At a Glance

- Over the past decade, Kazakhstan has made strong policy strides and responsibly absorbed large natural resource–based earnings by implementing a rules-driven fiscal framework.

- The baseline outlook is subject to downside risks, both external and domestic. External risks include a continued oil glut that may keep oil prices depressed and lower external demand from key trading partners.

- Domestic risks include potential production delays at the Kashagan oilfield and a deterioration in the health of the banking sector, suggesting that the recovery may take time, affecting job creation and poverty reduction.

- To foster economic diversification and increase resilience to external shocks, the Government needs to accelerate the implementation of institutional and structural reforms to promote private sector development and bolster investor sentiment.

Country Context

Kazakhstan has a land area equal to that of Western Europe but one of the lowest population densities globally. Strategically, it links the large and fast-growing markets of China and South Asia and those of Russia and Western Europe by road, rail, and a port on the Caspian Sea.

The country’s proven oil reserves are the ninth largest in the world, and hydrocarbon output was the equivalent of nearly 18% of GDP and about 60% of exports in 2015. Kazakhstan has transitioned from lower-middle-income to upper-middle-income status in less than two decades. The country moved to the upper-middle-income group in 2006. Since 2002, GDP per capita has risen sixfold and the incidence of poverty has fallen sharply.

Kazakhstan’s main short-term economic policy challenge is to adjust to the new reality of slower growth and lower income for the near future. This will entail effective measures to strengthen the sustainability of the macroeconomic framework as well as action to protect the vulnerable.

Kazakhstan’s longer-term development policy challenge is to transform its growth model away from reliance on natural resource extraction toward a more diversified, competitive economy. Although successive development strategies have all embraced this goal, economic diversification has proven difficult to achieve, especially up until mid-2014, when oil prices were high. Despite progress toward a more transparent, less-regulated, and more market-driven business environment, there continue to be constraints related to governance, infrastructure, institutions, the investment climate, the rule of law, and low incentives for investment in physical capital and new technologies.
The World Bank and Kazakhstan

Kazakhstan joined the World Bank in 1992. Since then, the Bank has approved 47 loans to the country for a total amount of more than US$9.1 billion.

The Country Partnership Strategy (CPS) for 2012–17 is designed to ensure continued strong government ownership of Bank-supported programs and to allow the Bank to adjust to changing government priorities and country circumstances, thereby maximizing the Bank’s contribution to Kazakhstan’s development.

The CPS concentrates on the Government’s key priorities of competitiveness and jobs; strengthened governance in public administration and service delivery; and the safeguarding of the environment.

Key Engagement

Over the years, the World Bank has significantly extended its Advisory Services and Analytics (ASA) provided under the Joint Economic Research Program (JERP) since 2003. Over 13 years, the program has proven to be an innovative solution, with a client-driven knowledge agenda and Bank-selected work, bringing in and building up international experience while developing wider lessons of a good public character.

The JERP is structured around the CPS pillars focusing on development gaps in growth, governance, and the public service delivery agenda. The program is designed to ensure strong government ownership while enhancing the Bank’s contribution to the country’s development in a way that goes beyond funding.

The JERP for the 2017 financial year comprises nine activities, eight of which are ongoing programmatic tasks, for a total of US$3.05 million.

Recent Economic Developments

Kazakhstan has been seriously affected by external shocks, including lower oil prices. GDP growth slowed from 4.1% in 2014 to 1.2% in 2015 and 0.1% during the first half of 2016. Falling oil prices led to a large terms-of-trade shock, while China’s growth slowed further and Russia’s recession continued, weakening both external and domestic demand.

Following the shift to a floating exchange rate in August 2015, the external balance improved from a deficit of over US$10 billion in 2015 to a surplus of over US$2 billion in the first half of 2016. Preliminary data suggest that although the current account remained in deficit, it was offset by increased foreign direct investment inflows and a reversal in capital outflow. The move to a floating exchange rate regime and a consecutive removal of administrative price controls initially led to a sharp depreciation of the tenge and an increase in the inflation rate from 3.8%, y-o-y, in August 2015 to 17.7% in July 2016, eroding real wages and consumer purchasing power. Low-income households are particularly vulnerable to increasing prices, declining real wages, and dampened employment opportunities.

Progress in poverty reduction has stalled, and the national poverty headcount rate (measured at US$5/day PPP terms) remained at an estimated 14% during 2014–15. The official unemployment rate rose slightly from 5% on average in 2015 to 5.1% in summer 2016, indicating that the fiscal slowdown has started to affect the labor market. Efforts to readjust the economy to lower medium-term oil prices have intensified in 2016. The Government has continued to consolidate its fiscal accounts by further cutting lower-priority public investments and transfers to state-owned enterprises.

The 2016–18 budget calls for a reduction in the nonoil deficit to 7–8% of GDP, improving fiscal sustainability. Meanwhile, social sector spending has been ring-fenced, thus protecting expenditures that benefit the poor. The central bank has taken monetary and fiscal steps toward the full adoption of inflation targeting; it reintroduced the policy rate in early February 2016 and worked on stabilizing the money market, targeting year-end inflation of below 8%. The currency depreciation has affected the banking sector and its credit activity, as it increased banks’ relative exposure to foreign exchange lending. To support the banking sector, the authorities postponed the introduction of Basel III standards, including measures to increase the authorized capital ratio (initially scheduled for January 2016).

Economic Outlook

Under the baseline scenario, Kazakhstan’s GDP growth rate is projected to remain close to zero in 2016, due to low oil prices and the continued sluggishness of the global economy. The ongoing fiscal adjustment is expected to keep public sector consumption subdued. Weak domestic demand will slow the recovery of production and retail trade, while low oil prices will continue to inhibit the growth of ancillary subsectors such as transportation and wholesale trade. Both the fiscal and current account positions are expected to improve somewhat from their 2015 levels but will remain in deficit in 2016. Against this backdrop, poverty is estimated to increase slightly in 2016 (using the US$5/day poverty line).

Over the medium term, a moderate recovery of oil prices and higher oil production are expected to boost domestic demand. Under the baseline scenario, GDP growth is projected to rise to 1.8% in 2017. Rising oil revenues and continued fiscal consolidation will improve the overall fiscal balance. In 2018, GDP growth is projected to accelerate to 3.4% as rising oil output bolsters consumer and investor confidence, and further improvements are expected in the fiscal and current account balances. Poverty is expected to gradually decline in 2017–18. However, the rapid poverty reduction seen in earlier years appears to have come to a halt.
**Project Spotlight**

**Improving Connectivity Between East and West**

Kazakhstan is the ninth-largest country in the world, with a land area equal to that of Western Europe. Strategically, the country has a potential to connect the growing markets of Southeast Asia and China to Russia and Europe.

To help the country improve connectivity along the Western Europe-Western China (WE-WC) International Transit Corridor, the World Bank provided a loan of US$2.1 billion, the largest single investment loan in its history, to support the construction and rehabilitation of the 1,230 kilometer road section along the corridor. It is the main road corridor crossing Kazakhstan from the border with China in the southeast, through Almaty, Taraz, Shymkent, Kyzylorda, and Aktobe, to the border with Russia.

The construction of the corridor started in 2009 under the South West Roads Project. Implemented on time, with satisfactory quality and costs kept low, the project is changing Eurasian land transport options and logistics, complementing the railway link, and providing an important lower-cost alternative from China to Europe. Facilitating the trade and transit through Kazakhstan, the Project also addresses transport agency reform and capacity building for better roads asset management, operation and maintenance, and road safety. Today, the road is 90% open for traffic and has already brought positive changes to people’s lives.

The East-West Roads Project is expected to provide an efficient transport link from Almaty—one of the major economic centers of Central Asia—to Khorgos, the primary road border crossing point between Kazakhstan and China, thereby completing the upgrade of the WE-WC Road Corridor. Upgrade of the 305-kilometer-long section in Almaty oblast would facilitate a more efficient movement of goods and people and improve road safety.

It would also facilitate industrial, agricultural, and commercial activities, with improved trade and services along the new road and in adjacent towns and cities. Along with construction, the World Bank also supports the Government in formulating the tolling strategy for the Almaty-Khorgos road section and encourages the Government to engage the private sector in the maintenance of the republican road network.

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*The “Country Snapshot” is a bi-annual update, highlighting the country’s recent developments, economic outlook and major overview of the World Bank’s partnership with the country. You can find the latest updates at [http://www.worldbank.org/kazakhstan](http://www.worldbank.org/kazakhstan)*