INTERNATIONAL MONETARY FUND

Kazakhstan: Staff Concluding Statement of an IMF Staff Visit

November 17, 2015

A Concluding Statement describes the preliminary findings of IMF staff at the end of an official staff visit (or 'mission'), in most cases to a member country. Missions are undertaken as part of regular (usually annual) consultations under Article IV of the IMF's Articles of Agreement, in the context of a request to use IMF resources (borrow from the IMF), as part of discussions of staff monitored programs, or as part of other staff monitoring of economic developments.

The authorities have consented to the publication of this statement. The views expressed in this statement are those of the IMF staff and do not necessarily represent the views of the IMF's Executive Board. This mission will not result in a Board discussion.

An IMF mission, led by Hossein Samiei, visited Astana and Almaty during November 12–17 to review economic and financial sector developments and policies. The mission thanks the authorities and other counterparts for their hospitality and productive discussions. At the conclusion of the visit Mr. Samiei issued the following statement:

The macroeconomic landscape remains challenging. Against the backdrop of large and persistent shocks—lower oil prices, Russia and China slowdown—economic growth has decelerated sharply relative to 2014. Financial conditions have also tightened, with credit to the private sector contracting significantly. The roughly 40 percent depreciation of the tenge against the dollar since the August 20 move to a floating exchange rate is expected to help reduce external imbalances, but is pushing up inflation above the 6-8 percent objective range and could adversely impact private sector balance sheets. We expect real GDP growth of 1.2 percent this year and 2.2 percent in 2016, well below the economy's potential, with external risks remaining.

Despite the difficult economic environment, the National Bank (NBK) has taken important steps toward overhauling the monetary policy framework and operations. In particular, the decision to float the exchange rate in August, followed by the introduction of a new policy interest rate (base rate) as the new monetary policy anchor in September, set in motion the process of modernizing the monetary policy framework. Subsequent minimization of NBK FX intervention starting November 5 allowed better accommodation of the shocks, thus moving the tenge more in line with fundamentals. Modernizing the policy framework is necessary as the previous fixed exchange rate regime was unsustainable in the face of ongoing external shocks. In this context, it is essential that the NBK as soon as possible, depending on developments in the FX and money markets, reinstate its new interest rate policy anchor (temporarily suspended on November 6), supported by open market operations and standing facilities, and resume its regular policy interest rate meetings.

Consistent communication about policy intentions, deliberations, and decisions is vital to strengthening policy transparency and predictability in the absence of an exchange rate anchor. Moreover, close cooperation with the Ministry of Finance on liquidity forecasting and debt issuance is critical for the success of the new framework. Given the need to alleviate inflationary pressures and lessen speculative pressures on the tenge, monetary policy may need to maintain a tightening bias for an extended period. Finally, to help facilitate the transmission mechanism of monetary policy and ensuring the efficiency of monetary operations: (i) NBK's long-term FX swap agreements should be unwound on maturity (or extended only at prevailing market rates) and (ii) the current cap on the commercial banks' deposit rates on individual accounts should be removed, or linked to the base rate, combined with the introduction of standard term deposits. The IMF stands ready to provide further technical assistance (TA) as needed.

Financial sector vulnerabilities stemming from weaker growth and the recent tenge depreciation require strengthening banking-oversight practices. In particular, despite some progress in adopting risk-based assessment tools and supervision more work is needed, including by closely monitoring the emergence of systemic risks based on the current regularly conducted stress tests. We welcome progress on the implementation of a number of 2014 FSAP recommendations, such as making the non performing loan (NPL) ratio an operational early-warning indicator, but further progress is needed, including enhanced solvency assessment in case of state support to financial entities. While mindful of the difficulties faced by the financial sector in the period ahead, we caution against regulatory forbearance. We also encourage a careful approach to implementing countercyclical banking sector measures, such as temporarily postponing the planned increase in the regulatory minimum on capital adequacy ratio.

Fiscal policy in the short term appropriately supports economic growth, but for the medium term requires a well-defined consolidation plan. The multiyear fiscal stimulus package (Nurly Zhol) is helping mitigate the effects of negative shocks but, together with lower oil revenues, is also resulting in a wider fiscal deficit in 2015. The non-oil fiscal deficit of the general government (IMF definition) is projected to reach 11 percent of GDP this year, compared to 9.3 percent of GDP in 2014. Over the medium term, the non-oil deficit is projected to decline only gradually to around 8 percent of GDP in 2020. To achieve a sustainable non-oil deficit (estimated at 5.5-6 percent of GDP), the authorities urgently need to formulate well-specified medium-term fiscal consolidation measures, especially on the revenue side. Such measures could include strengthening the enforcement of tax collection, closing fiscal loopholes, and reducing tax exemptions including in the Special Economic Zones. Early steps by the Ministry of Finance toward compliance with the IMF's Government Financial Statistics Manual (GFSM) are encouraging, but successful implementation requires enhanced high-level coordination between the Ministries of Finance and National Economy. We stand ready to provide additional TA in these areas.

We welcome the new privatization plans and urge speedy implementation of the structural reform agenda. With a view to promoting private-sector-led growth and attracting foreign investment, the authorities recently announced large-scale privatization plans. We welcome these initiatives and the authorities' objective of implementing the privatization program competitively and in a way that ensures genuine private ownership and control. In this regard, we support the efforts underway to consult closely with international experts on privatization modalities. In addition, the long-lasting nature of the current shocks requires steadfast implementation of previously-announced growth-enhancing reforms, which include, in particular, strengthening human capital and institutions, and economic diversification. Finally, we welcome Kazakhstan’s recent gains under the World Bank’s Doing Business indicators and its upcoming formal accession to the WTO.