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## **EURASIAN FINANCIAL MARKETS, MACROFOUNDATIONS UNDERNEATH DEVELOPMENT OUTLOOK. HOW HAS THE GLOBAL FINANCIAL CRISIS ALTERED PERSPECTIVES OF KAZAKHSTAN STOCK EXCHANGE?**

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**Summary:** The Kazakh Stock Exchange aims to be the leading stock market in Eurasia. In fact, the enormous exertion was taken to transform this former Soviet Republic into a place where influence and interests of many different parties, transactions involving not only commodities or raw materials but human capital or sophisticated financial instruments would meet. Due to after-effects of the recent global financial crisis Kazakh stock market suffered heavy losses and proven to be illiquid and very unstable. It struggled not only to attract foreign investors, but even own domestic companies, preferring to seek for financing on UK and US stock markets, listing GDR's rather than equity stocks on KASE. The purpose of this paper is to bring to the light advantages and drawbacks, strengths and weaknesses of this unique market.

**Keywords:** Kazakhstan Stock Market, Eurasian Financial Sector, Macrofoundations, KASE.

### **1. Macrofoundations under growth and decline of Kazakh Economy**

The key features of Kazakh's geopolitical position are related to country's placement between Russia, China and the Caspian Sea. As the former Kazakh Socialist Republic it lasted till December 16, 1991. Currently Kazakhstan is a presidential republic, with a new capital, Astana (a city built mostly "from scratch" in the middle of Kazakh steppe, Almaty was the former capital city till 1997). There are three most crucial pillars of Kazakh economy – raw materials and fossil fuel production, livestock and grain production on the vast and propitious terrain and last but extraordinary – space industry. The latter consists of the impressive *Baikonur* compound, which hosted most of the Soviet space exploration programmes. The collapse of the USSR has affected the economy of Kazakhstan in a dramatic way. In the early nineties it tumbled, with sharply decreased demand for the products of Kazakh obsolete heavy industry. Formerly domestic, now foreign co-partners and buyers mostly from Russia, were unable to sustain cooperation with Kazakh companies at previous

levels. The programme of complex reforms in order to create market-oriented economy, through the privatization and adjustment of priorities and relationships with foreign partners, was initiated in 1995. Despite combined government and private sector efforts, Kazakh economy has proven to be highly vulnerable to the situation in Russia. Thus the serious economic crisis, which hit Russian Federation in 1998, has also severely damaged the economy of Kazakhstan. It led to deep recession, reflected in 2.5% decline of Kazakh GDP. To understand how serious it was, we have to consider the sluggish GDP growth rate, from 1996 until 2000, when Kazakh economy started its impressive rally – 9.8% GDP growth rate p.a. The peak was reached in 2001, with 13.5% and later we were observing a dynamic and sustainable growth rate at the level of nearly 10% per annum (10.1% average GDP growth during 2000-2007). All of these figures are presented free of prices fluctuations.

GDP per capita in Kazakhstan rose from approximately one thousand USD in 1993, reaching almost 1500 USD on the eve of the Russian crisis, in 1998. Next year GDP tumbled to 1100 USD (level similar to that from 1995). It took two years to reach the previous peak. Kazakh GDP per capita was soaring from 2001 until 2008 when it reached 8400 USD. However, we have to consider these figures as nominal, while the inflation in Kazakhstan remained hardly under control, at least when compared to developed countries. In fact, Kazakh GDP soared from 17 billion US Dollars in 1995 to nearly 132 billion in 2008, when it was hit by financial crisis spreading across the world. The inflation is the major factor – during the period of prosperity, until 2008 the average CPI growth was 10.2% p.a. It is nothing extraordinary if we look for instance at average inflation in Russia (11.3% p.a.) or in Turkey (12.9% p.a.) in the similar period. What should be noticed is that in Kazakhstan we have witnessed significant division between the dynamics of GDP and CPI growth. Through the period of take off from 2000 till the end of 2001, when GDP real growth rate reached 14% p.a. inflation rate remained stable (it did not exceed 6% p.a.). From the end of the first quarter of 2007 until 2008 things went out of control, with CPI growth peak at 20% p.a. In the meantime, GDP real growth rate dropped to nearly 2%. What should be also taken into consideration is that since the end of 2000 industry production growth rate was remaining in the downward trend, from its top at the level of 25% p.a. to the current recession (0% growth was observed in 2008). Inflation rate measured by CPI is apparently highly correlated with the total domestic credit growth. Since the credit market plummet in 2007, we observe a slide in CPI growth, offset by approximately one year. Obviously this is a natural cause-effect situation, but Kazakhstan has still an industry-oriented economy. Such a strong correlation between demand-driven factors with inflation may only support the afflictive conclusions. First, the growth of CPI in Kazakhstan during the last 5 years matches almost perfectly the price of crude oil. As it is mentioned at the beginning, export of fossil fuels is a solid pillar of Kazakh economy. The oil itself and oil products constitute almost 60% of the overall value of goods and services that are

being sold outside Kazakhstan. It is no surprise how the state is exposed to changes in crude oil prices, but when you try to point-out some key features of Kazakh financial market, it is imperative to understand how vulnerable it is to exogenous factors. It is always extremely hard to counter the inflationary pressure of supply shocks with monetary policy, but in Kazakhstan we have observed the extensive growth of money supply due to the total credit growth as well. Anyway, Eurasian country's money market is highly sensitive to both exogenous factors and domestic money demand. Kazakh Central Bank has been so far ineffective in suppressing inflation. Although some people say it is a common feature in this type of countries, however, such volatility in commodity prices forced National Bank of Kazakhstan to commence KZT devaluation by 20% in February 2009. Currently, when the pressure of the financial crisis eases, sluggish money demand due to the crash on the local credit market may be the most important obstacle slowing fast recovery of Kazakh economy. It is also worth noting that in 2009 four major players on the Kazakh credit market have defaulted on their loans: the Kazkommertsbank, BTA Bank, Temir Bank and Alliance Bank. In 2008 analysts from Royal Bank of Canada described Kazakhstan along with Latvia as the most hazardous country in terms of credit default risk<sup>1</sup>. When trying to forecast the prospects of Kazakh economy in 2-3 years perspective, it cannot be neglected that their credit market is going to face a lot of difficulties in order to recover fully. Insufficient money for credit will mostly affect domestic households and companies. International ventures, specially the ones involved in fossil fuels and raw materials markets are likely to expand in spite of demand rising across the world. Probably the nature of future GDP growth in Kazakhstan will not shift quickly into more domestic market-oriented growth.

Let us point some of the strengths of Kazakh economy which may be found attractive for the ones who want to invest in Eurasia. First and foremost, although financial sector has proven to be vulnerable to external factors and money market is fragile, KZT exchange rate to other currencies remains considerably stable. From 2008 to February 2009, when the devaluation took place, KZT/USD FX Spot Rate remained around 120. Then it leveled-off at the average of 150. Currently (as on April 14, 2010) it is 146.65 as per Bloomberg. Regarding the attractiveness of Kazakh financial market to foreign parties, this is a very advantageous feature in particular while inflation does make domestic money market unstable. Actually, despite the circumstances there are three major roots leading to the decent performance of KZT.. Kazakhstan is still considered politically stable and predictable. There are controversies regarding the despotic nature of Nursultan Nazarbayev's presidency, the level of corruption and ineffectiveness of judiciary system. Anyway, the internal and external political situation in this biggest Eurasian country seems to be stable and secured. This is even more important concerning recent events in Kyrgyzstan (which is by the way the only WTO member in the region). What might be viewed

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<sup>1</sup> <http://frontiermarkets.wordpress.com>, 4 November 2008.

as worrying in foreign investors' perspective, are the latest attempts to regain control over oil industry, initiated by the Kazakh Government in 2007. Some issues have been related to Karachaganak gas field and Kashagan oil deposit. The government intends to increase its ownership, which leads to disarray with foreign investors who run these ventures. The outcome of governmental recovery and stimulus programme, especially concerning the four financial institutions, is also hard to predict. Anyway, overall political stability works to Kazakhstan's advantage compared to its neighbors. The constant influx of foreign investments and strong export do reinforce KZT exchange rate. Initially, in 1994 outside investors directly invested only 600 million USD in Kazakhstan. In 1997 the value of foreign direct investments exceeded 2 billion USD. Then, after the end of the Russian crisis, an impressive surge was witnessed from 4.6 billion USD in 2001 up to 17.5 in 2007. That trend has leveled off in 2008. Kazakhstan still has a lot to offer, with the 2<sup>nd</sup> world largest natural reserves of uranium, phosphorus and chrome, 3<sup>rd</sup> silver, zinc, copper and lead, 4<sup>th</sup> molybdenum, 6<sup>th</sup> gold and coal and 7<sup>th</sup> oil. Two major oil fields, Tengiz and Kashagan contain approximately 14-16 billion of barrels. There is still approximately 155 billion USD to be invested over there in the next couple of years, according to Kazakh Ministry of Energy and Mineral Resources. Kashagan field has been explored since 2000 and it is considered a very perspective investment. It caused a clash between the government and foreign participants (ENI, Shell, Total and ExxonMobil have 16.6% shares each). The development of oil deposit in Kashagan was frozen by Kazakh authorities in 2007, until foreign companies agreed to increase the share of state-owned Kazmunaigaz holding from 8.3% to 16.6%. Similar case is related to Karachaganak natural gas field (approximately 8 billion of barrels). Its ownership is divided between BG Group and ENI (owing 32.5% each), Chevron (20%) and Lukoil (15%). However, the government wants to control at least 10% of this field, mentioning the threats of performing more detailed investigation to assess whether current owners keep Kazakh regulations concerning environmental protection. Anyway, vast resources of raw materials will still attract foreign investors and boost Kazakh's export especially in the aftermath of the financial crisis, which has crippled the global output.

Third and possibly the most important aspect of KZT stability on international currency exchange market is related to fiscal and monetary policy factors. During the last ten years the economy of Kazakhstan featured very positive performance in terms of debt to GDP ratio along with foreign debt coverage with FX Reserves. Since 1995 we have observed substantial public debt growth, boosted by full-scale and expensive reforms. It must be also admitted that major part of Kazakh indebtedness was inherited from the Soviet Union. Public debt to GDP ratio rose from 15% in 1997 to almost 28% in 1999 because of Russian crisis. Then the trend reversed and during the next five years it leveled off at 20%. Since 2005 until 2008 the situation improved a lot: the debt to GDP ratio (in 4 years average) dropped slightly below 10%. Currently it is stabilized after a slight increase in 2008-2009. Some concerns

are related to how much the stimulus programme will cost and how it could impact public debt. Regardless, Kazakh authorities have run rather tight fiscal policy through the period of last ten years. Budget balance remained at debit side for the most of its time, but stayed at reasonable ratio to GDP. The biggest deficit in relation to total domestic product (4% of GDP) was reported in 1998 later a significant improvement was seen and from 2000 until 2003 Kazakh budget was almost equalized. Then, until the end of 2006 incomes were higher than withdrawals, with almost 1% surplus over the GDP. A fiscal balance ratio to GDP during 2004-2008 was at average -0.5%, recently along with the recession and tumbling GDP growth rate dropped to -4% in 2009. As it was mentioned before it is unlikely this trend continues since Kazakh economy is recovering from the financial crisis. A risk of further deficit growth is moderate and does not seem to affect KZT FX Rates. In comparison, in both Russia and Turkey fiscal balance to GDP ratio dropped to 6% in 2009. Another important feature is FX reserves to external debt relationship. In 1998 external debt to GDP ratio in Kazakhstan equaled approximately 45%, but due to the Russian crisis struggling Kazakh economy had to seek for more foreign financing. In 1999 external debt factor rose slightly over 70%. During the period of the rapid GDP growth, it stabilized until 2006 and in the meantime Kazakh FX reserves surged by about 400%. From 2007 until now we have observed slight growth of foreign debt. In 2008 it accounted for 82.9% of GDP, then in 2009 92.3%. Again, it seems unlikely that this trend will sustain as Kazakh export is able to catch a breath after 39.5% decline in 2009 (compared to 2008). Owing to direct investments and fossil fuel export a significant influx of hard currency related to the post-recession recovery will adjust Kazakh FX reserves to the increased external debt. This will backup KZT along with diminishing fiscal deficit<sup>2</sup>.

Overall, Kazakh economy has been severely wounded during the financial crisis. It is likely to bounce back in two years time, but the speed of its recovery may not be seamless for all of interested participants. Export will be boosted by increasing global demand for raw materials and fossil fuels, new foreign investments are also plausible to appear. Along with that fiscal situation is going to improve, even despite stimulus policy applied by authorities in 2009. With the growing FX reserves there is a chance, that KZT will remain moderately stable to foreign currencies in five year perspective. On the other hand, Kazakh credit market was crippled by the biggest national lenders defaulted on their debts. The process of domestic debt restructuring is going to be complicated and prolonged. The economy of Kazakhstan is also proven to be very exposed to external pro-inflationary factors, and the domestic money market is likely to become unstable after possible future exogenous shocks. Thus strained confidence for the banking system and central bank's struggle against inflation should be considered as the biggest obstacle for Kazakh financial markets in order to progress any further. It also caused ratings downgrade in 2009 – to BBB – by Fitch and S&P, Moody's Baa2.

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<sup>2</sup> The National Bank of Kazakhstan press release, 3 February 2009.

## 2. The Kazakh Financial Market Overview

The Kazakhstan Stock Exchange (KASE) is the primary financial market in the Republic of Kazakhstan. The interbank sector of currency exchange can be considered as the origin of KASE. It was founded in 1993, during the introduction of new national currency – the Kazakh Tenge (KTZ). Thus there was created demand for more sophisticated currency-exchange platform, than contemporary Centre of Interbank Currency Transactions, being a part of National Bank (the Kazakh Central Bank). New venture was undertaken by the Central Bank along with twenty three commercial banks. On December 30 the KAICE (Kazakhstan Interbank Currency Exchange) was officially founded in the city of Almaty, the capital of former Kazakh SSR. Nowadays it is still running there as a part of Almaty Financial Centre. At the very beginning the sole purpose of the financial market in Almaty was to serve as an intermediary in currency exchange transactions. On October 2, 1995 it received legal approval to organize stock exchange, however, limited at that time only to government's securities. First trades were executed on November 14, 1995. Due to insufficient liquidity and several issues tagged with financial law, which was still under evaluation, The Kazakhstan Interbank Currency-Stock Exchange terminated primary activities as a trading floor for debt related securities. From the third quarter of 1996 (until 1998) no trades in government's securities were executed in Kazakhstan. The next issue was caused by the President's decree named "About securities and stock exchange" dated April 21, 1995. It did prohibit exchanging stocks in the same way as commodities. Therefore the Interbank Currency Stock market had no legal right to operate any longer in its previous form. The most significant obstacle was related to the nature of combining stock and currency trades within one financial institution. The newly founded licensor, named National Securities Commission of Kazakhstan, requested that currency compartment should be excluded from the rest of the financial market. It led to its re-registration on April 12, 1996. As the "Kazakhstan Stock Exchange" the new company gained licence from financial authorities and was able to organize securities trading from the end of 1996. However, it did not mean that the mix-up caused by unclear legislation environment was going to be over. On March 5 1997 another decree, known as "About securities market" prohibited trading other types of securities than equities and debt instruments. In the meantime, KASE launched currency-futures submarket. Again, the lack of liquidity along with legal issues forced them to cease activities related to futures exchange (in the beginning of 1998). The decision was made to launch a new venture, the "Almaty Financial Instruments Exchange" (AFINEX). The new company handled the exchange of foreign currencies along with futures, while KASE focused entirely on equities and debt instruments. In 1998, when the accumulative pension system was initiated, new prospects of increased demand and therefore potential liquidity grow encouraged KASE to restart trading with government's bonds. Professional asset managing companies, such as pension funds managers began receiving permission to operate in Kazakhstan. Therefore the National Securities Commission allowed them to invest only on a regulated stock market. By having the

OTC market prohibited, KASE apparently became the exclusive option. Along with domestic government-related debt instruments the market evolved to organize trades in Eurobonds of Kazakhstan as well. Moving on, in 1999 municipal and corporate bonds were finally allowed to be listed on KASE. In the meantime, legal regulations were augmented once again, that time permission was granted for stock markets to trade not only equity and debt related instruments. That led to further reorganization, the mentioned AFINEX Market was merged with KASE's primary trading floor. Since 2007 KASE has been no longer non-commercial institution, being a part of Regional Financial Centre of Almaty (RFCA) and considered as the special trading floor, according to the latest legal statements. The RFCA itself was launched in 2006 as an effort to consolidate scattered financial institutions and create integrated business and financial centre. The key components became: KASE, National Rating Agency of Kazakhstan, Securities Market Academy, RFCA Media, Special Financial Court. The RFCA project was designed with support of Boston Consulting Group and many other foreign advisors. BCG took part in a preparation of feasibility study, commenced in 2003. The Government of Kazakhstan decided to enter such an enterprise in 2005 in order to create a full-scale financial centre, leading among Central-Asian CIS countries. Nowadays RFCA operates in a special economic zone, with limited taxation and eased legal regulations. Although Astana established its primary role, when it comes to the aspects of authorities and major companies settlement, hosting for instance the Kazmunaigaz, the flagship state-owned energy exploration and production holding, Almaty hosts most of foreign and domestic financial activity.

Since 1999 KASE has been operating as the sole financial market of Kazakhstan, aggregating spot, swap and forward currency exchange, primary and secondary government's bonds market, separated corporate bonds and shares trading floors and finally repo deals and futures sector. Total volume of trades executed in 2009 reached 155.659.3 million of USD. Its key compartments were currency exchange – value of almost 68 billion of USD, along with repo transactions – approximately 71.5 billion. Both of them make up at least 89.6% of total volume. Although shares sector adds only 4.3 billion USD, which is no more than 2.8% of TV, it is still emerging – in the rate of 12.4% comparing to the last year. Kazakh government's bonds sector is also soaring, up to 9.43 billion USD, 21% growth rate to the value from 2008. The futures sector is still thick and illiquid, with aggregate volume of trades at the level not exceeding 100.000 \$<sup>3</sup>.

On the shares market thirteen companies issue shares which are traded as the first category. One of them, the Kazakhmys PLC, a large copper mining company, operates sixteen open pits and mines along with two refining plants in Kazakhstan. The company lists as well GDRs (Global Depositary Receipts) on the London Stock Exchange. The following one, Eurasian Natural Resources Corporation PLC creates almost 5% of Kazakhstan's GDP. ENRC is an integrated consortium of exploring, processing, production and delivery of ferroalloys, iron ore as well as aluminum and

<sup>3</sup> Bloomberg 21. 24 June 2009.

energy production. Like Kazakhmys, ENRC is also listed on LSE and since March 2008 has been a part of FTSE 100 Index. The Kazmunaigaz Exploration Production JSC is the largest state controlled company, focused mainly on natural gas and oil exploration, fossil fuels production and supply. It is involved in all major international ventures in Kazakhstan concerning gas and oil exploration, with the most significant Tengizchevroil Joint Venture. The company seeks for financing outside Kazakhstan as well, listing GDRs on LSE. The Kazkommertsbank JSC is the biggest private bank in Kazakhstan. Founded in 1990, with the main office in Almaty, it controls almost a quarter of Kazakh banking services market. As a major provider of corporate banking products to the biggest companies in Kazakhstan, Kazkommertsbank shocked Kazakh financial market, when it defaulted on its debt related instruments. Currently, when debt restructuring programme is underway, bank's debt securities are rated B by S&P, B Fitch and Ba3 by Moody's. The next company which is worth mentioning is Kazakh Telecom JSC, the largest provider of telecommunication services in Kazakhstan, with its headquarter in Astana. It is rated BB by S&P, which makes it the highest rated first sector's company, not operating in natural resources business. The shares ranked as second category are listed by twenty four issuers and as third category by forty one issuers. Regarding debt securities market, only thirty four tranches of bonds listed by fourteen companies are rated by foreign rating agencies.

The sector division by the number of issued stocks separates KASE stock market into financial companies (26.3% share in the market), metal and mining industries (21.2% share) and oil and gas explorers and producers (18.2%). However, when compared with market capitalization, approximately 60% of the stock market, to be is credited to companies focused on metal and mining business, especially ENRC, while financial and gas & oil enterprises constitute 17% of shares each on the market. What is highly notable is that the emerging telecommunication services sector makes only 3% of shares of the stock market in terms of market cap. Consequently, companies listed on KASE, which do not belong to the companies dealing with natural resources, gas & oil, financial and banking services or telecommunication constitute less than 3% of shares of the market. It somehow depicts Kazakh economy. Despite extensive efforts undertaken by the authorities, it still relies mostly on the same basics like in the 90s<sup>4</sup>.

### **3. KASE performance due to the financial crisis, upcoming prospects and threats**

In order to provide any presumptions regarding RFCA prospects of emerging as a major regional financial centre and so called "hub" between European and Asian markets, it is imperative to take a closer look at how it performed during the financial crisis. It was the ultimate test for almost every emerging financial market, including Polish, Hungarian, Russian and Turkish markets. Although the magnitude of the

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<sup>4</sup> [www.kase.kz](http://www.kase.kz)

global crisis made it impossible for them to avoid the extensive damage, it also highlighted some key features, strengths and weaknesses. The stock market in Kazakhstan was no exception. It was created in the early 90s to transform local equity exchange platform into the most capable and influential financial centre in the region and the crisis determined its further development and evaluation. Huge investments were applied in order to build modern financial infrastructure in both Astana and Almaty. The major goal was to create conditions supporting the growth of previously underdeveloped business sectors. Of course, one of the most important tasks of RFCA is to organize trades and secure a capital flow in enterprises focused on fossil fuels, raw materials and other natural resources. However, it is not anything more than what other local exchange platforms offer, for instance Tashkent Stock Exchange (Uzbekistan) or KSE (Kyrgyz Stock Exchange). Nevertheless, the primary trading market for Kazakh oil, gas or other raw materials is located not in Eurasia, but in London. Banking and telecommunication services were considered the most promising sectors, like in Russia and Turkey. In fact, fuels and raw materials exploration and production companies still make up 75-80% of KASE stock market capitalization. The KASE Index (which consists of seven biggest companies, listing most liquid shares) performance during 2005-2008 prosperity reflected GDP growth boosted primarily by export. In December 2005 the index exceeded 500 points, in April 2006 it reached 2000 points. From February 2007 until July 2008 KASE Index was relatively stable in 2 year run. For the most part of that period it stabilized between 2500 and 2800 points, with local (and global as well) maximum at 2876.17 (July 2007). In the meantime, we observed the highest trade volume, reaching even more than 800 million USD (on the stock market). When most of the previous investors had gained their profits, trade volume dropped below 100 million USD before September 2008. Then, in the eve of thrilling news coming from US subprime mortgage financing sector, KASE Index tumbled to slightly above 500 points in January 2009. In comparison to the level of prosperity period, 80% slide was not exceptional when we look at stronger stock market indicators, which were falling across the world. It is the trade volume that became the worst factor. When stock prices were falling in September 2009, trade volume raised sharply to approx. 550 million USD, and then, one month later, it dropped to 50 million USD (figures related to the stock market only) and the stock market became almost illiquid. We have not observed more active trading activity (when compared to the level from the end of 2006) since October 2009. This is probably the most dangerous feature which concerns every investor looking for a short and mid-run investment opportunities. Kazakh stock market is not only exposed to negative shocks on foreign markets, but it can become completely frozen in some days. Total trading volume declined from almost 9 billion USD in 2007 to 3.3 billion USD in 2008. If volatility of trade volume could be considered extremely hazardous for those who invest on the shares market, then the credit default risk should be regarded as the most important risk factor on debt securities market. This problem is related not only to four already mentioned banks. In 2008 ten KASE listed companies defaulted on their bonds (as part of

fourteen Kazakh companies being unable to pay their obligations due to listed debt securities). Among them it was possible to see the representatives of different business sectors, such as fuel producers (Kazneftekhim), IT services (GLOTUR) and logistics (Doszhan Temir Zholy – DTZh, railway operator). These defaults crippled KASE bond market during the financial crisis and still serve as a warning to new potential investors. With regard to the banking sector, both BTA and Alliance Bank were taken under government's control in February 2009 and owing to that action debt restructuring process is underway. It applies also to Astana Finance and Temir Bank. BTA is likely to be sold to Sberbank, a Russian bank partially controlled by authorities.. On the other hand, such banks as Halyk, CenterCredit, ATF Bank and Eurasian Bank went through the crisis exceptionally well and they can be considered as bright spots for the future banking sector development. Anyway, ATF Bank's debt securities are still rated BBB (Fitch). Considerable credit default risk associated with debt securities on KASE ruins the market not only because of risk reluctant foreign institutional investors. Kazakh Pension Fund Programme, which was supposed to bring a vast influx of capital to the shallow market, has no opportunities to invest when accumulating B rated corporate bonds can hardly meet regulator's restrictions. Much safer government's bonds are still exposed to the inflation risk, due to the lack of stability on the domestic money market.

Returning to the market performance overview KASE index recovered by 81% (at the end of 2009), which is apparently a positive indicator, at least until being compared for example with RTS (110% growth in the same time) or PFTS (100% growth). Moscow's and Kiev's markets were hit extremely hard and were broadly considered as the ones of the worst performing in the global crisis. In two year perspective, despite soaring stock prices, the insufficient liquidity will limit the development of KASE. In spite of risk aversion for banking sector, the most attractive assets are still ones listed by fossil fuel producers and raw materials exporters, especially with promising prospects of further exploration of Karachaganak and Kashagan fields. But companies such as ERNC, KazMunayGaz or Kazakhmys will continue to seek for capital in foreign markets, mostly by GDRs listed on London Stock Exchange and ADRs on NYSE. The emerging stock market in Hong-Kong opens new options for financing by equity. Trading volume of Kazakh assets on LSE is currently approx. eight seven times higher than on KASE. Although, KASE might be still treated as an interesting alternative market for some hedge funds willing to achieve extraordinary profits, there are a few examples of successful asset managing companies, founded to operate on KASE, such as Compass Asset Management (part of domestic investment holding – Visor Group which manages Kazakh Compass and TAU Cayman hedge funds), Seven Rivers Capital (South Korean enterprises which launched Hanwha Kazakhstan Fund) or Kazyna Capital Management (which runs CITIC-Kasyna Investment Fund, in cooperation with Chinese investment holding – CITIC Group). Compass Management is currently the most successful one, with assets under management worth more than 200 million USD. As an example Kazakh Compass hedge fund lost 39.7% in 2008 (net annual rate), which is a decent

performance when compared to KASE or RTS index. Since its launch in 2003 until the end of the stock market crisis in April 2009, Compass soared by 42.96%, against all odds. By utilizing a flexible investment strategy, with short positions on one fourth of its portfolio, the fund was able to survive the crisis and in fact it offered one of the best performance among similar investment funds which are in Kazakhstan. In 3-5 year perspective, such an alternative investment managing companies are likely to continue their ventures on KASE, gathering profits from soaring commodity prices, natural resources exploration companies, possibly communications, IT and food producers. But currently raw materials and fossil fuels sectors are probably the only considerable powers, driving this Eurasian financial market. As Atul Patel, the CEO of Compass Management said: "The first wave of the recovery in emerging markets involved the areas investors felt very comfortable with, such as China, India, Brazil and Vietnam – all of which are much more developed than Kazakhstan. They are still concerned about the banking sector, as are we. However, the longer oil stays at \$60-70 per barrel, the more confidence will return<sup>5</sup>".

## Literature

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## **MAKROFUNDAMENTY ROZWOJU RYNKÓW FINANSOWYCH EURAZJI. W JAKI SPOSÓB KRYZYS FINANSOWY WPLYNAŁ NA PERSPEKTYWY ROZWOJU GIEŁDY PAPIERÓW WARTOŚCIOWYCH W KAZACHSTANIE?**

**Strzeszczenie:** Giełda w Kazachstanie aspiruje do roli czołowego rynku finansowego w Eurazji. Ogromne wysiłki zostały podjęte w celu transformacji byłej Republiki ZSRR w kraj, w którym skrzyżują się wpływy i interesy podmiotów z całego świata i gdzie zawierane będą transakcje z wykorzystaniem najbardziej zaawansowanych instrumentów finansowych. Globalny kryzys finansowy przyczynił się do utraty płynności i stabilności cen aktywów na kazachskim rynku finansowym. Problemy te ograniczają zaufanie nie tylko zagranicznych inwestorów, ale i krajowych podmiotów, podczas gdy największe lokalne przedsiębiorstwa w dalszym ciągu chętniej poszukują źródeł kapitału na giełdzie w Londynie niż w Ałmatach. W poniższym artykule przedstawione zostały makrofundamenty, na których opiera się KASE i wynikające z nich mocne i słabe strony tego unikalnego rynku.

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<sup>5</sup> <http://silkroadintelligencer.com/2009/09/03/foreign-investors-remain-sceptical-about-kazakhstan/>