Euler Hermes Economic Research

Country Risk Analysis

Kazakhstan

Improved short-term economic outlook

General Information

GDP	USD188.1bn (World ranking 49, World Bank 2011)
Population	16.56 million (World ranking 62, World Bank 2011)
Form of state	Republic / authoritarian presidential rule
Head of government	Nursultan A. NAZARBAYEV
Next elections	2016, presidential

Strengths

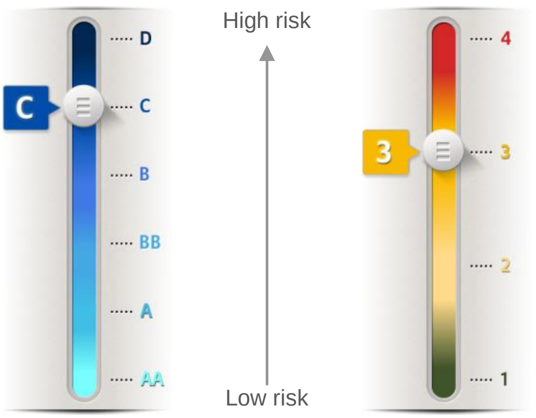
- Abundance of raw materials, in particular hydrocarbons
- The National Fund of the Republic of Kazakhstan held assets of around USD36bn in April 2011
- Healthy public finances
- Rising oil export capacities over the next decade

Weaknesses

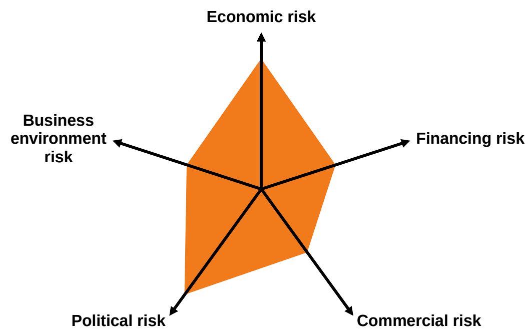
- Authoritarian political regime
- Increasingly interventionist and protectionist economic strategy
- Regional instability in Central Asia
- High vulnerability to world commodity prices
- Weak monetary policy track record
- Exchange rate vulnerability to external shocks
- Banking sector crisis not yet resolved
- High external debt burden

Country Rating

C3

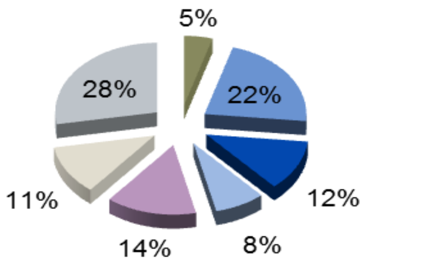


Risk Dimensions



Economic Structure

GDP breakdown (% of total, 2010)



Sources: Chelem, IHS Global Insight, Euler Hermes

Trade structure (% of total, 2010)

By destination/origin

Exports		Rank		Imports
China	22%	1	28%	Russia
Germany	10%	2	22%	China
France	8%	3	7%	Germany
Russia	8%	4	6%	Italy
Italy	6%	5	5%	Ukraine

By product

Exports		Rank		Imports
Crude Oil	58%	1	8%	Natural Gas
Non Ferrous Metals	7%	2	5%	Crude Oil
Iron Steel	6%	3	4%	Engines
Refined Petroleum Products	5%	4	4%	Electrical Apparatus
Basic Inorganic Chemicals	4%	5	4%	Commercial Vehicles

Economic Forecasts

	2009	2010	2011	2012	2013f	2014f
GDP growth (% change)	1.2	7.3	7.5	5.0	4.5	5.2
Inflation (%, end-year)	6.2	7.8	7.4	6.0	6.6	6.6
Fiscal balance (% of GDP)	-1.3	1.5	5.9	4.7	4.9	4.5
Public debt (% of GDP)	10.2	10.7	10.7	12.3	13.2	14.1
Current account (% of GDP)	-3.6	0.9	6.5	4.6	4.0	2.2
External debt (% of GDP)	97.9	79.9	65.9	68.0	67.0	65.0

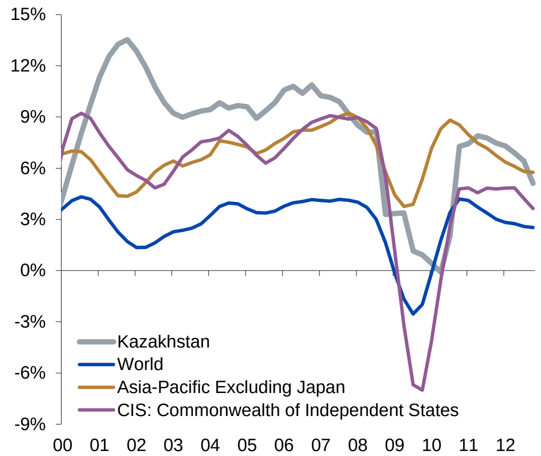
Sources: IHS Global Insight, national sources, Euler Hermes

Economic Overview

Kazakhstan possesses substantial crude oil and natural gas reserves, as well as plentiful supplies of other minerals and metals. It also is a large agricultural producer, mainly livestock and grain. Surging commodity prices supported a strong economic performance in 2000-2007, reflected in average annual growth of real GDP of 10.2%. On the demand side, growth had been driven by private consumption and private sector investment, fuelled by strong wage expansion and an excessive credit boom, with the latter increasingly funded by large-scale foreign borrowing of Kazakh banks. However, the 2007-2009 global financial crisis unmasked the high risks related to inadequate economic diversification and heavy dependence on international financial flows.

Growth fell sharply to +3.2% in 2008 and +1.2% in 2009 as oil prices plunged and the global credit squeeze pushed the Kazak banking sector into a systemic crisis. Growth has recovered thereafter though it has remained below the pre-crisis ratios, as a result of weaker external demand as well as the impact of the ongoing banking crisis on domestic demand. In 2012, real GDP growth decelerated to +5% from +7.5% in 2011, as agricultural output plunged by -17.8% (+26.7% in 2011) and industrial production expanded by just +0.5% (+3.3% in 2011). Construction grew by +2.9% in 2012 (+2.7% in 2011). Services were the key growth driver in 2012, increasing by +10% (+7.7% in 2011), with domestic trade (+14.6%) and business services activity (+16.2%) showing strong momentum. In Q1 2013, GDP growth slowed to +4.6% y/y. EH forecasts full year growth of about +4.5% in 2013 and +5.2% in 2014.

GDP growth (% y/y, 4 qtrs cumulated)



Sources: IHS Global Insight, national sources, Euler Hermes

Inflation has been somewhat elevated in recent years, mostly in the range of 5-10% since 2009. Headline inflation was 6.4% in April 2013, slightly down from 6.8% in March though higher than at end-2012 (6%). We expect it to remain broadly in the 6-7% range in 2013. Private sector credit growth has accelerated over the past two years and stood at 12.3% y/y in February 2013. This is not yet critical but needs monitoring.

The banking sector remains vulnerable as the second default of State-controlled BTA Bank in early 2012 underscored once again. While liquidity and capital adequacy ratios are good, profitability remains weak and non-performing loans stood at 17.4% of total loans in 2012.

The exchange rate will remain vulnerable to external shocks In February 2011 the central bank returned to a managed floating exchange rate regime, abandoning the 3% trading band around the KZT150:USD1 rate it introduced two years earlier in the wake of the banking crisis. However, although the probability of renewed downward pressure on the KZT has declined (the exchange rate stood at KZT151:USD1 at end-May 2013), it cannot be ruled out, for example if banking-sector instability re-intensifies or if commodity prices fall again rapidly.

Public finances are favourable. A fiscal surplus of 4.7% of GDP was recorded in 2012 and we expect further surpluses of more than 4% in 2013-2014.

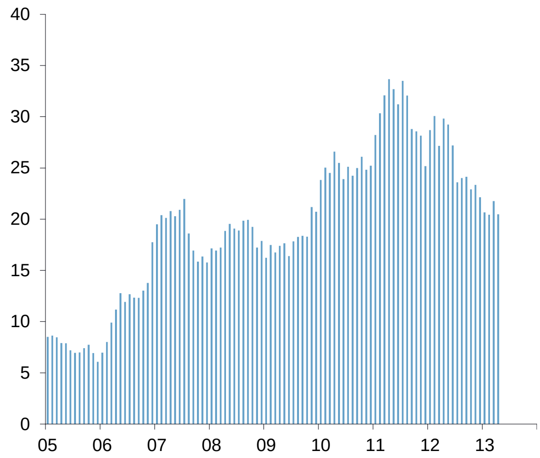
The current account posted a surplus of 4.6% of GDP in 2012 and is forecast to remain in surplus in 2013-2014.

Nonetheless, foreign exchange reserves have gradually fallen from a peak of USD33.7bn in April 2011 to USD20.5bn in April 2013. The current level of FX reserves is comfortable with regard to import cover (3.4 months). In other terms, however, reserves cover just about 55% of the estimated external debt payments falling due (ST debt plus principal repayments on M/LT debt) in the next 12 months, well below an adequate ratio of at least 100%.

However, the assets in Kazakhstan's National Oil Fund have steadily increased since 2009 and reached USD62.4bn in April 2013, providing some cushion in the event of a further downtrend in foreign exchange reserves.

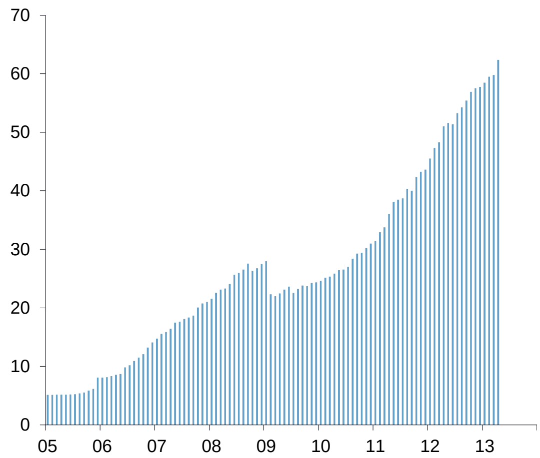
Gross external debt was relatively high at USD137bn at end-2012, equivalent to about 68% of GDP or 140% of export earnings. This is a legacy of the large-scale foreign borrowing of Kazakh banks until 2007. The debt service ratio will remain hefty for some time, estimated at 34% in 2013.

Foreign exchange reserves (USD bn)



Sources: National Bank of Kazakhstan, Euler Hermes

Assets of the National Oil Fund (USD bn)



Sources: National Bank of Kazakhstan, Euler Hermes

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