



## THE EFFECTS OF FLUCTUATIONS IN THE WORLD OIL MARKET ON BANK LENDING IN THE ECONOMY OF KAZAKHSTAN

Over the last two decades, the banking sector has expanded significantly in the economy of Kazakhstan. The highest development in the banking sector took place in the period between 2000 and 2008 (until 2008 world economic crisis). At that period, growing oil prices and cheap funding in external financial markets had positive effects on the country's banking sector. Along with the favorable external factors, the absence of strict regulation in the banking sector allowed it to grow at a rapid pace. However, the world economic crisis took the overheated Kazakhstani banking sector by surprise and caused serious destabilizing effects in the sector in 2009. The government of the country rescued the banking sector by nationalizing some commercial banks, namely, BTA Bank, Kazkommertsbank, Halyk Bank, getting a significant financial support amounted to 332 billion tenge (\$2.2 billion) from the National Fund of Kazakhstan. This measure helped to avoid the collapse of the banking sector, but the sector was still in a bad situation and even in 8 years after the global economic crisis, the sector was not able to return back to pre-crisis conditions.

One of the main indicators of crisis in the banking sector is the amount of loans in the system. The banking sector's loans were seriously affected by the crisis of 2009 in Kazakhstan, which created a vast amount of non-performing loans (NPLs) that exceeded 30% of total banking sector's loans. However, despite the high level of NPLs, the banking sector managed to grow and to continue crediting economy at relatively small pace in the period between 2009 and the middle of 2014. In the middle of 2014, the banking sector faced additional challenges. For instance, in two and a half years, from July of 2014 to November 2016 the loans of the banking sector increased by only 5.41% in nominal terms and reached 12.84 trillion tenge (\$38.91 billion), while inflation was more than 26% in this period. The sharp decline in world oil prices along with investment outflow from emerging countries and low metal prices have played a significant role in worsening the conditions in the banking sector in the country. The low oil prices had a negative effect on the national currency causing a negative impact on the bank lending in Kazakhstan. For instance, in its attempts to avoid rapid economic deterioration and social turbulences, the National Bank of Kazakhstan (NBK) delayed the national currency

devaluation. Until August 2015, the NBK maintained the fixed exchange rate by decreasing liquidity in terms of national currency, which in turn caused interest rates to increase in financial markets. Moreover, high devaluation expectations among the population, which resulted in dollarization in deposits caused further weakening of tenge liquidity in the banking sector. As a result, the banks' inability to issue loans in terms of foreign currency together with low funding in tenge caused negative growth in the bank lending. Therefore, from July 2014 until the devaluation in August 2015 the loans in the banking sector decreased by almost 13% to 10.64 trillion tenge (\$32.24 billion) from 12.19 trillion tenge (\$36.93 billion). During this pre-devaluation period, the decrease in loans in terms of national currency was 0.22%, while the decrease in loans in terms of foreign currency was 38.10%. Devaluating tenge in August 2015 slightly improved the situation with tenge liquidity in the financial markets. From the beginning of August 2015 to November 2016, or the post-devaluation period, the bank loans grew by 20%, which is a considerable growth. However, if we look at the loans in terms of currencies, it can be observed that the bank loans in terms of tenge grew only by 4.5%, while loans in terms of foreign currency grew by 74.2%. The huge growth of the bank loans in terms of foreign currency was not because of the growth of actual issuance of loans but the devaluation of tenge.

It is worth mentioning that not all sectors of the Kazakhstani economy suffered from the decrease in bank lending during the low oil prices period. For instance, the loans to the agricultural sector, communication sector, transport sector, industry and trade sectors grew by 68.4%, 56.9%, 43.3%, 34.8% and 24.7%, respectively, during the period. These high growth rates demonstrate the high level of governmental support, especially for the agricultural sector. In addition, due to the government's countercyclical policy aimed at developing the small and medium enterprises (SME's), the loans to the SME's grew by 90.57% and reached 2.96 trillion tenge (\$8.96 billion) in the reported period.

Meanwhile, the loans to the construction industry, to individuals and other sectors in the economy decreased by 23.7%, 2.9%, and 15.7%, respectively. These three industries account for 55.1% of total bank loans

or 7.01 trillion tenge (\$21.24 billion) in November 2016, while they accounted for 65.01% or 7.88 trillion tenge (\$22.67 billion) in July 2014. The loans to the construction sector decreased mainly due to the fact that it requires long-term loans to finance its activities making it too risky for the banks to provide lending during the period of the poor economic situation in the country. Moreover, the loans to individuals decreased because of the deterioration in the income level of the population, increased unemployment, and increased prices of imported goods.

Despite the fact that the loans to individuals decreased, the interest rates did not experience significant changes. For instance, the interest rates on loans to individuals in terms of tenge were 19.2% in July 2014 and the same rate was in November 2016, while the highest interest rate was observed in March 2015 (21.4%). The interest rates on loans to individuals in terms of foreign currency increased by 0.9% to 11.4% during the same period, and reached 14.6%, which is its highest rate in October 2016. On the contrary, the interest rates on loans to non-banking legal entities in terms of tenge increased significantly from 10.5% to 15.8% during the same period. Moreover, the interest rates reached 25.8% in February 2016. On the other hand, the interest rates on loans to non-banking legal entities in terms of foreign currency decreased by 0.9% from 8.8% in July 2014 to 7.7% in November 2016. The high increase in interest rates on loans in terms of tenge can be explained by the liquidity shortage in financial markets, which made funding sources too expensive for the Kazakhstani banks.

In conclusion, it is important to note that low oil prices had a significant effect on bank loans in the economy of Kazakhstan. Due to the decision of the NBK to focus on implementation of the inflation targeting, which could lead better economic results in the long-term comparing with short-term effects of monetary expansion, there was no opportunity to increase liquidity in financial markets that could improve the situation with weak bank lending. Therefore, it could be expected that in near future the bank lending in the economy of Kazakhstan will not increase rapidly, mainly because of the fact that the NBK would prefer the long-term stability rather than the short-term economic growth.

## Politics, Foreign Affairs and Security

- The Parliament of Turkey approved a constitutional reform package aimed to empower the role of the Presidency. The 550-seat Parliament approved the new 18-article Constitution in a final vote with 339 in favor and 142 against, while five empty ballots and two invalid. A new law is to be put to a referendum that will likely be held in early April.
- During the meeting of the Parliament of Kyrgyzstan, Daniyar Tolonov was elected as the Deputy Speaker. 104 parliamentarians voted in favor and 3 against Tolonov's candidacy.
- The First Deputy Prime Minister of Kazakhstan, Askar Mamin, and the Deputy Prime Minister of the United Arab Emirates, Minister of Presidential Affairs and member of the ruling family of Abu Dhabi, Mansour bin Zayed Al Nahyan, discussed the ways of implementation of the agreements reached at the highest level in energy, petrochemical, nuclear industry, transport and military fields.
- During his official visit to Tashkent, the EU Special Representative for Central Asia, Peter Burian, and the Foreign Minister of Uzbekistan, Abdulaziz Kamilov, discussed important issues of bilateral relations in political, trade-economic, cultural-humanitarian and other spheres. The parties also touched upon the new strategy of partnership between the EU and Central Asia.
- During his official visit to Astana, the Chairman of the Standing Committee on Foreign Affairs and International Development of the House of Commons of Canada, Robert Nolte, and the Prime Minister of Kazakhstan, Bakhytzhon Sagintayev, discussed prospects of cooperation between the two countries in socio-economic, agricultural, cultural and humanitarian fields, including interaction between business fields within the framework of Kazakhstan-Canada Business Council.
- During the visit of the Uzbek Foreign Ministry delegation to Moscow, the parties exchanged views on topical issues of bilateral cooperation within the Commonwealth of Independent States (CIS), focusing on preparing for the upcoming meeting of the CIS Council of Foreign Ministers in Tashkent.
- The Spokesperson of the Ukrainian Defense Ministry, Dmytro Hutsulyak, reported that around 7,500 foreign servicemen and about 12,500 Ukrainian soldiers would participate in military drills in Ukraine in 2017. Moreover, it was stated that about 1,500 Ukrainian

servicemen would take part in various drills abroad in 2017. The foreign troops were allowed to participate in multinational drills in Ukraine with the adoption of the corresponding bill by the Ukrainian Parliament. The bill outlines the admission in the framework of multinational drills of the NATO member states' military, as well as of the countries participating in the Partnership for Peace Program.

## Economy, Finance and Energy

- During the first meeting of the oil production monitoring committee under the Organization of the Petroleum Exporting Countries (OPEC) held in Vienna, OPEC and non-OPEC countries participating in the oil output cut deal discussed the ways to monitor and summarize initial outcomes of implementing the oil production cut agreement.
- Iran's Oil Ministry announced its plans to resume the development of the country's second biggest offshore gas field, Kish, with 1.4 trillion cubic meters of natural gas reserves. It is planned that within the first phase of project, 28.3 million cubic meters of gas as well as 11,300 barrels of gas condensate will be produced daily. The field would produce 85 million cubic meters of gas after becoming a full operational facility.
- Russia's Lower House of Parliament, the State Duma, ratified an agreement on the Turkish Stream gas pipeline construction. An explanatory note accompanying the ratification explains that the deliveries of the Russian gas through the gas pipeline would ensure annual export revenues to the Russian budget of approximately \$750 million through only the first branch of the pipeline.
- The opening ceremony of Mongolia's first solar power station took place in Khongor soum of Darkhan-Uul province. The solar power station with a capacity of 10MW was built by the domestic company Solar Power International in cooperation with Japan's Sharp Corporation and Shigemitsu Shoji Co. Ltd. The average annual electricity production of the solar power plant is expected to reach 15.2 million kWh.
- The Government of Turkmenistan announced about its plans to build a power-transmission line along the Turkmenistan-Afghanistan-Pakistan-India (TAPI) gas pipeline, which is being constructed since December 2015. It is expected that in addition to providing electricity to all infrastructural fa-

cilities of the gas pipeline, a power-transmission line will enable exporting electricity to other countries via Afghanistan. Turkmenistan plans to start producing 27.4 billion kWh of electricity by 2020 and increase this volume to 35.5 billion kWh by 2030.

- According to the National Bureau of Statistics of China, in 2016 the country's GDP increased by 6.7% compared to 6.9% in 2015. In total, China's GDP amounted to 74.41 trillion yuan (\$10.84 trillion) over the last year. During the reporting period, the primary industries in China grew by 3.3%, while the secondary industries and service sector experienced 6.1% and 7.8% growth compared with 2015. The total investments in China stood at 59.65 trillion yuan (about \$8.69 trillion) in 2016.
- According the Chairman of Iranian and Foreign Joint Venture Investment Association, affiliated to Iran's Chamber of Commerce, Industries, Mines and Agriculture, Hossein Salimi, the volume of direct foreign investments in Iran is forecasted to reach \$13 billion in the current fiscal year (ending March 21) compared to \$2.5 billion in 2015.

## Society and Culture

- Heads of Azerbaijan, Turkmenistan, Uzbekistan and Turkey and other Eurasian countries offer condolences to the Iranian President, Hassan Rouhani, regarding the site of the Plasco building in Tehran, which collapsed following a massive fire. A historic high-rise building in Tehran caught fire and later collapsed causing at least 30 firefighters to die. Iranian Government announced January 21 the national mourning day for the people died in the incident.
- A draft Presidential Decree titled Uzbekistan's Strategy for Further Development was published on the legal acts discussion portal. The project proposed to form a National Commission for the implementation of the Uzbekistan's Strategy on priority areas for 2017-2021, and a Commission on the implementation of the selected priority areas.
- During the meeting of over 25 non-governmental organizations from Kazakhstan, Kyrgyzstan, Tajikistan and the Netherlands held in Bishkek, the parties agreed to establish the Central Asian coalition on promotion of the women and children rights. The coalition will be focused on the enhancement of the socio-economic rights of 35 million women and 18 million children living in five Central Asian countries.