

## Rating-Agentur Expert RA confirmed at 'BBB-' the ratings of Kazakhstan. The rating outlook is stable.

Rating-Agentur Expert RA confirmed the sovereign government credit rating (SGC) 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.

### MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:

#### Positive factors:

- The economy is expected to grow by 3,7% for 2018 due to the oil price booming in 1H 2018 (from January till June 2018 crude oil price increased by 20% up to 74,45 USD per barrel). However, such dependency on the oil sector could seriously affect future economic output;
- For the first time for the past 20 years Kazakhstan issued a EUR-denominated sovereign bond seeking for lower interest rate and expanding new currency for borrowing. As of December 2018 it is trading only with a 2p.p. higher yield than the German government security with identical maturity. Such low spread indicates a relatively low risk level making it attractive for investment;
- After five years of government debt constantly increasing, it is forecast to decrease by 1,3 p.p. y-o-y in 2018 down to 18,1% of GDP. Furthermore, debt to budget revenues ratio will decrease by around 21p.p. in 2018. Short-term external debt almost doubled in 1H 2018, mainly from debt securities of the Central Bank trade credit and advances provided to the Central government; however, despite the increase, we expect it to remain very low at 0,5% of GDP in 2018;
- Monetary policy of the National Bank of Kazakhstan (NBK) allows for effective control of inflation. After the increase of the interest rate back to 9,25% in October 2018, the price index growth stabilized (monthly change since October to November 2018 was only 0,05%);
- The NBK's gross reserves are above the suggested adequacy range for a country with a floating exchange rate in the amount of USD 29,2 m as of October 2018. These reserves cover about 8 months of imports of goods and services and cover around 2x the short-term debt;
- GDP per capita in PPP terms is expected to reach an all-time high of around USD 27 490 in 2018 and remain one of the highest among its regional CIS peers<sup>1</sup>;
- The unemployment rate has been stable over the past years and remained at satisfactory levels in 2018 (5,0%);
- It has been reported that the national privatization program directed to decrease contingent liabilities risks and better management of the enterprises is 80% completed. As of November 2018, more than 670 entities have been sold or set for liquidation;
- FDI net inflows are expected to increase in 2018 after a sharp decline in 2017 due to the

<sup>1</sup> Estimated GDP per capita in PPP for 2018: Uzbekistan – USD 7 337; Tajikistan – USD 3 354; Turkmenistan – USD 19 526.

lower investment in mining and agriculture.

#### Restricting factors:

- For the first time since 2014 overall fiscal balance is expected to be positive and to reach a figure of around 0,6% of GDP in 2018 mainly driven by recovering prices on oil. Restructuring of the economy is progressing at a slow pace keeping budget revenues highly dependent on extracting industries. The non-oil fiscal balance will continue to be negative in 2018-2019, at around -6,9% of GDP;
- The ratio of bank assets to GDP has been developing in a negative trend since 2015 (expected to be 5p.p. down y-o-y in 2018) signifying that credit growth is recovering at a slower pace than economy. The key constraints are limited availability of long-term funding and insufficient demand by creditworthy borrowers. The level of deposit dollarization continues to be significant in 2018, at around 47%;
- The level of competitiveness of the economy remains satisfactory. The index of economic competitiveness from the World Economic Forum was 4,35 out of 5,7 in the 2017-2018 report.

#### Negative factors:

- The inflation rate remained high and expected to be around 6,2% at the end of 2018. Due to higher exchange rate volatility in October 2018, the NBK was forced to hike the base interest rate by 0,25p.p.;
- Underdevelopment of the capital markets remains a negative factor due to the high concentration of trades in a small amount of issuers as well as a very low market capitalization. As of October 2018, total capitalization to GDP had decreased by 2,5p.p. down to 26% since the beginning of the year. However, the creation of the financial hub – Astana International Financial Centre (AIFC) – as well as the opening of “Astana Stock Exchange” (the second stock exchange in the country), may play a key role in enhancing economic growth and further enabling the structural diversification of the financial market;
- The troubled banking sector keeps holding back the creditworthiness of the sovereign. The real value of problem loans in the system is still hard to estimate and it is expected to be higher than the official NPLs at 8,5% in November 2018. Moreover, the recent liquidity struggles of Tsesna bank (the second largest bank accounting for around 7% of total assets) have triggered an injection of funds by the government representing around 0,8% of GDP and have exerted further pressure in the system. Despite this, the sector presented significantly higher profitability indicators in 3Q 2018 as ROA reached 2,35% and ROE 19,01% increasing by 2,52p.p. and 20,61p.p. from the same date last year respectively. Taking into account all the restructuring efforts of the authorities (the NBK withdrew licenses of several medium-sized and small banks that were in violation of prudential requirements), the official NPLs ratio declined further but remained high;
- The share of total assets owned by state and municipal corporations vary among 30-40% of GDP which, alongside the banking system weakness, creates a latent risk of contingent liabilities’ materialization. However, as a result of the national privatization program, the amount of SOE’s will be decreased by 877 entities.

#### Stress factors:

- Concentration of tax revenues on one industry. Kazakhstan depends heavily on oil revenues, which make up around 41% of the state’s budget, that is 7,6% of GDP (moderately weak stress factor);
- Financial dollarization in Kazakhstan has remained quite stable along 3Q 2018 increasing slightly to around 23% of total loans and 47% of total deposits (very weak stress factor).

## SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Long-term sustainability of high oil prices will allow to accumulate sufficient budget revenues and decrease government debt;
- Continued industry diversification and building greener global economy which would make Kazakhstan less exposed to oil price shocks;
- Improvement of the banking system performance.

The following developments could lead to a downgrade:

- A renewed decline in hydrocarbon prices which would cause a deterioration of the country's fiscal stance;
- Further weakening of the banking system which would materialize contingent liabilities of the government;
- Low quality of restructuring and fiscal reforms.

“The confirmation of Kazakhstan’s rating at ‘BBB-’ with a stable outlook shows the stability of most macro and fiscal metrics across the board. Lower government debt, positive fiscal balance, favorable GDP growth and inflation levels as well as a solid external position are among the factors supporting the creditworthiness of the sovereign.

Despite this, the lingering weakness of the banking sector continues to be the key issue in regard to the country’s credit rating. A fragile banking system may cause contingent liabilities to materialize. Moreover, the economy continues to be highly dependent on the oil sector. Thus, the volatility of the oil market creates uncertainties towards economic growth and fiscal imbalances.”  
– Clarified Hector Alvarez, Rating Associate of Rating-Agentur Expert RA GmbH.

Responsible expert: Hector Alvarez, Rating Associate of Rating-Agentur Expert RA GmbH

Reviewer: Olena Kolokolova, Rating Analyst of Rating-Agentur Expert RA GmbH

Research report on Kazakhstan is available at:

[https://raexpert.eu/reports/Research\\_report\\_Kazakhstan\\_21.12.2018.pdf](https://raexpert.eu/reports/Research_report_Kazakhstan_21.12.2018.pdf)

Next scheduled rating publication: 14 June 2019. The full sovereign rating calendar can be found at <https://raexpert.eu/sovereign/#conf-tab-5>

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**RATING HISTORY:**

Date	Review reason	SGC		Outlook	
		National currency	Foreign currency	National currency	Foreign currency
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

## Minute's summary

The rating committee for Kazakhstan was held on 19 December 2018. 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 May 2018) can be found under the following link: [https://raexpert.eu/files/methodology/Methodology\\_Full\\_Sovereign\\_V3.pdf](https://raexpert.eu/files/methodology/Methodology_Full_Sovereign_V3.pdf). Descriptions and definitions of all rating categories can be found under the following link: <http://raexpert.eu/sovereign.php> 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.

**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.

## 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.

Rating-Agentur Expert RA GmbH is completely independent from the activities of other agencies of the RAEX group.

## Risk warning

The Agency disclaims all liability in connection with any consequences, interpretations, conclusions, recommendations and other actions directly or indirectly related to the conclusions and opinions contained in the Agency's press-release and research report.

This press-release represents the opinion of Rating-Agentur Expert RA GmbH and is not a recommendation to buy, hold or sell any securities or assets, or to make investment decisions.

## Office responsible for preparing the rating

The office responsible for the preparation and issuance of this credit rating is the office of Rating-Agentur Expert RA GmbH in Frankfurt am Main, Germany.

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.

Rating-Agentur Expert RA GmbH applies the Code of Conduct Fundamentals for credit rating agencies issued by the International Organization of Securities Commissions (IOSCO Code) and includes the basic principles of IOSCO Code in its Code of Conduct.