59.2	-29.0	16.6	25.2	3.7	-5.7
Russia								
Export prices	-28.3	-36.2	-35.8	-14.7	23.4	33.6	-25.2	9.4
Import prices	-28.6	-25.5	-23.2	-2.6	28.5	19.1	8.9	7.5
Terms of trade	0.4	-15.0	-16.4	-12.6	-3.7	11.0	-30.6	1.9

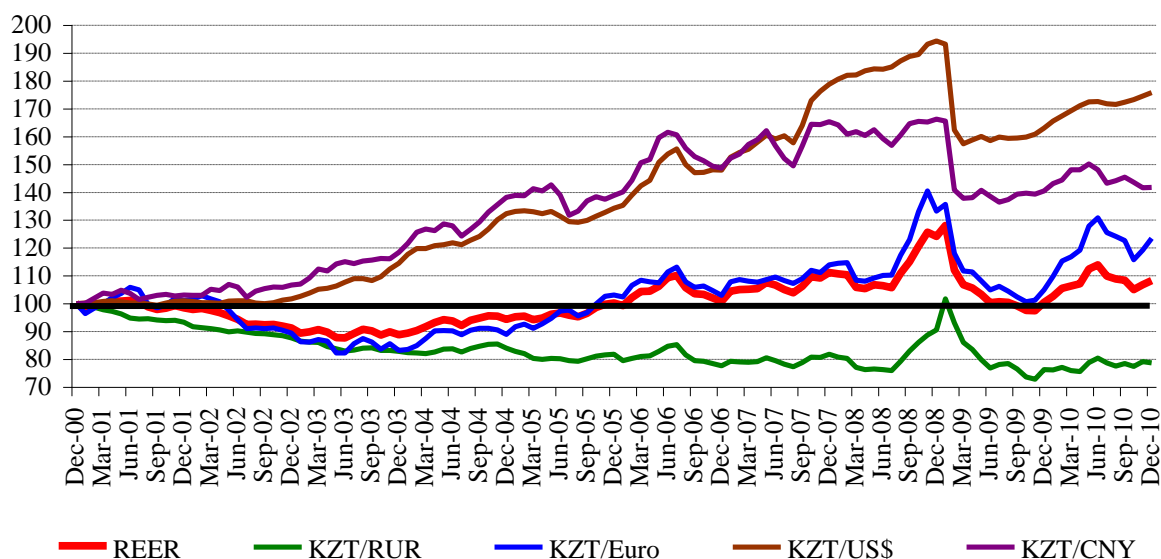
Source: National Bank of the Republic of Kazakhstan

Despite a relatively stable nominal exchange rate, the index of the real effective exchange rate of the Tenge depreciated by 2.1% in Q4 2010 as compared to the prior period. Alongside with that, the Tenge has depreciated versus the CIS currencies basket by 0.1%, versus the basket of other currencies – by 2.8%.

During Q4 2010 the Tenge has appreciated in real terms against the US Dollar by 1.4% as compared to the previous period, depreciated by 3.7% against the Euro and appreciated against the Russian ruble by 0.2% (figure 16).

figure 16

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



Source: National Bank of the Republic of Kazakhstan

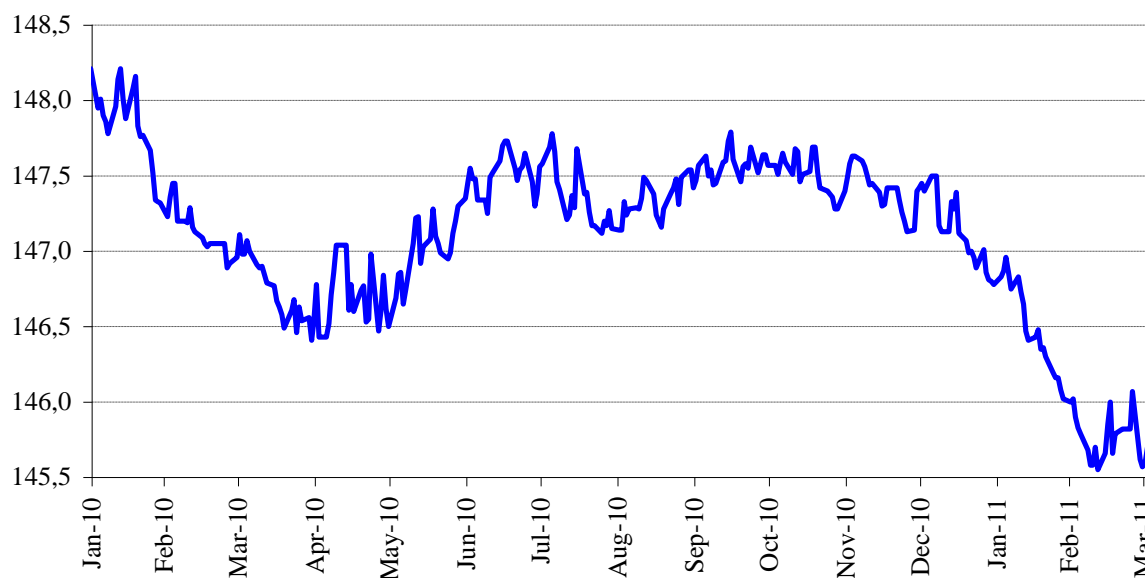
– Nominal exchange Rate of the Tenge

In February 2011 the National Bank has repealed the exchange rate band of the Tenge and moved to the managed floating exchange rate regime of the Tenge.

The average weighted exchange rate of the Tenge for Q1 2011 at the stock exchange was KZT146.37/1\$. The stock exchange rate at end-period was KZT145.70/1\$. Since the beginning of the year the Tenge has appreciated against the US Dollar in nominal terms by 1.2%. (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

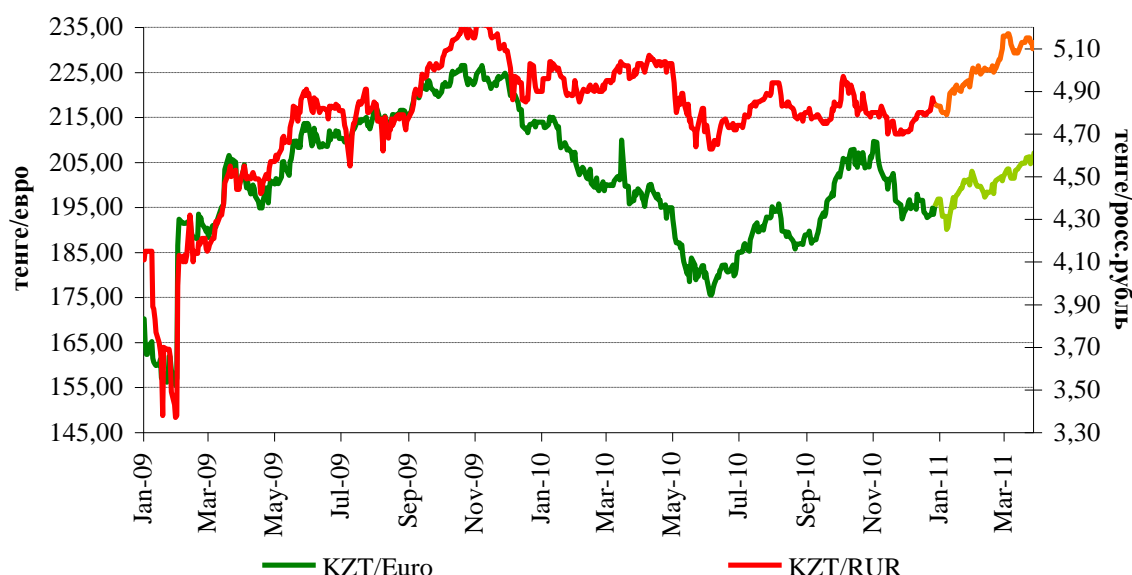
In January, February and March the Tenge appreciated against the US Dollar by 0.4%, 0.6%, and 0.2%, respectively.

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 was 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.

On the whole, during Q1 2011 the official exchange rate of the Tenge versus the Euro has depreciated by 5.2%, and versus the Russian ruble it depreciated by 5.4% (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

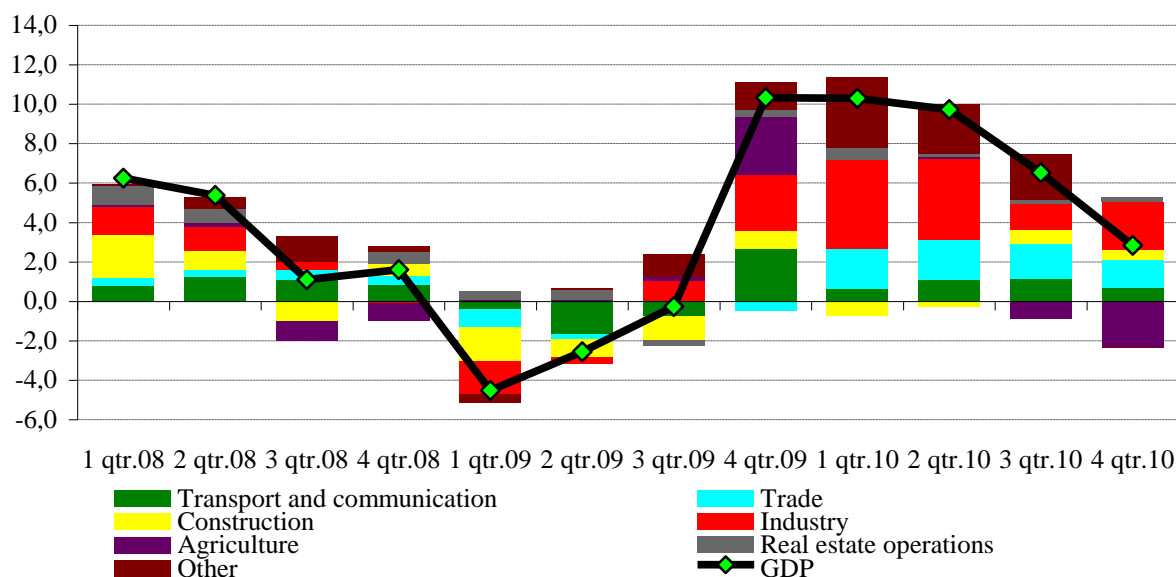
2.2. Production

The volume of GDP output in Q4 2010 amounted to KZT7008.4 bln. in current prices. Being positively influenced by the growth in production in virtually all sectors of the economy, except agriculture, financial and insurance activities, and other services the GDP in real terms increased, according to estimates, by 2.8% versus Q4 2009 (in Q3 2010 the growth accounted for 6.5%) (figure 19).

The slowdown in the growth rates of GDP in Q4 2010 was caused by a high comparative base, since in Q4 2009 GDP was characterized by high growth rates accounting for 10.3% according to estimates.

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 Q4 2010 the growth rate in the production of services slowed down to 1.8% (Q3 2010 – the growth by 3.6%), and in the production of commodities – to 1.2% (2.2%), at the same time the growth in the component of net taxes on products and imports accelerated significantly and reached 39.5% (18.6%).

In the production of commodities the industry and construction demonstrated growth whereas agriculture demonstrated decline. The index of physical volume in the industry was 107.9%, in the construction sector – 104.1%, and in agriculture – 73.7%, which on aggregate resulted in positive contribution to the GDP formation of 0.6%.

In the production of services the decline in the index of physical volume in financial and insurance activities by 3.3% as well as other services by 44.4% was fully neutralized by high growth in all other components, which resulted in positive contribution to the GDP formation at the level of 1.8%.

In Q4 2010 the growth in the volume of financial intermediation services indirectly measured which are used with a negative sign in the total volume of GDP, contributed negatively to the GDP formation in the amount of (-)1.8%, and the growth of net taxes on products and imports increased the GDP by 2.2%.

2.3. Labor Market

2.3.1. Employment and Unemployment

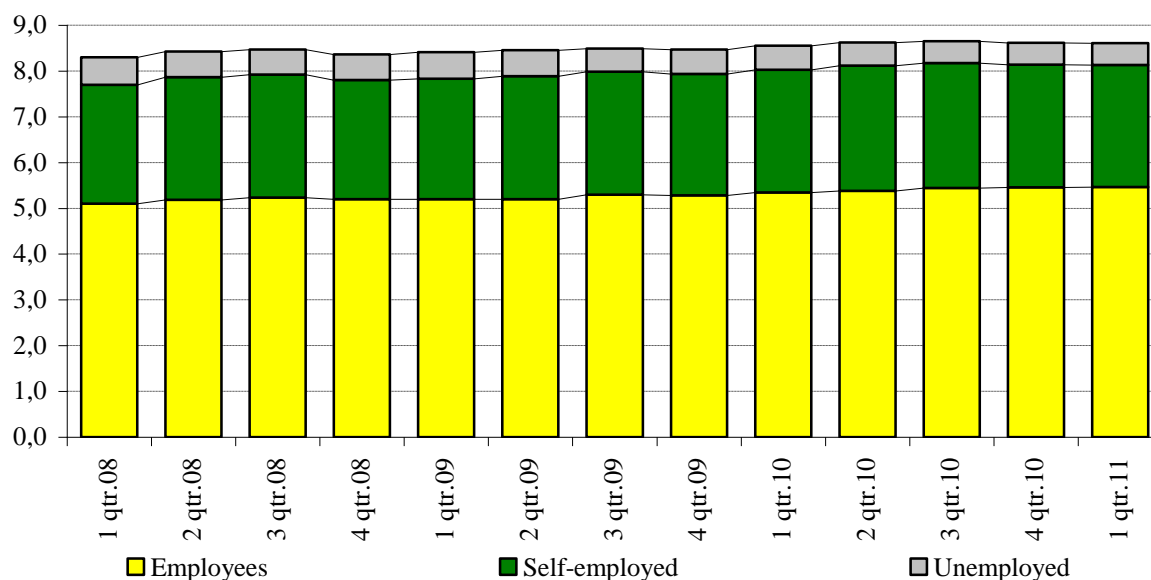
In Q1 2011 the number of people employed in the economy, according to tentative estimates, was 8.1 mln., having decreased by 0.1% versus the previous period (the growth versus Q1 2010 accounted for 1.3%). At the same time, the number of employees reached 5.5 mln. (the growth by 0.1%), the number of self-employed – 2.7 mln. people (the decrease by 0.5%).

In the structure of employees, 4.5 mln. individuals (82.0% of all employees) were working in public and non-public institutions, for natural persons – 0.7 mln. individuals (12.1%), at farms – 0.3 mln. individuals (5.9%).

In Q1 2011 the number of unemployed amounted to 475.9 thous. individuals, having increased by 0.3% as compared to the prior period and having decreased by 9.6% as compared to Q1 2010 (figure 20).

figure 20

The structure of economically active population, mln. individuals



Source: Agency of Statistics of the Republic of Kazakhstan

In January and February 2011 the following sectoral changes in the structural composition of employees were observed.

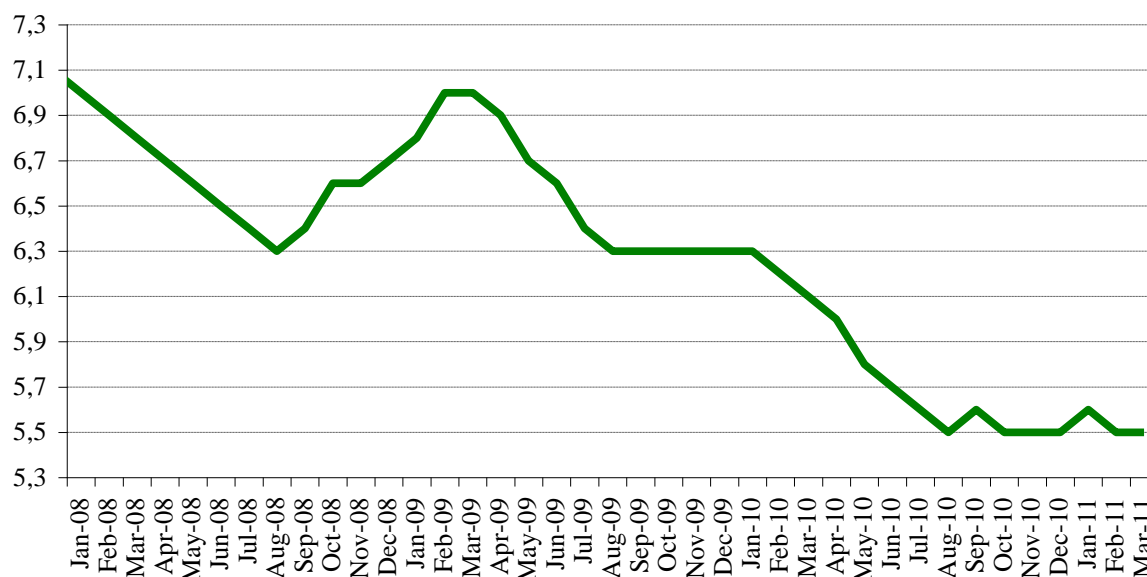
The main sectors that contributed to the growth in the employment rates, as compared to the respective period of 2010, were the industry; education; public healthcare and social services; construction, wholesale and retail trade; real estate operations; repair of cars and motorcycles; arts, entertainment and recreation; administration and ancillary services; accommodation and catering services.

The largest percentage of outflow of the employed was in the agriculture, forestry and fishery as well as in the general government and defense; and mandatory social welfare.

The decrease in the number of employed in some sectors was largely compensated by their growth in other sectors, whereby the unemployment rate in Q1 2011, according to preliminary information, remained unchanged from the prior quarter and accounted for 5.5% (figure 21).

The Road Map implemented as part of the Regional Employment and Staff Retraining Strategy had significant influence on decreasing the unemployment level and increasing employment of the population in 2009-2010. Despite the fact that arrangements under the Road Map were rolled back, the project completion has not yet had a material effect on the unemployment level.

figure 21

Actual unemployment rate, %

Source: Agency of Statistics of the Republic of Kazakhstan

2.3.2. Wages and Productivity

The twenty five percent increase in scholarships and wages to the public sector employees from Q2 2010, the growth in the business activity and improved condition of the Kazakh economy resulted in accelerated nominal and real growth in wages in 2010, as compared to 2009.

In Q4 2010, just as during the two prior quarters, the growth rates in nominal and real wages appeared to be significantly higher than in the respective periods of 2009. In Q4 2010 as compared to the indicator in Q4 2009 the average monthly wages in nominal terms increased by 16.2% (in Q4 2009 – by 12.1%), real wages increased by 8.0% (in Q4 2009 – by 5.8%).

The beginning of 2011 was also notable for the accelerated growth rates of wages. In January 2011 as compared to January 2010, wages in nominal terms increased by 16.2%, and in real terms increased by 7.5%. In February 2011 the growth rate accelerated and accounted for 17.7% and 8.2%, respectively.

In January 2011 wages in nominal terms increased in all areas of economic activities whereas in real terms the decline was noted in manufacturing industry, administrative and ancillary services, and in other services.

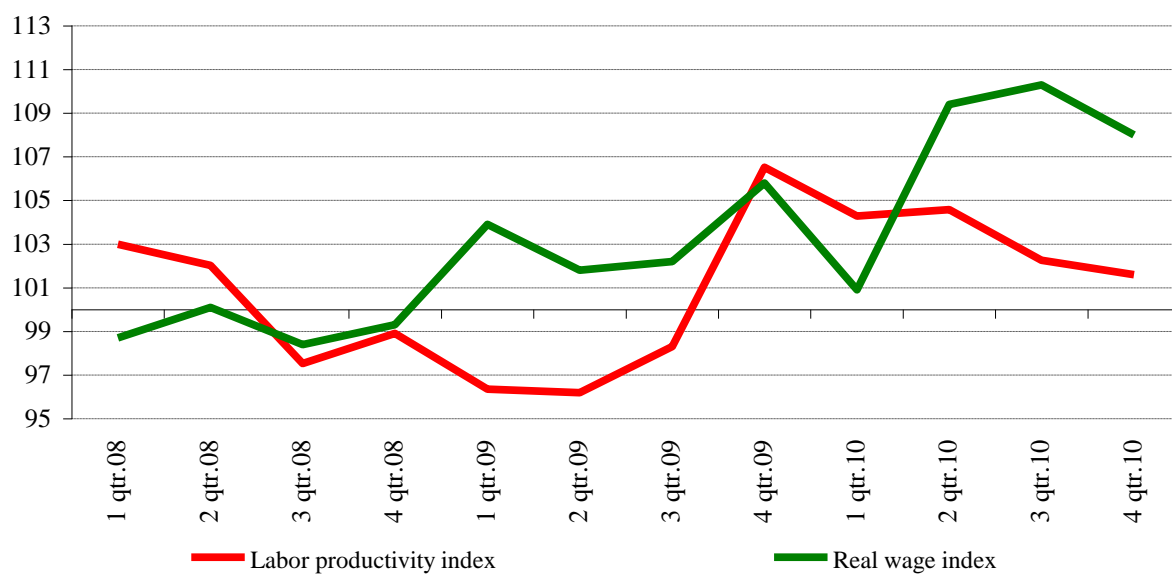
In February 2011 the decrease in real wages was noted only in administrative and ancillary services, at the same time the highest wage growth rates were recorded in the public healthcare and social services as well as in arts, entertainment and recreation, which grew up by 15.2% and 20.1% versus February 2010.

The highest wages in money terms in January and February 2011 were paid in the sector of financial and insurance activities, which amounted to KZT158610 and KZT167258, respectively.

The growth in the labor productivity index in Q4 2010 slowed down and, according to the National Bank's estimate, accounted for 1.6%, whereas in the prior quarter it amounted to 2.3% (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

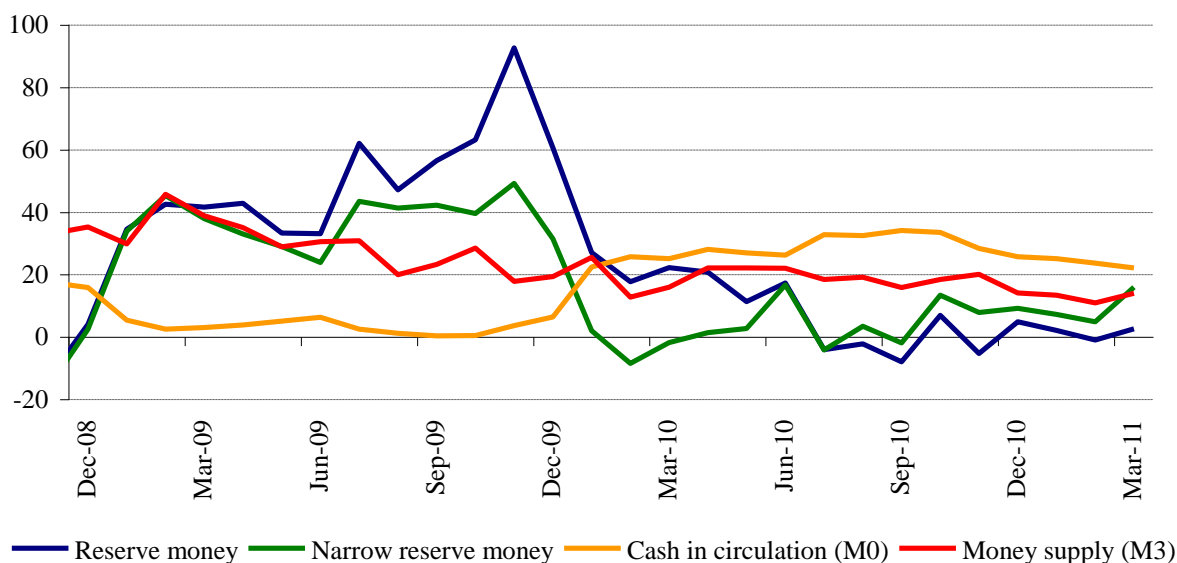
3. Money Supply

3.1. Monetary Aggregates

In Q1 2011 annual dynamics of cash in circulation demonstrated quite remarkable growth rates, whereas increases in money supply and narrow reserve money were moderate. The change in the reserve money was insignificant (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

Reserve money in Q1 2011 expanded by 9.2% and amounted to KZT2810.2 bln. at end-March 2011. Narrow reserve money expanded by 9.7% to KZT2351.4 bln.

In March 2011 as compared to March 2010, reserve money expanded by 2.7%.

Net international reserves of the National Bank increased by 30.3% to US\$34.6 bln. in March 2011, as compared to the respective period of 2010. Within their structure, despite operations on the servicing of the Government's external debt and the decrease in foreign currency balances with correspondent accounts of the second-tier banks at the National Bank, net currency reserves increased as a result of foreign exchange purchase in the domestic foreign exchange market and currency proceeds to the Government's accounts at the National Bank. Assets denominated in gold also increased.

In March 2011 as compared to March 2010, net domestic assets of the National Bank decreased (table 2), mainly because of a significant increase 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)

	2 qtr.10	3 qtr.10	4 qtr.10	1 qtr.11
Net international reserves	40.8	36.1	23.0	30.3
Net domestic assets	-341.1	-364.5	-498.0	-384.4
Net claims on the Government	-67.9	-83.5	-64.4	-0.3
Claims on the economy	-169.2	-154.3	-222.4	-352.7
Other net domestic assets	2.2	-18.8	-20.3	-34.9
Reserve money	17.3	-7.9	5.0	2.7
Narrow reserve money	16.8	-1.8	9.3	16.0

Source: National Bank of the Republic of Kazakhstan

3.1.2. Money Supply

In Q1 2011 money supply increased by 4.4% to KZT8923.9 bln.

In March 2011 as compared to March 2010, its growth accounted for 15.0% as a result of increase in net foreign assets of the banking system (table 3).

table 3

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

	2 qtr.10	3 qtr.10	4 qtr.10	1 qtr.11
Net foreign assets	132.6	138.3	63.3	50.3
Domestic assets	-12.3	-27.4	-14.2	-8.5
Claims on the Government	425.6	166.2	72.4	284.7
Claims on the economy	5.1	3.6	6.1	1.4
Other net domestic assets	-26.0	-42.1	-28.4	-11.1
Money supply	22.1	15.9	14.1	15.0
Cash in circulation	26.3	34.2	25.7	22.1
Deposits of residents	21.6	13.6	12.5	14.1

Source: National Bank of the Republic of Kazakhstan

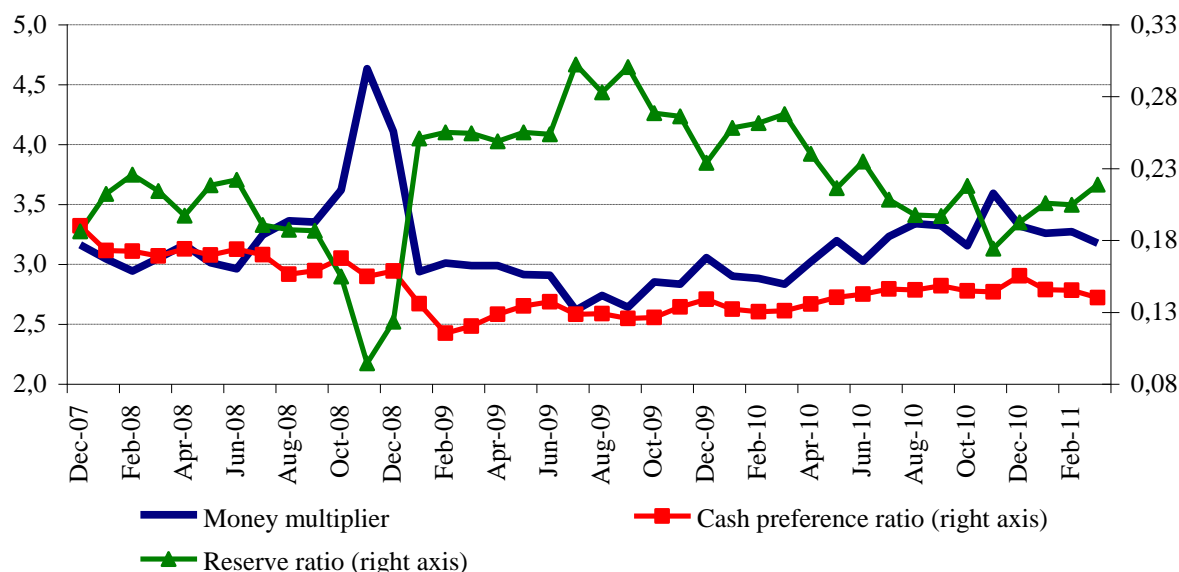
In the structure of net foreign assets of the banking system in March 2011 as compared to the respective period of 2010, net foreign assets of banks and of the National Bank increased. The growth in net foreign assets of banks was mainly stipulated by the decreased claims of non-residents on banks.

During the reviewed period in the structure of the main components of money supply the outstripping growth rates of cash in circulation were noted as compared to the growth rates of residents' deposits in the banking system. As a result, the share of deposits of residents in the structure of the money supply decreased from 88.4% in March 2010 to 87.7% at end-March 2011.

The money multiplier grew from 2.84 in March 2010 to 3.18 in March 2011 as a result of outstripping growth in the money supply against the rates of expansion of the reserve money. The reason for that was the decreased reserve ratio alongside with an 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 in Q1 2011 decreased by 4.5% to KZT1097.1 bln. The decrease in cash in circulation is explained by the seasonality factor that is related to a traditional decrease of net payouts on wages, and net proceeds from the sales of goods, works and services. At the same time, the impact of these factors was not neutralized by the growth in net proceeds from foreign exchange sales and net proceeds from loans to individuals and legal entities, based on the results of Q1 2011.

In March 2011 as compared to March 2010, cash in circulation increased by 22.1%. In Q1 2011 as compared to Q1 2010, payouts of cash from the bank cashier departments increased by 23.6% to KZT2.9 trln., cash receipts to the bank cashier departments – by 23.9% to KZT2.8 trln.

3.2. Financial Market

3.2.1. Deposits of Residents

At end-March 2011 deposits of residents amounted to KZT7826.7 bln., having increased by 5.8% during Q1 2011. Deposits of legal entities increased by 6.7%, deposits of individuals increased by 3.7%. Deposits in the domestic currency increased by 11.6% to KZT5367.1 bln., deposits in foreign currency – decreased by 5.0% amounting to KZT2459.6 bln.

In Q1 2011 the trend of preference to the domestic currency deposits over foreign currency deposits that appeared in 2010, persisted. The process led to a further decline in the degree of monetization of deposits, as a result of which the percentage of foreign currency deposits in March 2011 decreased to 31.4% versus 35% in December 2010.

Thus, the growth of the Tenge deposits served as a source for the overall deposit base growth (table 4).

table 4

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

	Mar.08	Mar.09	Mar.10	Mar.11
Deposits of residents	5.9	10.4	4.4	5.8
<i>of individuals</i>	<i>3.3</i>	<i>7.8</i>	<i>2.1</i>	<i>3.7</i>
<i>of non-bank legal entities</i>	<i>7.4</i>	<i>11.4</i>	<i>5.3</i>	<i>6.7</i>
Deposits in the Tenge	2.0	-10.6	13.3	11.6
Deposits in foreign currency	14.1	48.5	-7.2	-5.0

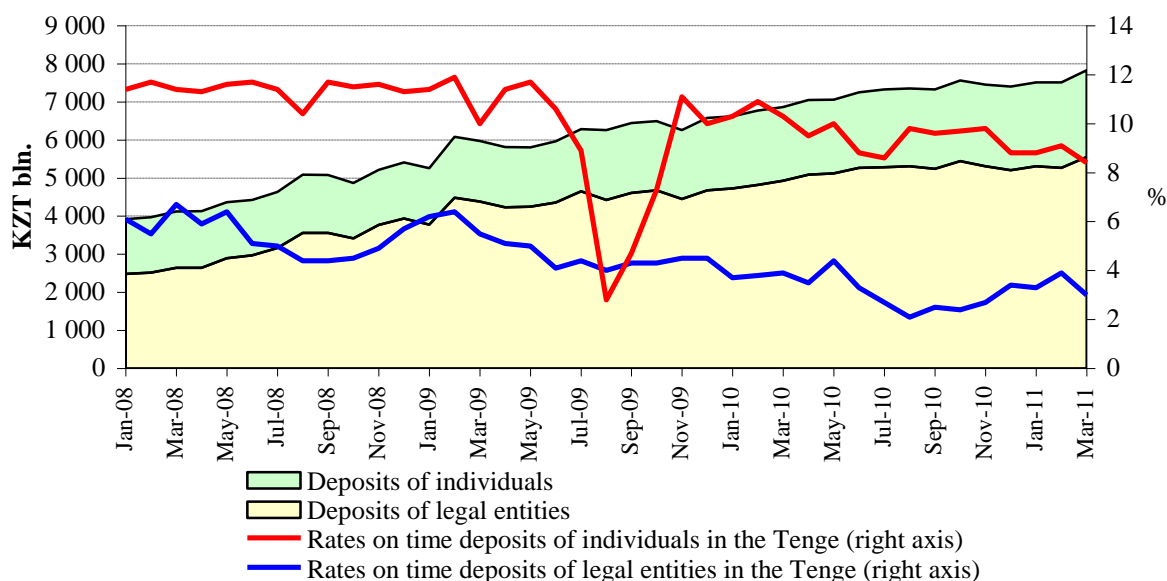
Source: National Bank of the Republic of Kazakhstan

The interest rates on deposits continued to decrease. The interest rates on deposits – both in the domestic currency and in foreign currency – have been generally lower during Q1 2011 than in Q1 2010.

The average weighted interest rate on the Tenge time deposits of non-bank legal entities was 3.0% in March 2011 (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

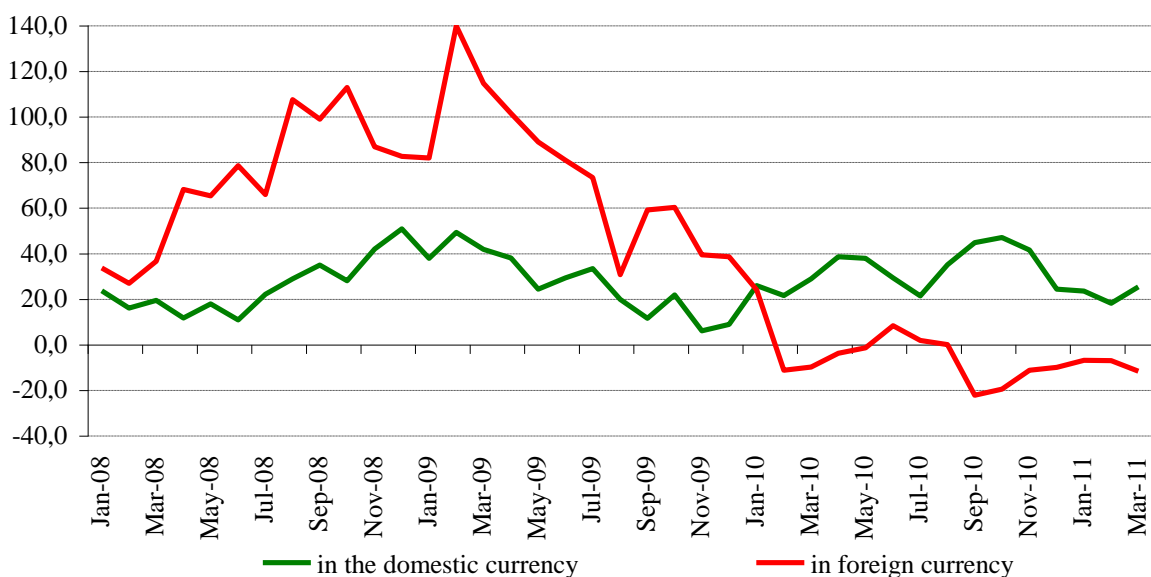


Source: National Bank of the Republic of Kazakhstan

Since the beginning of the year the volume of deposits of legal entities has increased by 6.7% to KZT5550.0 bln., and the annual growth (March 2011 to March 2010) accounted for 12.6%. Deposits of legal entities in the domestic currency increased in annual terms by 25.4% and deposits in foreign currency decreased by 11.6% (figure 26).

figure 26

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

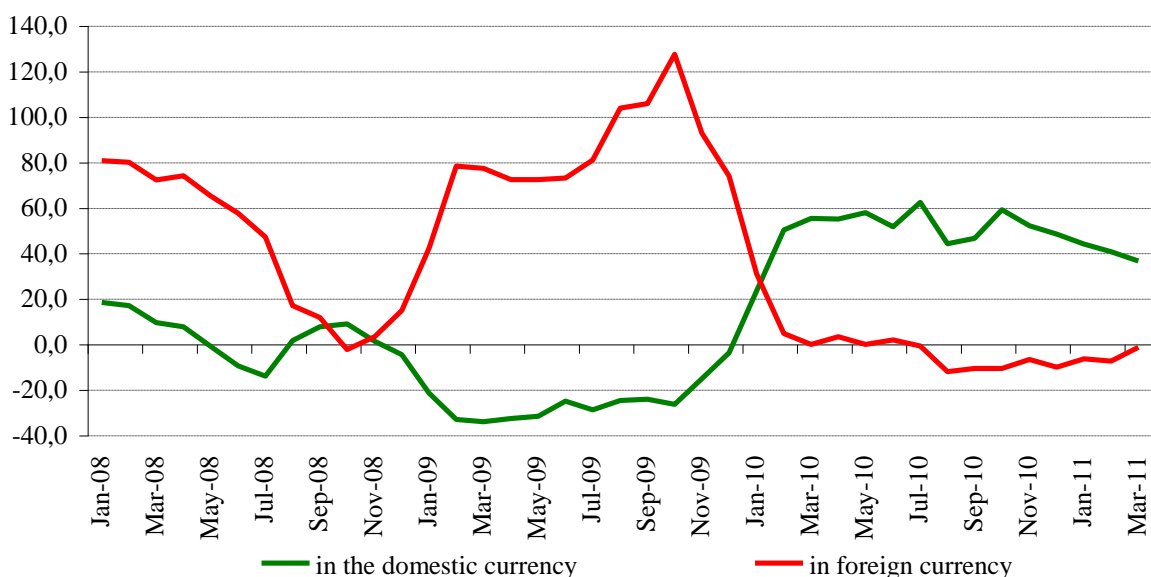


Source: National Bank of the Republic of Kazakhstan

The volume of deposits of individuals has increased by 3.7% to KZT2276.7 bln. since the beginning of the year, and the annual growth accounted for 17.8% in March 2011. Deposits of individuals in the domestic currency in annual terms increased by 36.8%, and foreign currency deposits decreased by 1.1% (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 Q1 2011 bank credits to the economy increased by 0.9% to KZT7665.9 bln. Credits to legal entities increased by 1.3%, credits to the population decreased by 0.2%.

Versus March 2010, the lending volume also increased by 0.9%, including the increase in credits to legal entities by 1.9%, and the decrease in credits to individuals by 1.7%.

The average weighted rate on credits to legal entities decreased from 11.9% to 10.9% in March 2011 as compared to December 2010. This was caused by the decrease in the cost of borrowing for legal entities, both in the domestic currency and foreign currency, with a more significant decrease in the rates on credits in the domestic currency.

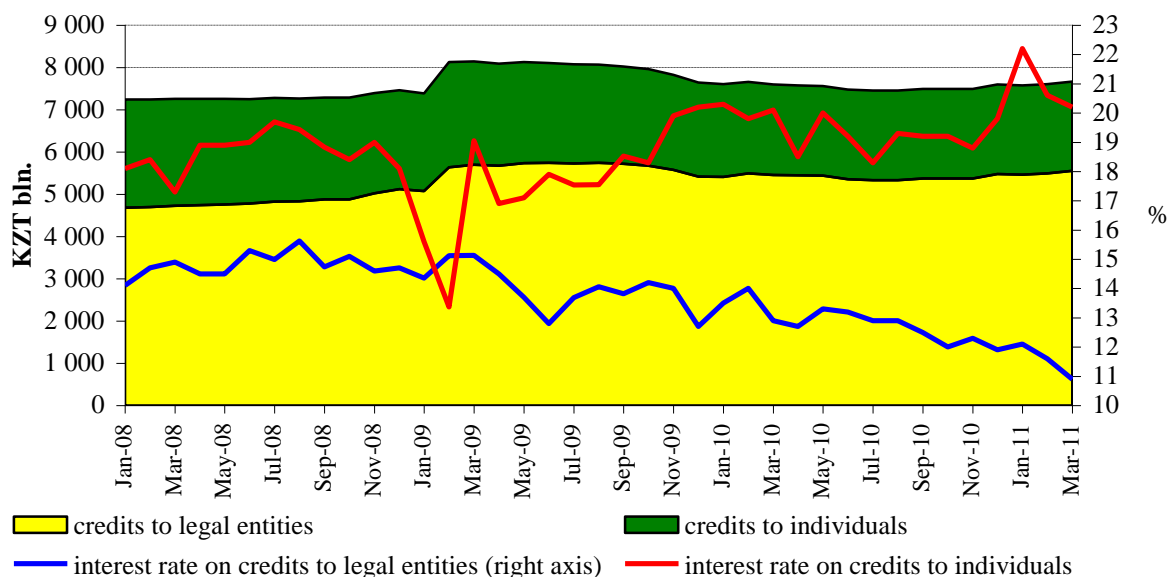
The average weighted rate on credits to individuals increased from 19.8% to 20.2% in March 2011, which was caused by the growth in rates on the domestic currency loans (figure 28).

In the structure of credits by objects of financing the major volume of debt fell on credits provided for the purchase of fixed assets (25.7%), for new construction and reconstruction (17.1%) as well as for other purposes (24.9%), mainly for refinancing of earlier loans.

In a sectoral breakdown, the highest debt on bank credits falls on non-production sphere and individual entrepreneurship (40.9%), trade (21.3%), construction (19.1%), and industry (11.1%).

figure 28

Dynamics of credits to the economy and their interest rates

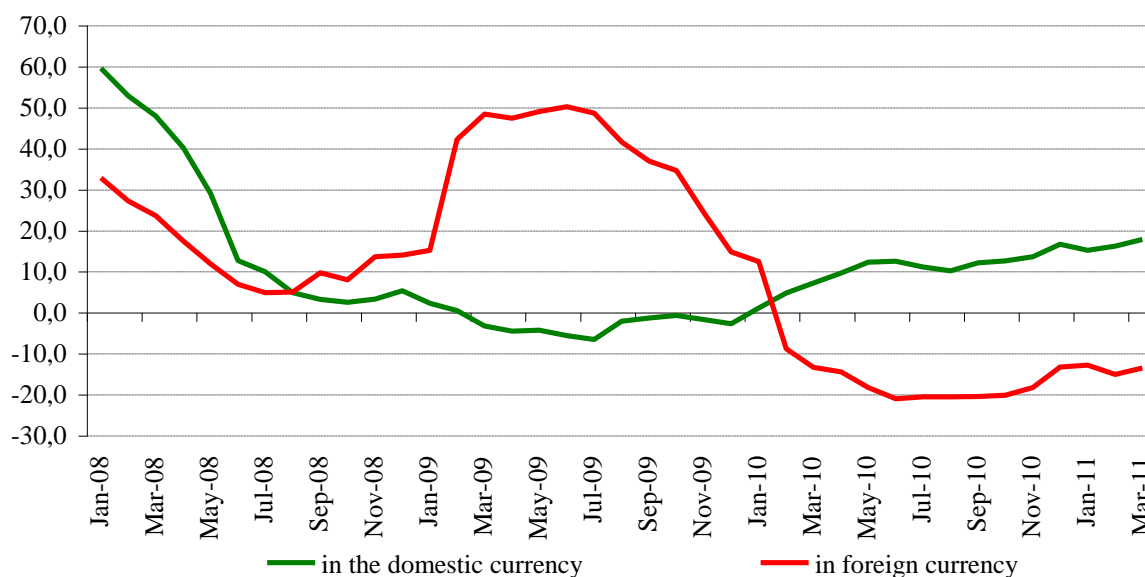


Source: National Bank of the Republic of Kazakhstan

The volume of credits to legal entities in March 2011 as compared to March 2010 increased by 0.9%. Credits to legal entities in the domestic currency increased by 17.9% in annual terms, and credits in foreign currency decreased by 13.4% (figure 29).

figure 29

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



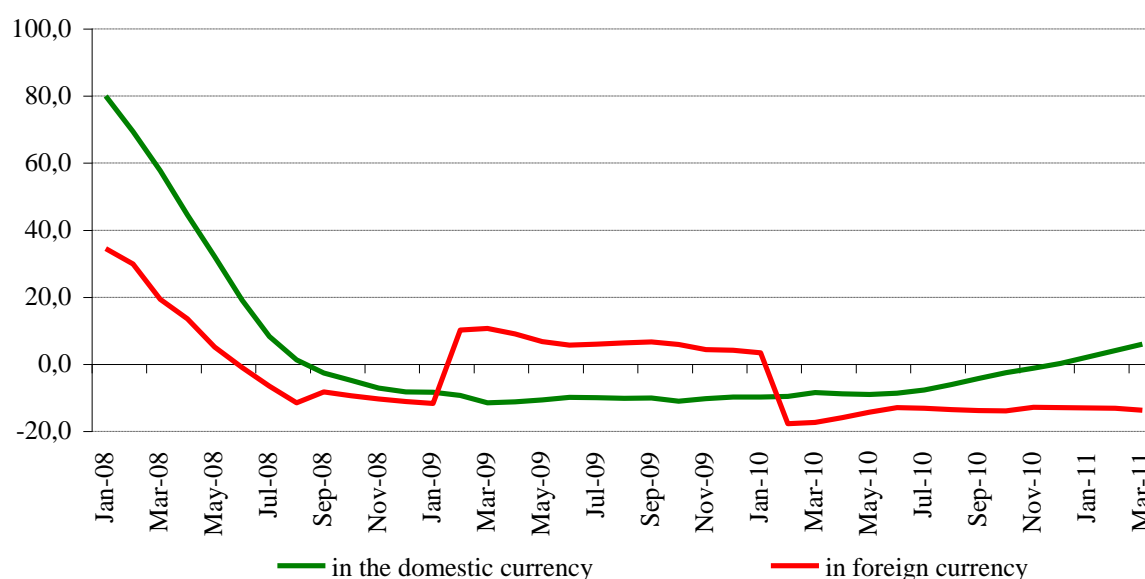
Source: National Bank of the Republic of Kazakhstan

The share of medium- and long-term credits at end-March 2011 amounted to 79.0% in the total volume of credits to legal entities (in December 2010 – 78.7%).

The volume of credits to individuals decreased by 1.7% in March 2011, as compared to the respective period of 2010. In the structure of credits to the population, credits in the domestic currency have demonstrated the increase by 6.0% and credits in foreign currency – the decrease by 13.7% (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

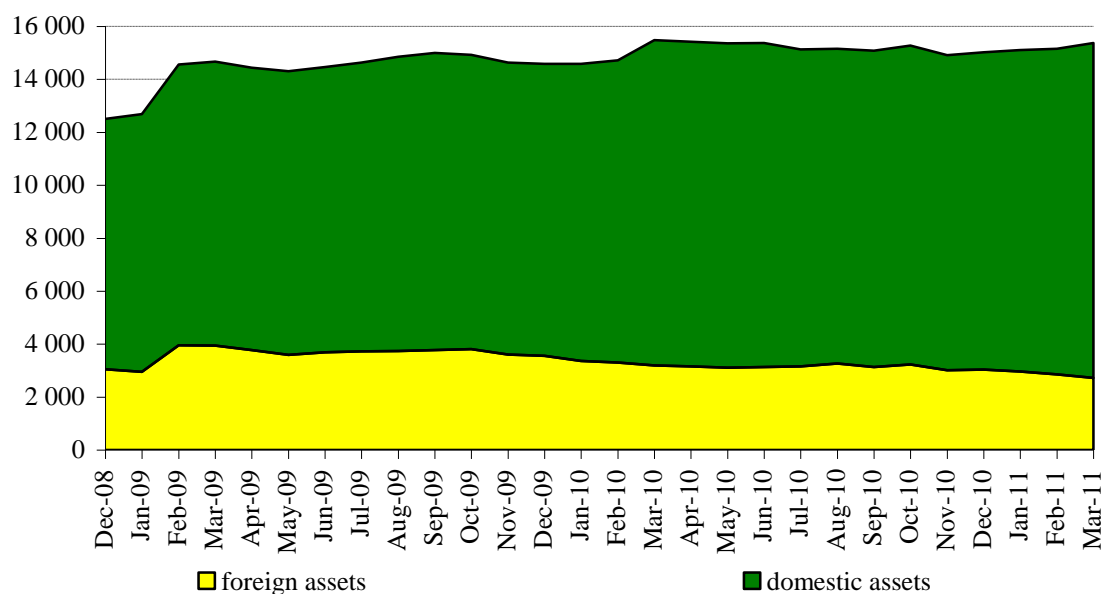
3.2.3. Bank Assets and Liabilities

– Assets

In Q1 2011 the amount of bank assets calculated under the Monetary Survey decreased by 2.4% to KZT15.4 trln. Bank assets decreased by 0.7% in annual terms (in March 2011 versus March 2010) (figure 31).

figure 31

Dynamics of bank assets, KZT bln.



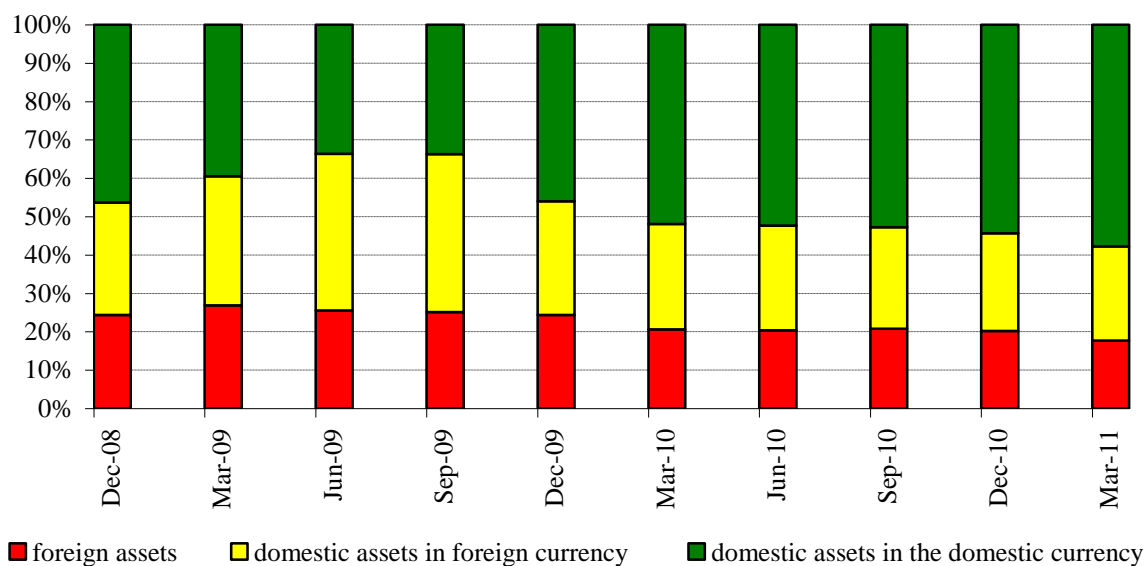
Source: National Bank of the Republic of Kazakhstan

Foreign assets of banks in March 2011 accounted for 17.7 % of the total volume of assets or US\$18.6 bln. They have decreased by 10.4% as compared to December 2010.

In the structure of foreign assets in March 2011, credits to non-residents accounted for 55.2% (in December 2010 – 49.6%), deposits placed with non-residents – 19.7% (in December 2010 – 28.5%), securities of non-residents – 5.9% (in December 2010 – 4.8%), other accounts receivable – 19.2% (in December 2010 – 17.2%).

Domestic assets in March 2011 accounted for 82.3% or KZT12.7 trln., where assets in the domestic currency amounted to 70.2% or KZT8.9 trln. and assets in foreign currency – 29.8% or KZT3.8 trln. (figure). In January-March 2011 domestic assets increased by 5.6%, including the increase in the domestic currency assets by 8.7% and the decrease in foreign currency assets by 1.2%. (figure 32).

figure 32

Structure of bank assets, %

Source: National Bank of the Republic of Kazakhstan

During January-March 2011 the quality of bank assets somewhat improved. The share of standard assets increased from 48.3% to 48.6%, share of doubtful assets decreased from 36.4% to 36.0%, and the share of bad assets didn't virtually change having increased from 15.3% to 15.4%.

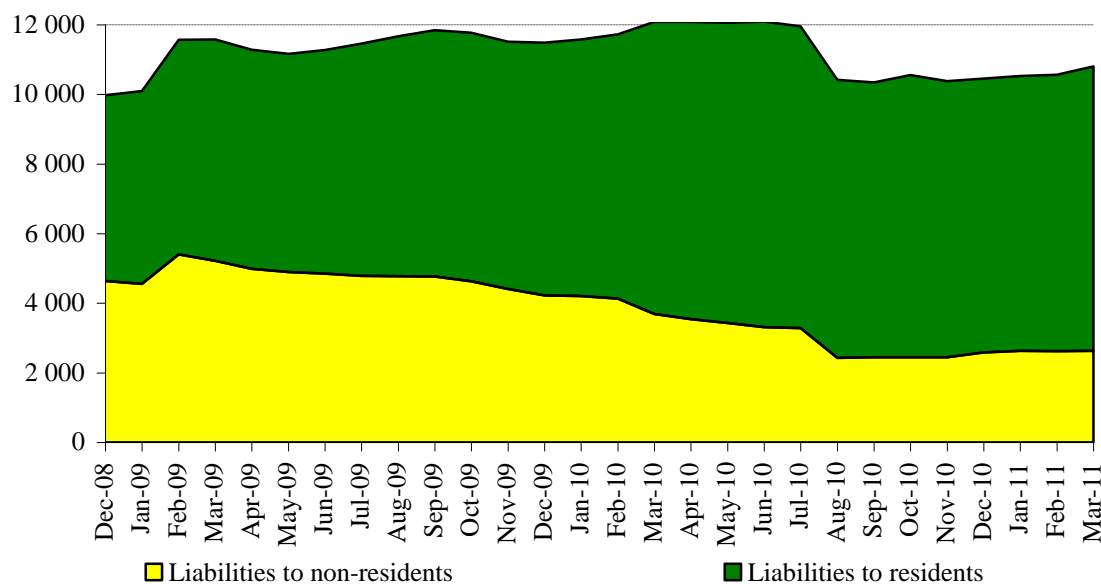
In addition, in the structure of doubtful assets a certain migration of assets focused on the concentration of assets of category 2 and 3, is observed. The share of assets of category 2 within the structure of doubtful assets increased from 11.6% to 13.5%, category 3 – increased from 19.5% to 22.3%, whereas the share of assets of category 1 decreased from 33.9% to 30.0%, category 4 – from 9.8% to 9.2%, category 5 – from 25.2% to 25.0%. 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 Q1 2011 bank assets demonstrated a slight growth. A high level of credit risk and low asset quality still represent weak aspects of the Kazakh banking system. As before, banks adhere to a conservative policy and avoid active crediting of the economy. At the same time, the quality of credit portfolio of Kazakh banks slightly deteriorated (the share of bad loans increased from 20.1% to 20.4%, and the share of standard loans decreased from 26.3% to 25.3%).

– Liabilities

In Q1 2011 total bank liabilities calculated in line with the Monetary Survey increased by 3.4 and amounted to KZT10.8 trln. at end-March (figure 33).

figure 33

Dynamics of bank liabilities, KZT bln.

Source: National Bank of the Republic of Kazakhstan

Bank liabilities to non-residents increased by 2.0% to KZT2.6 trln. (US\$18.1 bln.) in March 2011 as compared to December 2010. Bank liabilities decreased by 28.6% versus the respective month of 2010. At end-March 2011 they accounted for 24.4% of the volume of bank liabilities.

In March 2011, in the structure of bank liabilities to non-residents, the share of liabilities on deposits of non-residents increased from 9.6% (December 2010) to 11.6%, the share of liabilities on securities decreased from 65.0% to 63.6%, credits from non-residents decreased from 23.2% to 22.9%.

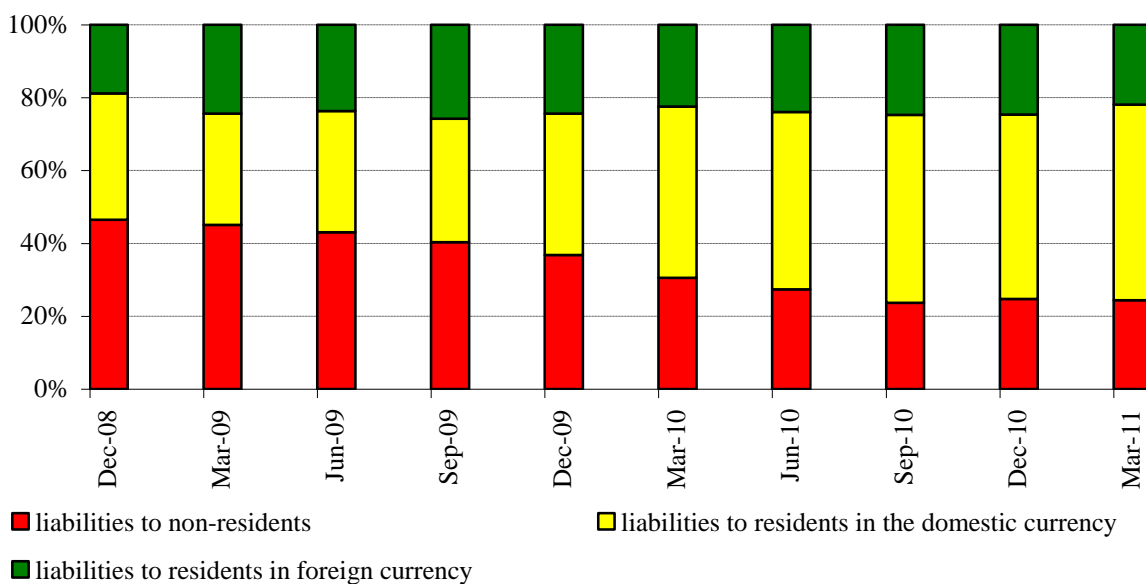
During January-March 2011 liabilities to residents increased by 3.8% to KZT8.17 trln. (US\$56.1 bln.), of which liabilities in the domestic currency increased by 9.4% to KZT5.8 trln., liabilities in foreign currency decreased by 7.8% to KZT2.4 trln. (figure 34).

Thus, in Q1 2011 there was a growth in liabilities, both liabilities to non-residents and liabilities to residents. The growth in liabilities to residents had a forward-looking nature and was secured by the increase in the Tenge component whereas the rate of growth in the liabilities to non-residents was lower and was achieved only due to the increase in deposits of non-residents.

Therefore, one may state that during the first quarter of this year the process of replacing the external funding by the domestic funding sources such as domestic deposits was continuing.

figure 34

Structure of bank liabilities, %



Source: National Bank of the Republic of Kazakhstan

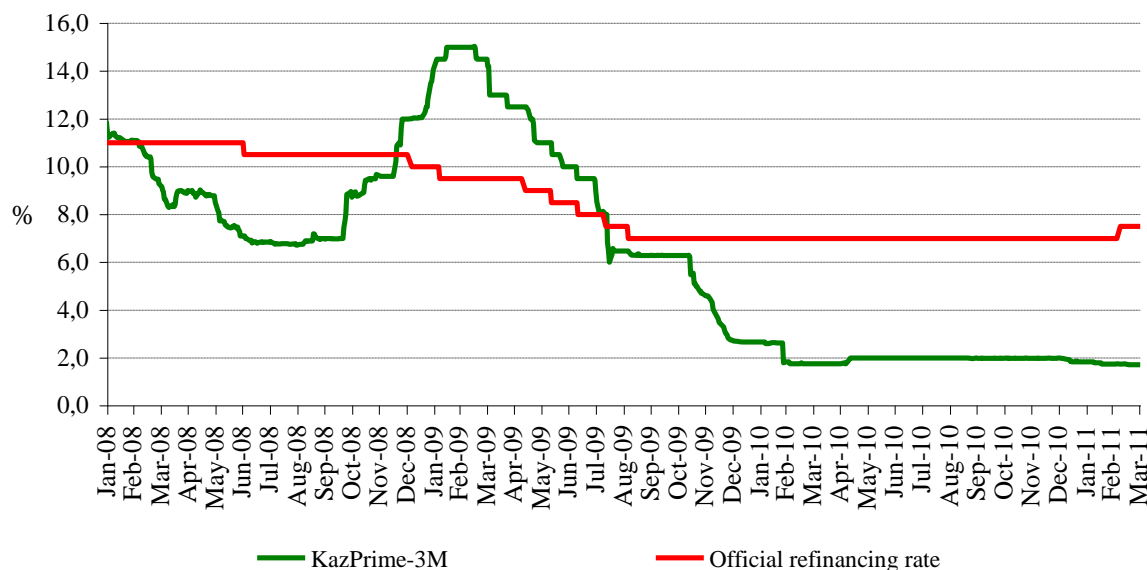
3.2.4. Financial Market Rates

In Q1 2011 there was a decrease in the interbank market rates.

The KazPrime index decreased from 1.98% on average in Q4 2010 to 1.79% on average in Q1 2011. At end-December 2010 this indicator was 2.00%, and at end-March 2011 – 1.71% (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

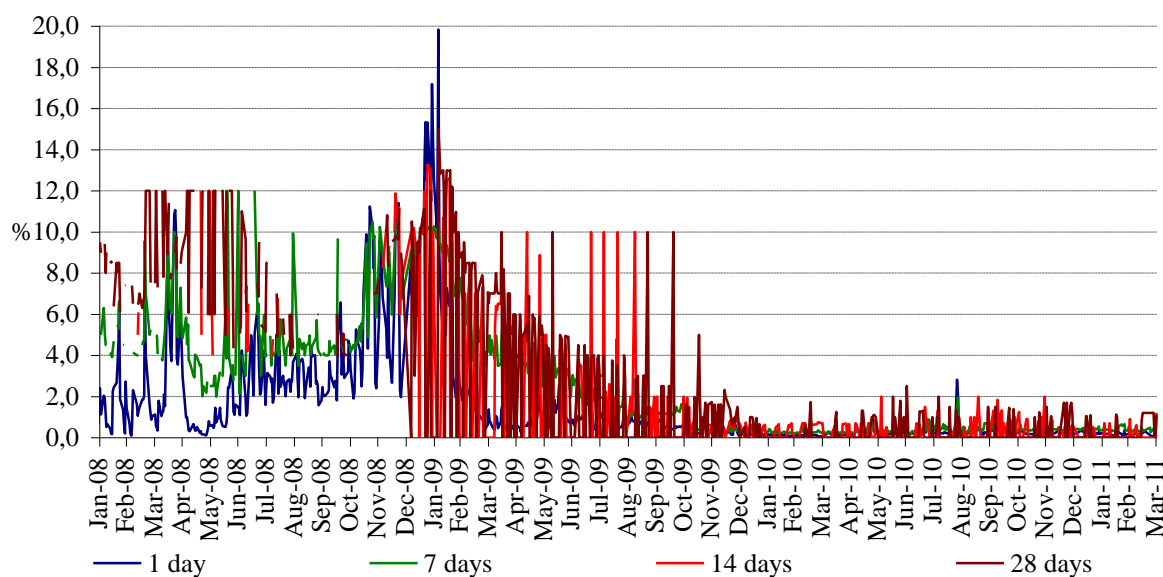
The average weighted rate on 1-day operations in the sector of the automatic REPO in Q1 2011 decreased and was 0.20% (in Q4 2010 – 0.28%). Its maximum level was 0.39% and minimum – 0.06%.

Rate fluctuations on 7-day REPO operations in Q1 2011 were within the range of 0.26% - 0.66% (the average weighted rate was 0.37%), on 14-day REPO operations – between 0.30% and 1.20% (the average weighted rate was 0.66%), and on 28-day REPO operations – between 0.87% and 1.20% (the average weighted rate was 1.12%) (figure 36).

The transaction volumes in the sector of automatic REPO in Q1 2011 decreased by 26.9% as compared to the prior quarter. At the same time, the volume on 28-day REPO operations increased as compared to Q4 2010.

figure 36

Dynamics of rates on REPO operations, %



Source: Kazakhstan Stock Exchange

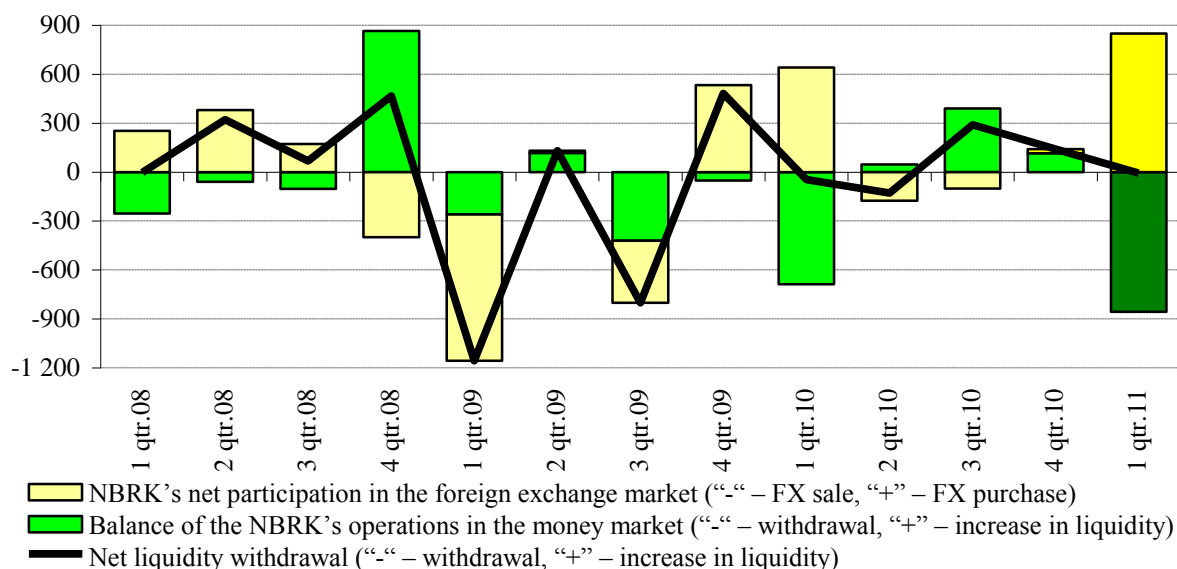
4. Monetary Policy Instruments and Operations

In Q1 2011 the situation in the financial market remained stable, banks had sufficient Tenge liquidity.

In Q1 2011 the National Bank's operations in the financial market resulted in the withdrawal of the Tenge liquidity, mainly because of the growth in balances with correspondent accounts of banks in the Tenge at the National Bank as well as the growth in the volume of short-term notes in circulation (figure 37).

figure 37

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

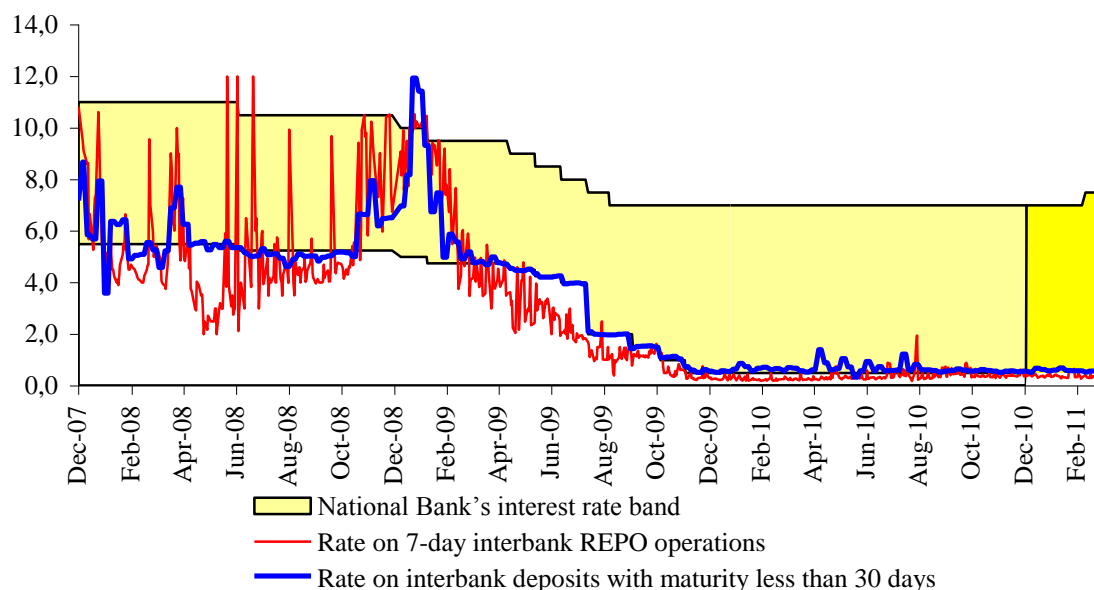


Source: National Bank of the Republic of Kazakhstan

In Q1 2011 the National Bank's rate band changed. Against the backdrop of increased inflationary pressure in the economy, at the resolution of the National Bank's Management Board the official refinancing rate was increased to 7.5% from March 9, 2011. The rates on deposits attracted from banks didn't change: the rate on 7-day deposits is 0.5%, on 1-month deposits – 1.0%.

In Q1 2011 the situation in the money market was characterized by the downward trend in interest rate behavior. On average, in Q1 2011 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 increased from 0.59% in Q4 2010 to 0.61% in Q1 2011. The average weighted rate on interbank 7-day REPO operations decreased from 0.41% to 0.37%, respectively (figure 38).

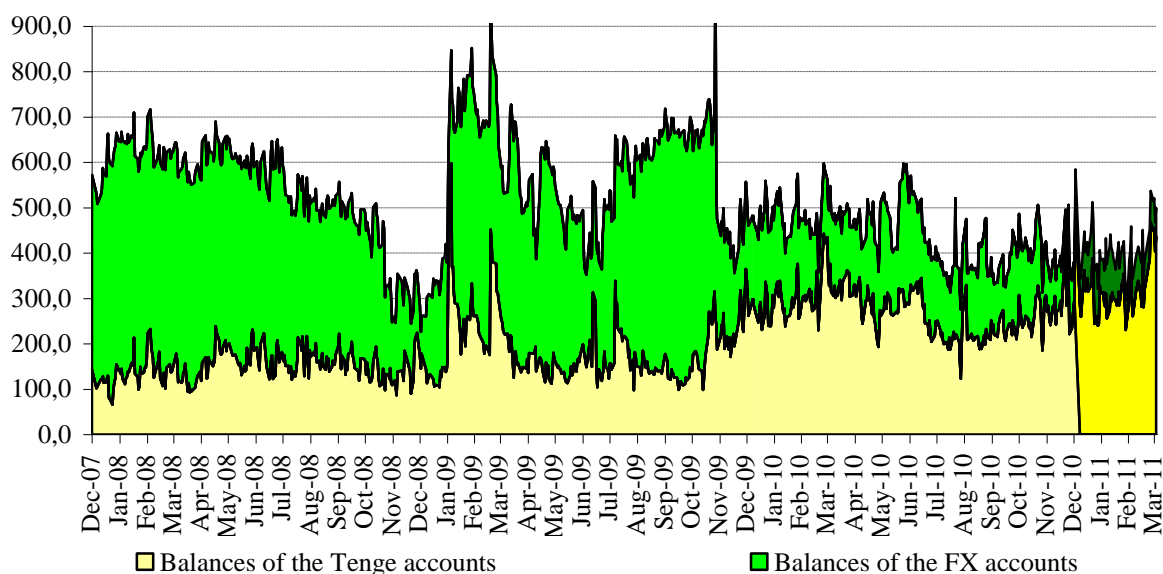
figure 38

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

Source: National Bank of the Republic of Kazakhstan

In January-March 2011 the dynamics in correspondent account balances of banks with the National Bank was multi-directional. In January correspondent account balances of banks in foreign currency were decreasing, in February they were increasing and in March – they were decreasing again. Correspondent account balances of banks in the domestic currency in Q1 2011 were volatile. From the second half of January and up to mid-February there was a downward trend in their volume, and in the following months the correspondent account balances of banks in the domestic currency were increasing. As a result, their volume increased by 1.8 times at end-March as compared to their volume at end-December 2010 (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

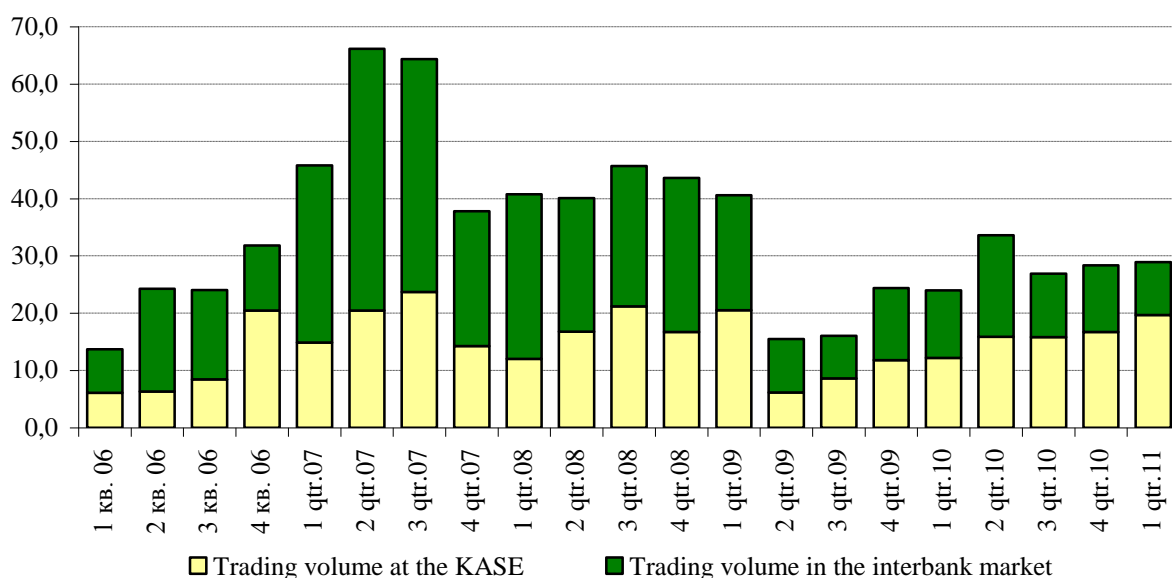
The situation in the domestic foreign exchange market was developing in the conditions where the supply of foreign exchange exceeded its demand.

In Q1 2011 the total trading volume in the FX segment of the Kazakhstan Stock Exchange and in the interbank foreign exchange market amounted to US\$28.9 bln., having increased (by 2.0%) as compared to Q4 2010.

The volume of trades in the Dollar position at the Kazakhstan Stock Exchange increased by 19.7% as compared to Q4 2010 and amounted to US\$19.7 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 in Q1 2011 decreased by 20.7% as compared to the previous quarter and amounted to US\$9.2 bln. (figure 40).

figure 40

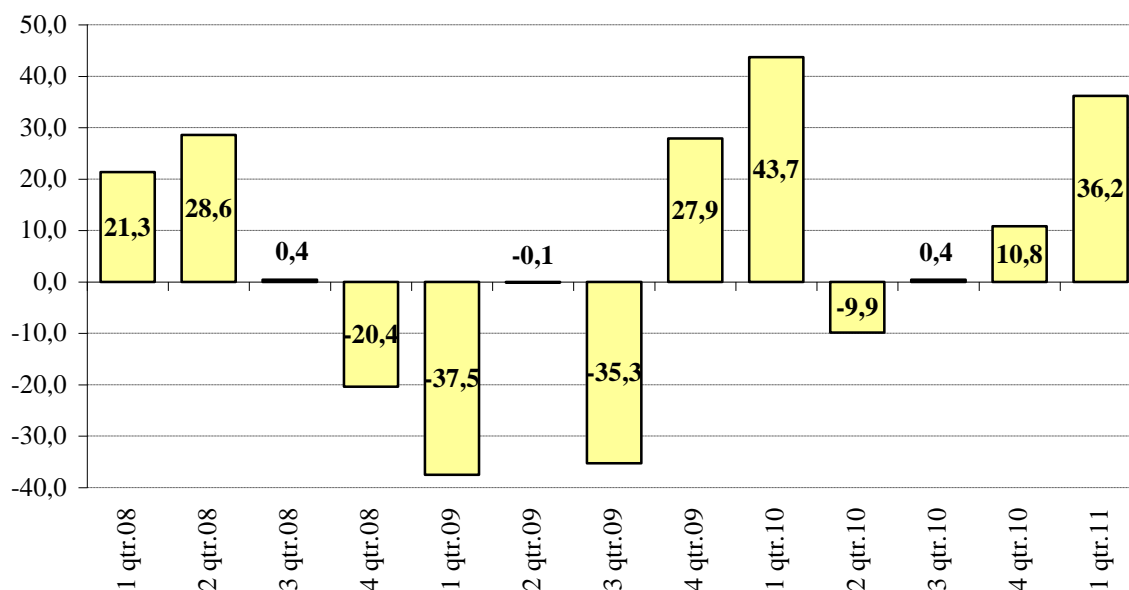
Volume of trading in the domestic exchange market, US\$ bln.



Source: National Bank of the Republic of Kazakhstan

In Q1 2011 the National Bank's participation coefficient in the Kazakhstan Stock Exchange was 36.2% (in Q4 2010 it was 10.8%) (figure 41). Thus, in Q1 2011 the National Bank was primarily the buyer of foreign exchange in the domestic foreign exchange market.

figure 41

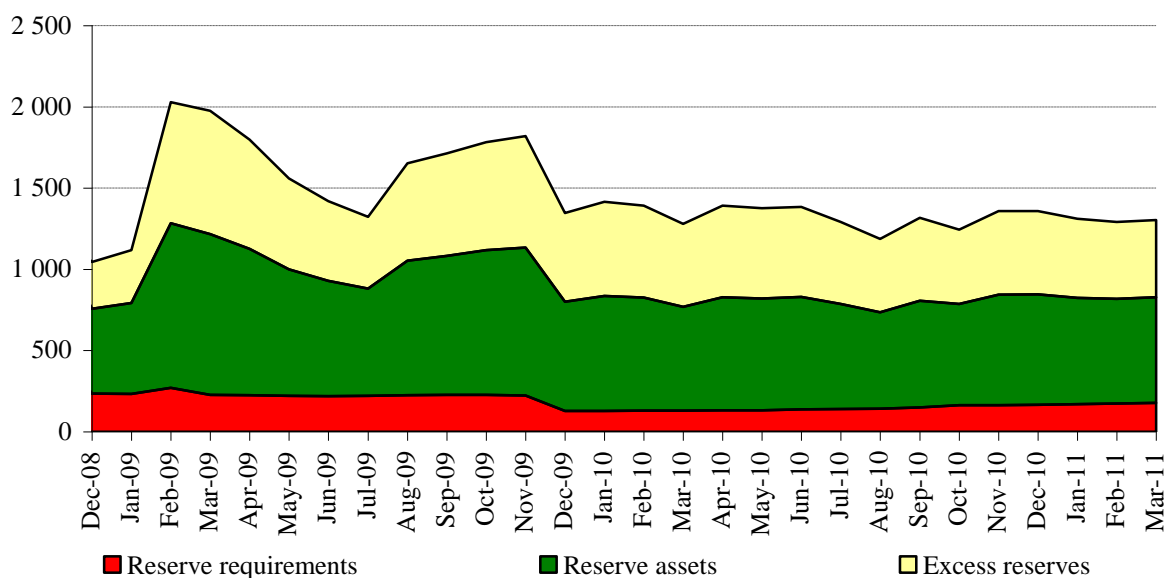
Coefficient of the National Bank's participation at the Kazakhstan Stock Exchange, %

Source: National Bank of the Republic of Kazakhstan

4.2. Minimum Reserve Requirements

During January-March 2011 reserve assets exceeded the required reserving volume by 3.7 times on average (in Q4 2010 – by 3.9 times on average, and in Q1 2010 – by 5.4 times) (figure 42).

figure 42

Compliance with minimum reserve requirements, KZT bln.

Source: National Bank of the Republic of Kazakhstan

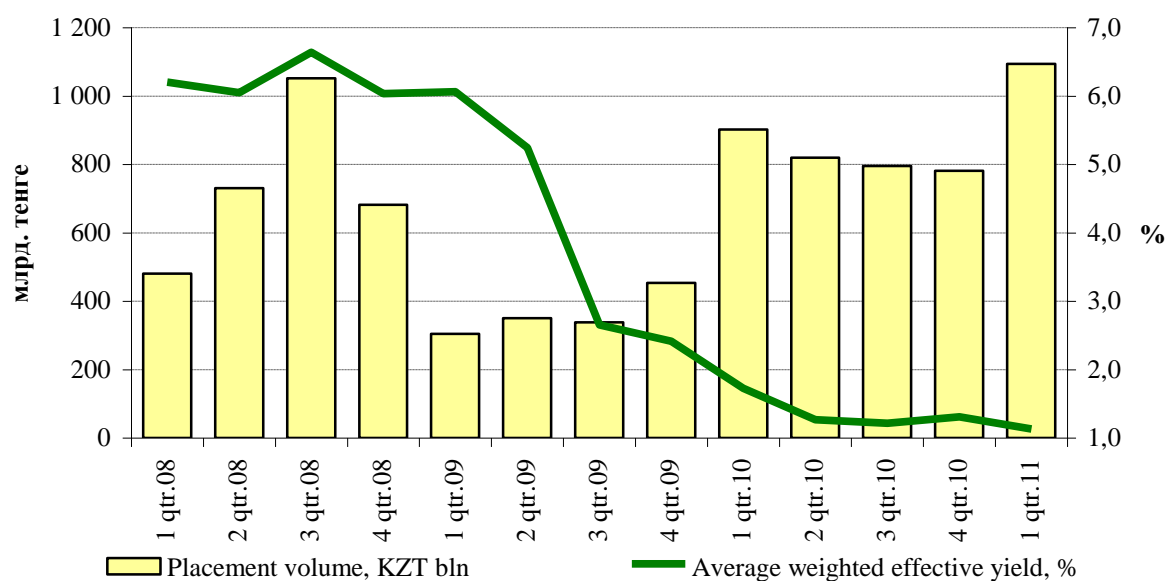
4.3. Open Market Operations

In Q1 2011 the demand of banks for short-term notes of the National Bank remained high. In January-March 2011 the National Bank continued issuing short-term notes with maturities of 3 and 6 months.

The volume of short-term notes issued in Q1 2011 increased by 40.1% as compared to Q4 2010 and amounted to KZT1094.4 bln. This was fully in line with the aggregate demand of the market participants for these types of government securities. The highest emission volume of short-term notes was in March (over 40% of the total volume issued during Q1 2011). The average weighted yield on issued notes decreased from 1.31% in Q4 2010 to 1.13% in Q1 2011 (figure 43).

figure 43

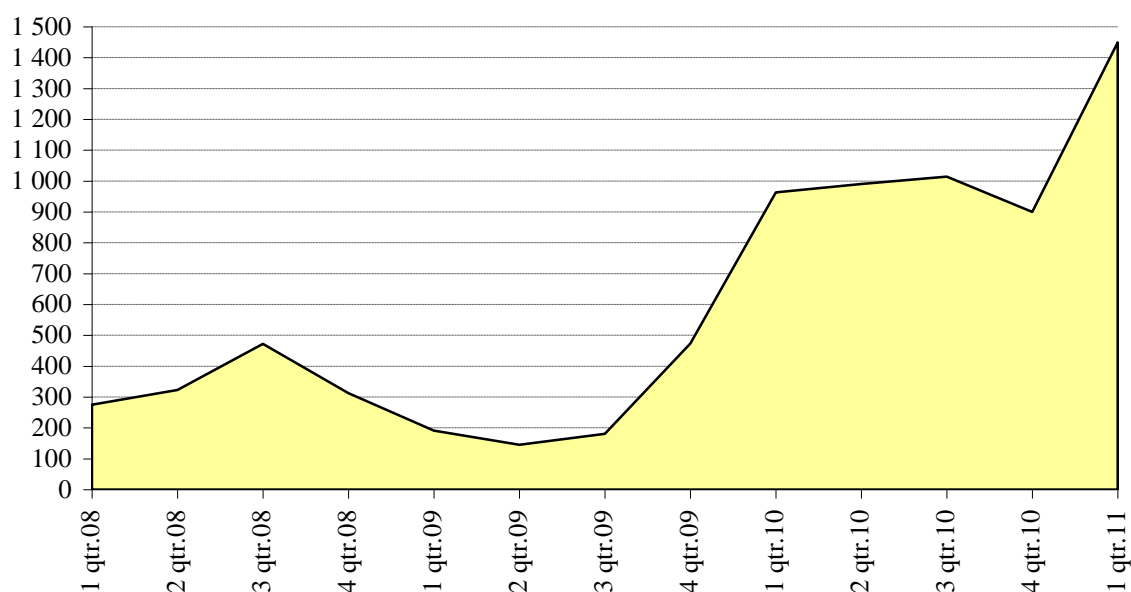
Volume of placed short-term notes and their yield (for the period)



Source: National Bank of the Republic of Kazakhstan

At end-March 2011 the volume of short-term notes in circulation amounted to KZT1449.1 bln., which exceeds the volume at end-December 2010 by 1.6 times (figure 44).

figure 44

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

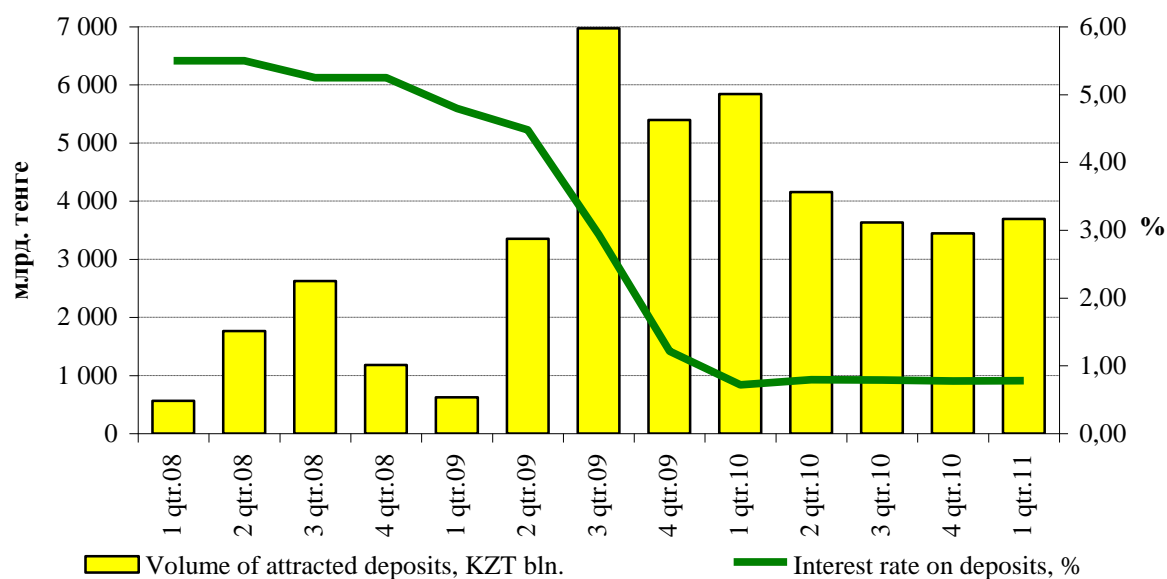
Source: National Bank of the Republic of Kazakhstan

4.4. Standing Facilities

In Q1 2011 the volume of deposits attracted from banks increased as compared to the previous quarter. The volumes of attraction were high during the entire period; the peak of attraction occurred in March (over 40% of the total attracted volume in Q1 2011). In total, during January-March 2011, KZT3691.7 bln. of deposits was attracted, which is by 7.2% higher than the volume of Q4 2010 and by 36.8% less than the volume of Q1 2010.

The average interest rate on deposits in Q1 2011 increased from 0.77% to 0.78% as compared to the previous quarter (figure 45).

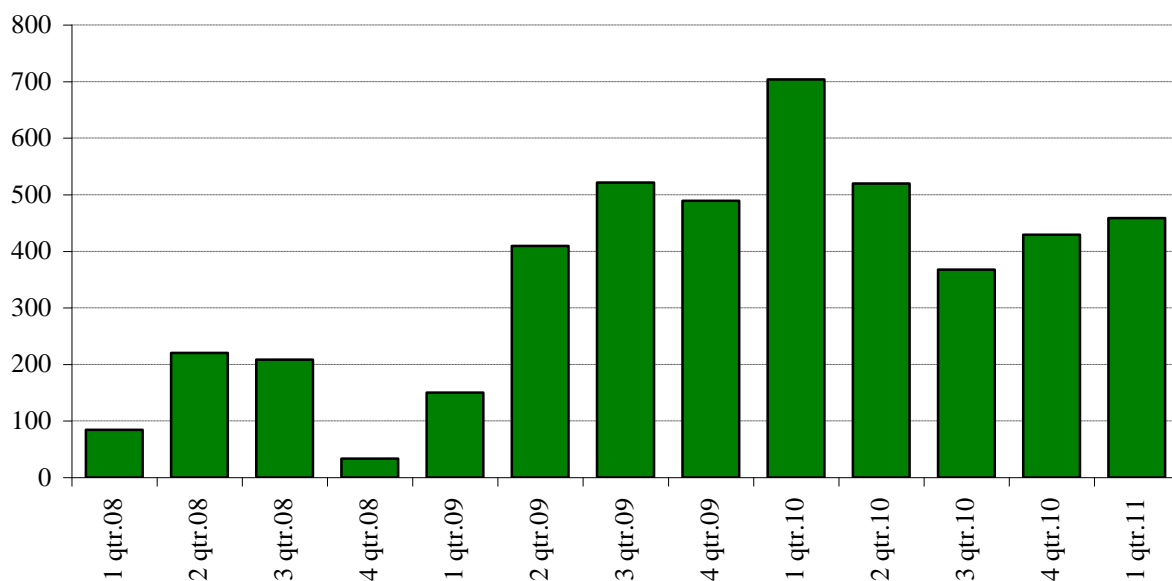
figure 45

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

Source: National Bank of the Republic of Kazakhstan

The increase in the volumes of attracted deposits was accompanied by the growth in the volume of the National Bank's outstanding liabilities on such deposits. In March 2011 the volume of outstanding balances on deposits of banks with the National Bank amounted to KZT 458.6 bln., which is by 6.9% greater as compared to the volume in December 2010 (figure 46).

figure 46

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

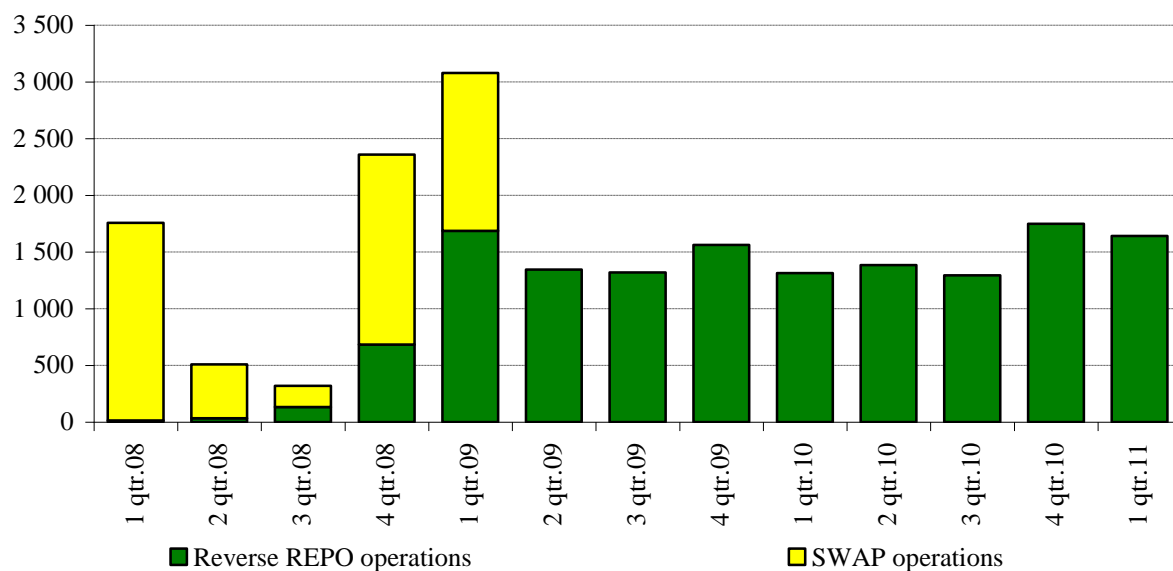
Source: National Bank of the Republic of Kazakhstan

In addition to sterilization operations, in Q1 2011 the National Bank continued to provide refinancing loans to the banking sector through reverse REPO operations. The total

volume of reverse REPO operations in January-March 2011 amounted to KZT1640.0 bln. Meanwhile, the volumes of these operations decreased by 6.1% as compared to the previous quarter (figure 47).

figure 47

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

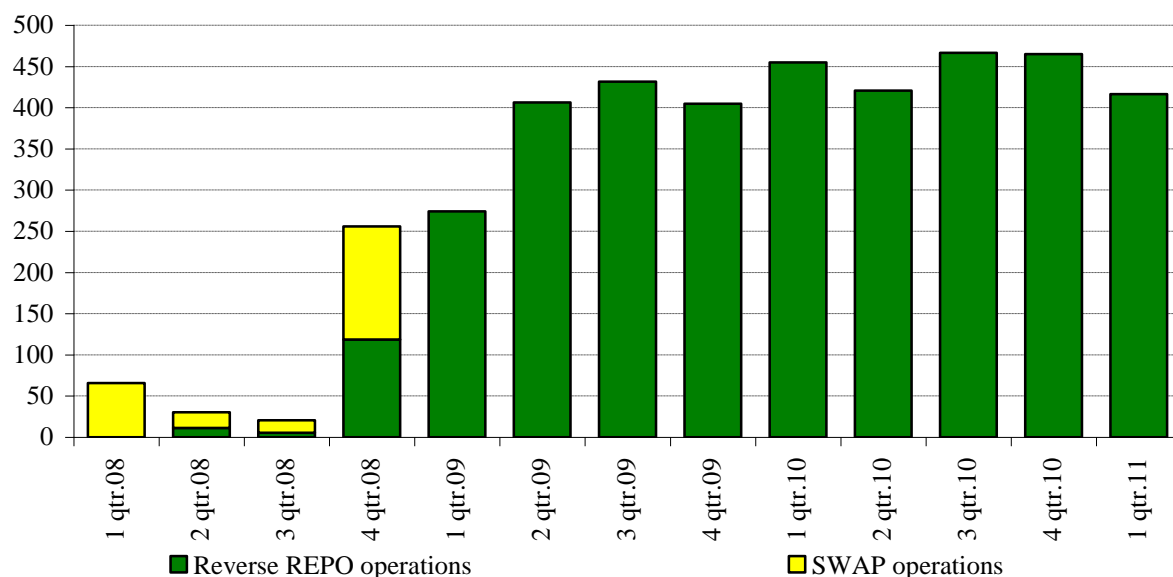


Source: National Bank of the Republic of Kazakhstan

At end-March 2011 the outstanding debt on reverse REPO operations amounted to KZT416.6 bln. (figure 48).

figure 48

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



Source: National Bank of the Republic of Kazakhstan