



SHIFTING TO INFLATION TARGETING STRATEGY IN KAZAKHSTAN'S ECONOMY

Theoretically, inflation targeting (IT) is a monetary policy strategy which is characterized by public announcement of official quantitative targets for the inflation rate over one or more time horizons and by explicit acknowledgement that low and stable inflation is the primary long-run goal of monetary policy. All IT strategies implemented by the central banks aim at stabilizing both the inflation around the inflation target and the real economy. IT was first implemented in New Zealand in 1990. Proven successful, it has been adopted by more than 25 developed and developing countries since 2010. Main characteristics of IT are an announced numerical inflation target, an implementation of monetary policy that gives a major role to an inflation forecast (forecast targeting), achieving price stability and a high degree of transparency and accountability. IT focuses on keeping inflation in line with a numerical inflation target in the medium term. Also, it has been successful in helping the central banks to embrace and to maintain robust macroeconomic policies.

Kazakhstan showed a considerably high macroeconomic performance after the global crisis. Between 2010-2011 GDP growth was around 7.5% but due to decline of oil and agricultural output, real GDP growth slowed down to 6% between 2013-2014. Especially in 2015, as a result of external factors (such as decline in oil prices and Russian recession, etc.) and internal factors (such as low domestic demand, etc.), real GDP growth reduced to 1.5%. On the other hand, despite 2009 devaluation, core inflation (excluding food, energy and administered prices) has averaged to about 6% since 2010. However, after 2014 devaluation, the risk of dollarization occurred in the economy. Due to the ongoing issues in money markets, tenge depreciated and temporary inflationary pressures have emerged.

Since the beginning of 2015 the inflationary pressures, which have a distortionary effect on price stability have increased. In these circumstances, the National Bank of Kazakhstan (NBK) decided to implement IT strategy to keep inflation at low levels (approximately between 6% and 8%). After accepting the floating exchange rate regime, the Government of Kazakhstan and the NBK jointly decided to imple-

ment IT strategy on August 20, 2015. As the immediate results of IT strategy could not be seen in the very short-term, inflation has continued to increase since August 2015 and the year-on-year inflation reached 9.4% in October 2015. According to the Committee on Statistics of the Ministry of National Economy of Kazakhstan, the inflation rate measured by Consumer Price Index (CPI) reached 5.2% in October 2015. In January-October 2015, the consumer prices have increased to 8.2% compared to the same period of 2014 (6.3%). Therefore, due to the recent devaluation of tenge and to an increase in import prices, in the short-term, the inflation rate in the economy of the country is expected to be above the targeted level. However, in the medium-term, the new monetary policy based on this strategy in Kazakhstan's economy is expected to contribute to the solution of the main problems of the economic policy and to achieve the long-term sustainable growth by keeping the inflation rate low and by achieving price stability.

In the international practice, mainly two indicators are used as IT parameters: the CPI and the core inflation. The CPI is a commonly used parameter which measures the average level of prices for goods and services that are part of the population's consumer basket. In Kazakhstan, the CPI includes more than 500 goods and services that are classified into three groups: food items, non-food items and paid services. The gathering of information on price changes, the monthly calculation and publication of information on the CPI are performed by the Committee on Statistics of the Ministry of National Economy of Kazakhstan. The CPI is presently used by the NBK as an IT parameter to achieve price stability.

In order to establish the target level of inflation, specific targets such as point, interval and point with tolerance band are used. The point target is characterized by the preciseness of the objective and the central bank's decisive intention to achieve it. The interval target (inflation target band) is able to react flexibly to changes in the economy and to allow sharp price changes which are caused by seasonal factors and by external shocks. The point target with tolerance band is the most commonly used IT in the world which combines the ad-

vantages of both targets defined above. Regarding the macroeconomic situation in Kazakhstan's economy, the NBK has planned to use the point target with tolerance band in transition to IT strategy.

It was announced by the NBK that IT strategy would make it more profitable to hold savings in terms of tenge and to reduce inflation expectations. The main purpose of this strategy is to avoid sharp fluctuations in tenge and to achieve price stability in the medium-term. In order to achieve this aim, together with the implementation of floating exchange rate regime, the NBK also implements a market targeting interest rate which will be achieved by open market operations and by minimum reserve requirements. The NBK introduces a new base interest rate, according to which, all interest rates will be pegged. In accordance with the tight monetary policy, the base rate may be raised or lowered. In this sense, the NBK announced the one day repo rate as its main monetary policy interest rate to target inflation within a corridor of 6%-8% in the medium-term. In the first half of 2015 the base interest rate was set at 12% with immediate effect. However, it was recognized by the NBK that 12% would have a limited effect on inflation because there would be lags between the real and the desired effects of IT on inflation. In this respect, in November 2015 the NBK decided to raise the base interest rate from 12% to 16% to keep inflation in the medium-term target corridor of 6%-8%. Besides, in order to improve the ability of banks to manage liquidity, calculation of minimum reserve requirements has been introduced by the NBK in 2015. By introducing a division of liabilities by national and foreign currencies with preserving residency and maturity principles, the NBK used the minimum reserve requirements to help IT strategy to achieve the aim of price stability in the medium-term.

In conclusion, it should be noted that when central banks implement IT strategy, they should carefully and honestly evaluate the extent to which they can effectively stabilize not only inflation around IT but also stabilize the real economy. Secondly, while implementing IT strategy, the central banks should engage in a serious dialogue with their constituents about the optimal rate of inflation.

- As a result of an official meeting between the President of the Republic of Azerbaijan, Ilham Aliyev, and the President of the People's Republic of China, Xi Jinping, the Joint Declaration on the Expansion and Deepening of Friendly Relations and Cooperation between Azerbaijan and China was signed. Moreover, the Memorandum of Understanding (MoU) on joint encouragement of the establishment of the Silk Road Economic Belt and the Agreement on prisoner handover between Azerbaijan and China were inked.
- The President of Turkmenistan, Gurbanguly Berdimuhammadov, has met with the President of Georgia, Giorgi Margvelashvili, who arrived in Ashgabat to participate in the celebrations on the occasion of the 20th Anniversary of the Turkmen Neutrality. The Presidents discussed topical issues of bilateral and multilateral cooperation related to the acceleration of the implementation of the Baku-Tbilisi-Kars railway project, to an increase of the throughput of the East-West transport corridor and to the new possibilities of transportation of the Caspian energy resources.
- During the official visit to Ashgabat, the President of Belarus, Alexander Lukashenko, and his Turkmen counterpart, Gurbanguly Berdimuhamedov, signed a Roadmap for bilateral cooperation in 2016-2017 and a Cooperation program between the Foreign Ministries for 2016-2017. Moreover, leaders of the two countries adopted a Joint statement about the deepening of relations, friendship and cooperation between Belarus and Turkmenistan.
- The meeting of the 2015 Paris Climate Conference (COP21) came to the first legally binding and universal agreement on climate change in over 20 years of the UN negotiations. 195 countries have struck an international deal to keep global warming below 2 degrees Celsius. The text of the deal foresees a revision of national plans, aiming to cut carbon emissions, as well as creating a \$100-billion support package for developing countries.
- Russian and Indian warships have left the naval base in the city of Visakhapatnam in India's southeastern state of Andhra

Pradesh, starting the second - active - phase of the 8th Joint Naval Exercise Indra following the on-shore phase. The sailors will practice antisubmarine operations and a live-fire exercise involving surface and aerial targets in the Bay of Bengal.

Economy, Finance and Energy

- The cost of future contracts of the Brent crude oil delivery on London's ICE trading in January 2016 went down by 2% to \$39.99 per barrel as it breached the psychologically important mark of \$40 per barrel for the first time since February 2009.
- According to a monthly report of the Organization of Petroleum-Exporting Countries (OPEC), oil production in Russia is to increase by 20,000 barrels per day (bpd) to 10.77 million bpd in 2015. In the meantime, Kazakhstan's oil production is expected to decline by 60,000 bpd to an average of 1.53 million bpd in 2016 compared to 2015. Also, Azerbaijan's oil production will decrease by 40,000 bpd to 0.82 million bpd in 2016.
- According to the State Oil Company of Azerbaijan, SOCAR, in January-November 2015 the volume of oil transported via Baku-Tbilisi-Ceyhan increased to 26.37 million tons compared to 26.05 million tons transported in the same period of 2014.
- The President of Turkmenistan, Gurbanguly Berdimuhammadov, the President of Afghanistan, Ashraf Ghani, the Prime Minister of Pakistan, Nawaz Sharif, and the Vice President of India, Mohammad Hamid Ansari, took part in the solemn ceremony of laying of the 214 km Turkmen section of the TAPI pipeline. The 1,814 km TAPI pipeline, named after the countries it is designed to cross, is expected to be operational by 2019 at an estimated cost of up to \$10 billion.
- During the meeting of the Azerbaijan-Turkey Joint Commission in international road transportation, the Deputy Head of the State Road Transport Service of Azerbaijan, Ibrahim Aliyev, and the Assistant Director General of Highways of the Ministry of Transport, Maritime Affairs and Communication of Turkey, Huseyin Yilmaz, signed the Pro-

ocol in the sphere of international road transportation. The Protocol will stimulate the transfer of cargos from Turkey to the Central Asian countries through Azerbaijan.

- The Finance Ministry of Russia expects the capital outflow of the country to be \$60 billion at the end of 2015. Being \$118.7 billion in January-November 2014, Russia's net capital outflow decreased to \$53 billion in the same period in 2015.
- The World Bank has decided to allocate a \$50 million loan to Armenia aimed to support a wide range of reforms, to enhance the fiscal, social and environmental stability in Armenia and to increase the competitiveness of local products.
- According to the Minister of Energy and Coal Industry of Ukraine, Vladimir Demchishin, the draft state budget for 2016 is based on average price of imported natural gas at around \$210-215 per 1,000 cubic meters.
- According to the Ministry of Economy and Development of Turkmenistan, country's GDP increased by 7.1% in January-November 2015. The GDP growth in the industrial sector, and construction amounted to 2.6% and 10.1% respectively, while the GDP growth in the transport and communication complex, trade and agriculture amounted to 10.2%, 11.1% and 10.4% respectively.

Society and Culture

- Search for missing oil workers in the Caspian Sea is currently underway at a distance of 100-150 kilometers from the rig No.10 of the Guneshli oil field where the fire occurred. Currently, 23 people are listed as missing.
- The official opening of the St. Prince Vladimir Church, the largest Orthodox Church in Central Asia, was held in Bishkek. The opening ceremony is dated to the 1,000th anniversary of the repose of the Baptist of Russia, St. Prince Vladimir.
- Nine people were reported as dead and the fate of 12 others remain unknown as a result of the fire in the building of a neuropsychiatric care home in the village of Alferovka in the Russian Voronezh region.