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ACRA SFSI KZ measures financial stability of the country and assesses its vulnerability to specific risks by aggregating information regarding maturities and currency profile of assets and liabilities of economic agents (financial companies, non-financial companies, households and state)

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Tenge volatility adds to instability in Kazakhstan's financial system

Structural Financial Stress Index for Kazakhstan

The Structural Financial Stress Index for Kazakhstan (ACRA SFSI KZ) rose to 3.63 pts in 2018 from 2.6 pts a year earlier. Greater instability of the Kazakh financial market is largely due to currency risks.

Last year's growth in ACRA SFSI KZ is mainly driven by the increase in the currency rate trigger (the volatility of the KZT exchange rate rose by 63% in the second half of 2018), while the refinancing risk trigger (calculated using the interest rate spread) edged up by 4% in the same period.

There was a trend towards a gradual decline in the Kazakh currency in the first six months of 2018, but the volatility of the tenge grew significantly in the fourth quarter of the year.

Meanwhile, the growth in the refinancing risk trigger was not considerable, which points to the weak volatility of market rates and stable liquidity imbalances, although high. The latter component's stability was generally ensured by a moderate interest rate policy of the National Bank of the Republic of Kazakhstan (NBRK).

Last October, NBRK hiked its interest rate by 0.25 pp to 9.25% on expectations of pro-inflationary pressure due to the external macroeconomic environment (the impact of inflation in Russia and prices of Kazakhstan's main export goods). Since then, the interest rate has remained unchanged beefing up the stability of the liquidity imbalance, which is still rather high on the whole.

Furthermore, there is a surplus in tenge liquidity in the market with the TONIA indicator having been at the low side of NBRK's target corridor for a long time. The liquidity surplus can be partially due to the exit of non-residents from NBRK's notes, and partially due to the stimulating policy pursued by the Kazakh government, which is aimed at supporting a handful of its commercial banks, as well as the launch of the "7-20-25" mortgage housing credit program.

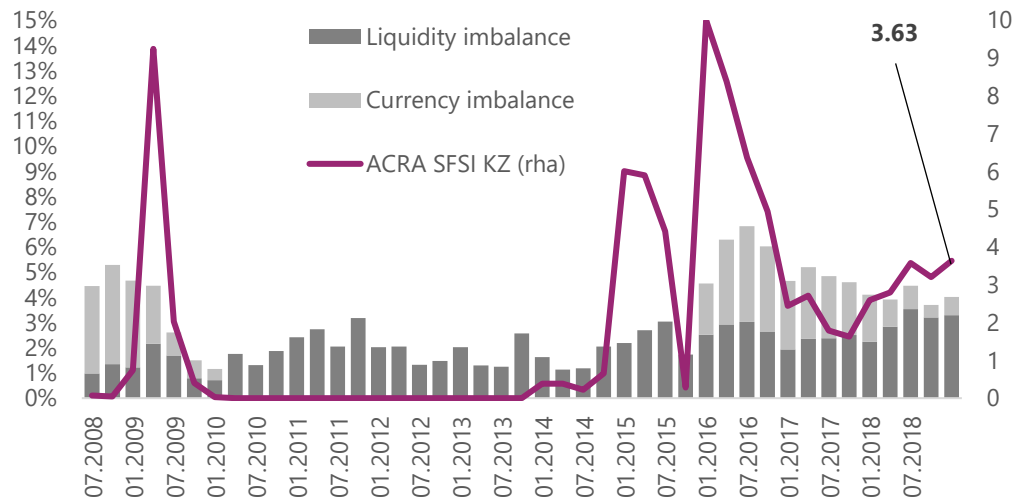
As for the liquidity imbalance by sectors, there is a growth in the tenge liquidity in the financial sector and even stronger one in the non-financial sector. The households saw a significant increase in the tenge liquidity in early 2018, which can be attributed to the surge in nominal income, while the growth in the tenge liquidity in the non-financial sector in the second half of 2018 is likely down to a lending recovery.

Currency imbalance is primarily driven by the non-financial sector, where currency interest expenses fell in the second half of 2018, while export revenues grew. Given this, the currency imbalance value has almost not changed. However, this factor is of a temporary nature because it greatly depends on what is happening in foreign markets.

Since the growth of ACRA SFSI KZ is stimulated by the above-mentioned triggers, the most significant potential risk for ACRA SFSI KZ is that of increased volatility of the KZT exchange rate, which is due to the fact that ACRA expects a decline in export revenues in 2019 coupled with a relatively high potential for primary income payments to non-residents.

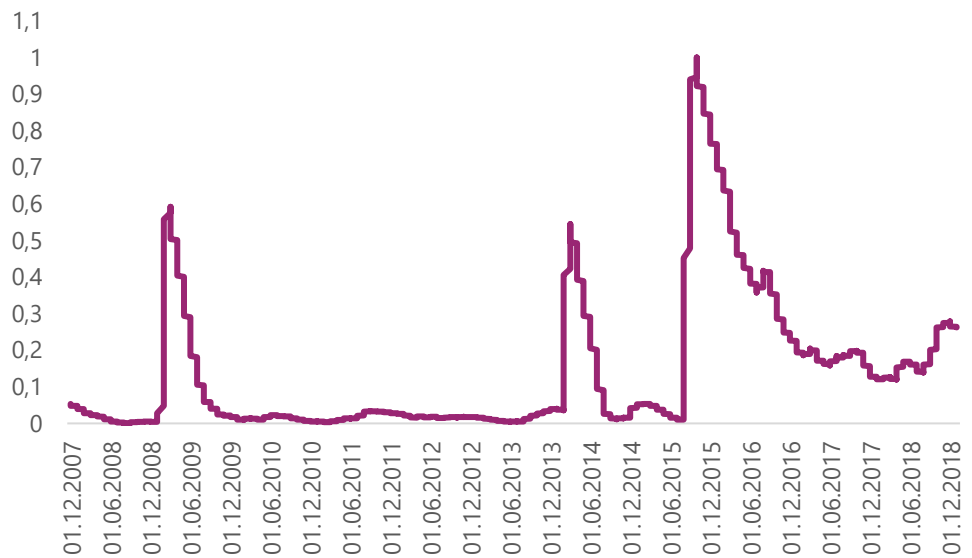
As far as the refinancing risk trigger is concerned, there are no major potential risks since the National Bank will most likely maintain a stable interest rate policy, enhancing current inflation and inflation expectations to remain at a moderate level.

Figure 1. Structural Financial Stress Index for Kazakhstan is moderately high, currency imbalance grew¹



Source: national agencies, ACRA estimates

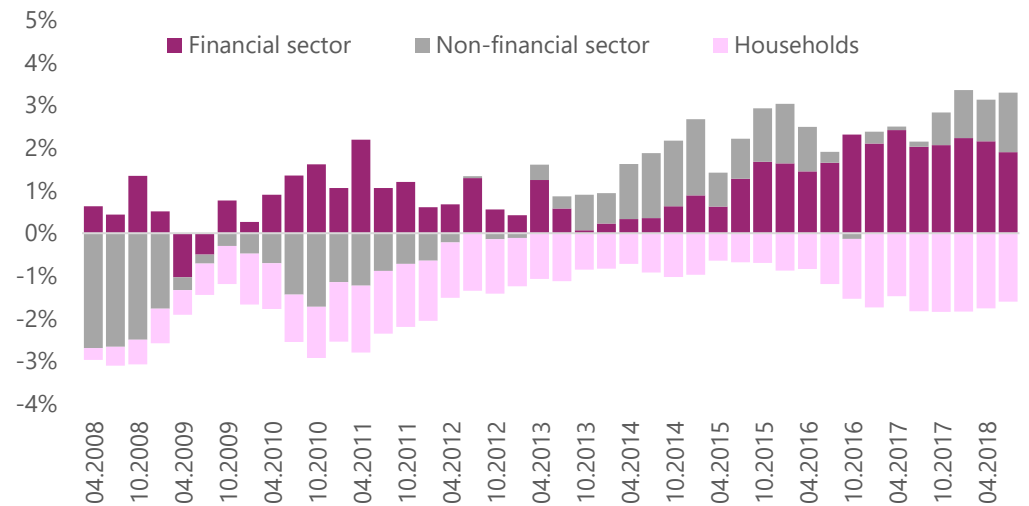
Figure 2. Volatility of the KZT exchange rate vs. the US dollar



Source: national agencies, ACRA estimates

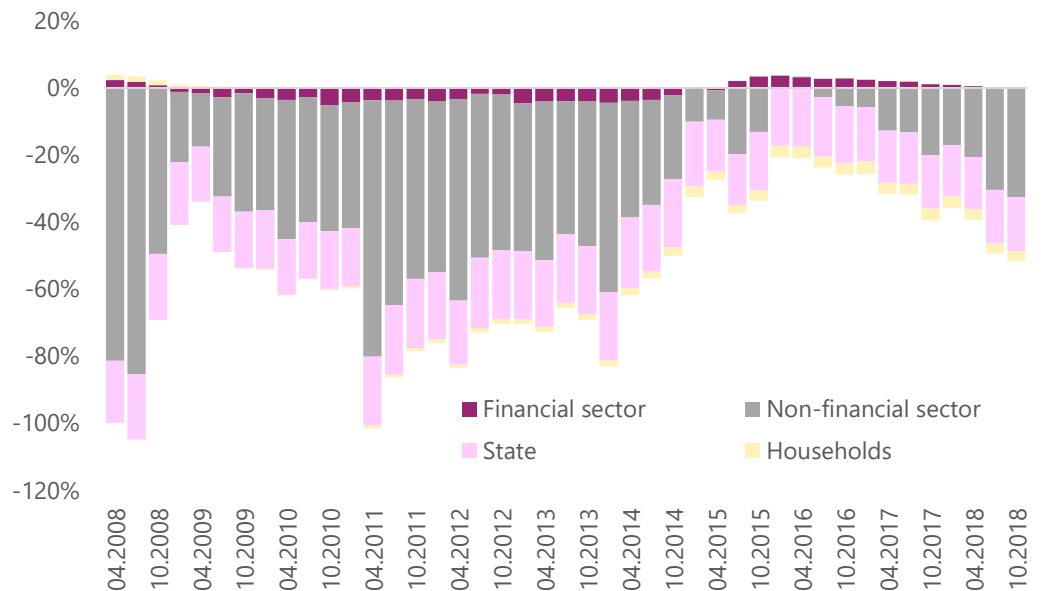
¹ The index's values for April-July 2018 have been recalculated due to the update of official statistics on some parameters.

Figure 3. Liquidity imbalances by sector (positive values indicate liquidity shortages)



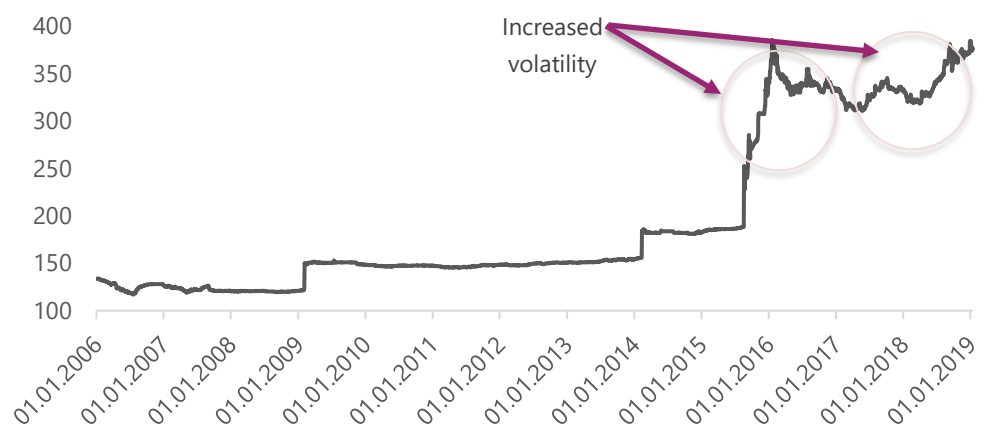
Source: national agencies, ACRA estimates

Figure 4. Currency imbalances by sector (positive values indicate the potentially unsecured portion of currency denominated obligations)



Source: national agencies, ACRA estimates

Figure 5. KZT nominal exchange rate vs. the US dollar



Source: national agencies

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