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## RAEX-Europe confirmed at 'BBB-' the credit ratings of Kazakhstan. The rating outlook is stable.

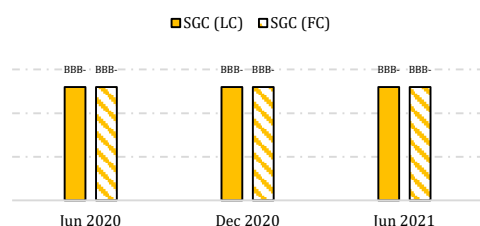
RAEX-Europe confirmed the sovereign government credit ratings (SGCs) of Kazakhstan at 'BBB-' (Moderately high level of creditworthiness of the government) in national currency and at 'BBB-' (Moderately high level of creditworthiness of the government) in foreign currency. The rating outlook is stable which means that in the mid-term perspective there is a high probability of maintaining the rating score.

## Ratings

Sovereign Government Credit (LC)	<b>BBB-</b>
Sovereign Government Credit (FC)	<b>BBB-</b>
Outlook (LC)	<b>Stable</b>
Outlook (FC)	<b>Stable</b>

\* These ratings are unsolicited

## Ratings dynamics



## Summary

The affirmation of Kazakhstan's sovereign ratings at 'BBB-' with a stable outlook largely reflects our expectation that the country's economy will recover this year from the severe adverse effects caused by the pandemic. We expect a recovery of the economy, stabilization of external conditions, public finances and macroeconomic indicators. The country's strong position expressed in accumulated external buffers enhances the resilience to external shocks and supports the budget.

However, Kazakhstan remains highly dependent on the oil sector making the economic performance and public finances highly dependent on oil production and price dynamics. In addition, the risks of asset quality deterioration and the materialization of contingent liabilities for the government remain in the weak banking sector.

## Main Economic Indicators of Kazakhstan

Macro indicators	2018	2019	2020
Gross gov. debt, KZT bn	12524	13867	18621
Nominal GDP, KZT bn	61820	69533	70714
Real GDP growth, %	4,1	4,5	-2,6
Gross gov. debt/GDP, %	20,3	19,9	26,3
Deficit (surplus)/GDP, %	2,6	-0,6	-7,0
Inflation rate, %	5,3	5,4	7,5
Current Account Balance/GDP, %	-0,1	-4,0	-3,6
External debt, USD bn	-	156,8	163,4
Development indicators	2020		
Inequality adj. HDI	0,77		
GDP per capita, USD th	26,6		
Default indicator	11.06.2021		
10Y Gov Bond Yield, %	1,2*		

Source: RAEX-Europe calculations based on data from the IMF, WB, Cbonds, Ministry of Finance of the Republic of Kazakhstan and NBK.

\* Maturity in 2028 (ISIN: XS1901718335)

**After the economic downturn in 2020, we expect a steadfast rise in 2021.** At the end of 2020, GDP declined by 2,6% as a result of lower oil prices and production, as well as the lockdown measures implemented by the authorities (see graph 1). The restrictive measures primarily affected the service sector, including transportation, where the contraction was 5,6%. Meanwhile, the losses were partially compensated by agriculture production and the robust development of construction, owing to the implementation of the Nurly Zher government program to stimulate housing construction.

In 2021, the economy is expected to recover with a GDP growth of 3,2%, driven by higher oil prices, a recovery in the services and transportation sectors, and continued government investment in road infrastructure and housing. Since April 2021, active vaccination of the population has started in Kazakhstan, which will contribute to propel activity in the retail sector. Unemployment, after reaching 5,5% in 2020, is projected to gradually return to below 5% in 2021. Given the high export orientation of the economy, increased production in the oil sector, including through the

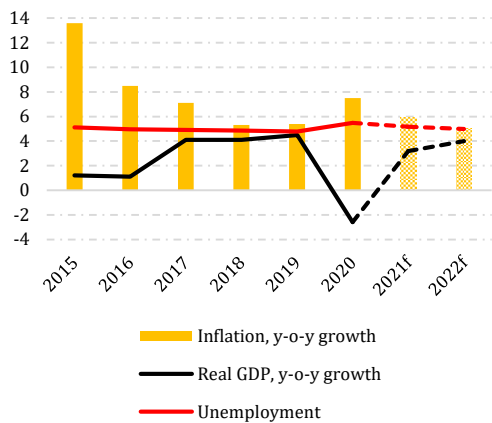
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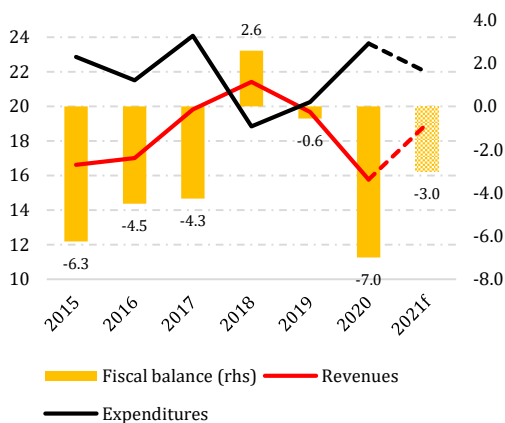
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**Graph 1: Macroeconomic indicators, %**



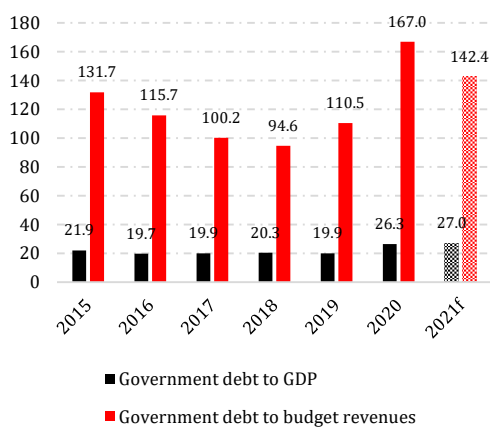
Source: RAEX-Europe calculations based on data from the IMF

**Graph 2: Fiscal budget dynamics, % of GDP**



Source: RAEX-Europe calculations based on data from the IMF

**Graph 3: Government debt dynamics, %**



Source: RAEX-Europe calculations based on data from the IMF

<sup>1</sup> The National Fund of the Republic of Kazakhstan

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expansion of production at the Tengiz field, will support further economic growth in 2021-2022.

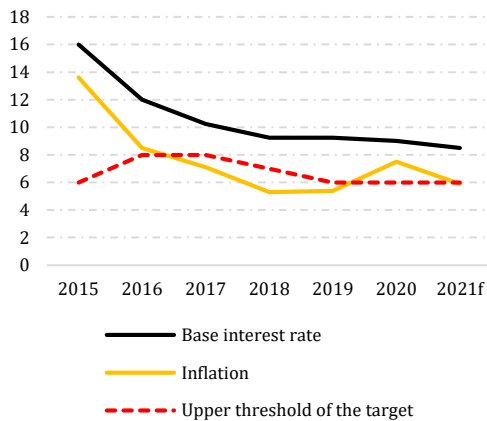
**Accumulated oil revenues support the expansion of government spending in 2020-2021.** By the end of 2020, the consolidated budget deficit totaled 7%, influenced on the one hand by a significant contraction of oil revenues, and on the other hand by an increase in expenditures on financing measures to combat COVID-19 (see Graph 2). Government spending expanded by 24%, taking into account the anti-crisis package for social and health care financing, which amounted to about 9% of GDP. Tax revenues fell by 11% due to a decline in income from oil. Moreover, the government introduced tax reliefs for businesses. However, the deficit was partially offset by unplanned receipts related to the NFRK<sup>1</sup> investment income and compensation following the settlement of the long dispute with shareholders of the Karachaganak field.

We also anticipate a negative balance of the consolidated state budget in 2021 due to the expansionary fiscal policy, but as oil revenues recover, the deficit will shrink. The strength for the government is that the NFRK's available assets, which amount to 39% of GDP and cover 187% of the national debt as of May 2021, additionally ensure budget execution through guaranteed transfers, which totaled 6,7% of GDP in 2020.

**Moderate growth in the level of government debt does not heighten the risks for the government.** With increased borrowing in the domestic market to finance the budget deficit, the level of gross government debt rose to 26,3% of GDP and 167% of budget revenues (see Graph 3). In 2021, the government continues to issue domestic bonds actively, which resulted in an increase of the share of domestic public debt to almost 60% of total gross government debt as of March 2021. However, we do not see significant risks to the government debt position, given the low share of short-term liabilities at less than 1% of GDP with coverage by reserves at 30x, as well the favorable conditions for the external debt; international development institutions debt share is around 26% and it is predominantly on concessional terms.

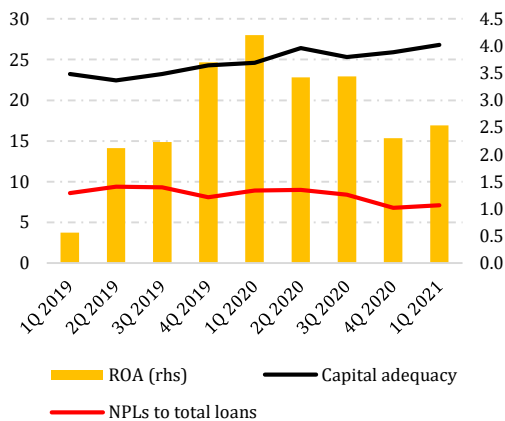
We expect government debt to increase modestly throughout 2021 on the back of a shrinking budget deficit and economic recovery. As the government does not increase FX borrowing (except for the debt issuance in the Russian market in September 2020), the share of foreign currency in the structure of liabilities remains below 40%. The yield spread between the German 10-year bonds and Kazakh government bonds in euros maturing in 2028 remains at an adequate level of 1.2 p.p. as of 11 June 2021, indicating a low sovereign risk perception of the country by international investors.

**Graph 4: Base interest rate vs inflation rate, %**



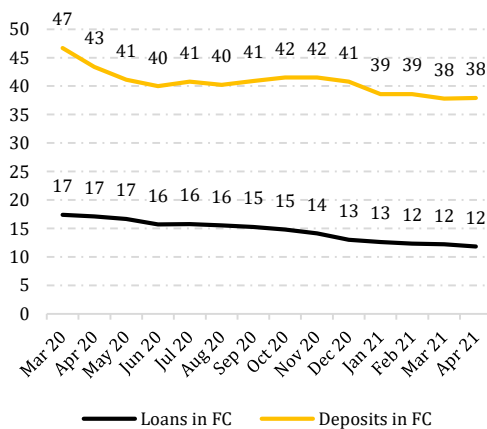
Source: RAEX-Europe calculations based on data from the NBK

**Graph 5: Financial soundness indicators, %**



Source: RAEX-Europe calculations based on data from the NBK

**Graph 6: Financial dollarization, %**



Source: RAEX-Europe calculations based on data from the NBK

**The regulator maintains a neutral monetary policy amid falling pro-inflationary risks.** Price stability and the transition to a free-float regime remain a priority for the monetary authorities. Against the backdrop of a slower-than-expected decline in inflation, as well as a gradual recovery of economic activity, the current monetary policy remains neutral and the base interest rate of the National Bank of Kazakhstan (NBK), after the last decrease in July 2020, remains at 9% (see Graph 4). Moreover, inflation remained elevated at 7,2% as of May 2021 on the back of KZT depreciation, as well as an increase in consumer prices.

As the exchange rate of KZT stabilizes and the price of oil rises, we expect inflation to gradually decrease towards 6%, within the NBK's target range of 4-6%. On the other hand, inflationary pressures may result from the pension reform, which allows early withdrawal of part of the savings from the Unified Accumulative Pension Fund<sup>2</sup> for improvement of living conditions, medical treatment, or for transfer to private trust management. Furthermore, we continue to believe that the effectiveness of monetary policy is limited by underdeveloped financial markets, and the existence of subsidized lending.

**The banking sector remains stable, but credit quality may deteriorate in the medium term.** Banks' assets rose 16% in 2020, while corporate lending continued to stagnate, pushing the corporate loan portfolio down 2,5% y-o-y as of March 2021. At the same time, this is partially offset by retail lending (especially for construction and purchase of housing), which grew 27% y-o-y as of March 2021. We expect that state programs of capital infrastructure construction and pension reform, which will allow the withdrawal of part of pension savings, will propel more active lending.

Despite the crisis, the sector's financial soundness indicators have remained quite stable. ROA and ROE figures were 2,5% and 19,8% respectively as of March 2021. However, we consider that profitability will continue to decline due to future possible credit losses (see Graph 5). At the same time, we should note the high concentration in the banking sector: the share of the top-5 banks in revenues was 92,5% in 2020, and their assets' share in total bank's assets was 64%.

As of March 2021, the capital adequacy ratio stood at 26,8%, while the ratio of NPLs to total loans, despite the deterioration of the solvency of a number of borrowers affected by the pandemic, has not increased in 2020 and stood at 7,1% (a slight increase of 0,2p.p., as compared to end-2020). Banks offered payment moratoriums and deferral of payments to the affected clients during the pandemic, thus postponing the deterioration of the loan portfolio quality. In this regard, we consider that the risks of contingent liabilities of state-owned companies and the financial sector may increase in the medium term. At the same time, we observe a reduction of currency

<sup>2</sup> Pension assets of UAPF JSC managed by the National Bank of the Republic of Kazakhstan together with the Council for Pension Assets Management under the President of the Republic of Kazakhstan

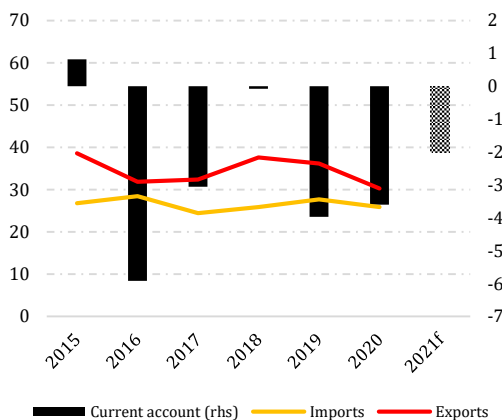
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**Graph 7: External sector indicators, % of GDP**



Source: RAEX-Europe calculations based on data from the IMF and NBK

risks for the banking system, as the dollarization of both deposit and loan portfolios have been gradually decreasing during the last four years and amounted to 37,9% and 12,0% in April 2021, respectively (see Graph 6).

**The external position remains firm.** Despite lower oil exports (due to the OPEC+ agreement) having caused a reduction of the trade balance to 6,1% compared to 8,6% in 2019, the current account deficit in 2020 did not exceed the 2019 mark and amounted to 3,7% of GDP. The external position received USD 1,3 bn support for the settlement of a long dispute with foreign shareholders over the Karachaganak field. In turn, imports of goods and services declined by 4% influenced by the KZT depreciation. In 2021-2022, we expect the current account deficit to shrink to 1-2% of GDP as oil exports increase and external demand recovers.

A strong position for Kazakhstan's creditworthiness is accumulated buffer reserves: NFRK and international reserves. As of May 2021, the assets of the NFRK amounted to USD 57,7 bn, which further supports the fiscal position. International reserves have grown 12% y-o-y to USD 34,2 bn as of March 2021, covering almost 10 months of imports in 2020.

**Stress factors:**

- Concentration of tax revenues on one industry remains high. Kazakhstan depends heavily on oil revenues, which make up around 44% of the state's budget that is more than 8% of GDP (weak stress-factor);

**SENSITIVITY ASSESSMENT:**

The following developments could lead to an upgrade:

- Faster and stronger than originally anticipated recovery from the current economic crisis with higher non-oil GDP growth and improvement of non-oil fiscal balance;
- Effective implementation of state programs to diversify the economy to reduce the concentration on the commodity sector;
- Improvement of the general stance of the banking system, especially asset quality.

The following developments could lead to a downgrade:

- Further deterioration of economic activity which will have a direct impact on public finances and external buffers;
- Substantial deterioration of the stance of the banking system with a sharp growth of NPLs levels and a drop of profitability and capitalization metrics, which can lead to the materialization of contingent liabilities for the government.

**ESG Disclosure:**

**Inherent factors**

- Quality of fiscal policy; quality of monetary policy; natural resources; natural and climatic threats; environmental threats; level of corruption, CPI; Government Effectiveness Index; quality of the business environment; position in Doing Business Ranking; level of investment in human capital, adjusted for inequality; Rule of Law Index; transparency of government policymaking Index; level of information transparency of the government; Political Stability and Absence of Violence/Terrorism Index; natural disasters, constant exposure to difficult natural conditions.

**Drivers of change factors**

- None.

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Next scheduled rating publication: 10 December 2021. The full sovereign rating calendar can be found at [Sovereign Rating Calendar 2021](#)

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## RATING HISTORY:

Date	Review reason	SGC		Outlook	
		National currency	Foreign currency	National currency	Foreign currency
11.12.2020	Scheduled revision of both types of ratings for the country	BBB-	BBB-	Stable	Stable
12.06.2020	Scheduled revision of both types of ratings for the country	BBB-	BBB-	Stable	Stable
13.12.2019	Scheduled revision of both types of ratings for the country	BBB-	BBB-	Positive	Positive
14.06.2019	Scheduled revision of both types of ratings for the country	BBB-	BBB-	Stable	Stable
21.12.2018	Scheduled revision of both types of ratings for the country	BBB-	BBB-	Stable	Stable
06.07.2018	Scheduled revision of both types of ratings for the country	BBB-	BBB-	Stable	Stable
12.01.2018	Scheduled revision of both types of ratings for the country	BBB-	BBB-	NA	NA
14.07.2017	Scheduled revision of both types of ratings for the country	BBB-	BBB-	NA	NA
20.01.2017	Scheduled revision of both types of ratings for the country	BBB-	BBB-	NA	NA
22.07.2016	Scheduled revision of both types of ratings for the country	BBB-	BBB-	NA	NA
29.01.2016	First assignment of both types of ratings for the country	BBB-	BBB-	NA	NA

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### Minute's summary

The rating committee for Kazakhstan was held on 11 June 2021. The quorum for the rating committee was present. After the responsible expert presented the factors, which influenced the rating assessment, the members of the committee expressed their opinions and suggestions within the framework of the Sovereign methodology. The chairman of the rating committee ensured that every member of the committee expressed his/her opinion before proceeding to the voting.

The following methodology was used for the rating assessment: [Methodology for Assigning Sovereign Government Credit Ratings – Full Public Version](#) (from August 2020). Descriptions and definitions of all rating categories can be found under the [Rating scale](#) section. The user of the rating shall read the methodology in order to have a full understanding of the rating procedure.

The definition of default can be found on the Agency's website in the section for [Internal policies](#).

**These ratings are unsolicited. The rated entity did not participate in the rating process.**

Main sources of information: National Bank of Kazakhstan, Ministry of Finance of the Republic of Kazakhstan, World Federation of Exchanges, International Monetary Fund, World Bank, Trading Economics, World Economic Forum, Doing Business, United Nations, Kazakhstan Stock Exchange (KASE), Cbonds, publications in the media.

### ESG Disclosure

We consider Environmental, Social, and Governance (ESG) risks and opportunities in the creditworthiness analysis of our Sovereign entities. The disclosure document can be found on the Agency's website in the section: [ESG factors in RAEX-Europe's Credit Ratings](#)

### Limits of the Credit Rating

During the rating assignment process, Rating-Agentur Expert RA GmbH (the Agency) used publicly available information that was considered to be reliable, complete and non-biased. The responsible expert performed the rating assessment of the country with information considered as the most reliable and up to date in accordance to the overall position of the country and the Agency's internal criteria for selecting data providers. The information and data used for this specific assessment can be considered as of sufficient quality.

### Regulatory use

SGC ratings can be used for regulatory purposes according to the ESMA definition.

### Conflict of interest

The responsible expert was neither influenced nor biased by third parties during the rating assessment. All employees involved in the rating assessment and revision of the rated entity have reported absence of conflicts of interests before initiation of the rating process.

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### Office responsible for preparing the rating

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Rating-Agentur Expert RA GmbH is a credit rating agency established in Germany and therefore shall comply with all applicable regulations currently in force in the European Union.

The European Securities and Markets Authority (ESMA), the EU's direct supervisor of credit rating agencies (CRAs), has registered Rating-Agentur Expert RA GmbH as a CRA under Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, with effect from 1 December 2015.

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