



QUARTERLY REPORT

KAZAKHSTAN MACRO & MARKET OVERVIEW

Q2 2023 // NATIONAL BANK OF KAZAKHSTAN

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KAZAKHSTAN CREDIT RATINGS HOLD STEADY

On May 26, Fitch Ratings reaffirms Kazakhstan's credit rating at 'BBB' with a stable outlook. The country's strong fiscal and external balance sheets, along with improvements in macroeconomic policies and low government debt, form the foundation for this positive evaluation by credit rating agencies.

Fitch anticipates that the Kazakh economy will receive a boost from increased oil production, attributed to the launch of the expanded Tengiz field. As a result, Fitch Ratings forecasts GDP growth rates of 4.5% and 4.8% for the years 2023 and 2024, respectively. Notably, the agency commends the implementation of a new fiscal rule that restricts public spending growth and guaranteed transfers from the National fund, which is expected to facilitate counter-cyclical fiscal policy.

Moody's expects the real GDP growth of Kazakhstan to moderately recover to around 3.8-4.0% year-on-year in 2023, up from 3.3% the previous year. Furthermore, the growth is projected to accelerate further, surpassing 4% in 2024. This growth is expected to be supported by the recovery of oil export volumes and production, particularly in the latter half of the year, following the European Union's approval of sanction exemptions for the CPC pipeline's maintenance, enabling the export of Kazakh oil through Russia. Additionally, the Kazakh government's expansionary budget, approximately 12% higher than that of 2022, with half of it allocated for social-related expenditure, is expected to provide further support to the economy.

S&P Global

BBB-
Stable

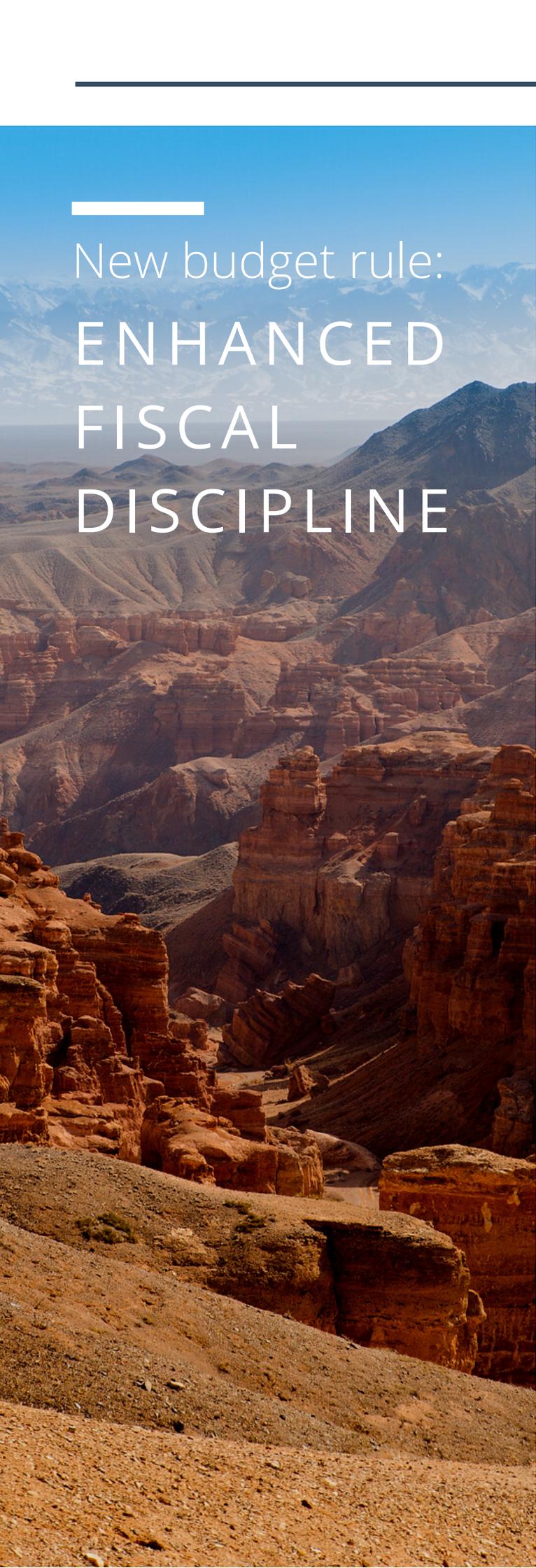
FitchRatings

BBB
Stable

MOODY'S
INVESTORS SERVICE

Baa2
Stable





New budget rule:
**ENHANCED
FISCAL
DISCIPLINE**

IMPLEMENTATION OF A NEW BUDGET RULE

In 2023, new fiscal rules were introduced to impose limits on the guaranteed transfer from National fund and the growth rate of the republican budget spending.

The set of fiscal rules defined by the Budget code consists of two main components:

1. The guaranteed transfer from the National fund must not exceed the level of receipts to the National fund from oil sector entities projected at the oil price (the "cut-off" price). The cut-off price is calculated based on historical dynamics of oil prices. In 2023 the cutoff price equals to 15th percentile of quarterly Brent oil prices for previous 15 years, in 2024 - 10th percentile. According to the Law "On a guaranteed transfer from the National fund" cut-off price for 2023 is 48.9\$, for 2024 - 42.2\$.

2. The growth rate of Republican Budget spending should not exceed the level of long-term economic growth increased by the inflation target. The long term economic growth is defined as average real GDP growth for previous ten years.

However, during the budget amendment process, the rule that restricted the growth rate of budget spending was temporarily suspended. This led to an increase in the republican budget spending from 21 trillion tenge to 22.5 trillion tenge through target transfers. Although there was only partial compliance with fiscal rules, this did result in a limitation of the size of the guaranteed transfer from National fund. Consequently, the share of transfers from National fund in government spending is projected to decrease to 17%, compared to the average of 28% observed over the previous five years. The fiscal policy is expected to fully comply with the fiscal rules starting from 2024.

By adhering to the fiscal rules in the future, several benefits are anticipated. This includes the accumulation of assets in the National fund, a reduction in non-oil deficits, and an enhancement of the fiscal policy's resilience to potential future shocks.

SLOWING INFLATION aligns with forecast trajectory

Considering the anticipated rise in maximum prices for housing and communal services tariffs, along with the actual increase in fuel and lubricant costs, and a stronger fiscal impulse - factors that were not accounted for in the National Bank's earlier forecasts - the inflation forecast has been revised. As per the baseline scenario, annual inflation for the present year is expected to range between 11% to 14%. Looking ahead, projections indicate inflation rates of 9% to 11% in 2024, and 5.5% to 7.5% in 2025.

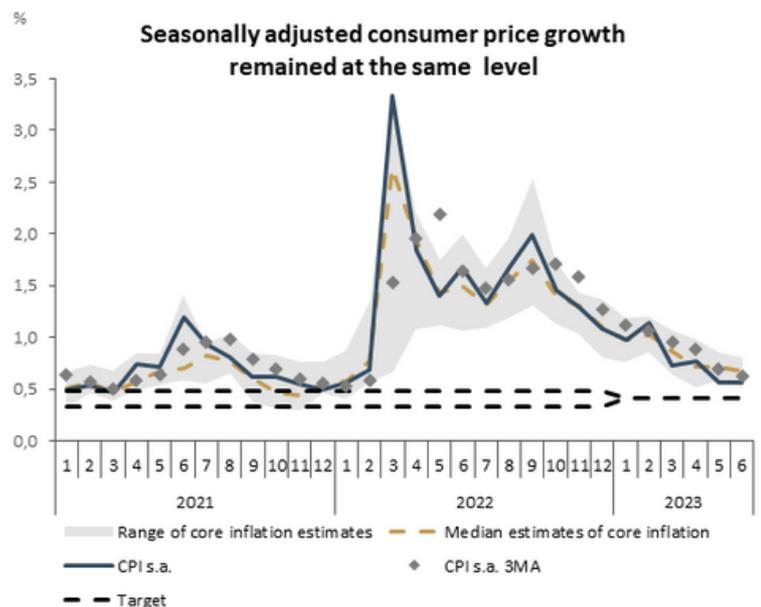
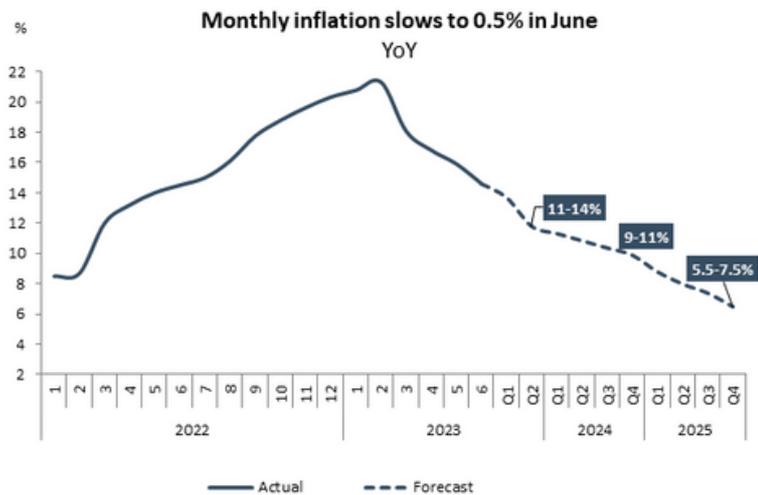
In recent months, there has been a downward trend in monthly inflation, with a slowdown to 0.5% in June. The annual inflation rate in June 2023 remained within the forecast range, amounting to 14.6%. As of now, indirect effects from the increase in fuel prices have not been observed, but core inflation indicators show that demand in the economy remains stable.

The National Bank's previous communications have emphasized that the slowdown in inflation creates room for a gradual reduction in the base interest rate in the future. Consequently, during the next decision-making process based on the forecast round results, the National Bank will assess the possibility of a prudent base rate reduction.

Notably, there has been a change in the format of the inflation target, shifting from interval values to point values. Previously, the interval values were set between 4-5% for 2023-2024 and 3-4% from 2025. However, the new medium-term inflation target is to maintain annual inflation close to 5%.

Since September 2022, seasonally adjusted and core inflation rates have been decelerating, while prices for a wide range of goods and services continue to rise. In June 2023, seasonally adjusted consumer price growth remained consistent with the previous month at 0.6%, with an annualized rate of 6.9% (compared to 9.7% in April).

INFLATION



CURRENT ACCOUNT

forecast was revised downward

In 2022, the current account of the balance of payments moved into a surplus zone for the first time in 9 years according to updated data and amounted to \$7.8 billion due to high commodity prices.

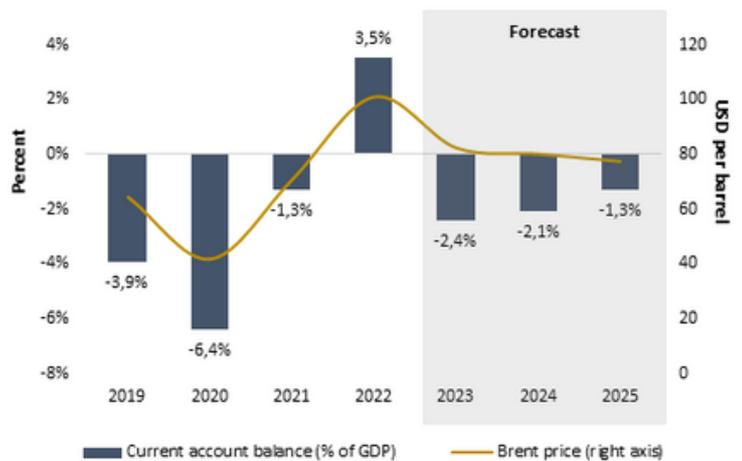
In the 1st quarter of 2023, the current account formed with the deficit of \$0.9 billion due to the worsening trade balance. The export of goods decreased by 12.3% to \$19.2 billion as a result of decline in export of oil, natural gas, metals and cereals. The import of goods increased by 41.3% to \$13.6 billion, with growth observed across all product groups – intermediate, consumer and investment goods.

During the forecasting round in May the current account projections have been revised downward. The revision was due to a significant excess of actual values on import of goods over the projected values under a conservative approach, primarily driven by higher growing needs of the population and businesses, higher contract prices on import deliveries caused by issues related to logistic chains, as well as the higher expansion of financing sources, including fiscal expenditures and consumer loans.

Thus, under the baseline scenario, the trend of the 1st quarter of 2023 will persist, resulting in a moderate deficit of the current account over the medium term. The expected deficit values will be driven by gradual decline in projected oil and metal prices, as well as continued growth in import of goods. Nevertheless, the current account deficit is expected to be moderate and narrow to near-zero levels by the end of 2025 due to rising oil production at the largest oil projects.

CURRENT ACCOUNT

Current account projections have been revised downward



Import of goods increased higher than expected in 1Q23

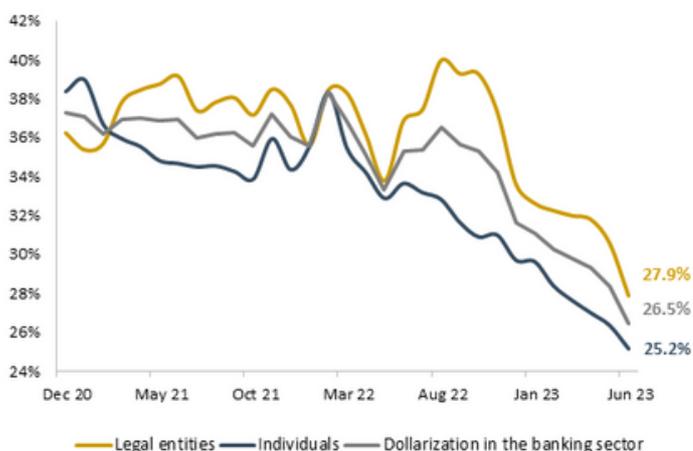


IMPROVED TRANSPARENCY enhances efficiency of FX market

FX MARKET & FX RESERVES

<i>mIn USD</i>	2022	1Q2023	2Q2023
FX Reserves	35 076	36 215	34 453
Assets in hard currencies	14 585	15 091	15 265
Gold	20 491	21 124	19 188
Share of gold,%	58%	58%	56%
USD/KZT total volume on KASE	29 704	7 771	8 493
USD/KZT rate	463	452	453
Interventions (net)	(-) 1 394	0	0
Mandatory FX sales by quasi-sovereign companies	5 055	988	906
Sales from National fund	(-) 4 285	(-) 1 539	(-) 1 950

Dollarization of deposits is decreasing



As of June 30, 2023, the tenge exchange rate has appreciated by 2.2% year-to-date to 452.26 tenge per US dollar, compared to 462.66 on December 30, 2022.

In pursuit of enhancing transparency, the National Bank has taken a step by expanding the scope of its published data. Apart from disclosing net interventions, the National Bank now also provides information regarding gross volumes. This move aims to offer more comprehensive insights and a clearer understanding of the National Bank's activities in the FX market.

Sales from the National fund accounted for 21% of the total volume on KASE (compared to 33% for the first 6 months of 2022 and 41% for the same period in 2021). Additionally, the National Bank now provides one-month forecasted sales volumes based on applications from the Ministry of finance for the allocation of transfers to the republican budget on a monthly basis.

The country's international reserves amount to \$94.2 billion, including \$34.5 billion in foreign exchange reserves and \$59.8 billion in National fund assets.

The dollarization rate has continued to decrease, reaching 26.5% in June 2023. Among legal entities, the minimum level of dollarization has been achieved at 27.9%, marking the lowest rate in the past ten years. One of the contributing factors to this decline is the attractiveness of tenge deposits.

The government securities market in 2Q2023 was characterized by high demand and a high share of market investors. In 2Q2023, the Ministry of finance issued fixed-coupon government securities for 2.8 trillion KZT with the market investors' share of 56%.

In previous year, predominant volume of issued securities was concentrated within the 5-years maturity segment. This year market participants have demonstrated a growing interest in long-term securities. During 2Q2023 more than 60% of the total securities issued had a maturity period exceeding 5 years.

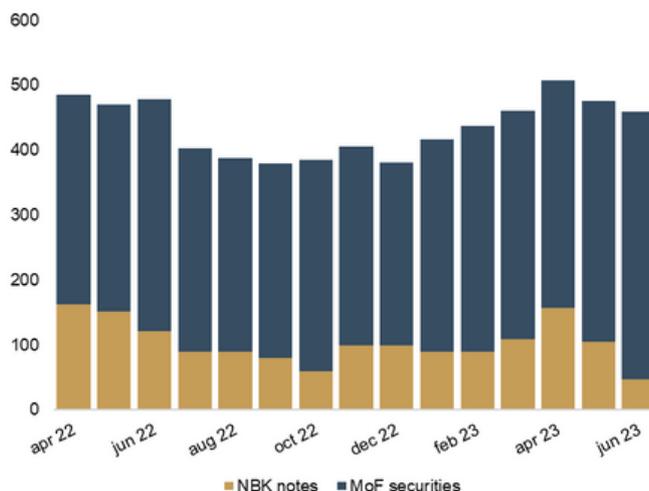
Meanwhile, the auction demand has exceeded the announced amount on average by 2.4 times. Moreover, with signs of inflation cooling, the yields on short- and medium-term government securities auctions declined compared to the beginning of the year.

Since the beginning of the year, there has been an increase in nonresidents' investments in Kazakhstan government securities. The growth in investments during 2 quarters amounted to 79 billion tenge (~175 mln.USD): the volume of non-residents in the securities of the Ministry of finance increased by 132 billion tenge, and in National Bank notes decreased by 53 billion tenge.

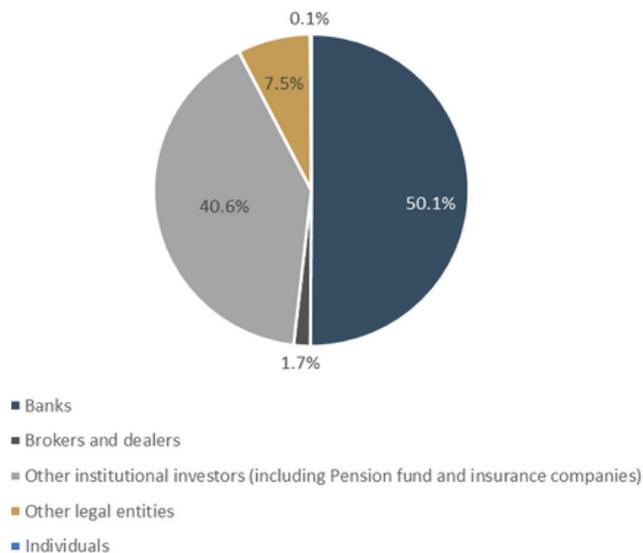
To address the preferences of market participants and to increase secondary market liquidity, Ministry of finance takes steps to reduce the number of issues and consolidate existing securities.

GOVERNMENT SECURITIES MARKET OVERVIEW

Holdings of government securities by foreign investors has increased YTD



During 6M23 about 50% of the primary market participants consisted of banks



Government securities market
EXPERIENCING HIGH DEMAND

UNLOCKING POTENTIAL:

Ongoing initiatives
to advance
government
securities market



FURTHER DEVELOPMENT OF GOVERNMENT SECURITIES MARKET

INFRASTRUCTURE

EUROCLEAR SETTLEMENT

The National Bank aims to create a settlement infrastructure with Euroclear as an additional step in the development of the local stock market and its integration with the global financial system.

At the moment, Euroclear has already finished 1 stage of due diligence process of local legislation.

LIQUIDITY

TRANSFERRING FUNDS TO MARKET

As of the beginning of 2023, the NBK managed 9 tenge-denominated funds, totaling 3.6 trillion tenge. This year, it was planned to transfer 7 funds to local professionals, of which 2 have already been successfully transferred and 5 yet to be transferred (1.6 trillion).

INTRODUCTION OF PRIMARY DEALERSHIP

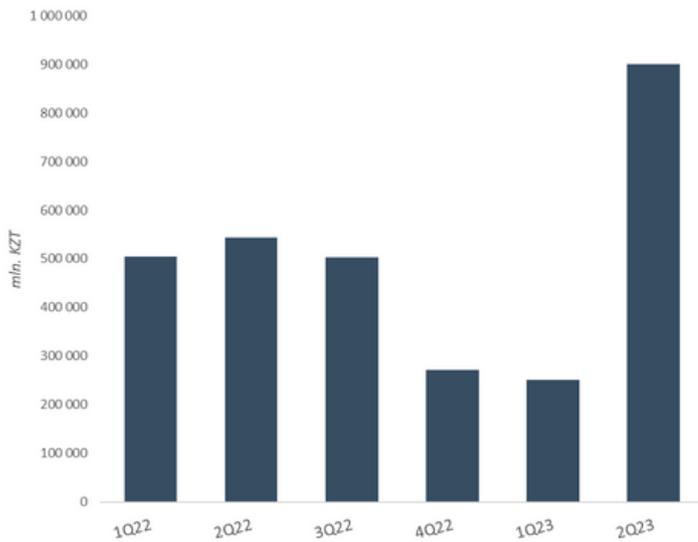
At this moment, more than 40 market participants have access to primary auctions with no market-making obligations, but the list will be reduced significantly.

Detailed information about the process of introduction of primary dealership is provided on page 10.

Secondary market LIQUIDITY TRIPLED in 2Q2023, QoQ

SECONDARY MARKET LIQUIDITY

Secondary market liquidity* increased significantly after the announcement of monitoring period in May



*Data on secondary market includes only tenge denominated securities of NBK and MoF traded on Kazakhstan Stock Exchange

To enhance liquidity in the secondary market for government bonds, a collaborative effort between the Ministry of finance and National Bank aims to introduce the concept of primary dealers. The primary goal is to streamline the primary auctions and foster a more specialized and efficient public debt market.

The proposed project involves reducing the number of participants with access to the Ministry of finance's primary auctions. Instead, selected participants will be designated as "primary dealers", entitling them to participate in these auctions while also taking on additional responsibilities as market makers in the government bond market.

To ensure a fair and transparent evaluation of market participants, a monitoring period commenced in May. During this period, the activity of participants in the government bond market is closely assessed. A scoring model has been devised to rank the participants based on their level of activity on both primary and secondary markets. It also evaluates the presence of analytical information for foreign and local investors and communication between market participants and Ministry of finance.

Ranking of market participants is publicly accessible on the Kazakhstan Stock Exchange's website on a monthly basis.

Following the commencement of the monitoring period, there have been significant improvements in the government securities market. Specifically, during the second quarter, the liquidity of the secondary market witnessed a threefold increase compared to the previous quarter.

Moreover, on a daily basis, numerous market participants actively set quotes for various government securities on both the Bloomberg Ebond trading system and the Kazakhstan Stock Exchange. This increased activity and participation from market players indicate a growing interest and engagement in the government securities market.

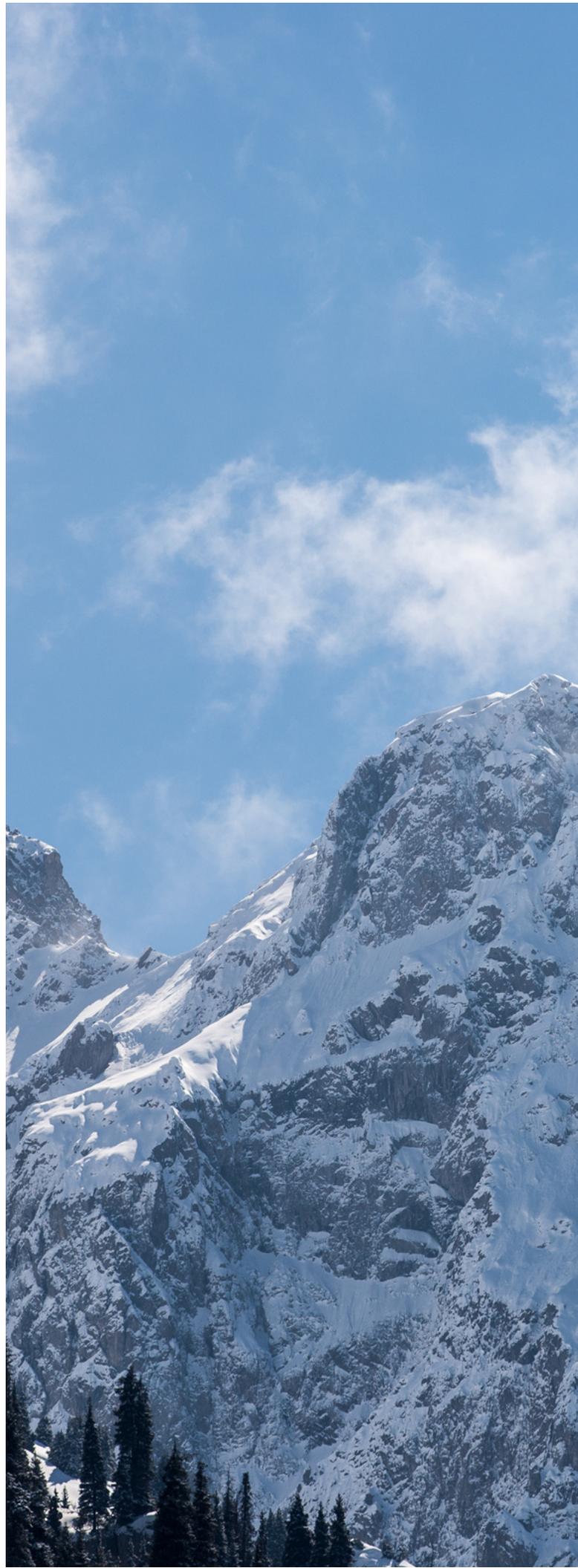
INVESTOR RELATIONS

On June 8, 2023, NBK management conducted a road show for key investors and analysts with participation in J.P. Morgan Frontier Markets Fixed Income Conference in London. The conference covered a wide range of investors, including sovereign, quasi-sovereign, and private sector corporates. Also a sequence of meetings with potential institutional investors and professional market participants was held in order to present a macro overview of Kazakhstan, inform about current investment opportunities and capital market instruments in Kazakhstan, update information on infrastructure and long-term plans for the development of the financial market in Kazakhstan.

Also, in June 2023, the NBK delegation participated at the XII Amundi World Investment Forum to conduct a series of meetings with investors.

Additional sources:

- [Recent Publications and Press releases](#)
- [Monetary Policy Report](#)
- [Kazakhstan: Balance of Payments and External Debt for 2022](#)



CONTACTS

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