Document of
The World Bank

FOR OFFICIAL USE ONLY

Report No: PGD285

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

PROGRAM DOCUMENT FOR A

PROPOSED LOAN

IN THE AMOUNT OF EUR 345.7 MILLION

(US$400 MILLION EQUIVALENT)

TO THE REPUBLIC OF KAZAKHSTAN

FOR

A Private-Sector-Led and More Sustainable Economic Recovery

DEVELOPMENT POLICY FINANCING

November 10, 2021

Macroeconomics, Trade And Investment Global Practice
Europe And Central Asia Region

Republic of Kazakhstan

GOVERNMENT FISCAL YEAR

January 1 – December 31

CURRENCY EQUIVALENTS

(Exchange Rate Effective as of September 30, 2021)

Kazakh Tenge

EUR 1 = US$ 1.157 = KZT 493.15

ABBREVIATIONS AND ACRONYMS

ADB	Asian Development Bank
AFD	French Development Agency
AFR	Agency for Financial Regulation
ASPR	Agency for Strategic Planning and Reform
CBAM	Carbon Border Adjustment Mechanism
CEM	Country Economic Memorandum
CPF	Country Partnership Framework
DPF	Development Policy Financing
ETS	Emission Trading Scheme
GDP	Gross Domestic Product
GHG	Greenhouse gases
GIZ	Gesellschaft für Internationale Zusammenarbeit
GNP	Gross National Product
GRS	Grievance Redress System
ICT	Information and Communication Technology
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
ISA	International Standards of Auditing
IMF	International Monetary Fund
LDP	Letter of Development Policy
MEGNR	Ministry of Ecology, Geology, and Natural Resources
MNE	Ministry of National Economy
MOF	Ministry of Finance
NBK	National Bank of Kazakhstan
NDC	Nationally Defined Contribution
NDP	National Development Plan
NPL	Nonperforming Loan
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PPL	Public procurement law
RAS	Reimbursable Advisory Service
SER	State energy register
SOE	State-owned enterprise
UNDP	United Nations Development Program
UNFCCC	United Nations Framework Convention on Climate Change
USAID	United States Agency for International Development

Regional Vice President:	Anna M. Bjerde
Country Director:	Tatiana Proskuryakova
Regional Director:	Lalita M. Moorty
Practice Manager:	Sandeep Mahajan
Task Team Leaders:	Ivailo V. Izvorski, Sjamsu Rahardja

REPUBLIC OF KAZAKHSTAN

A PRIVATE-SECTOR-LED AND MORE SUSTAINABLE ECONOMIC RECOVERY

DEVELOPMENT POLICY FINANCING

TABLE OF CONTENTS

This DPF was prepared by an IBRD team led by Ivailo Izvorski (Lead Economist and co-TTL EECM1) and Sjamsu Rahardja (Senior Economist and co-TTL EECM1) and consisting of: Azamat Agaidarov (Economist EECM1), Jane Olga Ebinger (Sector Leader SCADR), Sandeep Kohli (Senior Energy Specialist IECE1), Quamrul Hasan (Lead Procurement Specialist EECRU), Martin Melecky (Lead Economist EECF1), Mariana Iootty De Paiva Dias (Senior Economist EECF1), Juan Navas-Sabater (Lead Digital Development Specialist IDD01), Andrei Busuioc (Senior Financial Management Specialist EECG1), Harald Jedlicka (Senior Private Sector Specialist ETICI), Clara Maghani (ET Consultant EECG1), Alma Nurshaikova (public sector specialist EAEG1), Qing Wang (Senior Environmental Specialist SCAEN), John Bryant Collier (Senior Environmental Specialist SCAEN), Harshit Agrawal (Senior Gas Specialist IEEXI), Husam Mohamed Beides (Lead Energy Specialist, IECE1), Daniel James Besley (Senior Climate Change Specialist SCCAO), Paola Agostini (Lead Natural Resources Management Specialist SCAEN), Jamal Abdulla Abdulaziz (Senior Procurement Specialist EECRU), Nurbek Kurmanaliev (Senior Procurement Specialist EECRU), Kuat Sultan (Consultant KZOWB), Karlis Bauze (Senior Financial Sector Specialist EECF1), Davit Babasyan (Senior Financial Sector Specialist EECF1), Yeraly Beksultan (Senior Private Sector Specialist EECF1), Asset Bizhan (ET Consultant EECF1), Salamat Kussainova (Governance Specialist EECG1), Mikhail Bunchuk (Senior Digital Development Specialist IDD01), Arman Doskaliyev (ET Consultant IDD01), Alifiya Kazieva (Consultant, IDD01), Kanat Kaiyrberli (Country Officer ECCKZ), Yelena Yakovleva (Operations Analyst ECCKZ), Anara Akhmetova (Procurement Assistant ECCKZ), Ayesha Y. Vawda (Lead Education Specialist HECED), Marcelo Bortman (Lead Health Specialist HLCHN), Baktybek Zhumadil (Senior Operations Officer, HECHN), Katerina Levitanskaya (Operations Officer CEUA1), Fernando Blanco (Principal Economist CCER2), Cassandra Colbert (Manager CEUKZ), Aimilios Chatzinikolaou (Senior Strategy Officer CCER2), Patrick Avato (Principal Operations Officer CN2UP), Vadim Shcherbakov (Associate Investment Officer CN2UP), Ivan Shulga (Senior Social Protection Specialist HECSP), Nga Thi Viet Nguyen (Senior Economist EECPV), Will Seitz (Senior Economist EECPV), Metin Nebiler (Economist), Odil Akbarov (Social Development Specialist SCASO), Talimjan Urazov (Senior Agriculture Specialist SCAAG), Aliya Kim (Senior Financial Management Specialist EECG1), Waleed Haider Malik (Senior Public Sector Specialist EECG1), Audrey Sachs (Senior Social Development Specialist SCASO), Daria Goldstein (Lead Counsel), Adeliya Zhunussova (Consultant), Gulmira Akshatyrova (Program Assistant ECCKZ), and Sarah Babirye (Program Assistant EECM1).

The operation was prepared under the overall guidance of Tatiana Proskuryakova (Country Director ECCCA), Lilia Burunciuc (previous Country Director ECCCA), Lalita Moorty (Regional Director EECDR), Sandeep Mahajan (Practice Manager EECM1), and Jean-Francois Marteau (Country Manager ECCKZ).

SUMMARY OF PROPOSED FINANCING AND PROGRAM

BASIC INFORMATION

Project ID	Programmatic
P174367	No

Proposed Development Objective(s)

Support institutional and policy changes for (i) a more competitive economy driven by a more vibrant private sector and accountable public sector and (ii) a more sustainable economic transition.

Organizations

Borrower:	REPUBLIC OF KAZAKHSTAN
Implementing Agency:	MINISTRY OF FINANCE

PROJECT FINANCING DATA (US$, Millions)

SUMMARY

Total Financing	**400.00**

DETAILS

International Bank for Reconstruction and Development (IBRD)	400.00

INSTITUTIONAL DATA

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

Overall Risk Rating

Moderate

Results

Indicator Name	Baseline	Target
Number of investigations on anticompetitive practices that were resolved by issuing a decision.	0 (2020)	5 (2022)
Share of the population using the Internet.	82% (2019)	88% (2022)
Share of electronic commerce in the total volume of retail trade.	1.8% (2019)	3% (2022)
Procurement contracts by value awarded through an open competitive method.	Less than 35% (2020)	More than 50% (2022)
Number of banks which have violated three or more times over the preceding 12-month period any capital adequacy ratios or liquidity coverage ratio.	3 (end 2020)	0 (end 2022)
Annual National Anti-Corruption Report detailing progress of anti-corruption measures both across the public and the quasi-public sector.	Not published with such detailed progress (2020)	Published (2022)
Heat consumption in budgetary organizations.	0.26 GCal/m^2 (2020)	0.24 GCal/m^2 (2022)
Accounts opened to register carbon offset projects in the carbon registry.	0 (2021)	10 (March 2023)
Renewable energy capacity.	1635 MW (Dec 2020)	2400 MW (Dec 2022)
Reduction in flaring volume relative to 2014.	25% (2019)	50% (Dec 2022)
Green technology service operator established and staffed to provide business incubation services.	Not established (Dec 2020)	Established (2022)
Strategic Environmental Assessment initiated for Government programs launched after July 1, 2021.	0 (2020)	10% of all government programs (2022)

IBRD PROGRAM DOCUMENT FOR A PROPOSED LOAN TO THE REPUBLIC OF KAZAKHSTAN

1. INTRODUCTION AND COUNTRY CONTEXT

1. **This proposed standalone Development Policy Financing (DPF) of EUR 345.7 million (US$400 million equivalent) supports the authorities' reform program to deliver a more competitive economy and lay the foundations for a more sustainable economy.** The authorities, keenly aware of the perils of the narrow, energy- and carbon-intensive, and state-led economic structures currently in place, are beginning to tackle these constraints. The COVID-19 crisis has also put these challenges into sharper focus and provided an impetus for reforms. With higher and more inclusive and sustainable growth as the overarching objective, since last year there has been a stronger emphasis on government-wide strategic planning and policy prioritization, coordination, and implementation.[1] This operation builds on these positive developments and responds to the authorities' call for support. The Program Development Objective of this DPF is to support institutional and policy changes for: (i) a more competitive economy driven by a more vibrant private sector and accountable public sector; and (ii) a more sustainable economic transition. The operation is aligned with the authorities' *Kazakhstan 2050* and *Transition to Green Economy 2050* strategies, and the *National Development Plan 2025*. It is also aligned with the World Bank's own Green, Resilient, Inclusive Development (GRID) approach.[2]

2. **The authorities have gone beyond short-term measures and view the crisis as an opportunity to tackle long-standing structural challenges.** In doing so, they are using lessons from the end of the commodity super-cycle five years ago and the COVID-19 pandemic to rethink their development strategy**.** GDP growth rates in Kazakhstan have declined after each downturn.[3] Productivity growth has also fallen steadily over the past two decades, shifting to a contraction since 2010. GDP per capita declined from US$13,891 in 2013 to US$9,056 in 2020. The COVID-19 crisis, aggravated by the disruptions in global value chains and the decline in global demand for oil, reduced Kazakhstan's real GDP by 2.5 percent in 2020, the first year of negative growth since 1998. These weaker outcomes reflect the approaching limits of what an extractive economy, highly dependent on hydrocarbons with little progress toward diversification, can deliver.[4]

3. **The roots of these developments lie in the various structural and institutional bottlenecks that suppress the private sector and the economy's ability to compete globally, while leading to high energy and carbon intensity**.[5,6] The constraints to competitiveness include economic concentration, the dominance by a few large state-owned and state-connected enterprises (SOCEs), unequal application of business regulations, opportunities

---

[1] In late 2020, the Agency for Strategic Planning and Reform (ASPR) was set up directly under the President to provide policy coordination. The Agency, with a former Prime Minister as its head, also serves as the secretariat for the Supreme Council of Reform chaired by the President.
[2] World Bank. April 2021. From COVID-19 Crisis Response to Resilient Recovery: Savings Lives and Livelihood while Supporting Green, Resilient, and Inclusive Development (GRID).
[3] Real GDP growth averaged 10 percent between 2000 and the 2008 global financial crisis, about 6 percent between 2010 and the end of the commodity super-cycle in 2014, and about 4 percent since 2017.
[4] The 2017 Kazakhstan Systematic Country Diagnostic (SCD) and the 2018 Productivity Country Economic Memorandum (CEM).
[5] The World Bank. 2018. Kazakhstan SCD: A New Growth Model for Building a Secure Middle Class. *https://documents.worldbank.org/en/publication/documents-reports/documentdetail/664531525455037169/kazakhstan-systematic-country-diagnostic-a-new-growth-model-for-building-a-secure-middle-class*
[6] The World Bank. 2019. Kazakhstan: Reversing the Productivity Stagnation. *https://documents.worldbank.org/en/publication/documents-reports/documentdetail/615051550479498194/kazakhstan-reversing-productivity-stagnation-country-economic-memorandum*

for corruption, inadequate access to finance, and weak accountability of the institutions of governance. At the same time, the extensive use of hydrocarbon resources that are often underpriced and subsidized has made Kazakhstan the largest per-capita greenhouse gas (GHG) emitter in Europe and Central Asia, the 21st largest globally by overall emissions volume, and the 18th in terms of gas flaring.[7] This has adversely impacted human health through air pollution and contributed to climate change.[8] Kazakhstan needs to accelerate climate change mitigation measures to meet its international commitments to the United Nations Framework Convention on Climate Change (UNFCCC) and implement adaptation measures given its vulnerability to climate change and natural disasters.[9]

4. **Kazakhstan has set ambitious objectives to transform its economy in the coming decades by advancing two transitions.** The first is the transition to a globally competitive market economy that is driven by a vibrant private sector and an accountable and transparent public sector. The expectation is that this will propel Kazakhstan to high-income status and place it among the top 30 most developed countries in the world by 2050. The other transition is for Kazakhstan's economy to become more sustainable and to reach carbon neutrality as committed by the Government by 2060. This transition requires a gradual shift toward a more sustainable, less energy- and hydrocarbon-intensive economy that substantially lowers its GHG emissions. This transition will allow Kazakhstan to meet its long-term environmental and climate goals, while safeguarding its economic and developmental interests.

5. **This DPF lays the foundations for the second transition to a more sustainable economy; Kazakhstan's journey along that road is only just the beginning, and it also has to be managed in tandem with the market economy transition.** More robust market and service delivery institutions, and a more vibrant private sector—supported by this operation—are important prerequisites for any economic transition, a green transition included. Globally, few countries have been transformed into sustainable, inclusive high-income economies without the institutions to manage macroeconomic volatility, ensure a competitive environment for all enterprises, and deliver high-quality education, health, and other public services. And even fewer countries have established such institutions in the presence of large resource rents. The main elements of Kazakhstan's long-term green transition are fleshed out in Box 1.

6. **The opportunity for course correction comes at a time when three major changes at the global, regional, and domestic levels have altered the balance of forces affecting the economy of Kazakhstan and renewed reform momentum.** Global economic prospects have deteriorated for oil exporters given the focus on green transitions worldwide. Regional dynamics have changed with reinvigorated reforms in neighboring Uzbekistan. Until recently, Kazakhstan stood out as the economy of choice for foreign investors in Central Asia; Uzbekistan's reforms are changing this dynamic and motivating a reform push in Kazakhstan. Domestically, the pandemic has increased the premium to having a government that citizens can trust to respond to immediate needs and

---

[7] *https://www.canadianenergycentre.ca/wp-content/uploads/2021/04/CEC-FS-31-Gas-Flaring-2021-FINAL.pdf*

[8] Average annual temperatures in Kazakhstan are projected to rise, with potential warming of 1.5-1.7°C by 2030 and more extreme temperatures. Drought frequency and intensity is likely to increase, contributing to land degradation, desertification, and a higher risk of wildfires. Such temperature rises will also accelerate the melting of Central Asia's glaciers, including those in Kazakhstan, leading to higher flood risk and a longer-term decline in river flow. Increased flooding and mudflows pose threats to transportation, energy, and urban infrastructure. While some cereal producing areas could benefit from a longer growing season and warmer climate, more frequent droughts and reduced water security could damage agricultural productivity and threaten industrial production. Source: https://www.ipcc.ch/report/ar5/wg2/asia/

[9] *Ministry of Energy of the Republic of Kazakhstan, UNDP and GEF "Seventh National Communication and Third Biennial Report of the Republic of Kazakhstan to the UN Framework Convention on Climate Change." (2017).*

facilitate the recovery. These dynamics have renewed the reform momentum reflected in Kazakhstan's new development strategies and economic reform plans (Box 5). A new Agency for Strategic Planning and Reform has been set up directly under the President to coordinate and monitor more boldly on economic change and reform implementation.

7. **This DPF supports Kazakhstan's important steps toward reaching its long-term goals, while recognizing its capacity to play a catalytic role regionally**. Kazakhstan accounts for two-thirds of Central Asia's GDP, is a major export destination and a source of remittances for the rest of the region and, geopolitically, balances close relationships with the Russian Federation, China, and the West. Its success, therefore, is of significant regional importance. The substance of this operation is underpinned by a two-pronged reform agenda:

- **The first pillar supports a decisive shift to a more competitive economy driven by a more vibrant private sector and accountable public sector.** To improve the environment for private sector growth, an independent Agency for Protection and Development of Competition (henceforth, Competition Agency) has been set up to oversee competition policy, reduce explicit and implicit preferences for SOCEs, and otherwise help level the playing field for all enterprises. Reforms are also targeting a more stable and vibrant financial sector. The DPF also supports reforms of procurement by the Government to make it more open to competition, more transparent, and less costly. Given the size of public procurement, these reforms should support a more competitive economy. In addition, the DPF supports strong anti-corruption efforts to enhance the integrity of state institutions.

- **The second pillar of the DPF helps lay the foundation for a more sustainable economic transition.** The Government recently introduced legislative amendments to integrate sustainable development principles into sector policies and programs, improve the operation of its Emission Trading System, promote energy efficiency, and facilitate more investments in renewable energy. The new Environmental Code also translates Nationally Determined Contribution (NDC) commitments into legislation and introduces measures to address climate change vulnerabilities in agriculture, water management, and forestry.

Box 1. Elements of a long-term green transition

Decarbonization of the energy sector will unfold over decades. It will require near-term planning to support a range of reforms and investments across the following areas (this list is illustrative):

- **Building energy efficiency:** deep renovations in existing buildings, or replacement of building stock to align it with global best practice.
- **Revamping industrial technologies and processes** that are competitive in an increasingly decarbonizing global marketplace.
- **Greening of power generation and transport infrastructure:** e.g., mobilizing private investment and innovations in the efficient use of natural gas as transition fuel to green hydrogen; scaling-up and better integrating renewables through storage and load following technologies; and promoting electricity and clean fuels in the transport sector.
- **Transforming coal-dependent heating infrastructure** through new policies, technologies, urban planning, and transparent prices.
- **Addressing institutional and investment gaps** by ensuring a level playing field for all enterprises, a dominant role for the private sector, improved business environment, and an economy much more open to foreign investment outside hydrocarbons.
- **Managing social impacts:** supporting job creation and economic diversification, especially in legacy industrial and mining monotowns, through re-training, new opportunities in sunrise industries, and cleaning

up practices in existing operations of fossil, extractive, and manufacturing sectors. Managing impacts on vulnerable people and communities as market and full cost recovery tariffs are adopted, and externalities are priced into energy use.

8. **The proposed operation is a key part of the World Bank Group's overall engagement in Kazakhstan**. The Bank's Systematic Country Diagnostic (SCD) and the 2020–2025 Country Partnership Framework (CPF) identify the lack of institutional capacity—with many key institutions in need of strengthening—and a poor regulatory framework as key impediments to Kazakhstan's transition to more inclusive and sustainable growth.[10] Although this operation was not originally in the CPF, DPF support was requested by the Government and the operation's support for policy and institutional strengthening is aligned with the CPF and its selectivity criteria (contributing to the inclusion and shared prosperity agenda, improving conditions to attract private investment or mobilize additional resources, helping strengthen key institutions, and contributing to regional or global public goods).

9. **The operation reflects significant inputs from International Finance Corporation (IFC) on the private and financial sectors, and collaboration with other multilateral and bilateral partners.** The Bank has also collaborated closely with the Asian Development Bank (ADB), the International Monetary Fund (IMF), and the French Development Agency (AFD).

10. **The operation has been designed as a standalone to provide maximum flexibility for the policy dialogue, and provide the authorities the space to build capacity and flesh out the medium-term reform framework.** The operation is a standalone, but the Bank's engagement with Kazakhstan is not. The DPF responds to the current window of opportunity for supporting long-standing and increasingly more complex reforms. These reforms are important initial steps but, as discussed in Section 4.2, much further work remains to flesh out the long-term reform program. A programmatic operation, while considered, was not pursued at this stage as it risked a less coherent program. There would also be the possibility of significant changes in the future to the triggers of a potential second operation of a programmatic DPF, given the uncertainty on the actions and difficulty in defining result indicators.

11. **The Bank's engagement is essential, and the risk lies in not supporting the authorities at this stage.** The last DPF in Kazakhstan was in 2015, in the aftermath of the collapse of oil prices. The engagement with the authorities then supported reforms to strengthen the sustainability of the macroeconomic framework and help improve the competitiveness of the non-oil economy.[11] Because of the six-year hiatus in the DPF engagement and the Government's recent reform push that is still taking shape, a standalone operation was considered more appropriate for re-engagement.

[10] Kazakhstan Country Partnership Framework for 2020-2025, Report Number 143372-KZ, which discussed with the Board on December 12, 2019.

[11] The DPF was designed as programmatic and the first operation was approved on November 3, 2015. However, the second operation in the programmatic DPL series did not materialize as initially expected by June 2016 and was cancelled by the World Bank in July 2017. The anti-crisis program implemented by the Government in 2014 and 2015, partly financed from external sources, led to an escalation of Kazakhstan's foreign debt burden. The depreciation of the tenge also contributed to increasing the burden of foreign debt. Total debt rose substantially, the share of foreign debt rose to 50 percent of GDP, and Kazakhstan's sovereign credit rating was downgraded. These developments led the government to rethink its debt policy, toward substituting domestic debt to foreign debt. The whole IBRD pipeline portfolio was impacted by this change, which eventually led to the cancellation of the second DPL. For more details, see http://documents1.worldbank.org/curated/en/348981513176835115/pdf/ICR00004236-2-11292017.pdf.

12. **The next steps of the World Bank's engagement with Kazakhstan will focus on the need for institutional strengthening and improving the regulatory environment, including by supporting the ambitious transition to a greener economy.** The transition to a more competitive economy driven by a more vibrant private sector and accountable public sector will be underpinned by analytical support and policy dialogue on competition policy, public finances, public procurement, and support to the implementation of the Anti-Corruption Strategy. Financial sector development has been actively supported by the Bank and IFC through technical assistance on the market for distressed assets and access to finance for micro, small, and medium enterprises (MSMEs). The Bank has started work on a core diagnostic tool, the Country Climate and Development Report (CCDR) for Kazakhstan, which will help align policy efforts and development strategies, and inform the policy dialogue on subsequent DPFs (Box 1). The Bank is also supporting the strengthening of the Emissions Trading Scheme (ETS) and steps toward a reduction in GHG emissions through other ongoing analytical and advisory support.

Box 2. Kazakhstan's Country Climate and Development Report (CCDR)

The World Bank's Country Climate and Development Report (CCDR) aims to capture the interplay between Kazakhstan's development goals and climate change in the context of the Paris Agreement**.** The CCDR will analyze how Kazakhstan's development goals can be achieved in the context of mitigating and/or adapting to climate change. It is an analytical piece, based on rigorous data analysis and research. The CCDR will also consider and reflect the country's commitments as embedded in their Nationally Determined Contributions (NDC) or longer-term domestic and international commitments and identify ways to support implementation through public and private sector solutions. The CCDR will have the following structure:

- **Part I. Climate and Development.** This chapter assess the climate change issues and the country's development objectives. In doing so, it highlights the risks associated with climate change impacts as well as with the global low-carbon transition. It will also examine the opportunities that arise from building a more climate resilient and low-carbon economy.
- **Part II. Climate commitments, policies, and institutions.** This chapter assesses Kazakhstan's commitments to reduce emissions or build resilience to climate change, as well as the policies and institutional capacities in place to achieve these targets.
- **Part III. Sectoral actions to address climate change.** This chapter assesses the climate policies and investments that should be implemented over the next five years to reduce emissions and improve resilience while advancing the country's development goals.
- **Part IV. Macroeconomic impacts and policies.** This chapter examines the macroeconomic and financial implications of climate change (and action to address climate change) on the country, and the opportunities and risks to economic growth, poverty eradication and shared prosperity, and financial stability.
- **Conclusions and recommendations.**

The CCDR report will take stock of current and planned analytical work and lending initiatives by the World Bank Group and other development partners. It will be developed through dialogue with government counterparts and key economic institutions including the private sector. The themes of low carbon development, climate resilience, and fostering private investments in the green economic transition, are very much in line with the two pillars of this operation. The CCDR is expected to be delivered in mid-2022.

13. **The proposed operation will have a positive, indirect, medium-term impact on economic growth, job creation, citizen welfare, poverty, and environmental sustainability.** Specifically:

- The operation will help create jobs and help reverse the 2020 increase of poverty. A more level playing field for all enterprises, along with deeper financial markets and better broadband access, will facilitate private business entry and development, resulting in more and better-paying jobs over the medium term.

- More competition should help improve the availability of goods and services and moderate price increases, benefiting all citizens, but especially the poor.
- As the NDC commitment is realized, reduced GHG emissions and air pollution will be particularly important for the poor and vulnerable, as they live near industrial sites or in rural areas, have less voice and fewer means to cope with pollution.
- Citizens will benefit from lower cost of mobile broadband, higher speed, and expanded coverage, especially in rural areas.
- The proposed DPF will help reduce the financial burden on the Government and firms through more competitive and transparent public procurement and intensified anti-corruption efforts. On the budget side, this will leave more space for education, health, and social protection. These efforts could also help boost the citizens' confidence in the Government.

14. **The macroeconomic policy framework is adequate for this operation.** This reflects prudent macroeconomic management despite global and domestic economic stresses. The authorities intend to withdraw policy support only gradually to help sustain the recovery from the COVID-19 crisis and to contain long-term scarring. Fiscal policy is disciplined overall and fully aligned with a sustainable public debt profile. Inflation is likely to moderate to near the upper bound of the inflation target range, after one-off shocks that pushed it substantially higher wear off. Monetary policy is prudent, targeting price stability while being appropriately accommodative in the short-run response to the crisis. The exchange rate has become progressively more flexible to allow the economy to adjust better to external shocks.

15. **The overall risk related to this operation is assessed as moderate.**

2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

16. **Solid economic growth during 2017–2019 turned into an economic contraction in 2020 due to the COVID-19 pandemic.** Real GDP growth averaged 4.2 percent a year during 2017–2019, recovering from the substantial slowdown in 2015–2016 caused by the end of the commodity super-cycle. But 2020 was marked by the first economic contraction in Kazakhstan in almost a quarter of a century. Real GDP fell by 2.5 percent following mobility and activity restrictions introduced in March and again in August 2020—some of which continue to this day—and a slump in global commodity demand (Figure 3). The growth decomposition suggests the fall in real GDP growth was largely due to a sharp contraction in total factor productivity and in the labor market. Private consumption dropped due to employment and income losses, and corporate revenues declined in the face of supply disruptions, the drop in demand, and the reduction in income of the oil and gas industry, all against a backdrop of extreme uncertainty. Mobility restrictions and social distancing measures have had an especially strong negative impact on the services sector and less on agriculture and manufacturing. Even though economic activity bottomed out in the third quarter of 2020, and the recovery has continued through mid-2021 with GDP reportedly growing by 2.3 percent in January–June year-on-year, employment, income, and output in 2021 are still below pre-pandemic levels.

17. **The COVID-19 pandemic has had a profound impact on lives, livelihoods, and the economy.** As of

September 13, 2021, there were 842,587 officially registered COVID-19 cases and 10,354 people had lost their lives. The recent resurgence of the COVID-19 virus because of new mutations and a slower-than-planned initial inoculation process resulted in nearly 4,570 new cases a day by August 31, 2021, significantly above the nearly 2,700 cases a day during the peak in May 2021. After enforcing nationwide mobility restrictions during the state of emergency in March to May 2020, the Government has been imposing restrictions in cities and regions where COVID-19 cases grew rapidly. In mid-July, Almaty city, Nur-Sultan, Shymkent, and 13 out of 14 Kazakhstan's regions are in the red-zone category of COVID-19 pandemic.[12]

18. **The authorities have countered the substantial impact of the COVID-19 pandemic with a large and well-targeted fiscal package.** As of October 30, 2021, there were 939,217 officially registered COVID-19 cases and 12,096 people had lost their lives (Figure 1). The Government's stringent containment measures, while necessary, affected employment and economic activity, with an adverse impact on government finances, household incomes, and firm and bank balance sheets. Reduced employment and lower earning, particularly for those in the bottom 40 percent, increased the poverty rate from a pre-crisis projection of 8.4 percent to 14 percent in 2020 (Figure 2).[13] Unemployment, firm closures, setbacks in education and health, and widening regional disparities have produced lasting scarring effects, with long-term impacts on output and welfare. The government fiscal package included increased outlays on social protection, health, and education, and was supplemented by robust provision of liquidity by the central bank. The post-crisis recovery will depend on preventing more COVID-19 waves from emerging, accelerating the pace of vaccination, leveraging the global economic turnaround, and vigorously implementing structural reforms, many of them supported by this operation.

19. **In February 2021, the Government launched a national vaccination program against the COVID-19 virus and has set an ambitious target of having 53 percent of the population vaccinated by end of September 2021.**[14] The pace of vaccination was slow initially but is now gaining pace, with about 43 percent of the population inoculated with at least one dose by October 25, 2021 (and 38.5 percent fully vaccinated).[15] Nevertheless, vaccine hesitancy among the population and the misuse of vaccination passports present an obstacle to fully achieving the September target.[16] The slower vaccination campaign presents a risk to the recovery in employment and output and may require additional government support to households and firms.

[12] The Government uses the following zone classification for COVID-19 cases: red zone if more than 50 cases per 100,000 population and R (the reproduction number for SARS-CoV-2) greater than one; yellow zone if cases are between 25 and 50 cases per 100,000 population and R greater than one; green zone is for cases less than 50 per 100,000 population and R is less than one.

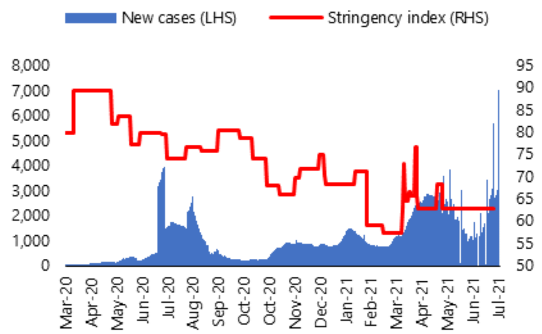
[13] Using the upper-MIC poverty line, resulting in as many as 1.5 million additional poor.

[14] Mainly using the Sputnik V vaccine, a domestically produced vaccine, QazVac, China's Sinovac, and Hayat-Vax produced in UAE with the Chinese Sinopharm technology. All require two doses of vaccination.

[15] The authorities reported on August 6 that 50.2 percent of their target group (ages 18–64, or 60 percent of the population) has already received one dose and 37.4 percent have received two doses of the vaccine.

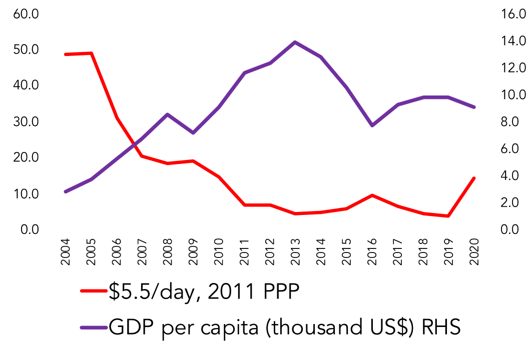
[16] "Kazakhstan is Awash in Fake Vaccinations Passports: Corruption Helps Spread Covid-19" *The Economist*. July 24th, 2021 edition.

Figure 1. COVID-19 cases and stringency of restrictions
(number of people and index)



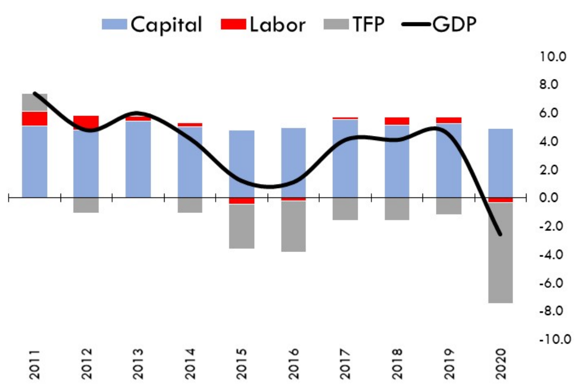
Source: Our World in Data.

Figure 2. GDP per capita and poverty rate
(US$ ’000 and in US$ per day)



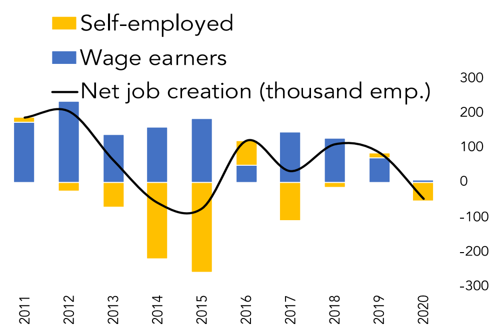
Sources: WBG estimates; Bureau of National Statistics.

Figure 3. Decomposition of real GDP growth
(percentage points, percent)



Sources: Staff calculations based on data from the Bureau of National Statistics.

Figure 4. Net job creation by occupation
(’000)



Sources: Bureau of National Statistics.

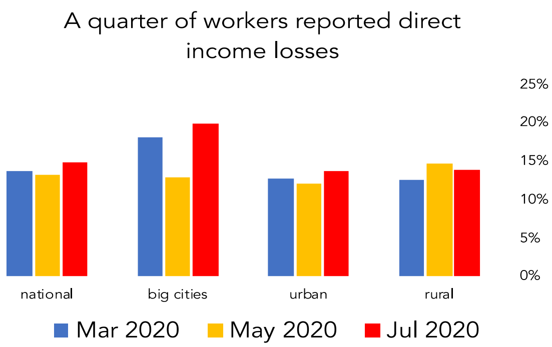
20. **The COVID-19 pandemic has resulted in a substantial loss of jobs.** According to official statistics, job losses were absorbed largely by the self-employed and mainly those in agriculture (largely from disruptions to value chains) and services; there were no officially reported job gains among the formal salaried employees (Figure 4). During 2016–2019, by contrast, officially reported job gains amounted to about 87,000 a year. One-quarter of respondents to a recent survey reported job losses in mid-2020, and the number of online job adverts in December 2020 was about 50 percent below the year earlier levels (Figures 5 and 6).

21. **Kazakhstan’s reliance on hydrocarbons and limited diversification continue to influence growth.** Oil accounts for about 21 percent of Kazakhstan’s GDP and 70 percent of exports. Similar to the end of the commodity super-cycle in 2014–2015, a 33 percent fall in the average oil price and 5.5 percent drop in oil

production in 2020 caused Kazakhstan's goods exports to drop by 18.7 percent.[17] Such a drop caused the oil sector to contract by 5.4 percent and amplified the overall impact of the COVID-19 crisis on growth in 2020.

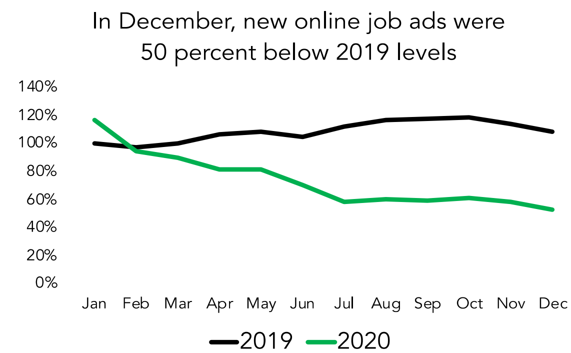
22. **Higher increases in food prices and the pass-through from exchange rate depreciation pushed inflation above the central bank's 4 to 6 percent target range.** Twelve-month inflation rose from 5.4 percent in December 2019 to 7.5 percent by December 2020 and to 8.9 percent by September 2021 (Figure 7). Food prices, which grew by 11.5 percent in September 2021 YoY, contributed the most to the jump in inflation. Nonfood goods inflation has also picked up since mid-2020, reflecting the earlier depreciation of the exchange rate and the pandemic's impact on supply chains. At the start of the pandemic, as oil prices fell sharply, the National Bank of Kazakhstan (NBK) hiked its key policy rate by 275 bp to 12 percent, concerned about the impact of the crisis on the currency and the feedback into inflation. The central bank also stepped up its efforts to mitigate the negative impact of external factors on the domestic exchange market in 2020. As the exchange rate stabilized, the NBK cut its policy rate to 9 percent by July 2020 and held it steady through June 2021. In September and October, the NBK increased its policy rate by a cumulative 50 bp to 9.75 percent to contain rising inflation.

Figure 5. Workers reporting income losses
(Percent of total)



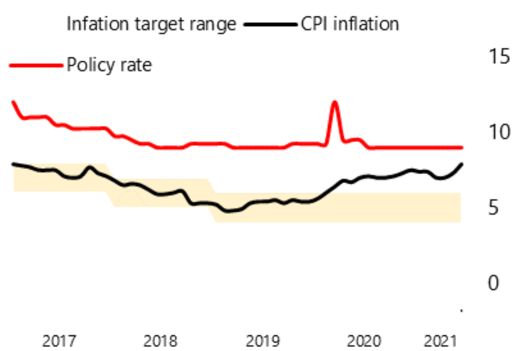
Source: Listening to the Citizens of Kazakhstan.

Figure 6. New online jobs adverts
(Index, January 2019=100)



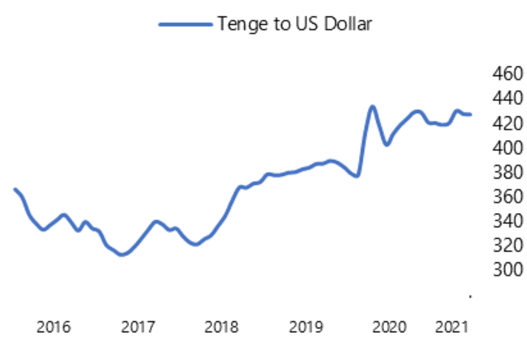
Source: robotanur.kz

Figure 7. Consumer price inflation
(YoY percent)



Sources: Bureau of National Statistics.

Figure 8. Exchange rate of the tenge
(Tenge per US dollar)



Source: NBK.

[17] Based on balance of payment data published by the National Bank of Kazakhstan.

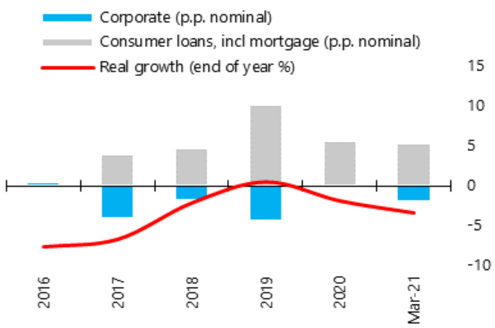
23. **A large drop in profit repatriations to foreign investors and a reduction in imports more than offset a collapse in exports to reduce the current account deficit to 3.8 percent of GDP in 2020.** Imports fell because of reduced private consumption and investment but their decline was limited by the spillovers from the large fiscal expansion. The current account deficit narrowed in the first half of 2021, although the dynamics of its components were different. Profit repatriations in the first half of 2021 rose substantially and so did imports, the latter owing to the recovery of domestic consumption and the continued fiscal stimulus measures. Exports also picked up markedly after the precipitous fall in international demand for oil in early 2020, but remained below pre-pandemic levels. Gross foreign exchange reserves remained comfortable at US$36.8 billion in August 2021, equivalent to more than nine months of imports and about 278 percent of short-term external debt. External debt amounted to about 95 percent of GDP because of intercompany loans to the foreign-owned oil companies in Kazakhstan from their foreign parents. Excluding these loans, external debt amounted to 37.8 percent of GDP at the end of March 2021, of which about 10.5 percentage points was accounted for by public debt and guarantees. (Eurobonds and bonds issued on the Russian market accounted for about one-half of external government debt; the rest are obligations to multilateral and bilateral lenders.) Rollover risks are modest and easily manageable. External debt of SOEs accounted for 10.9 percent of GDP in 2020 compared with 15 percent in 2017.[18]

24. **Lower oil prices pushed down the value of the tenge.** From January to April 2020, as the early stages of the COVID-19-induced restrictions, the currency fell by 17 percent against the US dollar. As economic activity and international oil prices began to pick up, the currency regained one-third of its earlier losses, also supported by exchange market interventions by the central bank. The tenge ended December 2020 about 10 percent weaker against the US dollar than a year earlier and remained little changed during the first half of 2021 (Figure 8). In 2020, the NBK spent US$1.9 billion to support the tenge, more than in 2017–2019 combined; the largest intervention was in March 2020, amounting to about US$1.5 billion. Transfers from the US$58.7 billion National Fund to the government budget in 2020 also supported the currency, because the foreign currency assets of the fund are converted into tenge during the transfer.

25. **The banking system has weathered the crisis relatively well thus far.** This was thanks to the state support to firms and individual borrowers since the start of the pandemic, and improved balance sheets after a series of bailouts in previous years combined with the authorities' efforts following up on the 2019 Asset Quality Review. Nonetheless, financial intermediation has stalled. While retail credit remained robust, increasing by 35.6 percent for mortgages YoY in June 2021 and 19.4 percent for consumer loans, corporate credit growth was still weak (Figure 9).[19] Deposit dollarization has declined substantially since 2015, indicating the recovery of confidence in the currency lost during the larger depreciation in 2014–2015 (Figure 10). Nonperforming loans (NPLs) are officially reported to have decreased to 4.8 percent of the loan portfolio in June 2021 from 6.9 percent in December 2020. Government support measures, such as loan guarantees, subsidized loans, and regulatory forbearance, helped avoid substantial corporate insolvencies during the lockdown. However, the still unresolved legacy NPLs and new NPLs due to the COVID-19 crisis are a substantial burden on the financial system and have increased the risk aversion of banks in lending to firms, notably SMEs without other access to financing.

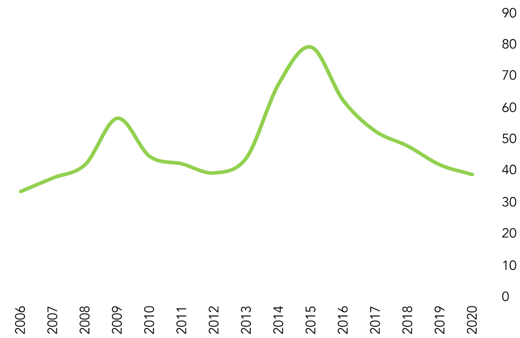
[18] External debt of SOEs under two large holding companies Samruk-Kazyna and Baiterek (which includes KazAgro).
[19] Mortgage here includes home construction loans.

Figure 9. Credit growth
(percent change, YoY)



Sources: NBK and World Bank staff calculations.

Figure 10. Dollarization of bank deposits
(percent of total)



Sources: NBK and World Bank staff calculations.

26. **The authorities responded swiftly and with force to mitigate the fallout from the COVID-19 pandemic.** The Government implemented a fiscal stimulus package worth US$15 billion, or 9.0 percent of GDP, that included additional spending on health, tax, and social contribution deferrals for SMEs, and cash transfers to households (Box 3). The Government raised education spending by 1.1 percent of GDP to facilitate remote learning and upgrade the digital infrastructure for education.[20] Income support was provided for workers affected by the State of Emergency, and to the poor and vulnerable households. In addition, the central bank has injected liquidity amounting to about US$1.9 billion and provided subsidized loans to firms through the commercial banks, thereby helping limit the reduction of credit growth and prevent a larger decline in economic activity.

Box 3. Kazakhstan's Fiscal Anti-COVID-19 Package

Protecting lives

- Purchased additional health equipment, allowed citizens to access regular health services under the mandatory social health insurance (MSHI). Temporary deferred payment of health insurance contributions.
- Provided bonus payments to medical personnel engaged in emergency responses.

Supporting livelihoods

- Provided cash-transfer to about 3 million people who have lost their jobs during the State of Emergency period (the equivalent of US$95 per person per month).
- Adjusted the social benefit payments for higher cost of living and provided food and household kit for about 1 million low-income households and people with disabilities.
- Fixed the costs of local internet for households and reduced utility bills during the period of the State of Emergency, and provided subsidies for utility bills for socially vulnerable families.

Employment creation program

- Introduced an employment program on maintenance work of infrastructure facilities and scaled up public housing program.
- Increased subsidies for concessional lending for SMEs and working capital.

Supporting businesses

- Extended due date for all taxes paid by SMEs and eliminated all related fees for the delay. Reduced the VAT rate for SMEs operating in agro- and food- processing industries and suspended custom duties for imports of essential goods during the state emergency period.
- Suspended property tax for one year for SMEs in the service industry and temporarily suspended the rental payments owed by SMEs to local governments and SOEs for renting their properties.

[20] Based on data published by Ministry of Finance.

Source: Ministry of National Economy.

27. **As a result of the fiscal stimulus package and the economic contraction, the consolidated budget deficit is estimated to have widened to 7.1 percent of GDP in 2020 from 0.6 percent in 2019.** The non-oil deficit (the deficit excluding oil-related revenues) rose to 10.6 percent of GDP, substantially above the Government's 6 percent medium-term target. The Government financed the 2020 budget deficit by stepped up borrowing from domestic capital markets and issuances of international bonds in Russian rubles. Government debt rose by almost 5 percentage points to nearly 25 percent of GDP in 2020. Even with this increase, debt is moderate and sustainable. The increased transfers to the state budget reduced the value of the foreign exchange assets of the National Fund of the Republic of Kazakhstan (NFRK) to US$58.7 billion in 2020 from US$61.8 billion in 2019. The fund was established in 2000 as a savings and stabilization fund, and accumulates assets from oil revenues besides export duties and investment returns from its assets.

Box 4. The National Fund of the Republic of Kazakhstan

The National Fund of the Republic of Kazakhstan (NFRK), established in 2000, is a sovereign wealth fund that is integrated into the general government budget. The NFRK accumulates tax and royalty revenues from the oil sector, proceeds from privatization in the oil sector, proceeds from the sale of agriculture land by the Government, and investment income from its assets. Excise taxes on oil exports, by contrast, go directly into the government budget. As a stabilization fund, the NFRK helps stabilize the fiscal position across the economic cycle and helps reduce volatility from revenue inflows. As a saving fund, it distributes the oil windfall across generations.

The use of the NFRK—exclusively through the government budget—is approved by the President based on inputs from the NFRK Management Council. The National Bank of Kazakhstan manages NFRK's assets in line with the Fund's strategy. Since 2016, the NFRK is prohibited from investing in domestic securities issued by the Government and from financing extrabudgetary activities. The decree "On the Concept for the Formation and Use of the Funds of the National Fund of the Republic of Kazakhstan" (2016) set the rule that the assets of the NFRK should not fall below 30 percent of GDP. Between 2016 to 2020, the return on NFRK assets averaged about 4.1 percent a year (average yield on 10-year US government bonds amounted to 2.02 percent), compared with 3.0 percent a year average between 2005 to 2015 (US 10-year government bond average yield of 3.2 percent).

As part of its stabilization function, each year the NFRK transfers a predetermined amount to the budget ("guaranteed" transfer). The guaranteed transfer is periodically reviewed by the NFRK Management Council. In 2016, the Government adopted a new framework that envisages a gradual reduction of the annual guaranteed transfer to KZT 2 trillion (about US$ 4.8 billion) a year by 2020. In addition to the guaranteed transfer, the President can authorize an additional transfer ("targeted" transfer) to the government budget. The discretionary transfers provide flexibility to the use of the NFRK assets but at the cost of uncertainty to the fiscal stance.

The NFRK is an integral part of both the country's fiscal framework and the country's economic structure, namely, the dependence on hydrocarbons. As a result, the main risks to the NFRK stem from the future prospects for diversification of the economy, the level of oil prices, exports, and revenues, and changes to the fiscal framework that the authorities will be introducing based on the speeches of the President in 2019 and 2020. While in the near term a pickup in global demand for oil and higher oil prices bodes well for the NFRK, global and national efforts toward decarbonization will have a negative long-term impact on the Fund.

Table 1. Kazakhstan: Key Macroeconomic Indicators, 2018–2023

	2018	2019	2020	2021f	2022f	2023f
National income and prices	(Percent of GDP unless otherwise indicated)					
Real GDP growth	4.1	4.5	-2.5	3.5	3.7	4.8
Oil sector growth	8.6	5	-5.4	-0.4	1.2	9.5
Non-oil sector growth	3	4.4	-1.7	4.5	4.4	4.0
CPI inflation (end of period)	5.3	5.4	7.5	7.7	6.0	5.6
External accounts	(Percent of GDP unless otherwise indicated)					
Current account balance	-0.1	-4.0	-3.8	-2.4	-1.2	-0.3
Exports of goods and services	37.4	36.3	30.6	38.2	35.6	35.2
Oil exports	21.1	18.5	13.9	18.4	17.3	18.0
Imports of goods and services	-25.8	-28.3	-26.4	-34.4	-32.1	-31.0
Foreign direct investment, net	2.6	3.0	3.5	3.4	3.3	3.3
NRFK assets, end-period	32.3	33.4	32.9	31.5	31.5	31.1
NBK reserves (US$ billion, end-period)	30.9	29.0	35.6	...	...	...
Total external debt	89.1	87.6	95.9	90.5	78.4	71.8
Debt service ratio (% exports of GNFS)	34.1	32.7	34.4	29.3	27.5	25.7
Monetary accounts	(In percent, y-o-y growth rate)					
Reserve money growth	20.1	3.6	41.8	9.2	5.8	6.6
Policy rate, year-end (in %)	9.3	9.3	9.0	…	…	…
Consolidated fiscal accounts */	(In percent of GDP unless otherwise indicated)					
Revenues	21.4	19.7	17.6	19.3	19.7	19.4
Expenditures	18.9	20.3	24.7	24.0	21.7	20.9
Consolidated budget balance	2.5	-0.6	-7.1	-4.7	-2.0	-1.5
Public Debt **/	(In percent of GDP unless otherwise indicated)					
Government debt	19.9	19.6	24.6	26.7	29.4	30.1
External	6.4	6.8	8.2	11.9	13.0	13.4
Domestic	13.5	12.8	16.4	14.9	16.3	16.7
Government debt service (% of state revenues)	8.4	10.6	12.5	14.8	15.5	18.5
Memoranda						
Nominal GDP (US$ billion)	179.3	181.7	171.2	181.4	196.3	216.2
Nominal GDP per capita (US$ ’000)	9.8	9.8	9.1	10.3	11.2	11.9

Sources: Government and NBK data and WBK staff estimates and projections. f=forecast.
Note: */ The consolidated budget comprises the state and local governments, and the National Fund of the Republic of Kazakhstan.
***/* Includes only the debt of the state and local government and government guarantees. It does not include SOE debt.

Table 2. Kazakhstan: Consolidated Government Fiscal Accounts, 2018–2023 */

(percent of GDP)

	2018	2019	2020	2021f	2022f	2023f
Revenues	**21.4**	**19.7**	**17.6**	**19.3**	**19.7**	**19.4**
Oil revenue	7.4	6.9	3.4	6.2	6.2	6.1
Non-oil revenue	14	12.8	14.2	13.1	13.5	13.3
Expenditures	**18.9**	**20.3**	**24.7**	**24.0**	**21.7**	**20.9**
Current spending	15.7	17	20.6	20	18.2	17.5
Wage bill	2.7	2.9	3.7	3.7	3.3	3.3
Goods and services	5.1	5.7	7.7	7.0	6.7	5.9
Interest payments	0.7	0.8	1.1	1.1	1.2	1.3
Subsidies, transfers, others	7.2	7.6	8.1	8	7	7
Capital spending and net lending	3.2	3.3	4.1	4.2	3.5	3.4
Consolidated budget balance*	**2.5**	**-0.6**	**-7.1**	**-4.7**	**-2.0**	**-1.5**
Non-oil fiscal balance	-4.9	-7.5	-10.5	-10.9	-8.2	-7.6
Gross financing needs **/	3.6	3.0	6.4	4.1	6.6	5.8
A. External borrowing (net)	2.0	0.2	-0.1	1.4	2.2	1.7
Disbursements	2.2	0.7	0.4	1.6	2.7	2.5
Amortization	0.2	0.5	0.5	0.3	0.5	0.8
B. Domestic borrowing (net)	0.8	1.7	5.4	1.2	2.7	2.1
Disbursements	1.4	2.3	6.0	2.1	3.8	3.3
Amortization	0.6	0.6	0.6	1.2	1.1	1.2
C. NFRK ***/	-5.3	-1.3	1.8	2.1	-3.0	-2.2

Sources: Government data, IMF, and WBG staff estimates and projections. f=forecast
Notes: */ The consolidated budget comprises the state and local governments, and the National Fund of the Republic of Kazakhstan. The financing of the consolidated budget is the sum of A, B, and C.
**/ Gross financing needs is equal to the sum of the deficit, plus amortization on external and domestic debt, minus financing from the NFRK.
***/ Change in the assets of the Fund, including from valuation changes (below the line). The overall oil-related revenues of the National Fund and the state budget are part of revenues (above the line).

Table 3. Detailed Consolidated Gross Financing Needs and Sources, 2020–2021

(US$ billion, and percent of GDP)

	US$ billion		Percent of GDP	
	2020	2021f	2020	2021f
Financing of the consolidated fiscal deficit */	**12.1**	**8.5**	**7.1**	**4.7**
A. External borrowing (net)	-0.2	2.4	-0.1	1.4
Disbursements, of which	0.7	2.9	0.4	1.6
ADB		1.1		0.6
AIIB		0.7		0.4
WBG		0.4		0.2
Russian market and others	0.7	0.7	0.4	0.4
Amortization	0.9	0.5	0.5	0.3
B. Domestic borrowing (net)	9.2	2.0	5.4	1.2
Disbursements, of which	10.2	3.6	6.0	2.1
Pension Fund	4.8	0.5	2.8	0.3
Commercial banks and market participants	5.4	3.1	3.2	1.8
Amortization	1.0	1.6	0.6	1.2
C. NFRK **/	3.1	3.8	1.8	2.1
Gross financing needs */**	**10.9**	**6.8**	**6.4**	**4.1**

Sources: Government data and WBG staff estimates and projections. f=forecast
*/ The financing of the consolidated deficit is the sum of net external borrowing (A), net domestic borrowing (B), and the National Fund of the Republic of Kazakhstan (C).
**/ Change in the assets of the Fund, including from valuation changes (below the line). The overall oil-related revenues of the National Fund and the state budget are part of revenues (above the line).
***/ Gross financing needs is equal to the sum of the deficit, plus amortization on external and domestic debt, minus financing from the NFRK.

Table 4. Kazakhstan's External Debt, 2020–2021Q1

(US$ billion, percent of total, and percent of GDP)

	US$ billion		Percent of total		Percent of GDP	
	2020	**2021 /1**	**2020**	**2021 /1**	**2020**	**2021f /1**
Total external debt	164.2	164.1	100.0	100.0	95.9	90.5
By borrower:						
Monetary authorities	1.3	1.8	0.8	1.1	0.8	1.0
General government	13.9	14.5	8.5	8.8	8.1	8.0
Banks	4.8	5.0	2.9	3.0	2.8	2.7
Other sectors	144.1	142.8	87.8	87.0	84.2	78.8
of which intercompany lending	102.2	100.7	61.0	61.4	58.5	55.5
By maturity:						
Short-term	10.0	11.3	6.1	6.9	5.8	6.2
Long-term	154.2	152.8	93.9	93.1	90.0	84.3

Source: NBK and WBG staff projections. f=forecast

Table 5. Balance of Payments Financing Requirements and Sources, 2017–2023
(US$ billion)

	2018	2019	2020	2021f	2022f	2023f
Financing requirements	22.3	33.3	23.2	26.3	22.4	21.5
Current account deficit	0.1	7.3	6.5	4.9	2.8	0.8
External debt amortization	20.7	19.5	15.9	19.4	18.1	19.6
Gross reserve accumulation	1.5	6.5	0.9	2	1.5	1.1
Financing sources	22.3	33.3	23.3	26.3	22.4	21.5
FDI (net)	4.7	5.5	6.1	6.1	6.4	7.1
External debt disbursements	21.3	19.8	17.1	20.3	19.4	21.6
Other capital (net)	-3.7	7.9	0.1	-0.1	-3.4	-7.3

Sources: NBK and WBG staff estimates and projections. f=forecast

2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

28. **After the decline due to COVID-19 in 2020, the economy is rebounding in 2021.** The rebound is supported by the resumption of domestic activity, positive spillovers from stronger global demand (including for oil), continued fiscal support measures, easing of mobility restrictions, and the implementation of the national vaccination campaign. The economy is likely to grow by 3.5 percent in 2021, but with considerable uncertainty around this baseline projection. Private consumption is forecast to pick up, driven by continued social protection and unemployment programs and the release of pent-up demand, as employment and incomes recover. Higher demand for housing is expected to support residential investment, as the government program will allow pensioners to use their savings to purchase a home or pay down mortgages. On the supply side, manufacturing and construction—which continued to grow in 2020 because of government support—will pick up further as domestic demand, including for housing, rebounds. Mining, notably oil extraction, is projected to recover in the second half of 2021 after a slump in the first, leaving output little changed for the full year. The easing of mobility restrictions and the vaccination campaign should provide renewed impetus to the services sector after a difficult year in 2020.

29. **Even with the projected resumption of growth in 2021, the recovery of real output to pre-pandemic projections will take time.** Real GDP both in 2021 and 2022 is likely to be about 7 percent lower than the path projected pre-pandemic. In 2023, the expected completion of an expansion of the giant oil field Tengiz will boost production capacity by about 10 percent and raise overall real GDP growth. A more broad-based and sustainable recovery will depend on the progress in advancing reforms to remove the structural impediments to economic development. Kazakhstan's economy is dominated by large SOEs and connected enterprises, limiting the vibrancy of private sector activities outside oil and gas, and undermining the overall efficiency of resource allocation. SOEs contributed about 19 percent of total gross value-added of the economy in 2015.[21] Total debt of large SOEs holdings (Samruk-Kazyna, Baiterek, and KazAgro) amounted to 23.6 percent of GDP in 2020, compared with 28 percent of GDP in 2016. The playing field is tilted in favor of the SOCEs and against private firms that lack connections, with the former granted better access to resources, markets, credit, and licenses. Furthermore, distortionary state lending programs support non-viable firms and obstruct efficient capital reallocation, the

[21] OECD. 2016. Multi-Dimensional Review of Kazakhstan: Volume 1. Initial Assessment.

entry of new firms, and the exit of unproductive ones. Distortions in the land market also hinder expansion of productive activities in agriculture and mining. Hydrocarbons remain the mainstay of the economy, dominating exports and production outside services. The economy has diversified little outside hydrocarbons over the past two decades, with large resource rents squeezing other productive activities.

30. **Inflation is likely to remain above the upper limit of the 6 percent central bank inflation target range in 2021.** Food price inflation—the main driver of rising overall inflation—is projected to remain elevated because of rising international food prices, despite supply disruptions tapering out and precautionary food purchases by households easing. Due to a strong rebound in domestic economic activities and imported inflation, mainly from the Russian Federation, which supplies 37 percent of Kazakhstan's imports, non-food inflation is also expected to rise. Nevertheless, the upward adjustment of the policy rate by NBK suggests that the monetary policy will remain guided by the NBK's commitment to inflation targeting and its free-floating exchange rate.

31. **The current account deficit is projected to narrow, supported by higher oil prices and a rebound in demand abroad.** Kazakhstan's oil exports are expected to pick up on the back of higher world demand and the increased OPEC Plus production quota and from expansion of the Tengiz oil field. The increase in exports will more than offset the rise in imports driven by the pick-up in domestic demand and the higher demand for foreign machinery and foreign business and professional services by the FDI firms. Foreign exchange reserves are projected to pick up modestly in US dollar terms but remain broadly unchanged at about 8–8.5 months of imports of goods and services. Risks remain, however, about the sustainability of higher oil demand and higher oil prices. Should the oil price fall US$5/barrel below the projected level, Kazakhstan's export revenues will be substantially affected, widening the current account deficit this year and next year by 0.6–1.1 percent of GDP above the baseline projections.

32. **The Government is planning to withdraw its fiscal stimulus only gradually.** With the pandemic not easing as fast as expected, the authorities introduced a supplementary budget in April 2021 that will boost spending by nearly 1.7 percent of GDP in 2021. As a result, the consolidated fiscal deficit is likely to ease to only about 4.8 percent of GDP in 2021 from 7.1 percent in 2020. The 2021 budget assumes further increases in spending on social assistance, health, and infrastructure. To finance the deficit, the authorities intend to increase borrowing from multilateral lenders (the WB, the ADB, the AIIB, and the AFD), and maintain issuance of Russian ruble-denominated bonds on the Russian market. Financing from the National Fund of Republic of Kazakhstan (NFRK) is helping reduce borrowing. In addition, transfers from the Fund to the state budget amounted to 6.7 percent of GDP in 2020 and are planned at about 6 percent of GDP in 2021. They count as revenues in the state budget and are part of overall oil revenues in the consolidated budget. Without these transfers, the deficit of the state budget would be much larger. The non-oil fiscal deficit is projected to increase to 10.9 percent of GDP. From 2023, the Government intends to amend its main fiscal rule to improve the counter-cyclical stance of fiscal policy and increase savings in good times to rebuild the assets of the NFRK.

33. **Kazakhstan's public debt is low and sustainable.** Public debt, which in this document includes general government debt and guarantees but does not include SOE debt, is projected to reach almost 27 percent of GDP in 2021; about 55 percent of it is denominated in domestic currency, which helps moderate foreign exchange rate risks (Figure 11 and Figure 12). Public debt is projected to increase further through 2023 as the authorities withdraw the fiscal support to the economy only gradually. Overall, from 2019 to 2023, public debt is projected to increase by nearly 10.5 percent of GDP; this post-COVID-19 path compared with little change in public debt from 2019 to 2023 projected before the COVID-19 pandemic. Rollover risks for public external debt are largely

mitigated by the sizable assets of the National Fund of the Republic of Kazakhstan, which are projected to remain above 30 percent of GDP, and the central bank's foreign exchange reserves equivalent to 20.3 percent of GDP. Gross financing needs are projected to moderate from 6.4 percent in 2020 to 4.1 percent in 2021 before rising to 6.6 percent by 2023 under the assumption that the authorities will reduce drawdowns from the NFRK to help rebuild its assets. Given the importance of hydrocarbons for the economy, a drop in oil prices may result in slower growth, exchange rate pressures, and widening of the budget deficit. Under this scenario, results from individual stress tests and the associated combined shocks indicate that public debt remains sustainable (Figure 13).[22]

34. **The Ministry of Finance regularly publishes detailed data on public debt and guarantees, including a breakdown by creditors.** The large SOEs and the two SOE conglomerates—Samruk Kazyna and Baiterek—also report their domestic and external debts in their financial statements. The central bank publishes regular and detailed data on external debt, including the maturity, interest-rate, and creditor structure. Kazakhstan is current on its debt reporting to the Bank. One gap is the lack of an explicit government debt management strategy in place; liability operations, including borrowing, are being done discretionally. The World Bank debt team has long collaborated with the State Borrowing Department at the Ministry of Finance (MoF) on debt management, and advised the Government to prioritize the development and publication of a debt management strategy. Following the Bank's recommendations in several pieces of analytical work undertaken with the MoF, the President instructed the Government to develop a strategy in his annual address in September 2020. Currently, the ministries of economy and finance and other stakeholders are working on the development of a new concept of fiscal policy, to include a debt management strategy.

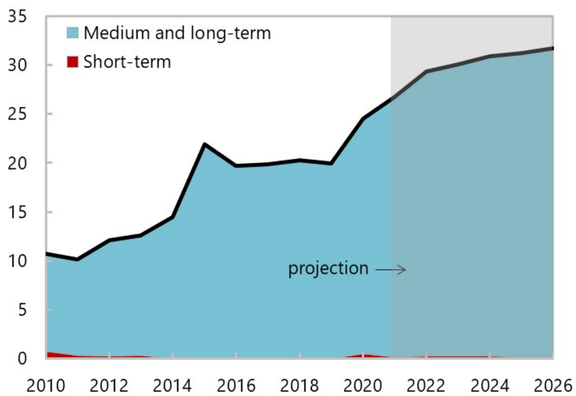
35. **The outlook is subject to downside risks, and the economic recovery could lose momentum because of both domestic and external developments.** Should COVID-19 cases continue to rise, the authorities may tighten the restriction measures and that will hamper the recovery of activity. The authorities' ambitious goal of inoculating 53 percent of the population by the end of September will be met only with a delay, given that 38 percent of the population was fully vaccinated by mid-September. Global uncertainties also remain, and weaker-than-expected increases in foreign demand for Kazakhstan's exports, especially oil, could also dent the growth outlook, as could renewed commodity price volatility. Under a downside scenario where these risks materialize, with oil prices about US$5/barrel lower than in the baseline scenario, output growth could amount to 2–2.4 percent in 2021 and 2.7–3 percent in 2022. Potential new supply disruptions may limit the slowdown in inflation and may prompt more tightening of monetary policy despite the slower growth. The fiscal deficit may be higher than under the baseline scenario, as the authorities further step up support to households and firms. This would put government debt on a higher—but still sustainable—trajectory. Risks to the economy from continued substantial reliance on hydrocarbons and limited diversification are sizable; growth potential will be substantially constrained and the economy's integration into regional and global value chains—essential for its transition to high–income status—will be hampered. Achieving a more diversified economy less dependent on hydrocarbons is a longer-term process that will require substantial structural reforms, as supported by this operation.

36. **The macroeconomic policy framework is adequate for this operation, reflecting prudent economic management despite weaknesses in global and domestic economic conditions.** After the 2020 contraction, the economy is likely to grow by 3.5 percent in 2021, thanks to a robust recovery in private consumption, investment, and net exports. The government budget will prudently support the recovery, reducing the fiscal deficit only

[22] The stress tests are: one standard deviation correction of GDP growth from the baseline for two consecutive years; a one-time 115 percent decline in nominal exchange rate; one-half standard deviation correction of primary balance from the baseline; and four percent increase in interest rate compared to baseline. The combined shocks incorporate the largest effect of the individual shocks.

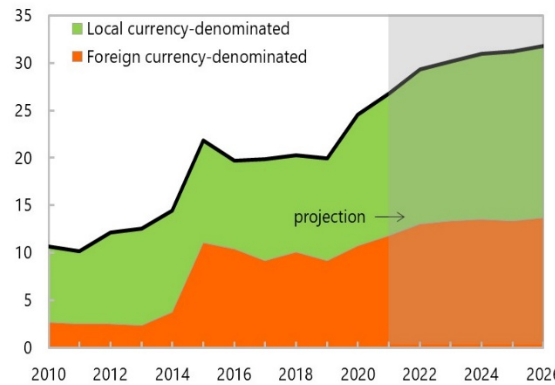
gradually in 2021 and beyond, avoiding a premature withdrawal of fiscal support. Government debt is likely to remain low and sustainable. Nonetheless, there are likely to be spending pressures on the budget over the medium term as the authorities transition from the current resource- and energy-intensive growth model to a more inclusive and greener one. Stepped-up social protection, increased expenditures on education and infrastructure, among others, are also part of the Government's strategic priorities that will have substantial fiscal implications. These pressures will need to be countered with stronger efforts on domestic revenue mobilization, expenditure prioritization, and debt management. After one-off shocks from supply chain disruptions and higher increases in food prices, inflation is set to moderate toward the upper bound of the central bank's inflation target range. The NBK targets inflation with appropriate flexibility for temporary shocks to prices, and the exchange rate has become progressively more flexible to allow for better adjustment to external shocks, including the price of oil.

Figure 11. Public debt by maturity */
(Percent of GDP)



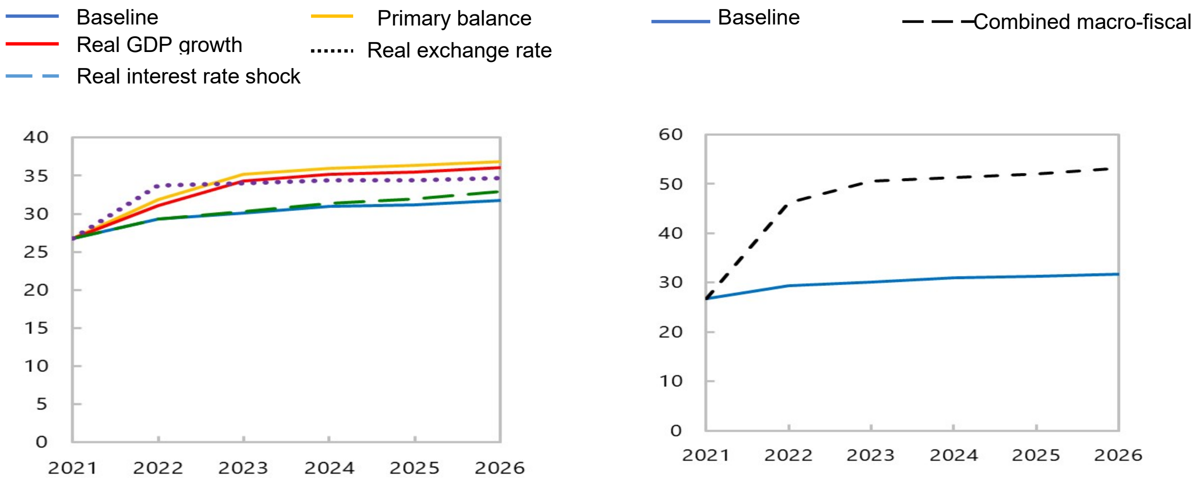
Sources: MNE, IMF, and World Bank staff calculations.
Notes: */ Does not include SOE debt.

Figure 12. Public debt by currency */
(Percent of GDP)



Sources: MNE, IMF, and World Bank staff calculations.
Notes: */ Does not include SOE debt.

Figure 13. Public DSA stress tests */ (Percent of GDP) — **Gross Nominal Public Debt** (Percent of GDP)



Sources: MNE and World Bank staff calculations.
Note: */The combined shock includes one standard deviation correction of GDP growth from the baseline for 2 consecutive years; a one-time off 115% decline in nominal exchange rate ; one-half standard deviation correction of primary balance from the baseline; and four percentage point increase in the interest rate compared to baseline.

2.3. IMF RELATIONS

37. **The IMF Board concluded the 2019 Article IV Consultation with Kazakhstan on January 29, 2020.** An IMF team conducted a virtual mission during November 2–13, 2020. The IMF has no financing arrangements with Kazakhstan but has provided technical support on monetary policy, fiscal policy, and statistics. The IMF and the World Bank maintain close collaboration on macroeconomic and structural issues.

3. GOVERNMENT PROGRAM

38. **A prominent feature among the government's strategic objectives is for Kazakhstan to become one of the 30 most developed countries by 2050 and become a carbon-neutral economy by 2060.** These objectives are articulated in several government strategies and plans (Box 5). The first is the 2012 long-term development strategy, Strategy Kazakhstan 2050, that aims to position Kazakhstan as one of the most developed countries in the world by 2050 by supporting new sources of growth, creating a favorable investment climate, and effectively developing and modernizing the public and private sectors. Progress is ongoing, and many of the reforms needed to accomplish this objective are supported by this DPF. The second is the 2013 government Concept on Transition to Green Economy until 2050, which aims to support the economy's transition from high dependence on hydrocarbons and substantial carbon intensity to carbon-neutrality with lower environmental impacts and degradation of natural resources. Kazakhstan has additionally outlined an ambitious target for economy-wide GHG emission reductions of 15 percent (unconditional) to 25 percent (conditional) by 2030 compared with 1990 levels in its 2016 NDC in support of the Paris Agreement. The third—and the overarching plan for the medium term—is the National Development Plan (NDP) 2025, which was revised in 2020 to reflect the challenges from the COVID-19 pandemic and the main domestic, regional, and global changes. The priority areas of the plan relevant for this operation are: building diversified and innovative economy through improving market

competition and better public procurement system; strengthening financial stability and increasing the role of the banking sector in the economy through better supervision and effective implementation of the banking resolution framework; and improving the accountability and transparency of public institutions. To help implement the strategies and the NDP, the authorities adopted the national action plan in September 2020 (agreed by the Government, the NBK, the Agency for Financial Regulation, AFR, and signed by the President), that lays out the institutional and legislative changes to be implemented by 2022 to mitigate the impact of the COVID-19 health crisis and support the recovery.

Box 5. Kazakhstan's Development Strategies and Action Plans Relevant for this Operation

Strategy Kazakhstan 2050 (adopted in 2012): This is a long-term development strategy that sets the target of Kazakhstan becoming one of the 30 most developed countries by 2050. The strategy focuses on: a strong national identity; more competitive economy and greater entrepreneurship; more efficient social policy, more modern and efficient education and healthcare systems; more accountable, efficient, and functional state apparatus, and improved security.

Kazakhstan Transition to Green Economy 2050 (adopted in 2013): This is an ambitious sector strategy for the economy to transition to a greener path through greater resource efficiency, infrastructure modernization, reduced impact on the environment, natural capital restoration, increased use of renewables, and improved water security. The strategy sets the following goals: significantly increase the share of renewables in electricity production to 50 percent by 2050; increase the share of gas power plants in electricity power generation to 30 percent by 2050; decrease energy intensity of GDP by 30 percent by 2030 as compared to 2008; provide access to water for the population and agriculture, improve agriculture land productivity; and reduce CO_2 emissions in electricity production by 40 percent by 2050, and increase waste recycling.

Republic of Kazakhstan's Nationally Determined Contribution (NDC, 2016): Kazakhstan submitted its Intended NDC to the United Nations Framework Convention on Climate Change (UNFCCC) in December 2016, signaling its commitment to the negotiations process and support for the Paris Agreement. The NDC lays out the intent to achieve an economywide reduction in GHG emissions by 15 percent (unconditional) to 25 percent (conditional) by 2030 as compared with 1990 during 2021–2030. The target includes the following sectors: energy, agriculture, waste, land-use, land-use, and forestry. Kazakhstan aims to submit an updated NDC ahead of the UNFCCC Conference of Parties (COP26) by November 2021. The draft updated NDC—which is under consultation within government—notes that Kazakhstan should retain the 2016 target and proposes additional measures to support the realization of this target by 2030. These measures include a strengthened Emissions Trading Scheme (ETS), the introduction of a carbon tax for non-ETS sectors, energy efficiency and renewable energy measures, and circular economy measures such as waste recycling.

National Development Plan 2025 (adopted in 2018 and amended in 2020): The plan supports the country's transition to a more inclusive, sustainable, and greener growth model. The NDP was amended recently to respond to new challenges resulting from the COVID-19 pandemic, regional developments, and a global push toward decarbonization. The priority areas of the NDP relevant for this operation are: building diversified and innovative economy through improving market competition and better public procurement system; strengthening financial stability and increasing the role of the banking sector in the economy through better supervision and effective implementation of the banking resolution framework; and improving the accountability and transparency of public institutions.

National Action Plan 2020 (adopted in 2020): The action plan was adopted to help implement the NDP 2025 and respond to the growing economic challenges imposed by the COVID-19 pandemic. The plan contains legislative and institutional reforms to be achieved by 2022. Several of the key goals are aligned with this operation, such as: the establishment of an independent competition agency, adoption of a new Environmental Code, adoption of new legislation to improve the public procurement system, and introduction of measures to reduce corruption in the public sector.

Source: Ministry of National Economy and World Bank staff.

39. **The authorities' focus has now shifted to developing several national programs that cover the specific**

legislative and institutional changes supported under the NDP 2025. First, the Competition Agency has defined key targets for the development of competition in key commodity markets with specific deadlines and has assigned the specific authorities responsible for the implementation of these measures; this is now part of the National Project of Entrepreneurship Development for 2021–2025. The authorities' goal is to address challenges that inhibit innovation and entrepreneurship and ensure a greater role for the private sector in the economy. The NDP 2025 aims to deliver equitable social protection, a more accessible and efficient health system, and quality education. It also aims to improve the quality, transparency and accountability of public institutions. Second, in 2021, the Government intends to start implementation of the Green Kazakhstan National Project, a multiyear program informed by the 2013 Concept of Transition to Green Economy and aligned with the 2021 Environmental Code. With support from Gesellschaft für Internationale Zusammenarbeit (GIZ, German international development agency), the Government intends to prepare in 2021 a low carbon development concept, which explores scenarios for decarbonizing the economy by 2060.

40. **To coordinate, prioritize, and ensure the effectiveness of the implementation of reforms, the Agency for Strategic Planning and Reform was set up directly under the President.** The Agency is also the secretariat for the Supreme Council of Reform chaired by the President with a well-known international advisor as a deputy. The new planning system is based on the combination of high-level concept complemented by time bound "national projects" linked to specific budget expenditures and with clear outputs.

4. PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

41. **The Program Development Objective of this DPF is to support institutional and policy changes for: (i) a more competitive economy driven by a more vibrant private sector and accountable public sector; and (ii) a more sustainable economic transition.** This operation is aligned with the Strategy Kazakhstan 2050, the Government's concept Transition to Green Economy by 2050, and the National Development Plan 2025. All prior actions supported by this operation are fully aligned with the government strategies and action plans. This operation is also aligned with the GRID and the World Bank Climate Change Action Plan (CCAP).

42. **The first pillar of this DPF focuses on a more competitive economy driven by a more vibrant private sector and accountable public sector.** The pillar supports Kazakhstan's transformation through reforms of competition, public procurement, telecommunication and the broader digital economy, the financial sector, and anti-corruption. The establishment of an independent Competition Agency to oversee and enforce competition policy will help level the playing field for all enterprises. A more open and transparent procurement both for the Government and the SOEs, by giving a better chance to private companies to participate in public procurement, will have a strong impact on private sector growth. This pillar also supports the NDP goal to strengthen the enabling environment for telecommunications and the broader digital economy. It also strengthens the implementation of the Digital Kazakhstan state program, which requires regulatory improvement in the telecom sector and private sector-led data services. This pillar furthermore supports the NDP 2025 priority of improving the functioning of the financial market. A more dynamic and stable financial sector, along with a reduced role of the state in credit markets, is essential for supporting viable SMEs. Finally, this pillar supports the NDP 2025 priority to improve the accountability, fairness, and transparency of public institutions by strengthening anti-corruption measures.

43. **The second pillar lays the foundation for a more sustainable economic transition.** The pillar focuses on Kazakhstan's energy transition: from high carbon-dependency, high energy intensity, and elevated GHG emissions to a larger share of renewables in the country's energy mix, strengthened operation of the emission trading scheme, and environmental sustainability. This operation will put in place the following building blocks. First, reforms will strengthen the legal and policy foundations for energy efficiency, ETS operation, and increased renewable energy use. They are important because Kazakhstan's hydrocarbon abundance contributes to the country's reliance on fossil-fuels based energy, high energy intensity of the economy, and high GHG emissions. The country's cold climate also results in high demand for heating in winter. At the same time, an underdeveloped regulatory regime limits the adoption of more energy-efficient and cleaner technologies and discourages private sector participation. In this regard, this pillar supports actions that establish a framework to report and monitor industrial emissions and energy consumption, and strengthen the operation of the ETS and the allocation methodology for the ETS National Allocation Plans so they can more effectively contribute to the GHG emission reductions required to meet the NDC by 2030 in future. These important initial steps will require additional regulatory reforms to be effective. Second, this pillar supports improvement in the arrangement for energy power purchases from renewable sources, which will positively impact private investment in renewable energy. Third, this pillar supports environmental protection, preservation, and restoration by encouraging the use of best available technologies, introducing 'polluter pays' principle, incentivizing green investments, mandating accurate and timely reporting of emissions, translating the NDC commitment into law, and supporting climate adaptation, among others. This pillar will further support Kazakhstan in meeting the following Sustainable Development Goals (SDG): SDG #7 on Affordable and Clean Energy; SDG #11 on Sustainable Cities and Communities; SDG #12 on Responsible Consumption and Production; SDG #13 on Climate Action; and SDG #15 on Life on Land.

44. **The design of this operation considers lessons learned from the last Kazakhstan DPF in 2015.[23]** As a result, the operation is underpinned by a strong partnership with the Government on analytical work and technical assistance. Most of the reform areas supported by the operation result from years of policy engagement through analytical work by the WBG, including in the fields of environment, climate change, budgetary operations and public expenditures, productivity, competition, procurement, and the financial sector (with joint work by the IBRD and IFC). The DPF has also benefitted from analytical work by other institutions, including the ADB, the EBRD, the IMF, the OECD, and the UNDP. Furthermore, this operation is designed as a standalone to provide maximum flexibility for the policy dialogue. Some reforms require substantial time to develop, reflecting the country's political economy and the challenges of the post-COVID-19 global economy. This operation is setting the stage for further policy dialogue to support implementation and deepening the reforms supported in this operation.

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

Pillar 1. Support a more competitive economy driven by a more vibrant private sector and accountable

[23] The objective of the First Macroeconomic Management and Competitiveness Programmatic Development Policy Loan (P154702) was to support the Government of Kazakhstan to implement reforms that (i) strengthen the sustainability of the macroeconomic framework while protecting the vulnerable and (ii) help improve competitiveness of the non-oil economy. The second DPF did not materialize because the government decided to tap domestic borrowing to finance its deficit. However, the authorities managed to continue implementing important reforms, such as floating the exchange rate and establishing an independent central bank. See also paragraph 8 and the footnote to it, referring to the ICR of the 2015 DPF.

public sector.

Prior Action #1. To foster competition and level the playing field for all enterprises in the economy, the Borrower has created and operationalized the Agency for the Protection and Development of Competition as an independent state authority with powers to, among others, (i) investigate and prevent anti-competitive practices and mergers, and (ii) impose sanctions.

45. **Rationale.** Competition is crucial for private sector development and productivity growth. When competition is limited, efficient firms are prevented from entering the market and growing faster, incumbents have fewer incentives to invest in productivity-enhancing technologies, while inefficient firms are less likely to exit the market. Investors' perceptions about the state of competition in Kazakhstani markets are relatively poor. According to the World Economic Forum–Global Competitiveness Indicator (WEF-GCI), Kazakhstan ranked 70th in 2019 in terms of the extent of market dominance out of 141 economies. In a similar vein, the effectiveness of anti-monopoly policies in Kazakhstan is perceived to be the lowest among its ECA comparators.[24] Also, the perceptions that vested interests impair the ability of firms to compete on merit reached the worst level in 2020.[25] Meanwhile, according to the OECD Product Market Regulation (PMR) indicator for 2019, Kazakhstan's overall regulatory framework is more restrictive to competition than that of OECD average; it also fares worse than all ECA peers, except for Turkey.[26] Most of the regulatory constraints to competition in Kazakhstan come from distortions induced by state involvement in the economy, in particular, the direct state participation through SOEs. [27] Out of 29 sectors covered by the 2019 PMR, the Government controls SOEs in at least 20 of them, which significantly exceeds the average number of sectors, with at least one SOE both in OECD and non-OECD economies.[28] Another source of regulatory distortions is the lack of competitive neutral policies among private and public operators, as most Kazakh SOEs are not covered by the same laws as private firms. All these factors have undermined competitive pressure and left limited space for private sector development.

46. The Government recently approved the new privatization law for 2021–2025 (Decree #908 of December 29, 2020). The plan lists 673 objects for privatization (including eight at the republican level and 448 municipal properties), 64 subsidiaries of national holding companies (NHC), and 153 social entrepreneurial corporations

[24] According to the 2020 Bertelsmann Transformation Index. This index assesses the transformation processes toward market economy. The specific question on antimonopoly policy assesses whether "antitrust or competition laws exist and are enforced against monopolization (for example, mergers, dominant market positions, concentration) and cartelistic conduct (for example, collusion, price fixing, predatory pricing)." Scores vary from 1—no legal or political measures are taken to prevent monopolistic structures and conduct—to 10—comprehensive competition laws to prevent monopolistic structures and conduct exist and are strictly enforced. In 2020, Kazakhstan scored 5, well below the OECD average score (8.7) and several of ECA peers; for instance: Czech Republic (10), Estonia (10), Poland (10), Latvia (10), Romania (8), Hungary (7), Turkey (7), Russian Federation (7).

[25] According to the Intelligence Economist Unit- Risk Tracker. According to this methodology, risks are scored on a scale from 0 (very little risk) to 4 (very high risk). In December 2020, Kazakhstan scored 4 on risks associated to vested interests and cronyism.

[26] The economy-wide version of the aggregate OECD PMR indicator assesses the extent to which public policies promote or inhibit market forces via two main pillars: (i) distortions induced by state involvement and (ii) barriers that can hamper entry of domestic and foreign firms and products into the market. The indicator scale varies from (0 – least restrictive to competition) to 6 (most restrictive to competition). In 2019, Kazakhstan scored 2.12, while the OECD average scored 1.43. Among the ECA countries covered by the PMR analysis, all perform better than Kazakhstan, except for Turkey.

[27] According to the 2019 OECD PMR result in 2019, 65% of the total PMR score in Kazakhstan is due to restrictions related to state involvement in the economy.

[28] In particular, Kazakh SOEs participate in product markets where there is a less clear economic rationale for state intervention. As an example, Kazakhstani SOEs are active in sectors such as gas supply, retail e-communication services, air transport, manufacturing, accommodation, and banking services.

(SEC).[29] This plan follows a similar privatization plan for 2016–2020 adopted in December 2015. The authorities executed more than 90 percent of the 2016–2020 plan. The non-executed part was mostly for assets of the sovereign wealth fund Samruk-Kazyna. Under the previous plan, the authorities sold or transferred into concession with the right to purchase 506 companies, resulting in privatization proceeds of almost KZT 630 billion (US$1.5 billion).

47. **Substance of the prior action.** Enabling a sound competition policy regime is key to achieving a level the playing field for all enterprises, and encouraging the smooth functioning of markets and boost private sector development. Kazakhstan already has few, but not all, elements needed to ensure a robust competition regime. For instance, the Competition Law is in place; specifically, Part 4 of the Entrepreneurial Code, enacted October 29th, 2015.[30,31] Against this backdrop, the establishment and operationalization of the new Agency for Protection and Development of Competition—through adoption of Presidential Decree #407 (September 8, 2020) and Presidential Decree #428 (October 5, 2020)—come as complementary steps and important milestones. The new Competition Agency is directly accountable to the President. It replaces the Committee for the Protection and Development of Competition, which was subordinated to and legally dependent on the Ministry of National Economy (MNE). The establishment of the Competition Agency outside the government ministries is a major achievement in limiting the scope for political interventions in the Agency's activities. Its creation outside the Government is aligned with best practices; for instance, the competition authorities of the EU member states, the Federal Trade Commission (FTC) in the United States, the Canada Competition Bureau, and the Australian Competition and Consumer Commission are all independent agencies.

48. The Competition Agency is tasked with several responsibilities. According to Presidential Decree #428, the Agency's mandate encompasses not only the traditional enforcement of the Competition Law and competition advocacy, but also other strategic tasks such as: monitoring of public procurement of goods; the responsibility to approve the establishment of new SOEs, as well as the expansion or change of activities of existing SOEs, and the power to submit proposals to the Government to transfer SOEs or their activities to a competitive environment (See Article 16 [28,50,59,60]) of the Decree. Having this 'SOE monitoring role' conferred to an independent body entrusted with a mandate to safeguard market competition represents an important milestone and may positively affect competition dynamics**.**

49. According to Kazakhstan's Budget Code, the Agency receives budget from the state and has the autonomy to spend its resources under budget program lines previously agreed with the Ministry of Finance as part of the multi-year budget exercise. The Agency is already functioning: its senior staff—Chairman, three Deputies and a Chief of Staff—has already been appointed, the budget has been allocated, and 36 investigations of violations of the legislation of the Republic of Kazakhstan in the field of competition protection have been launched since the Agency's creation. The Agency has 267 staff, of which 154 in regional departments and 113 in the headquarters.

50. **Expected Results.** If properly implemented, competition reform is expected to increase the ability of firms to compete on a level playing field. An independent agency can exercise its powers and apply, interpret, and

[29] According to OECD estimates, SOEs account for 19 percent of gross value added. This compares with about 20 percent in Russia, 9 percent in Ukraine, and less than 5 percent in Czechia, all in 2016, according to IMF. 2019. Reassessing the Role of SOEs in Central, Eastern and Southeastern Europe. In the same of countries in this paper, the share of the state in value added fell by 5-10 percentage points from 2005 to 2016.

[30] Part 4 of the Entrepreneurial Code incorporated and superseded the 2008 Law on Competition and Natural Monopolies and Regulated Markets and introduced some new tools of antitrust response as well as tools to combat cartels, such as "dawn raids."

[31] No 375-V-ZRK. The 2015 DPF supported amendments to this Chapter of the Entrepreneurial Code.

enforce competition rules on the basis of legal and economic arguments, free from political influence or pressure. This is expected to enhance the consistency and predictability of decisions and creates an environment where market players and the general public have confidence in the process by which the authority exercise its functions.

51. **Indicator.** Number of investigations on anticompetitive practices that were resolved by issuing a decision. Baseline (2020): 0; Target (2022): 5.

52. **Next steps.** The effective independence of this new Competition Agency and its capacity to level the playing field for all enterprises remains to be seen in practice. It will depend on three main steps. First, its ability to formulate and implement strategic documents that will set the Government's vision and strategy in the area of competition. These documents include: the National Project of Entrepreneurship Development for 2021–2025 and the Competition Agency's Strategic Development Plan.[32,33] Second, the adoption of clear rules for hiring and dismissing high-level officials of the Agency (Chairman, Chief of Staff, and Deputies) to build the Agency's institutional safeguards against undue private or public interference. Third, the Agency's capacity to coordinate with other state bodies with concurrent powers to implement competition policy in Kazakhstan (such as the sector regulators). In addition to these measures, there is a need to deepen pro-competition reforms beyond the Competition Agency's control. For instance, adopting a mechanism and methodology for assessing the impact on competition of draft regulatory legal acts, according to international best practices. This mechanism will allow identification, on a systematic basis, of the costs to competition of a particular regulatory-policy proposal and potential remedies to mitigate these costs.[34] Moreover, the implementation of the privatization plan, especially for entities that are subsidiaries of major holding companies, as well as by strengthening the governance of SOEs that will remain in state ownership. The rationale for state ownership needs to be clearly defined.

Prior Action #2. To strengthen the enabling environment for telecommunications and the broader digital economy and to attract private investment into the sector, the Borrower has: (a) Adopted amendments to legislation on digital technologies to enhance the regulatory environment for personal data protection and facilitate the development of private sector led data-driven technology; and (b) Adopted amendments to legislation on licensing of wireless broadband internet services to simplify the requirements and promote investment by introducing the technological neutrality principle in the license and reducing by 90 percent for at least five years the fees for the use of radio frequency spectrum.

53. **Rationale.** Over the past decade, Kazakhstan has made notable progress in advancing digital

[32] This National Project should: (a) identify and prioritize the main constraints to competition in Kazakhstan; (b) identify detailed (horizontal and sector-specific) measures designed to reduce or eliminate impediments to well-functioning markets that arise from public policy interventions; (c) assign specific authorities (together with the Competition Agency) to implement these measures; (d) identify specific timelines (and stages of implementation) to accomplish these measures; and (e) identify performance indicators that will help to track the progress of reforms.

[33] The Competition Agency's Strategic Plan should: (a) contain the mission statement of the Agency, broken down into operational objectives that cover each agency function; (b) define priorities in terms of short- and longer-term goals; (c) indicate how resources will be allocated to each goal; and (d) clarify how progress will be measured, with specific indicators to facilitate monitoring at the end of the period.

[34] According to the Presidential Decree # 484, issued in December 2020, the Government of Kazakhstan has committed to introducing – by the end of 2021 - amendments and additions to the legislation of the Republic of Kazakhstan, providing for the introduction of a mechanism and methodology for assessing the impact on competition of draft regulatory legal acts, following the OECD methodology.

development, with more than 82 percent of the population using the internet. Furthermore, its mobile tariffs are among the most affordable in the world. Much more remains to be done, nonetheless, particularly to ensure universal access to digital services, attract private investment, and support private-sector-led innovation. There are currently three mobile operators in Kazakhstan, and a fourth is in the process of entering the market. Although the issue of access to spectrum is problematic, the Competition Agency is helping increase competition in the market. The state-owned incumbent controls 64 percent of the telecom market. It controls key elements of the fixed, mobile, and backbone infrastructure, and has a minority 49 percent private stake. Of the existing three mobile operators, only one is fully private, one is majority-owned by the state incumbent, and another is fully owned by it. There are also three smaller private operators in the fixed segment of the market, but they are not serious competitors to the state-owned incumbent, and they do not use the radio spectrum. The digital connectivity infrastructure has improved over recent years in large urban areas, while significant gaps remain in rural areas, where the gap between men and women is also larger, due to an unfinished reform agenda and low private investment. Deployment of innovative digital technologies in the private sector, including robotics and blockchain, is further constrained by a complex regulatory environment and an absence of adequate enablers and safeguards for developing trust in the digital economy, particularly an adequate regime for personal data protection.

54. **Substance of the prior action.** The prior action constitutes a useful first step in helping strengthen the enabling environment for the digital economy. The adoption in June 2020 of the “Digital Technologies Law” introduced concepts such as “blockchain” and “intelligent robot” into the legal framework, and supported improvements to the data protection enabling environment.[35] This includes data depersonalization in the conduct of analysis by the state and the designation of an authorized body for the protection of personal data, among others. In relation to the telecommunications sector, the reforms introduced through this action will make it easier and less costly for operators of mobile internet services to invest in the expansion of their networks to provide services in rural areas. Specifically, the Law on Permits and Notifications implements the principle of technological neutrality in the issuance of licenses to use the radio frequency spectrum for cellular communications, by removing the requirement to specify the name of the standard in the license, which will allow operators more flexibility in upgrading their networks. Furthermore, recent amendments to the Tax Code reduced the fees for the use of radio frequency spectrum by at least 90 percent for the provision of internet broadband access for at least four years, which will enable operators to expand service provision in rural and remote locations. (The authorities will decide later what happens after the 90 percent discount expires in four years.) These actions will increase the trust of users in digital technologies and will have a direct impact on the efficient allocation of resources by mobile network operators. They will lower the cost of delivering mobile broadband services with higher speed and broader coverage, especially in rural areas, thus increasing investment in network rollout and the ability to reach clients who would otherwise be left unserved. These actions will also contribute to a reduction in CO_2 emissions, as users will have less need to travel for routine services, since they will now have suitable alternatives to obtain services, and serve other business and personal needs remotely. It is also expected that these actions will address the gender gap in access to internet services in rural areas: while the gap is small at the national level (the share of internet users among men is 81.6 percent and among women 81.1 percent), this gap is estimated to be significantly higher in rural areas. This action can also potentially increase accessibility of digital services, and in line with Kazakhstan’s program to promote gender equality for access to public services and resources for entrepreneurial activities.[36] Overall, the reforms supported through

[35] Law № 347-VI ЗРК of June 25, 2020 "On Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on the Regulation of Digital Technologies” (aka “Digital Technologies Law”).
[36] As reflected in the Concept of Family and Gender Policies in the Republic of Kazakhstan until 2030.

this prior action are expected to improve the regulatory and policy frameworks of the telecom sector, as well as to reduce barriers to operation in few market segments. This is expected to create an enabling environment for the development of the telecom sector, and open space for private sector mobilization and additional investments.

55. **Expected results.** This prior action will contribute to attracting private sector investment into the digital economy of Kazakhstan and will also help accelerate the adoption of digital technologies by citizens and businesses in cities and rural areas. This, in turn, will in turn lead to productivity increases across all sectors of the Kazakhstan economy.

56. **Indicators.** (a) Share of the population using the internet. Baseline: 82 percent (2019). Target: 88 percent (2022); (b) Share of electronic commerce in the total volume of retail trade. Baseline: 1.8 percent (2019). Target: 3 percent (2022).

57. **Next steps.** Implementation of the adopted Digital Technologies Law will require further amendments to the personal data protection legislation, as the initial amendments are not yet fully in line with good international practice. Specifically, additional amendments will be needed to ensure that the Law on Personal Data (dated May 21, 2013) incorporates international good practice provisions on data portability, consent, data protection, data management, right to information and notification, surveillance, and rights of citizens (including use limitations, data minimization, data accuracy, data retention, and others). Amending the Law on Personal Data is included in the Government's draft National Project on Digital Development, currently under preparation, and scheduled for approval in 2021. The Bank team has been working with the Ministry of Digital Development (including in the context of the recently completed JERP task on the topic and the preparation of the Resilient Digital Kazakhstan PforR) to identify the legal gaps in relation to the safeguards, data protection in particular, and to ensure that the amendments to the law incorporate international good practice provisions on data portability, consent, data protection, data management, right to information and notification, surveillance, and rights of citizens (including use limitations, data minimization, data accuracy, and data retention).

58. Furthermore, the telecommunications sector reforms supported by this operation will need to be supplemented by additional amendments to the sector legal and regulatory framework. Specifically, the Law on Communications (dated July 5, 2004) will need to be amended to ensure that the regulatory framework for the telecommunications sector is in line with good international practice, in particular the need to strengthen the capacity and autonomy of the regulatory authority, increase competition to enable new entry, and withdraw the state from its role as a market operator. To address issues related to the heavy dominance of the state in the telecom sector, the Bank continues to support the strengthening of the capacity of the new Competition Agency to implement competitive-neutral policy to level the playing field, and strengthening the capacity and autonomy of the regulatory authority.

Prior Action #3: To improve open competition, transparency, and accountability in public procurement, the Borrower has (a) Submitted to Parliament amendments to the Public Procurement Law (PPL) to: (i) Set open tender as the default procurement method; (ii) Reduce single sourcing and clarify the exceptional circumstances where it can be permitted; and (b) Submitted to Parliament amendments to the PPL and adopted new procedures to reduce the right to use single sourcing procurement by the SOEs.

59. **Rationale.** Kazakhstan has a dual public procurement system: the Public Procurement Law (PPL) for the

government procurement conducted by the general public administration (and the few SOEs that are not part of the Samruk-Kazyna Sovereign Wealth Fund) and the Samruk-Kazyna's Procurement Regulations for procurement conducted by SOEs part of the conglomerate. Public procurement by the Government and SOEs in Kazakhstan is estimated at about 13 percent of GDP, slightly higher than the OECD average (12.6 percent in 2019).[37] Procurement under the PPL accounts for more than 60 percent of public procurement. The Government has made efforts over the past two years toward strengthening its public procurement system. However, certain weaknesses need to be addressed in line with international good practice to achieve better competition and value for money, substantial gains in service delivery, stronger SME and private sector growth, and more robust positive social impacts.

60. This procurement prior action has been underpinned by the findings of the country procurement system assessment report (MAPS) delivered to the authorities by the Bank in 2019. As part of the report, the Government acknowledged the key issues in the report and agreed to the recommendations to address them. Kazakhstan's procurement system was rated D in the 2018 Public Expenditure and Financial Accountability (PEFA) assessment, reflecting the fact that the majority of public procurement contracts is decided through non-competitive procurement methods. This operation is a window of opportunity to accomplish some foundational changes in the procurement system that will help make it more competitive, inclusive, and transparent. Defining the hierarchical order of the different procurement methods is critical to mandate open tender as the default method, which will ensure better competition and cost savings. The legal framework continues to allow more than 50 circumstances for direct award of contracts through single-source procurement. Moreover, the Samruk-Kazyna's Procurement Regulations allow preferences for SOEs for in-house procurement through single-source contracts. As reflected in the MAPS report, single-source procurement in 2017 accounted for 82.8 percent of procurement transactions by number and 81.8 percent by value. In 2020, the share of single-sourced contracts declined to a still very high 65 percent of the public procurement.

61. **Substance of the prior action.** Through part (a) of this prior action, the PPL has required procuring entities to prioritize open competitive procurement methods, such as, open tendering, e-reverse auction, and request for quotations (RFQ) over non-competitive methods. The RFQ method (open but less competitive amongst the three new methods) has been allowed to be used for contracts with a value of less than the equivalent of US$27,000 under the. Open tender or e-reverse auction methods are required to be applied for purchases with estimated cost above the RFQ thresholds.

62. In the amended draft PPL submitted to Parliament, the authorities have removed four circumstances allowing single-sourcing of contracts.[38] This is expected to contribute to reducing the share of single-sourced contracts from 65 percent in 2020 to 44 percent in 2022. The exclusion of only one single source circumstance under Article 39(3)(19) will help reduce by about 16 percentage points the share of single-sourced contracts.[39] The amended PPL has also incorporated the applicability of the single-source method in the case of exceptional circumstances, procurement of proprietary items, continuity of ongoing contracts when justified, and force majeure circumstances. It has also incorporated an accountability and transparency framework for single-source

[37] Data for Kazakhstan is for 2018 based on the 2019 report "Assessment of the Public Procurement Systems of the Republic of Kazakhstan and the Sovereign Wealth Fund Samruk-Kazyna." Data for OECD is based on OECD. 2019. "Public Procurement in Kazakhstan: Reforming for Efficiency."

[38] Proposed amendments and additions to Certain legislative Acts of the Republic of Kazakhstan on Public Procurement, Procurement by Subsoil Users and Subjects of Natural Monopoly, Communications, Automobile Transport and Defense, as submitted to Parliament.

[39] Purchase of services related to the state educational order for individuals (if an individual has selected the educational organization by himself/herself).

contracts by requiring that all single-source contracts, their value, justification, and the person who approved them to be published. Going forward, these additional control and transparency mechanisms are expected to contribute to a significant reduction of the share of single-source contracts in 2022 and beyond.

63. While the proposed amendments to the PPL, as submitted to Parliament, reduce the right of SOEs to use single-sourced procurement, Samruk-Kazyna Board has already adopted a reduced list of items eligible for single-source procurement. Even for these items, the SOEs are now required to consider open competitive methods when a competitive procurement approach appears to be viable based on the market conditions.

64. **Expected Result.** The implementation of this procurement prior action is expected to result in a more transparent, competitive, and efficient public procurement system which will facilitate more private participation in the market because of more opportunities in public tendering and fewer preferences for the SOEs. The reforms supported by this operation will help create additional fiscal space, which will reduce the burden on the budget and on businesses. It will also help provide better quality of goods and services to the citizens by ensuring better accountability in public spending.

65. **Indicator.** Procurement contracts by value awarded through open competitive methods. Baseline: less than 35 percent (2020). Target: more than 50 percent (2022).

66. **Next steps.** Building on the current reforms, the authorities should consider strengthening of the current provision of sustainable procurement to incorporate the provision of green and, possibly, the circularity in procurement. To further strengthen the current framework of accountability and transparency in the public procurement decision-making by public and quasi-public sectors, the country procurement system may incorporate a requirement for publication of the names of the ultimate beneficial owners (B/O), based on the detailed B/O information to be provided by the winning firm before the contract is signed. Finally, to enhance transparency and accountability of public spending, an appropriate provision needs to be incorporated in the legal framework that will facilitate the engagement of citizens by giving them access to public procurement data and to reports on public procurement performance indicators. The quality versus price aspect of large contracts, as well as the role of estimated cost in contract awards, are currently being discussed with the Government under the ongoing Roads projects, and we will continue working on these issues to ensure value for money in public spending of all types. The Bank will continue engagement with the Government to ensure proper implementation of the regulatory changes and their adoption by the procuring entities. Adequate training and awareness events will be organized to bring the procuring entities on board the amended procurement procedures and processes. The Bank is also discussing with the Government the quality versus price aspect of large contracts and the role of estimated cost in contract awards under the ongoing Roads projects to ensure value for money in public spending of all types.

Prior Action #4: To support market discipline and fair competition in the banking sector, the Borrower has, through the Agency for Financial Regulation, resolved regulatory non-compliance of three commercial banks in accordance with the Law on Banks and Banking.

67. **Rationale.** Kazakhstan's financial sector does not allocate capital efficiently to contribute to productive, inclusive, and sustainable growth. Financial deepening has stalled, and private sector credit growth has been contracting in real terms. The share of loans extended to enterprises with negative capital is still substantial, especially for SMEs, while new and financially constrained firms are lacking credit. In 2019, only 17 percent of

SMEs have a bank loan compared with an ECA average of 39 percent. And the loan application of about 23 percent of SMEs was rejected recently compared with an ECA average of 9 percent. Regional variations in both statistics are large within Kazakhstan.

68. Addressing problems in the banking sector is critical for the sector to support Kazakhstan's development. The two financial crises in the past decade led to transfers of NPLs to public asset management companies and quasi-fiscal bailouts largely without recourse on future bank profits—socializing private losses of bankers. Bank regulation needs to ensure that NPLs are properly disclosed and provisioned for, and that failing banks exit timely the system. In parallel, vast, subsidized financial programs—channeled through banks at below-market funding costs and recently scaled up as part of the COVID-19 relief efforts—help banks roll-over/evergreen loans to existing borrowers while preserving their profit margin and not feeling the urge to search for new productive projects—notably in non-extractive industries and lagging regions. This policy can undermine market discipline, competition, and fuel moral hazard.

69. The political economy of Kazakhstan's banking sector presents a difficult terrain to navigate for the purpose of improving transparency, public accountability, risk governance, and fair competition. By June 1, 2021, the bank loan portfolio to GDP stood at 22.3 percent and the five largest banks covered almost 70 percent, suggesting larger concentration. All 23 banks that operate in Kazakhstan include one 100 percent state-owned bank, 14 banks with foreign participation, and nine subsidiaries of banks. About 70 percent of the banking system assets is controlled by banks with powerful shareholders. Another about 20 percent is controlled by foreign (state) banks. Independent private commercial banks control less than 10 percent of banking assets.

70. Since January 1, 2020, financial supervision was transferred from the National Bank to the new Agency for Financial Regulation and Development (AFR). The Agency has been working on the improvement of the quality of its supervisory framework, and the IMF has been providing technical assistance on bank supervision through a resident advisor. The capacity to resolve some failing banks in timely matter has not been strong enough, including for likely political economy reasons. The new agency needs to continue building credibility—notably through timely enforcement of regulation—to foster leveled playing field and competition in the banking system.

71. **Substance of the prior action.** The resolution of problem banks remains a challenge and this DPF has provided support to policy implementation. In early 2020, the bank resolution framework was amended largely in line with sound international standards. Despite the revised resolution framework and despite the enforcement efforts of the Agency for Financial Regulation (AFR), not every bank with capital shortfalls has been fully recapitalized. The AFR has though taken steps in dealing with troubled banks, including by resolving banks with regulatory deficiencies that have been breaching minimum prudential standards for over a year, and required other problem banks of weak financial standing to submit and follow financial rehabilitation plans. During 2020, three non-systemic banks, accounting for 0.7 percent of the banking system's assets, were failing the prudential norms for more than a year; three mid-sized banks were following financial rehabilitation programs previously agreed with the AFR; and one mid-sized bank was looking to merge with another bank to resolve its problems. The Prior Action focuses on the resolution of three non-systemic banks that were failing the prudential norms for more than a year who have had their licenses withdrawn in September 2020, February 2021, and June 2021. Because the AFR has not been able to share confidential information, the World Bank team has not been able to verify the soundness of the supervisory plans for the three mid-size banks or the timely fulfillment of the prescribed actions. Based on data as of April 30, 2021, published by the NBK, none of the three mid-size banks is violating prudential ratios.

72. **Expected results.** Decisive enforcement actions on the banks' regulatory deficiencies will increase market discipline in the future.

73. **Indicators.** (a) The number of banks that have violated three or more times over the preceding 12-month period any capital adequacy ratios or liquidity coverage ratio.[40] Baseline: 3 (end 2020). Target: 0 (end 2022).

74. **Next steps.** The authorities are determined to advance reforms to create a more vibrant and competitive financial sector. In this regard, the continued policy dialogue is expected to address the following issues: (i) The AFR needs to improve the prudential regulatory framework related to NPL identification, provisioning, and derecognition in line with Basel Committee on Banking Supervision and other international practice, both on an individual bank (solo) and bank group (consolidated) bases, especially in relation to (affiliated) asset management companies; (iii) The authorities need to end the Problem Loan Fund (PLF) purchases of NPLs at nominal price to stop public bailouts without taxpayers' recourse, increase the transparency of public support, and enable the PLF to better play its market maker role in opening the market for distressed assets; and (iii) The state financial support programs to firms need to be rationalized based on rigorous impact evaluation and focus on indirect approaches rather than interest subsidies and directed credit. These reforms will help reduce bank moral hazard, strengthen bank competition, and create room for new productive lending provided that demand-side constraints related to real sector competition, SOE practices, firm capabilities, and cost of doing business are addressed in tandem. Well-performing banks will compete and grow, including through mergers and acquisitions. Poorly performing banks will have to innovate or leave the market—and possibly create space for new entrants or leave a niche that could be better served by non-bank financial institutions.

75. **Broader engagements to carry the financial policy stream forward.** The Bank is continuing the dialogue with AFR, PLF, MoF, NBK, and the secretariat of the Financial Stability Committee on making decisions about bank resolution more transparent—in particular under which conditions public support can be provided and what instruments can be used to protect taxpayers and prevent bankers from socializing private losses. Through discussions on possible RAS and/or IPF, the team is engaged with the authorities on rethinking and streamlining the GoK financial support programs to MSMEs to make them fairer, competitive, and less distorting to private markets. This includes improving agriculture finance based on recently delivered RAS on the topic. The IFC-WB team is about to complete the diagnostic of NPLs and development of distress asset markets in Kazakhstan at the request of MNE. The EBRD is working on a complementary diagnostic at the request of AFR. These diagnostics will provide a robust foundation and platform for the policy dialogue on needed changes to bank public support, NPL identification and provisioning and, in particular, the use of PLF as a vehicle for market creation rather than one-way bailout of banks with large NPLs. The FCI and Procurement teams will continue the dialogue on the placement of deposits of SOE and quasi-fiscal entities in banks on competitive basis to address hidden bank support rooted in the political economy issues. In parallel, the IMF continues with its technical assistance to improve bank supervision—including focusing on risk-based supervision. The upcoming FSAP—which was postponed from FY22 to FY23 at the request of the IMF—will benefit the authorities and all IFIs through a comprehensive financial sector diagnostic, focused on both stability and development, and prioritized recommendations for the medium term.

Prior Action #5. To reduce corruption and improve accountability in the public and quasi-public sector, the

[40] The number "three or more times" is specified in the Kazakhstan Banking Law, article 48.

Borrower has: (a) Prohibited civil servants, persons subject to anti-corruption restrictions, and members of their families from accepting gifts, remuneration and services in exchange for actions or inactions within their official powers, and from opening and owning foreign bank accounts; (b) Expanded liability for corruption offenses to all persons authorized to perform public functions, including the management of quasi-public sector entities; and (c) Strengthened control over the enforcement of anti-corruption legislation by requiring the creation of anti-corruption compliance monitoring services across the quasi-public sector.

76. **Rationale.** Robust anti-corruption institutions are essential for boosting economic growth and social inclusion by creating trust in the Government. However, systemic corruption remains a serious problem and severely undermines citizens' and businesses' confidence in public institutions. Kazakhstan's authorities have stepped up efforts to reduce corruption in the public and quasi-public sector. Kazakhstan has made several high-level commitments to improve governance and combat corruption, as a result of which the country was able to considerably improve its ranking in the Corruption Perceptions Index: in 2020 Kazakhstan ranked 94 out of 180 countries compared with 123 out of 167 countries in 2015.[41] Nevertheless, Kazakhstan still scores slightly below the average of emerging markets and developing economies on public perception on control over corruption.[42] The 2019 OECD Anti-Corruption Progress Update for Kazakhstan also highlighted gaps in the integrity in the public and quasi-public sector; political officials; law enforcement and the judiciary; public procurement; access to information; regulatory framework relative to corruption offences and related liability; and institutional framework and capacity.

77. **The new anti-corruption measures set forth in recent amendments (to the Law on Countering Corruption, the Criminal Code, and the Civil Code) seek to address these gaps and align anti-corruption legislations in line with international best practices.** They also expand the compliance and enforcement functions of anti-corruption services to both the public and quasi-public sector, ensuring better oversight and controls over the operations of SOEs. Within this framework, the measures supported by this operation represent important milestones of the Government's National Anti-Corruption Strategy until 2025 to increase the effectiveness of the detection, prevention, and prosecution of corrupt practices by reducing corruption opportunities in the performance of the functions of public servants; expanding the scope of public servants subjected to anti-corruption restrictions and related liability; strengthening penalties to promote deterrence; and developing anti-corruption services across the quasi-public sector, which is a major part of the governance and economic structure of Kazakhstan.

78. **Substance of the prior action**. The Kazakh Government's objective is to strengthen its anti-corruption legislation to enhance the integrity and accountability of state bodies and state-owned enterprises. In line with this objective, recent legislative amendments have significantly expanded the scope of public servants subjected to anti-corruption restrictions. The scope of public servants now includes the management and employees of the quasi-public sector. It further encompasses parliament deputies, law enforcement officials, and judges. The prior action also strongly complements improvement in public procurement, by including officials in public and quasi-public sector involved in procurement-related decision-making, and those responsible for the selection and implementation of government-funded projects. In addition, these officials and their family members are subject to enhanced restrictions, such as the complete ban on gifts irrespective of their value and the introduction of a prohibition for public servants and their families to open or own foreign bank accounts, as well as heightened criminal and administrative sanctions (e.g., the exclusion of parole for grave and especially grave corruption

[41] https://www.transparency.org/en/cpi/2020/index/kaz
[42] Republic of Kazakhstan. 2019 Article IV Consultation. IMF Country Report No,20/32. Figure 1, page 17.

offences). The liability has also been expanded to persons occupying managerial functions in the quasi-public sector, as well as officials in public and quasi-public sector involved in public procurement-related decision-making, and the selection and implementation of government-funded projects. In parallel, the new legislation aims to strengthen oversight, compliance, and internal controls mechanisms by requiring the establishment of anti-corruption services across the quasi-public sector.

79. **The Bank team reviewed the regulatory framework presented as evidence of the prior action.** Based on its assessment, the team is satisfied that the prior action is fully aligned with international anti-corruption and compliance standards and that the evidence reflects the substance of international recommendations.[43] The team is further satisfied with the review they carried out of the anti-corruption prevention, detection, investigative and enforcement entities in Kazakhstan, including the Anti-Corruption Agency ANTIKOR, and anti-corruption compliance services in the quasi-public sector.[44] The team is therefore satisfied that the prior action supported by this DPF falls within the development goals of the Bank, grounded on the appropriate and objective rationale, and does not involve the Bank in the political affairs of the Borrowers.

80. **Expected Results**. Over the long term, the expansion of anti-corruption restrictions and compliance services to both the public and quasi-public sector is expected to build a culture of transparency and integrity among public servants, particularly in their administrative, judicial and economic relationships with the private sector. The proposed indicator (below) aims to ensure appropriate reporting and assessments on the implementation of the new anti-corruption measures in both the public and quasi-public sector by Kazakhstan's anti-corruption authorities. These include not only ANTIKOR but also the newly created anti-corruption compliance services. ANTIKOR's annual National Anti-Corruption Reports have been published since 2016.

81. **Indicator.** Annual National Anti-Corruption Report detailing progress of anti-corruption measures both across the public and the quasi-public sector. Baseline: Not published with such detailed progress (2020). Target: Published (2022).

82. **Next steps.** The authorities are committed to implementing in full the Anti-Corruption Strategy by 2025 and, together with actions on public procurement, to reduce corruption and the burden on the budget while improving accountability and transparency. They are aware that effective implementation of the strategy will require further actions in the following key areas: (i) Strengthen internal systems and bring international experience in quality and performance standards; (ii) Train competent ANTIKOR staff and build the capacity of anti-corruption services in both the public and quasi-public sector to deliver on their prevention, detection, investigation, and enforcement mandate; (iii) Improve audit capabilities to fulfill the requirements of the new legislation and build monitoring and evaluation functions within ANTIKOR; and (iv) Raise awareness of anti-corruption measures and effectively build a culture of integrity across state bodies, state-owned entities, and the public.

Pillar 2: Support a more sustainable economic transition.

[43] See OECD, Anti-corruption reforms in Kazakhstan, 4th round of monitoring of the Istanbul Anti-Corruption Action Plan, 2017 at *https://www.oecd.org/corruption/acn/OECD-ACN-Kazakhstan-Round-4-Monitoring-Report-ENG.pdf*.

[44] The anti-corruption compliance services referred to in the prior action item (c) are the compliance and good governance structural units to be created in the quasi-public sector (e.g., SOEs) which will be responsible for providing services within their entities to monitor, prevent and detect potential and/or existing corrupt practices with a view to ensure the compliance of their entity with anti-corruption legislations in the quasi-public sector

Prior Action #6. To improve energy efficiency and reduce GHG emissions, the Borrower has submitted to Parliament amendments to the Energy Saving and Energy Efficiency Act of January 13, 2012 that: (a) Expand energy consumption reporting to include all state-owned and budget sector entities; (b) Update the reporting requirements to enable better tracking of energy consumption; (c) Require procurement of goods and services by all public entities to include energy efficiency requirements; and (d) Adopt a new certification system for individual energy auditors.

83. **Rationale.** To achieve Kazakhstan's 2016 NDC of reducing GHG emissions and cutting the energy intensity of GDP by 30 percent by 2030 (compared with 2008), the Government needs to prioritize the reduction in GHG emissions from the largest emitters, with energy-related activities in the economy accounting for 85 percent of the country's total GHG emissions. Achieving this GHG emissions reduction target requires the timely and accurate reporting and monitoring of energy use by energy consumers, expanding the scope of entities that must report, and including energy efficiency criteria in procurement practices. As of end-April 2021, there were 8,600 entities, both public and private, that were required to report their energy consumption into the State Energy Register (SER). Of these, about 2,300 public and private entities must undergo energy audits every five years. Thus, as more entities report their energy use, there is also a need to enhance the country's capacity to provide services that meet this expanded need for energy audits, reporting, and monitoring.

84. **Substance of the prior action.** The tracking, monitoring, and reporting of energy use—a needed first step to have credible movement toward efficient energy use—has not been a priority at many enterprises and organizations in Kazakhstan. To correct this, in mid-2020 the authorities submitted to Parliament amendments and additions to the Law of the Republic of Kazakhstan No. 541-IV "On energy conservation and energy efficiency" that will improve the reach, quality and transparency of such reporting. Prior reporting requirements produced a lot of data without providing the authorities with the ability to make appropriate comparisons or use it in a meaningful manner to help improve performance. Part (a) of the prior action expands the scope of entities that have to report to the SER to about 26,000 by including all SOEs and all budgetary units. Part (b) updates the reporting requirements for all entities reporting to the SER to enable easier comparison of emissions across different types of energy consumers. As per part (c), all SOE and budget sector public procurement will be subject to energy efficiency requirements. To meet the reporting requirements in (a) and (b) and to further expand awareness and monitoring of energy use, including the private housing sector, part (d) introduces new certification procedures for energy auditors. In total, these amendments will provide the authorities with improved tools for monitoring and enforcement in the medium term and are setting the stage for the bylaws that will follow. The SER will also help track progress in achieving the NDC goals and foster corrective actions through stricter energy consumption standards. This data from the SER can also help inform ongoing work in developing a new Concept Heat Supply Law, as well as national standard on Best Available Technologies.

85. **Expected Results.** These amendments will streamline reporting and monitoring across the country, with all public entities included in the scope of reporting. By including energy efficiency requirements in all public procurement for goods, to be followed by setting up better standards for energy efficiency, the government will lead in the purchase of energy efficient equipment and services. Expanded capacity for timely and better quality energy audits will further improve awareness of energy efficiency, as well as help with implementing follow-through measures to economically reduce energy usage, helping reach the targeted result indicator of 0.24 GCal/m^2 consumption of heat in budgetary organizations by 2022. Finally, the new amendments will help reduce uncertainty and improve transparency and accountability around GHG reductions and the achievement

of the NDC and energy intensity targets.

86. **Indicator**. Heat consumption in budgetary organizations. Baseline: 0.26 GCal/m^2 (2020). Target: 0.24 GCal/m^2 (2022).

87. **Next steps.** Implementation of the amendments will go a long way toward operationalizing the new monitoring system. Together with additional bylaws that set stricter energy performance standards for buildings and structures, the prior action will help Kazakhstan develop a more reliable and integrated trajectory toward meeting the country's NDC goals. Scaled up actions to address energy efficiency and energy saving measures across the economy will also be necessary. Under the Kazakhstan Energy Efficiency Project (KEEP), the World Bank has supported the completion of deep renovations in nearly 100 budget sector buildings across all oblasts of Kazakhstan. Learning from the KEEP, new energy initiatives will include elements of digitization. Possible models for industrial decarbonization are also being explored, with analytical work supported by ESMAP's industrial decarbonization funding. The Bank has also completed a broad survey of geothermal resources in the country and is engaged in completing the legal review and the technical pre-feasibility studies to inform policymakers on options for "greening" the heating sector through use of geothermal resources in Almaty and Turkestan. Through the CCDR, as well as the other analytical work already underway, the Bank will inform policy improvements in energy efficiency of state-owned and budget sector enterprises, by taking a deeper look at benchmarking energy consumption in budget sector buildings and key industry segments.

Prior Action #7. To strengthen the Emission Trading Scheme (ETS), a key instrument for meeting Kazakhstan's NDC commitment to reduce GHG emissions, the Borrower has: (a) Adopted a requirement to allocate emission allowances by benchmarking the emission intensity of production process for all enterprises under the ETS; and (b) Strengthened the operation of the ETS with regard to the trade in carbon units and the operation of the carbon unit registry.

88. **Rationale.** Kazakhstan is the largest GHG emitter in Central Asia and the 29th largest globally (2019). The country's NDC has an ambitious target under the Paris Agreement to reduce GHG emissions by 15 percent (unconditional) to 25 percent (conditional) from the 1990 level by 2030. Kazakhstan's Emission Trading Scheme (ETS)—the first in the region—has been operating since 2013 with a pause in 2016–17. About 40 percent of total GHG emissions, for more than 200 installations emitting more than 20,000 tCO_2 each per year, are regulated under the national ETS.[45,46] However, national emissions have steadily increased since 2013 and are now above the 1990 baseline, posing a significant challenge to Kazakhstan in meeting its NDC commitment. Contributing factors include: the process for allocating emission allowances under previous National Allocation Plans (NAPs), that set caps on emissions close to, or even above, the historical emission levels of some of the regulated emitters; and the scope of the ETS instrument that does not regulate emissions from smaller installations, transport, and agriculture accounting for about 60 percent of total GHG emissions.

89. In 2021, Kazakhstan has taken several steps toward reversing the future trend in emissions and strengthening ETS operations. Kazakhstan's NDC commitment was translated into legislation through the new Environmental Code (supported under Prior Action #9), which sets a maximum permissible volume of total national CO_2 emissions ('carbon budget') for carbon budgeting periods of five years starting in 2021 (including

[45] Operated by Zhasyl Damu JSC under the Ministry of Ecology, Geology, and Natural Resources (MEGNR).
[46] Energy sector (including oil and gas), mining, metallurgy and chemical industry, processing (production of building materials: cement, lime, gypsum, and brick) (>20,000 t CO_2/year).

both ETS and non-ETS sectors),[47] and requiring a benchmarking approach to allocate emission allowances to ETS installations based on the emission intensity of production processes rather than historical emissions.[48] This is consistent with the practice in the EU ETS.

90. In 2021, two regulations ('bylaws') were adopted to strengthen ETS rules for trading and maintaining the carbon registry. Two other regulations were also introduced to strengthen ETS rules for carbon offsets, and for validation and verification. Kazakhstan also drafted an updated NDC and NDC Implementation Roadmap that are expected to be adopted by the UNFCCC Conference of Parties (COP26) in November 2021. The draft updated NDC and roadmap that are under consultation within government and were supported by the World Bank's Partnership for Market Readiness (PMR) and other international partners, indicate that significantly strengthened actions are needed to meet the NDC commitment. These include progressively tightening the ETS cap; introducing carbon taxes for non-ETS sectors such as transport; facilitating renewable energy development; improving energy efficiency; and applying a circular economy approach for waste management.

91. **Substance of the prior action.** With the Environmental Code entering into force on July 1, 2021, this is a transitional year marked by the country's fragile economic recovery from the COVID-19 pandemic. The Environmental Code requires the carbon budget for 2021–2025 to be developed and approved by the end of 2021. This operation supports the transition in the design of ETS NAPs to allocate emission allowances for all ETS installations based on a benchmarking method, and bylaws to strengthen ETS operations. These are necessary foundational steps to enable gradual tightening of emission caps for ETS-covered entities over 2022–2030 (under NAP5 and NAP6) and enable effective contributions from the ETS to the 2030 national NDC target.

92. Using a benchmarking approach to allocate allowances to all ETS enterprises based on the emission intensity of production will reward efficient enterprises and will allow for an easier inclusion of new enterprises into the ETS. Benchmarking is consistent with the approach used in the EU ETS. In the past, NAP1 (2013) and the NAP2 (2015–2015) allocated emissions based on historical emission levels, which rewarded firms that had high emissions levels. The NAP3 (2018–2020) used a hybrid approach based on historical emissions and benchmarking, with enterprises selecting the method they preferred.

93. Beyond benchmarking, the authorities have stressed the urgent need for Kazakhstan to improve the ETS system for monitoring, reporting, and verification (MRV) by updating methodological tools and enhancing existing validation and verification processes. Tighter emission caps under the NAP5 (2022–2025) and the NAP6 (2026–2030) will drive an increase in the price of carbon units over time. The bylaws of the ETS, in the areas reflected in this prior action, should help strengthen the ETS' operations to trade, and record offset units. As of September 15, 2021, the Rules for Maintaining the State Register of Carbon Units and the Rules for Trading in Carbon Units have been approved by a ministerial order from the MEGNR and disclosed. In addition to these two approved bylaws, the authorities are working to approve and disclose, Rules on Carbon Offsets and Rules for Carrying out Validation and Verification. Online public consultations on these bylaws were held during March 1–

[47] Environmental Code, Article 286 sets the carbon budget periods for five years starting in 2021–25. The carbon budget for 2021 should be at least 1.5 percent below the 1990 carbon budget and reduced in subsequent years by at least 1.5 percent annually compared to the previous year's carbon budget up to 2030. After 2030, the annual budget should be at least 15% below the 1990 carbon budget.

[48] Environment Code, Article 290(2) and 291. Carbon allowances for installations are based on benchmarks—a specific volume of GHG emissions subject to allowances per production unit–in regulated economic sectors. Fifty-two benchmarks were approved in 2017 (https://adilet.zan.kz/rus/docs/V1700015396).

17, 2021.

94. **Expected results.** The bylaws supported by this prior action will strengthen the operation of the ETS, providing clarity on the rules related to the trade and registration of carbon units. Completing the approval process for the remaining two bylaws will also be needed to enable enterprises to engage in the delivery and trading of carbon offset projects. Collectively, these bylaws can have a significant impact in strengthening the operation of the ETS. In the coming 18 months, the MEGNR will increase the capacity of enterprises to engage in offset projects through targeted training on the relevant ETS bylaws in at least three of the seven emission sectors under the NDC, and by developing methodologies for carbon offset projects. This will enable enterprises to successfully submit offset projects for assessment by the MEGNR, and on approval to open accounts in the registry. Following project completion, offset projects will be subject to validation and verification before accounts are credited with offset units to enable trading.

95. **Indicator.** Accounts opened to register carbon offset projects in the carbon registry. Baseline: 0 (2021). Target: 10 (March 2023).

96. **Next steps.** The forthcoming National Allocation Plan for 2022–2025 (NAP5), which should be approved in December 2021 following consultation with affected enterprises, and NAP6 (for 2026–2030) that will follow are expected to adopt progressively tighter emission quotas to reduce the emissions in the sectors covered by the ETS. There is a consensus that further work is required to deepen the use of the ETS as a key mechanism to achieve the NDC targets alongside the removal of subsidies, introduction of a carbon tax, and efforts to decarbonize the energy sector, among other measures.

97. The Government plans to adopt key policies and reforms identified in its draft updated NDC and draft implementation roadmap, including: strengthening of the ETS so it can play a central role in the national mitigation strategy; expanded coverage of carbon pricing, for example, by introducing a carbon tax for non-ETS sectors such as transport; increasing renewable energy capacity; improving energy efficiency; developing a pipeline of decarbonization projects; mobilizing private financing; and applying circular economy principles.

98. The World Bank is well placed to support the Government with these reforms. Collaboration between the World Bank and Kazakhstan on carbon pricing is expected to continue through the Partnership for Market Implementation (PMI) program. The Bank also envisages additional support for NDC implementation in the near-term including a CCDR, technical assistance for the implementation of the Environmental Code, and energy sector engagement. In parallel, Kazakhstan is developing a Doctrine (strategy) for Achieving Carbon Neutrality of the Republic of Kazakhstan until 2060 with support from the GIZ. This doctrine will provide strategic directions on pathways to realize this transition around mid-century, including the transition from fossil fuels, and may have implications for the NDC in the medium term. Public consultations on the doctrine took place between September 14 and 22, 2021. The doctrine is being prepared by a high-level, cross ministerial working group chaired by the Deputy Prime Minister. Further sectoral analysis to develop implementation roadmaps will also be required. The EBRD signed a memorandum of understanding with the Ministry of Energy in March 2021 to provide support on long-term decarbonization of the electricity sector and work is expected to start in September 2021.

Prior Action #8. To increase the installed capacity of renewable energy generation, the Borrower has adopted amendments to the Renewable Energy legislation of July 4, 2009 (No. 165-IV) that: (a) Established procedures to determine monetary support for the use of renewable energy sources, starting from July 1, 2021; (b) Enables state financial support to the Financial and Settlement Center of Renewable Energy in case it is unable to fulfill its financial obligations; (c) Enabled contracts for the purchase of electricity for a period of 20-year based on the auctions held after January 1, 2021; and (d) Adopted rules for waste-to-energy auctions, including determining the maximum auction prices and a model contract for waste-to-energy projects.

99. **Rationale.** Aging coal-fired plants supply 65 percent of the country's electricity, using inexpensive and plentiful domestic coal; this compares with 38 percent globally, according to the IEA. As the country's coal plants reach the end of their useful lives, clean affordable alternatives must be found that do not strain the government budget. The authorities aim to provide viable alternatives to fossil-based generation in a phased manner, by preparing the right enabling environment for private investments in renewables through establishing and scaling up competitive auctions to obtain the best priced renewable energy. The authorities plan to increase the share of wind, solar, small hydropower, and waste-to-energy in the energy mix from 3 percent at present to at least 10 percent by 2030. These numbers compare with a share of renewables of 7.2 percent in the global electricity production in 2018, 8 percent share in Azerbaijan in 2018, and 9 percent share in Ukraine in 2020.

100. Reaching the 2030 renewables target will require a focused approach on developing the country's solar and wind resources, alongside enhancing the grid flexibility to facilitate absorption of more renewables in the generation mix. The Government has plans to introduce more flexibility into the grid using gas-fired plants, which will also allow for greater grid resilience. The use of appropriately structured PPAs for scaled-up renewables' auctions will ensure proper sharing of project risks between public and private sector partners. Such PPAs are critical for bringing in investments into this sector on competitive terms, thus keeping clean renewable power affordable. Increased private sector investments in renewables, including through public-private partnerships (PPPs), will help move the country closer to achieving its decarbonization targets.

101. In parallel, life extensions are being considered by the Ministry of Energy (MoE) for coal-fired plants with cumulative capacity of about 2,400MW. However, the plan for only one 500MW plant has been approved. The domestic price for coal for power generation is about US$13/ton in Kazakhstan and about US$36/ton in the United States. Part of the price difference is an implicit subsidy that does not include the cost of GHG emissions, and the low input prices directly impact the competitiveness of renewable and other low-carbon alternatives. Despite this, under current conditions, the price of electricity generated by renewables through auctions is only about US¢2/kWh higher than the price of electricity generated by legacy coal plants. The GIZ already has a study underway, charting different technology scenarios and their effect on decarbonization of the economy. Building upon this the Bank's CCDR under preparation will analyze policy measures such as higher carbon pricing and their effect on renewable energy competitiveness. This will help inform a lower carbon path to development, that is aligned with the NDC commitment of carbon neutrality by 2060.

102. Additionally, the tariff-setting system in Kazakhstan is complex and subject to significant discretionary actions without analytical backing. Large enterprises and municipalities have average power tariffs that are 80 and 150 percent of household tariffs, respectively. This large cross-subsidy is likely unsustainable as large enterprises, that consume about 55 percent of the electricity produced in Kazakhstan, can procure power through bilateral contracts, and avoid the higher tariffs. Currently MoE provides marginal electricity tariffs for generators across the country and estimates average electricity tariffs for 15 zones in Kazakhstan. These tariffs are then reviewed and approved by the Committee for Regulation of Natural Monopolies (CRNM) under the Ministry of National Economy (MNE). This lack of independence results in a tariff setting that does not ensure

the long-term financial sustainability of the sector. A professionally managed and reasonably autonomous regulatory institution is crucial to attract investors to the sector and realize the high potential of renewables. With greater transparency and independence in rate-setting practices, renewables will become more competitive against other alternatives in a world that properly prices in GHG emissions.

103. The domestic price for coal for power generation is about US$13/ton in Kazakhstan and about US$36/ton in the United States. Part of the price difference can be assumed to be a subsidy. Low input prices directly impact the competitiveness of renewable alternatives and even natural gas. Moreover, about 55 percent of the electricity produced in Kazakhstan is consumed by large enterprises that procure most of it through bilateral contracts.

104. The tariff-setting system in Kazakhstan is complex and subject to significant discretionary actions without analytical backing. The MoE provides marginal electricity tariffs for generators across the country and also estimates average electricity tariffs for 15 zones in Kazakhstan. These tariffs are then reviewed and approved by the Committee for Regulation of Natural Monopolies (CRNM) under the Ministry of National Economy (MNE). This lack of independence results in a tariff setting that does not ensure the long-term financial sustainability of the sector. A professionally managed and reasonably autonomous regulatory institution is crucial to attracting investors to the sector, and realize the high potential of renewables. When there is greater transparency and independence in rate-setting practices, renewables will be able to compete against other alternatives. Key areas that the independent regulator could address include an emphasis on increased transparency around costs, subsidies, competition, and alignment of retail tariffs with the cost of wholesale power.

105. **Substance of the prior action.** The Law of the Republic of Kazakhstan "On Amendments and Additions to Certain Legislative Acts of the Republic of Kazakhstan on Supporting the Use of Renewable Energy Sources and Electricity" (dated December 7, 2020 No. 380-VI) improves the environment for scaling up renewable energy investments in the country, in line with the NDC goals. Specifically, (a) lays out the rules for computing renewable energy surcharges to end-consumer billing to ensure availability of sufficient revenues to pay for renewable energy procured through competitive auctions. Point (b) provides for state support to renewable energy suppliers in case revenues from the surcharges levied are insufficient. The experience gained from this should also inform rate-setting practices for the 15 zones mentioned earlier, such that fiscal liabilities are kept in check. Point (c) facilitates the signing of longer term PPAs that in turn allow for longer term financing and more affordable pricing through auctions. Finally, point (d) lays out the rules for inclusion of waste-to-energy methodology and PPA terms for procurement through auctions. Cumulatively, points (a), (b), and (c) strengthen the financial underpinnings for procuring affordable renewable energy through auctions, while point (d) expands the scope of auctions by including waste-to-energy. Points (a) and (b) are essential for ensuring proper and timely payment to private sector investors in renewables. These points will provide an impetus for private investments by alleviating the key payment risk. Additionally, (a) and (c) also help in keeping the price of power affordable by calibrating how much renewables should come in, and by matching closely the useful life of RE assets with the PPA term. This, in turn, allows for longer-term financing and spreading of the repayment burden.

106. **Expected Results.** The reforms supported by this operation are likely to lead to broad progress on the two transitions and, in turn, to more private investments in renewable energy, including from international developers with expertise in much larger scale renewable plants (e.g., over 1,00MW of wind or solar). The reform momentum and the authorities' commitment, supported by Bank technical assistance, should help encourage the introduction of energy storage technologies that would lead to a more maneuverable and flexible grid.

Overall, these amendments will also lead to a reduction in GHG emissions from 2020 levels and a more resilient grid. They will provide the foundations for the more significant energy transformation that will be needed to support a carbon-neutral economy by 2060.

107. **Indicator.** Renewable energy capacity. Baseline: 1,635 MW (2020). Target: 2,400 MW (2022).

108. **Next steps.** As the renewables' contribution in the energy mix increases, additional legislative work is already under discussion for developing a more flexible electricity grid and the adoption of energy storage technologies that will allow greater penetration of renewables. By focusing on assured payment for competitively procured renewables and more advanced PPAs that restrict variance from renewable plants, the new legislation will seek to raise the profile of renewables as an alternative to coal-fired plants, while also keeping renewable power within an affordable range. A more autonomous regulator with enhanced analytical capacity will be a positive for attracting investors, and further steps in this area are needed. In parallel, the Government is working on the Concept Heating Law that also will focus comprehensively on the heating sector, and lead to bylaws that will increase efficiency norms for heating. Together, these next steps will help green the country's power sector. The World Bank is engaging with other development partners, including the GIZ, the EBRD, the ADB, and the USAID to coordinate resources and efforts in charting and implementing a plan for scaling up renewable energy development. This operation and the CCDR are effective tools in deepening this dialogue with the government.

Prior Action #9. To protect, conserve, and restore the environment, the Borrower has adopted legislation that introduces requirements for : (a) Permits and reporting on emissions from facilities with a harmful impact on the environment, including flaring and venting of associated gas, with administrative penalties for misreporting and for exceeding permitted limits; (b) Applying reference books on Best Available Techniques (BATs) to prevent pollution and minimize anthropogenic impacts on the environment in selected economic sectors; (c) Mandatory strategic environmental assessment (SEA) of government projects and the territorial development program; and (d) Climate vulnerability assessment and adaptation planning for agriculture, water management, forestry, and civil protection.

109. **Rationale.** The global community is aiming toward a "green" economic transition that equates to a growing respect for the environment; recognition of the imperative to mitigate and adapt to climate change; and their joint importance for ensuring the health and resilience of people, communities, and the economy.[49] Kazakhstan's approach to building back in a more sustainable and greener fashion is aligned with that of the global community. Kazakhstan adopted its first post-independence Environmental Code in 2007 with the aim to protect the environment. Despite some positive sectoral results, the environmental situation remains critical, with environmental pollution at a high level and a lack of economic incentives for reducing environmental pollution.[50] The 2013 Presidential Decree on the transition of Kazakhstan to a green economy by 2050 and the country's 2020 pledge to reach carbon neutrality by 2060 are some of the policy actions that laid the foundation for updating and strengthening the Environmental Code. Following recommendations by the OECD, Kazakhstan introduced considerable changes into the 2021 Code. Several new provisions were inspired by the European Union environmental legislation. The new Code was adopted on January 2, 2021, and came into force on July 1, 2021. This Code significantly strengthens and extends the ambition and scope of Kazakhstan's environmental legislation by extending the focus from the protection of the environment to also include its preservation and

[49] https://www.devcommittee.org/sites/dc/files/download/Communiques/2021-04/Communique%28E%29%20final%20version%204.9.pdf
[50] Kazakhstan Environmental Performance Reviews – Third Review, UNECE 2019.

restoration. It introduces measures to translate Kazakhstan's NDC commitment into legislation, strengthen the allocation of emission allowances in the ETS, address climate change mitigation and adaptation, stimulate green investments, and it emphasizes the sustainable management of natural resources. The new Code also applies the 'polluter pays' principle while ensuring a favorable environment for human life and health.

110. **The Code addresses reporting on associated gas flaring and venting.** Kazakhstan is among the top 20 flaring countries in the world: about 0.6 billion cubic meters of gas was wastefully flared in 2019 according to official sources.[51] Reducing gas flaring and venting from oil and gas production has been identified as one of the most promising emission reduction opportunities in the country and will be important to realize Kazakhstan's NDC. Flaring volumes declined by 25 percent from 2014 to 2019 but they still remain elevated.[52] It is important to promote more transparency and accountability on flaring and venting emissions.

111. **Substance of the prior action.** The Environmental Code provides the legal framework, objectives, principles, and mechanisms for the implementation of a unified government environmental policy in Kazakhstan. The provisions of the Code have been developed in line with the environmental objectives of the EU. In 2021, the MEGNR plans to develop and introduce about 150 bylaws to implement the provisions of the Code. As of September 15, 94 bylaws have been approved by Order if the Minister of Ecology and/or government resolution.[53] In parallel, the Supreme Council of Reforms aims to introduce a Green Kazakhstan National Project in the second half of 2021 that outlines a five-year plan, aligned with the Environmental Code, and supported by a results framework and budget at the national and local levels. The goal of the Project is to reduce air pollution, support effective waste management and landscape restoration, enhance eco-education, and improve environmental culture, among other things.

112. The new Code mandates that owners of natural resources make accurate, timely reports on emissions, including flaring and venting of associated gas, and face substantial monetary penalties for misreporting. In addition, the Code introduces requirements to minimize gas flaring and the use of best available technology. The development of a necessary regulatory framework on monitoring and reporting is a critical first step to improve transparency on reported emissions, including flaring and venting volumes. Enhanced reporting and monitoring in association with existing monetary penalties, specifically on flaring emissions, will stimulate a further flaring reduction in Kazakhstan.[54] The Bank team intends to support further improvement in transparency and accountability on emissions reporting by facilitating collaboration between the MEGNR, MoE, and the WBG to compare reported data (by operators) with the satellite data (from the World Bank GGFR team) and to conduct satellite surveys of the key locations in Kazakhstan for detection of methane leakages in the country.

113. The legal regime for large industrial facilities that have the most significant environmental impact will be

---

[51] The latest satellite estimates from the World Bank-managed Global Gas Flaring Reduction Partnership suggests the amount of flaring was about 1.6 billion cubic meters in 2019, down from 3.9 billion cubic meters in 2014. *https://www.canadianenergycentre.ca/wp-content/uploads/2021/04/CEC-FS-31-Gas-Flaring-2021-FINAL.pdf.*

[52] World Bank estimates suggests a higher reduction of flaring volume of 60 percent from 2014 to 2019.

[53] https://www.gov.kz/memleket/entities/ecogeo/documents/1?directions=14691&lang=ru

[54] The largest environmental payments result from lawsuits that are brought by the environmental authorities against the major oil and gas projects and concern the gas flaring claims. In 2016, Karachaganak Petroleum Operating Company, which operates one of the largest fields in the world (the Karachaganak field located in West Kazakhstan Oblast), was ordered to pay a fine of 526 million tenge (over US$1.5 million) for releasing pollutants into the atmosphere. In 2011, fines equal to US$11.5 million were imposed on the Tengiz oil field operator for gas flaring (Reference: *UNECE).* In the US, violating the federal requirements for flares can result in a penalty of up to $37,500 per violation, per day (https://www.epa.gov/sites/production/files/documents/flaringviolations.pdf).

toughened under the new Code. Mandatory environmental permits with emission standards and controls will be required to operate facilities classified as having a harmful effect on the environment. Pollution charges will be introduced for exceeding permit limits, and compulsory environmental insurance will also be required for environmentally hazardous activities. It is expected that the 50 largest companies that account for 80 percent of emissions in Kazakhstan will replace their old technologies with best available technologies (BATs) by 2025 when a national standard on BATs to prevent environmental pollution and minimize and control anthropogenic impacts on the environment will be in place. The Code will bring air pollutant emission standards for large combustion plants to par with those of the EU; and establish a national policy on air protection with specific sectoral and municipal air quality programs. It requires waste generators and owners to apply the waste hierarchy principle to prevent waste generation and manage waste in a descending order of prevention/reduction, reuse, recycle and disposal, which is in line with the circular economy principles.

114. Other key changes in the Code, to improve sustainability and combat climate change, include designating a Green Technology Service Operator to promote green projects and foster green investments including through business incubation services. Strategic environmental assessment (SEA) will be mandatory for key government programs to assess significant environmental impacts, examine reasonable alternatives, and consult stakeholders. The Code improves the legal regime for climate mitigation and adaptation, translating the NDC commitment into law and strengthening systems for allocating emission allowances under the ETS (see Prior Action 2), and prioritizing climate vulnerability assessment and adaptation planning for agriculture, water management, forestry, and civil protection. Measures to improve awareness of climate change, and strengthen research and monitoring are also introduced.

115. **Expected results.** While the Environmental Code will provide the basis for a green transition including GHG mitigation, enhanced adaptation to climate change in vulnerable sectors, and more sustainable natural resource management, most impacts from adoption of the Environmental Code will be realized in the medium to longer term as associated regulations get adopted, guidelines developed, and provisions are implemented. This operation has opened dialogue on implementation of the Code which will determine the ultimate extent of the Code's ambition and impact. The national green Kazakhstan program will provide a five-year implementation framework aligned with the Code. Among the results that can be achieved in a shorter time period is the accurate monitoring and reporting of emissions that would result in reducing uncertainty and improving transparency and accountability on flaring and venting emissions. This will lead to better governance and provide a more leveled playing field. Measures are expected to initiate planning for BATs and SEAs, establish the green technology service operator, and advance adaptation planning. In particular, related to the indicators below, Article 274 (4) of the Environmental Code focuses on requirements to minimize gas flaring as a major source of emissions.

116. **Indicators.** (a) Percentage reduction in flaring volume from year 2014 (4.0 bcm). Baseline: 25% (December 2019) Target: 50% (December 2022); (b) Green technology service operator established and staffed to provide business incubation services. Baseline: Not established (2021). Target: Established (2022); (c) Strategic Environmental Assessment initiated for Government programs launched after July 1, 2021. Baseline: 0 (2020) Target: 10 percent of all government programs (2022).

117. **Next steps.** With the new Environmental Code in force, the authorities' efforts are focusing on preparing and adopting the bylaws needed for its effective implementation and developing a taxonomy of green projects in line with the government's NDP 2025 and the concept for a green transition. The borrower will adopt a National Project on Green Kazakhstan in the coming months as an umbrella program, aligned with the

Environmental Code, to implement actions at the national and local level over the next five years. Follow-up actions will be required to ensure the effective implementation of adopted bylaws and the national program Green Kazakhstan. The full implementation and ultimate impact of the Code will take time, based on the experience of other countries.[55, 56] The World Bank is well-positioned to support this through ongoing analytical and advisory support, including on: national air pollution study and deep dive assessment on cost-effective implementation policies and measures in Nur Sultan and Almaty (in progress); circular economy assessment and roadmap for the construction sector (in progress); landscape and forest restoration under Global Environment Facility Grant and RESILAND program (signed on July 9, 2021); ETS and NDC support under the Partnership for Market Readiness and expected follow-on support for their implementation through the Partnership for Market Implementation (under discussion); and Kazakhstan's forthcoming Country Climate and Development Report (CCDR) that was initiated in July 2021. This body of analysis can also support strengthened engagement on implementation and measurement of the impact of the new Environmental Code's adoption.

118. To implement the Code's mandate of timely and accurate reporting of flaring and venting of associated gases, the authorities will need to create an automated monitoring system. Monitoring needs to be accompanied by reconciliation of the operators' reported flared volumes with World Bank satellite data on both flaring and. The World Bank's Zero Routine Flaring by 2030 initiative has been endorsed by the Kazakhstan government, KazMunayGaz, and KazPetrol Group. Additionally, the authorities plan to provide annual reporting of flaring data consistent with their endorsement of World Bank's Zero Routine Flaring by 2030 initiative.

Table 5. DPF Prior Actions and Analytical Underpinnings

Prior Actions	Analytical Underpinnings
Operation Pillar 1: Support a more competitive economy driven by a more vibrant private sector and accountable public sector.	
Prior Action #1 on competition policy	The IFC and World Bank report on *Creating Markets in Kazakhstan: Country Private Sector Diagnostic (2017)* and OECD's *Reforming Kazakhstan: Progress, Challenges and Opportunities (2016)* underlines the need for a more effective competition policy and having an independent competition agency to improve the level playing field for the private sector. The World Bank study on *Kazakhstan Priority Sectors: Competitiveness Study of Obstacles to the Diversification of Kazakhstan's Economy (2019)* stresses the need to reform the competition authority to have the capacity and operational independence to regulate market appropriately.
Prior Action #2 on telecommunications and digital economy	The World Bank RAS on *Technical Assistance in Digital Economy Regulatory Environment* Analysis benchmarked Kazakhstan's legal and regulatory frameworks for the digital economy against international practices. The Bank's *Assessment of the Digital Enabling Environment (2019)* recommends modernizing the legal and

[55] The World Bank has recently provided technical assistance to Ethiopia, Togo, Mauritania, Turkey, Indonesia, and Uzbekistan to support environmental legal reforms, including on changes related to climate change and environmental impact assessment, and in the context of development policy operations.
[56] In addition, time will be needed to prepare, consult, and adopt implementing regulations (bylaws) and have them enter into force. Once bylaws are in effect, in some cases time is allowed for judicial challenges to new regulations by industry or civil society, which can further delay their operationalization by several months or years.

	regulatory framework for the telecommunications sector in to adopting a best practices data protection legal framework.
Prior Action #3 on public procurement systems	The World Bank and OECD study on *Assessment of the Public Procurement Systems of the Republic of Kazakhstan and the Sovereign Wealth Fund Samruk-Kazyna (2019)* highlight gaps in the public procurement laws that contributes to the significantly high level of single-source sourcing and the cumbersome process in obtaining digital signature that limits participation of foreign bidders.
Prior Action #4 on financial stability	An internal assessment by the World Bank, *Kazakhstan Financial Sector Monitoring Note (2020)* highlights the need for the AFR to promptly resolve banks with regulatory deficiencies to restore market discipline, competition, and lending to productive firms.
Prior Action #5 on anti-corruption	The OECD report on *Anti-corruption Reforms in Kazakhstan: Fourth Round of Monitoring of the Istanbul Anti-Corruption Action Plan (2017)* recommends extending the notion of public officials in the legislation on combating legalization of criminally received proceeds to the national officials performing important public functions, heads of state enterprises, their family members, and leading officials of political parties.
Operation Pillar 2: Lay the foundation for a more sustainable economic transition.	
Prior Action #6 on energy efficiency	World Bank analysis on *Energy Efficiency Transformation in Astana and Almaty (2017)* identifies the need to establish data collection and monitoring systems of energy use as key horizontal activities for implementing effective measures on energy efficiency.
Prior Action #7 on reducing GHG emission	The OECD study *Kazakhstan Multi-Dimensional Review (2017)* identifies underdeveloped regulations for conducting monitoring and verification of GHGs as one of the weaknesses of the ETS system. A joint study by the World Bank and the MEGNR under the Kazakhstan Partnership for Market Readiness (PMR) project recommends to further improve the ETS's MRV system and establish the rules for creation of offset units, the trade in offset units, and the operation of the unit registry, among other suggestions.
Prior Action #8 on renewable energy	The World Bank study *Stuck in Transition: Reform Experiences and Challenges Ahead in the Kazakhstan Power Sector (2017*), highlights the need for a well-functioning trading floor to integrate renewable energy into the wholesale market. UNDP's *De-risking Renewable Energy Investments (2018)* also highlights the improvement of PPA as one of key elements to reduce risks for private investors in the renewable energy.
Prior Action #9 on the Environmental Code	*OECD's Kazakhstan Multi-Dimensional Review (2017)* discusses gaps in the environmental legislation, such as weakness in setting environmental standards for adopting BAT, cumbersome permit processes for most economic activities, and the absence of "polluter pays" approach to emission and environmental damage. UNECE's study *Kazakhstan Environmental Performance Reviews (2019)* highlights the

	needs for implementing environmental permits, introducing a strategic environmental assessment as a tool to develop sound and coordinated sustainability policies that integrate climate change, strengthening the national legislation to specifically address air protection and supporting local authorities to draw up air pollution plans and programs, and creating effective incentives for waste reduction, and others.

4.3. LINK TO CPF, OTHER BANK OPERATIONS AND THE WBG STRATEGY

119. **The proposed operation is an important part of the World Bank Group's engagement in Kazakhstan and its focus on institutional strengthening, even though no DPF was planned before the COVID-19 outbreak.** The reforms under the proposed DPF are fully aligned with the 2020–2025 CPF underpinned by the 2018 SCD. The SCD stresses the need for Kazakhstan to implement a new development model to deliver more inclusive and sustainable growth. In that regard, the SCD highlights priority reform areas for markets to work efficiently and transparently; for human and natural capital to be more productive, and management of policy and natural wealth to build economic resilience and support environmental and growth sustainability. The SCD also puts improving the capacity of institutions to be more efficient and open as a cross-cutting area. This proposed DPF which, as required for all new IBRD financing under the CPF, supports institutional strengthening in a significant way, provides a unique opportunity to deepen the policy dialogue on those development priorities and further strengthen WBG partnership in Kazakhstan. In addition, the DPF meets all of the further selectivity criteria that each new lending operation should satisfy at least one of: (a) contribute to the inclusion/shared prosperity agenda; (b) improve conditions to attract private investments or mobilize additional resources (in the MFD mode); and (c) contribute to regional or global public goods.

120. **The CPF initially did not envisage policy-based lending, as the Government intended to use financing only sparsely and in support of specific sector programs.** The main tool for Bank reform support was through technical assistance (Joint Economic Research Program for economic and competitiveness reforms and Trust Funded activities such as the Partnership for Market Readiness and the RESILAND Program for Climate and Resilience reforms, respectively). Following the outbreak of the pandemic, the Government decided in late March 2020 to seek support from the World Bank to help advance its greener economic transition and a shift to a more competitive economy. This was confirmed after the President's address in September 2020 that led to the creation of the National Supreme Council of Reform and the Agency for Strategic Planning and Reform (also see Annex 5).

121. **The reforms supported by this operation are aligned with two of the three focus areas of the CPF.** They are focus area one (promoting inclusive growth) and focus area two (securing sustainable growth). To promote inclusive growth, this operation helps supports measures to improve the environment for private sector development through leveling the playing field for all enterprises, a more competitive and open public procurement system, and better functioning financial systems and markets. To help secure low-carbon growth, this operation is supporting the Government to strengthen the institutional capacity and regulatory foundations to improve energy efficiency, and promote more investments in renewable energy. Finally, this operation also supports the cross-cutting theme of the CPF, which is effective governance and strengthened market and social institution, by supporting reducing corruption in public institutions. Several reforms supported by this operation, including on the greener growth agenda, public procurement system, and the telecom sector, are laying the foundations for further DPF and project support Kazakhstan authorities in implementing its medium-term

development plan.

122. **The operation is aligned with parts of the Green, Resilient, Inclusive Development (GRID) approach but is not focused on implementing all its pillars.** The program supported by the DPF should help mobilize private capital at scale and help support stronger macroeconomic fundamentals and the institutional foundations of the economy, two of the cross-cutting areas of the GRID.

4.4. CONSULTATIONS AND COLLABORATION WITH DEVELOPMENT PARTNERS

123. **Kazakhstan has a well-defined process for public consultation on new law concepts, new laws, and the engagement of civil society.** The government approves and publishes on an annual basis its legislative work plan. The two houses of Parliament place their annual plans along with information related to individual legal acts on their external internet portals. Thus, citizens have the opportunity to track the legislative acts that are expected to be developed and adopted every calendar year. The procedures for public hearings to discuss draft legislative acts at various levels are stipulated in several laws and regulations. The Law on Legal Acts (№ 480-V, 2016), for example, outlines the procedure for public consultations at the different stages of the lawmaking process. It stipulates that concepts of laws and drafts of legal acts must be placed for public consultations on a dedicated internet portal of legal acts (*https://legalacts.egov.kz*). If they affect the business environment or business entities, they have to be discussed with the National Chamber of Entrepreneurs of Kazakhstan (Atameken) and expert councils on private entrepreneurship issues. The Law of Public Councils (No. 383-V, 2015) outlines the procedure for public hearings on proposed legislative changes affect the rights and freedoms of citizens. Under the Law on Access to Information (No. 401, 2015), the Government also facilitates public hearing through the open government web portal.

124. **The legislative changes supported by this operation followed the established consultation process.** For example, drafts of the Environmental Code, the laws "*On procurement of individual subjects of quasi-public sector*," "*On amendments and additions to some legislative acts of the Republic of Kazakhstan on procurement of individual subjects of the quasi-public sector*," and "*On amendments and additions to some legislative acts on anticorruption issues*" were published for public comments and shared with the Atameken for expert opinion. Once the draft laws are approved, they are available in open portals such as http://adilet.zan.kz in Kazakh and Russian languages. Despite measures taken by the country in relation to transparency and increasing citizens' engagement, further improvements are needed to facilitate civil society's and other stakeholders' participation in the legislative process, including through capacity building. Comments from the public emphasize the need for more transparency of the legislative process.

125. **Reforms supported by this DPF have benefited from strong collaboration with other development partners.** The team has had a close dialogue with the ADB, the AFD, the EBRD, UNDP, and USAID on the policy reform agenda in energy efficiency and renewable energy. On environmental sustainability and climate change, the team is working closely with UNDP. The preparation of this DPF has also benefited from close coordination with the AFD. The team has also coordinated with OECD on improving the governance of SOEs and promoting private-sector-led growth, and with the ADB on their preparation for a policy-based lending. The Bank has worked closely with IFC on the private and financial sectors. On the latter, the Bank and IFC are collaborating to help the authorities establish a sustainable process for valuing and dealing with NPLs. The team has worked closely with the IMF, notably on the macroeconomic framework and the mix of macro policies and structural reforms to help support a stronger and more sustainable economic growth.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

126. **Private sector-led growth and the foundations for a more sustainable transition supported by the proposed operation are expected to improve the welfare of Kazakhstan's citizens.** The actions proposed under Pillar 1 will help foster a more competitive economy, increase public sector efficiency, and improve accountability. More transparent and efficient public procurement opens up additional fiscal space for social spending. Measures to reduce corruption and improve accountability can build citizens' confidence in government policies. Other actions under Pillar 1 aim to create better mechanisms to promote fair competition and attract private investment which are expected to provide better quality of goods and services, and promoting private sector-led growth and job creation, therefore bringing an overall medium- and long-term effect on poverty and shared prosperity. Most of the prior actions will have an indirect impact on poverty, shared prosperity, and welfare. The actions supported under Pillar 2 aim to reduce air pollution and set the framework for improving energy efficiency and protecting the environment. These are expected to improve the livelihood for all segments of the population, especially the vulnerable communities living in more industrialized and polluted areas.

127. **While some of the prior actions proposed in this DPF are expected to have minimum negative social and distributional impacts in the short term, they are likely to have a positive impact on people's wellbeing in the medium and long term.** PA#1, PA #3 and PA#5 are not expected to have immediate effects on poverty. The promotion of a competitive and private sector-led economy under PA#1 is expected to improve the quality and perhaps lower the prices of goods and services that will benefit consumers. In addition, it will likely create more and better paid jobs in the long run. More transparent and efficient public procurement supported by PA #3 and anti-corruption measures under PA #5 can reduce the burden on the budget, providing more resources for education, health, and social protection. In addition, these two actions could significantly help boost the citizens' confidence in government; less than half of the population currently believe that the Government does enough to fight corruption. Although the steps taken to resolve two banks under PA#4 may translate into unemployment for some employees, the overall implication for poverty is expected to be negligible because of the very small number of workers affected. As of December 2019, there were fewer than 800 employees employed by both banks. As formal employees, workers of those two banks are eligible for unemployment benefit from the State Social Insurance Fund.[57] In the medium and long term, these actions are envisioned to help reduce poverty and have a positive social impact. Finally, all these actions should also create additional fiscal space for pro-poor spending, including through better social protection, which is expected to help reduce poverty over the medium and long term.

128. **Prior Action #5 could have negative social impacts.** The engagement of civil society in oversight and accountability roles is still nascent in Kazakhstan. As a result, until systems have been developed, civil society groups and media may face challenges or scrutiny when providing oversight of the implementation of these

[57] The size and payment period are calculated individually depending on the salary and the length of formal employment. They last for six months (for an individual formally employed for 60 months) and should not exceed 40 percent of the average monthly salary for the previous two years). To be eligible for the unemployment benefits, workers need to be officially registered as unemployed.

reforms. Whistleblowers may face negative social consequences, citizens may be unwilling to get involved in providing oversight, and there may be a lack of transparency and access to justice for those prosecuted. To mitigate these impacts, there is a need for the Government to create genuine and safe spaces for citizen engagement in the reform through: (i) high levels of transparency and flows of information; (ii) the development of existing and digital mechanisms that enable open dialogue on the reform process and policies, and feedback on implementation; and (iii) joint capacity building for government and civil society, including the media.

129. **The actions supported under Pillar 2 aim to strengthen the policy framework to reduce pollution and the carbon footprint, and promote energy efficiency, with an expected positive impact on people's wellbeing in the medium and long term.** The country continues to face increasing exposure to climate change through rising temperatures, frequent and intense droughts, and floods that could severely affect the livelihood of the people. Moreover, global evidence suggests that climate change represents a significant challenge to poverty reduction as it disproportionally affects poor people in low-income communities. The amendments to the Energy Efficiency Legislation in PA #6 provide stronger mechanisms to monitor enterprises' energy consumption and improve energy efficiency. Its requirement for annual reports and appointment of energy management specialists may increase operational costs for both public and private enterprises but this additional cost is unlikely to be substantial for firms to lay off workers or to pass the costs to customers. The adoption of legislation in PA#8 and PA#9 aims to reduce the economy's carbon footprint and protect the environment by introducing strategic environmental assessment of government programs, reporting on industrial emissions, and climate vulnerability assessment and adaptation planning for agriculture, water management, forestry, and others. These actions together will be beneficial for both human and economic health and productivity. Those benefits will be particularly important for the poor and vulnerable, whether they live near industrial sites or in rural areas, as they often have less voice and fewer means to cope with pollution or build resilience to climate change.

130. **In the short term, PA #6 could have short-term negative social impacts if the monitoring causes social facilities, including health clinics and schools, to reduce heating or electricity.** As energy efficiency cannot be achieved without necessary renovation of buildings, some social facilities may be obliged to reduce the energy consumption in public buildings. There is a need for careful monitoring by users and the Government for these negative impacts.

131. **Prior Action #8 will enable balancing significant regional disparities in power generation, consumption, and demand.** About 80 percent of electricity is produced in the northern parts of Kazakhstan closer to the coal mines. Establishing auction pricing methodologies and standard PPA regimes for renewable energy generation under PA#3 may address disparities in generating capacity in the southern regions by stimulating private sector investments in renewables through PPPs. Southern Kazakhstan, which accounts for half of the country's population, may see an increase in electricity capacity, bringing generation closer to the consumers. In the medium to long term, PA#8 is expected to have positive direct and indirect social and economic impacts by: (a) creating jobs in renewable energy and associated constructions, material and spare part production, supply, and services; (b) improving agricultural productivity and creating value chain opportunities; and (c) improving the sustainability of irrigation water management and drinking water supply and sanitation. However, in the short term, there are potential social impacts of PA#8 related to land acquisition and economic displacement. Though, potential impacts on current land use from investments in renewable power generation plants may not be avoidable, they can be mitigated through compensatory measures. Some of the economically displaced families may not be able to continue their former work which may lead to unemployment and increasing vulnerability. Targeted social assistance system has the potential can support these families in the short-term. The State

Program of Productive Employment and Mass Entrepreneurship Development (Enbek) has the potential to promoting productive employment and engaging citizens in entrepreneurship. It aims to expand vocational education to less skilled and unemployed individuals. Moreover, mobile employment centers can help skills activation policies of more vulnerable individuals. In addition, potential risks related to negative environmental and social impacts from these investments will also be mitigated through this operation by supporting proper institutional building for the sector which follows international best practices along with strengthening of related broader country systems, as through the implementation of the 2021 Environmental Code as discussed below.

132. **Change in policy requirements for emission standards under PA#9 may potentially result in some negative impacts on Kazakhstan wellbeing through prices and employment.** Requirements for permits with emission standards, monetary penalties for violations, and compulsory environmental insurance may result in cost increase for firms that can fully or partially be transferred to customers through rising prices and/or cause firms to scale back their workforce. An Integrated Environment Permit is required for facilities with harmful environmental activities in Category I, which includes enterprises in many important sectors of the economy, including energy, production and processing of metal, mineral industry, chemical industry, waste management, and food industry. An environmental impact permit is required for facilities in Category II, e.g., non-metallic mineral products, electricity, gas, steam, and others. These permits cover environmental conditions for carrying out activities and using best available techniques for certain technological processes. Information on firms being affected (such as size of operations and number of employees) and additional costs to firms (such as costs of technological changes, strictness of the environmental permit, penalties for violator and compulsory environmental insurance) are not yet available. While the permit-associated costs to firms are not yet clear, the number of firms in affected industries is likely to be large over the medium term. These costs could have negative employment implications for workers. There is need for the Government to monitor these impacts and to address job losses with social assistance, including the existing channels of unemployment support and vocational skills training. The Government has the capacity and necessary mechanisms to manage the potential negative impacts on employment. As proved during the financial crisis in 2015–2016 and the COVID-19 pandemic in 2020–2021, the Government acted swiftly to counter the substantial impact of pandemic with a large and well-targeted fiscal package. The Government has also been strengthening their capacity to support poor and vulnerable households. The currently piloted conditional cash transfer program (Orleu) can improve labor market outcomes for poor and vulnerable families, while also promoting labor market activation rather than long-term dependency on social safety nets.

133. **Several prior actions can potentially promote gender equality and aligned with Kazakhstan's policies to promote gender equality.**[58] Several reforms supported by this DPF are expected to improve upstream activities and policy framework that can have positive impact on gender equality.[59] They are also aligned with the Concept for Family and Gender Policy 2030 which aims to address key gender gaps, including access to services and ability to perform entrepreneurial activities. For example, PA #2 on strengthening the telecommunication sector might help improve access to the internet for women and girls in remote areas. In 2021, Kazakhstan ranks 50th out of 120 countries with available data on gender gaps in internet access, and 62nd in the Inclusive Internet Index.[60] Amendments to the legislation on digital technologies to simplify the requirements, promote investments, protect personal data, and reduce internet fees could not only extend internet coverage but also have internet access more affordable to low-income families and vulnerable groups, including women and girls. PA #3 on open

[58] The Concept of Family and Gender Policies in the Republic of Kazakhstan until 2030.
[59] The team has been exploring potential options with the Gender Focal Points to link gender gaps with related results indicators.
[60] https://theinclusiveinternet.eiu.com/explore/countries/KZ/performance/indicators/availability/usage/gender-gap-in-internet-access

competition, transparency and accountability in public procurement could potentially provide more opportunities for women-owned companies to bid for public contracts where they are likely to face more challenges in accessing information and business connection. In today's global economy, women-owned businesses account for less than 1 percent of spending by large businesses on suppliers despite representing more than one-third of all firms worldwide.[61] Other prior actions under Pillar 1 might help increase employment among women whose labor force participation is already some 10 percentage points lower than that of men.

134. **To realize the full potential of private development, countries need to ensure that men and women have equal access to economic opportunities.** Kazakhstan is classified as having "very high human development" according to the Gender Development Index (GDI). It is one of only 21 countries worldwide and the only one in Central Asia in which the female human development index is equal to or greater than that of the male score.[62] Despite a higher female human development index, UNDP's Gender Inequality Index finds that women in Kazakhstan are still not reaching their full human development potential due to greater inequalities across three dimensions: (i) reproductive health; (ii) empowerment, measured by educational attainment and political participation; and (iii) labor market participation.[63] Similarly, according to the 2021 World Bank report "*Women, Business and the Law*," women in Kazakhstan still face laws and regulations that restrict their economic opportunities. Kazakhstan scores 69.4 (out of 100), lower than the regional average observed across Europe and Central Asia (83.4). According to this report, Kazakh women still face discrimination when it comes to: laws affecting women's decisions to work, laws affecting women's pay, laws affecting women's work after having children, constraints on women's starting and running a business, and regulations affecting the size of women's pension. For example, there are no applicable provisions in the current legislation prohibiting discrimination in access to credit based on gender. Likewise, the legislation does not mandate equal remuneration for work of equal value. Such a restrictive environment might be impacting the entrepreneurial performance of female-managed businesses and inhibiting female labor participation.

5.2. ENVIRONMENTAL, FORESTS, AND OTHER NATURAL RESOURCE ASPECTS

135. **Prior actions supported by this operation are expected to have significant positive effects on the environment, forests, and other natural resources.** The prior actions under the first pillar focus on a more competitive private sector and a more accountable public sector which will help promote more sustainable environmental practices as mandated by the new Environmental Code. The prior actions under the second pillar are expected to lay the foundations for a greener economy and each of them should improve the overall environmental situation.

136. **Significant positive effects, in the medium to long term, are expected under the proposed Pillar 2 prior actions that are directly related to a sustainable recovery**. Specifically, PA#6 should help reduce GHG emissions; PA#7 will lay the foundations for a strengthened ETS and through an improved mechanism for allocating emission allowances to enterprises, will contribute toward meeting Kazakhstan's NDC in the medium-term. PA#8 should help reduce the economy's carbon footprint; and under PA#9, the adoption of the 2021 Environmental Code will help protect and conserve the environment. The proposed Pillar 1 prior actions may also have impacts on the environment. Strengthened competition and digital economy will help bolster efficiency gains across the

[61] See UN Women (2017). The Power of Procurement: How to Source from Women-Owned Businesses
[62] World Bank. 2021. Gender in Kazakhstan, A Background Note.
[63] Ibid and UNDP. 2018. Human Development Report.

economy that will result in better use of resources and waste reduction. Under PA#3, more efficient and greener procurement practices are expected to be established.

137. **The 2021 Environmental Code strengthens the existing policy framework, and its implementation will provide a robust system to address environmental protection and ensure sustainable implementation of projects.** In this regard, the Government is in the process of enacting 156 bylaws to support the enforcement of the Environmental Code. These bylaws address a range of practical issues including rules and regulations on environmental licensing and fees, environmental enforcement and fines, emissions controls, and carbon pricing. The Environmental Code also strengthens the environmental assessment regime and introduces the requirement for Strategic Environmental Assessments for all government programs. Thus, all necessary measures and steps needed during the lifecycle of the investment projects are clearly defined to identify, mitigate, and prevent potentially negative impacts on the environment.

138. **The MEGNR is the main state body for environment- and climate-related monitoring and regulations.** The MEGNR is divided into committees (including Environmental Regulation and Control, Fisheries, Forestry and Wildlife, Geology, and Water Resources) and departments (including Climate Policy and Green Technology, Transboundary Rivers, Digitalization and Informatization, and Public Relations). The Committee for Environmental Regulation and Control has the overall responsibility for ensuring environmental safety, protecting natural resources, and promoting sustainable development through: the enforcement of environmental regulations; organization and conduction of state expertise or environmental assessment compliance; regulation of emissions; and issuance of environmental permits. The Bank has interacted with the authorities on environmental policies and licensing through a series of projects and technical assistance activities since independence. The Government maintains a good record of environmental performance and enforcement that has improved steadily over the past two decades, particularly with regards to larger infrastructure projects. The 2021 Environmental Code further strengthens the Government's regulatory and enforcement provisions and, with the establishment of the planned bylaws and strengthening of capacity at national and local levels, should raise the profile and importance of MEGNR within the cabinet.

139. **Institutional capacity constraints are the main barrier to implementation of policy reforms and will be addressed through parallel technical assistance.** Currently, the MEGNR requires additional technical capacity to fully enforce the Environmental Code. Kazakhstan is working with the EU, the AFD, the GIZ, the EBRD and other development partners in line with the European Green Deal, including on activities that will strengthen MEGNR's capacity. Additionally, the World Bank's engagements include technical assistance (TA) on developing a circular economy action plan in the construction value chain and on supporting implementing the "Circular Economy Opportunities in Almaty" adopted in 2019. The Bank also provides TA support to Almaty and Nur-Sultan in developing air quality management roadmaps taking into account synergies and tradeoffs with climate change mitigation measures. The Government has sought the Bank's support through the Partnership for Market Implementation to support the ETS implementation and its related action plan.

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

140. **The latest PEFA assessment from 2018 finds overall improvement of the PEFA system performance since 2009, with 21 out of total 28 performance indicators (PIs) rated "B" and above.** The PEFA also confirmed that enacted state budgets as well as budget execution reports are published regularly on the external website of the Ministry of Finance and on the websites of budget administrators. The PFM arrangements are acceptable for

this operation.

141. **Despite the progress observed since 2009, some of the critical PFM elements remain weak while the Government puts notable efforts to improve its PFM system.** Many aspects of PFM are regulated by the Budget Code which covers both central and subnational governments. The Code sets out how the budgets of both central and local governments are to be planned, prepared, and executed, including the timing of different stages and the responsibilities of different institutions and the two Houses of Parliament. All revenues and expenditures of the budgets of central and local governments flow through the Treasury Single Account at the NBK, which is managed by the Treasury Committee under the Ministry of Finance. Aggregate information about the state budget—which brings together the budgets of the central government and all regional and district governments—is available in budget execution statements. The activities of 2020 republican state enterprises (RSEs)—entities owned by ministries which carry out government functions—are not included into budget execution reports. With the World Bank support, improvements in accounting/financial reporting system are under way. Nevertheless, the implementation of International Public Sector Accounting Standards (IPSAS) is still a challenge and will require the Government's continued reform efforts.

142. **Internal control and internal audit are coordinated by the Committee for Public Internal Audit under the Ministry of Finance (CIPA) in accordance with the law on State Audit and Financial Control enacted in November 2015.** The same law also covers external audit. CIPA oversees the performance of internal audit throughout the Government, as well as undertaking a wide variety of financial, compliance and performance audit tasks.

143. **There is considerable overlap both in the legislation and in practice between the activities of CIPA and those of the Accounts Committee (AC) under the President.** The AC—which acts as the external auditor at the central government level—only covers subnational governments and SOEs when they are using funds provided by the central government. Regions and districts have their own audit commissions. Other SOEs prepare financial statements in accordance with International Financial Reporting Standards (IFRS) and are audited by corporate sector auditors applying International Standards on Auditing (ISA). The AC is responsible for supervising the qualification of auditors working in the public sector, and for maintaining the single database of all public audit work, including that carried out by CIPA. The quality of performance and financial audit needs to be improved further. In June 2021 the AC issued an audit opinion on Republican level Consolidated Public Financial Statements covering 2020 for the first time. The audit opinion is modified due to material non-compliance with accounting policies and failure to account for large share of investments in quasi-state sector entities. Despite having the financial audit methodology developed based on international standards and good practices, international standards for supreme audit institutions (INTOSAI Standards) are not always followed in practice by AC and CIPA, and further improvement in this area will require additional time and resources.

144. **Audit of the central bank.** The NBK has been audited annually by internationally recognized audit firms. The financial audit of the 2019 consolidated financial statements was conducted by the KPMG, LLC Kazakhstan. The auditors issued a modified opinion on the NBK's consolidated financial statements, which are available on the NBK's website.[64]

145. **Disbursement and auditing.** Loan proceeds would be made available to Kazakhstan upon the effectiveness of the Loan Agreement and the submission of a withdrawal application. The World Bank will

[64] The reason for modification was that certain securities were not reported at fair value.

disburse the amount into a foreign currency deposit account that forms part of the country's official foreign exchange reserves held by the NBK. The Government can use the proceeds to: (i) make budgeted foreign currency payments directly from this account; (ii) transfer amounts from the foreign currency account to a local currency bank account of the Government, which the Government uses to make payments for budget expenditures; or (iii) a combination of these two approaches. The authorities will report the amount deposited in the account to the World Bank and confirm its availability to finance budget expenditures within 30 days of receiving the funds. If after depositing funds in this account, the proceeds of the loan are used for ineligible purposes as defined in the Loan Agreement, the World Bank will require the authorities to refund the amounts to the World Bank. Amounts refunded to the World Bank in respect of ineligible expenditures will be cancelled from the loan.

146. **No additional fiduciary arrangements will be required for the deposit account and the fiduciary risk of this operation is assessed as moderate.** This assessment is based on the World Bank's knowledge of the country's public finance management systems and the availability of regular audit reports of the NBK's recent financial statements that are acceptable to the World Bank.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

147. **The Ministry of National Economy, in collaboration with the Ministry of Finance, coordinates the implementation of the actions supported by this operation.** The First Deputy Prime Minister has tasked the MNE to oversee the overall preparation of the program, coordinate the dialogue on the policy matrix, and lead the implementation and monitoring of the program, with the support from the WBG. Data on results indicators are available within the respective line ministries and can be retrieved upon request from the MNE.

148. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported by prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the World Bank's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service, please visit *http://www.worldbank.org/GRS*. Information on how to submit complaints to the World Bank Inspection Panel can be found on *http://www.inspectionpanel.org/*.

6. SUMMARY OF RISKS AND MITIGATION

149. **The overall risk of the operation is assessed as moderate.** The risks on Sector Strategies and Institutional Capacity for Implementation are rated as substantial, reflecting challenges in institutional coordination and the effective shift from preparing laws, strategies, and plans to their timely and appropriate implementation. Macroeconomic risks are low given the adequate macroeconomic framework and management and the substantial fiscal and external buffers. All other risks are rated as moderate, including the "other" risk that

reflects the uncertain duration and severity of the pandemic.

150. **The Sector Strategies risk is substantial.** This reflects the sensitivity of reforms, which may not be difficult to conceptualize but for which there is the risk of delays in implementation or even reversal of several of the more sensitive reforms, given the political economy of change and the significant power of market participants. This can be the case of the procurement and environmental PAs, as implementation will fall under a multitude of stakeholders which will need to adapt to the new context, testing the capacity. Likewise, several clauses related to procurement and the financial sector may diminish the market power of major actors and trigger a push for reversals. Moreover, the persistence of the pandemic may also delay some sectoral reforms.

151. **The Institutional Capacity for Implementation risk is substantial.** The assessment reflects challenges in institutional coordination and ability to deliver on reforms with longer-term payoff that involve numerous ministries or agencies. The continuing pandemic is also putting pressure on institutions to deliver on immediate and essential priorities to protect lives and livelihoods and limit the scarring from the crisis.

152. **The authorities are well aware of the Sector Strategies and Implementation risks and are advancing reform measures to mitigate them.** The new Agency for Strategic Planning and Reform, accountable to the President, and the Supreme Council of Reform chaired by the President, are essential to strengthen intra- and inter-agency coordination, cooperation, planning, and execution of reforms. The authorities have also tapped a well-known international advisor as a deputy head of the Agency and are working to attract talent to help address any gaps. The authorities are working closely with the Bank to improve capacity and accountability through technical assistance, analytical work, and targeted lending operations. Workshops with relevant stakeholders are also part of these mitigation efforts. Popular support for reforms will require stepped-up communication with the general public on the benefits and risks of such operations.

153. **In coordination with other IFIs, the Bank is engaging the authorities and performing analytical work and technical assistance to mitigate the implementation risk.** This includes, for example, providing inputs to the Development Plan of Competition Agency 2020–2024 and its target indicators and the National Project on Development of Entrepreneurship; providing continued support for building the capacity of the procurement entities in collaboration with different government agencies; and conducting monitoring of the Kazakhstan financial sector and engaging in a dialogue with the AFR. Together with the IFC, the Bank conducted a diagnostic on the market for the non-performing loans to assist the authorities in reform implementation and help develop a market for distressed assets. Through the Justice Sector project, the Bank is engaging with the ANTIKOR to strengthen the capacity and support the digitalization of their work. The Bank team is also supporting the transition toward a low carbon economy through the CCDR, analytical work and technical assistance on strengthening the ETS, a regulatory review for carbon taxation, and the development of a decarbonization fund. Finally, the Bank also provides technical assistance to identify and develop appropriate investments for energy efficiency improvements and adoption of the Best Available Technologies in selected energy-intensive sectors in Kazakhstan.

154. **Other risks stemming from the uncertain duration of the pandemic and public oversight over foreign borrowing are moderate.** The seriousness of the first risk is underpinned by the rising third wave of cases and mortality, despite the recent pickup in daily vaccination. Only if the recent pace of vaccinations is sustained, the authorities are likely to get close to their target of vaccinating 53 percent of the population by September. Further, the risk from a resurgence of COVID-19 virus is partially mitigated by increased health spending,

improved management of hospitals and ICUs, and the ongoing vaccination plan. Should the number of cases continue to increase, more serious mobility restriction measures may be needed. In turn, this may well slow economic growth again, with negative implications for jobs, exports, and the fiscal balance. On the second, the Government internal processes and stringent parliamentary oversight over new foreign borrowing by the Government could delay the ratification of the DPF. This risk is mitigated by the MNE and the MoF efforts to communicate transparently the budget plan, its financing, and the various borrowing risks to the general public.

155. **The macroeconomic risk is assessed as low because of improved economic management, substantial buffers, and the uptick in growth projections.** However, while economic prospects have improved both for the world and for Kazakhstan, the potential spread of new variants of COVID-19 virus, the availability of vaccines, and the slower than initially expected implementation of the vaccination campaign are risks that may affect the macroeconomic, social, and health developments for all countries. In addition, the stronger recovery in the United States—much faster than anticipated in late 2020—may pose challenges for developing countries, including Kazakhstan. With inflation in the United States trending up—even if temporarily—there are risks that the US Federal Reserve may start tightening monetary conditions earlier than currently expected, resulting in capital outflows from developing countries and weaker currencies against the US dollar. A mitigating circumstance for Kazakhstan is that improved global prospects will help boost global demand for oil, a positive development in the medium term but a long-term challenge given global and national commitments to decarbonization.

Table 6. Summary Risk Ratings

Risk Categories	Rating
1. Political and Governance	Moderate
2. Macroeconomic	Low
3. Sector Strategies and Policies	Substantial
4. Technical Design of Project or Program	Low
5. Institutional Capacity for Implementation and Sustainability	Substantial
6. Fiduciary	Moderate
7. Environment and Social	Moderate
8. Stakeholders	Moderate
9. Other	Moderate
Overall	Moderate

ANNEX 1: POLICY AND RESULTS MATRIX

PDO: Support institutional and policy changes for (i) a more competitive economy driven by a more vibrant private sector and accountable public sector and (ii) a more sustainable economic transition			
Prior actions	**Results**		
Prior Actions under the DPF	**Indicator Name**	**Baseline**	**Target**
Pillar 1: Support a more competitive economy driven by a more vibrant private sector and accountable public sector			
Prior Action #1. To foster competition and level the playing field for all enterprises in the economy, the Borrower has created and operationalized the Agency for the Protection and Development of Competition as an independent state authority with powers to, inter alia, (i) investigate and prevent anti-competitive practices and mergers, and (ii) impose sanctions.	Number of investigations on anticompetitive practices that were resolved by issuing a decision.	0 (2020)	5 (2022)
Prior Action #2. To strengthen the enabling environment for telecommunications and the broader digital economy and to attract private investment into the sector, the Borrower has: (a) Adopted amendments to legislation on digital technologies to enhance the regulatory environment for personal data protection and facilitate the development of private sector led data-driven technology; (b) Adopted amendments to legislation on licensing of wireless broadband internet services to simplify the requirements and promote investment by introducing the technological neutrality principle in the license and reducing by 90 percent for at least five years the fees for the use of radio frequency spectrum.	Share of the population using the Internet.	82% (2019)	88% (2022)
	Share of electronic commerce in the total volume of retail trade.	1.8% (2019)	3% (2022)
Prior Action #3: To improve open competition, transparency, and accountability in public procurement, the Borrower has (a) submitted to Parliament amendments to the Public Procurement Law to: (i) Set open tender as the default procurement method; (ii) Reduce single sourcing and clarify the exceptional circumstances where it can be permitted; and (b) Submitted to Parliament amendments to the PPL and adopted new procedures to reduce the right to use single sourcing procurement by the SOEs.	Procurement contracts by value awarded through an open competitive method.	Less than 35% (2020)	More than 50% (2022)
Prior Action #4: To support market discipline and fair competition in the banking sector, the Borrower has, through the Agency for Financial Regulation, resolved regulatory non-compliance of three commercial banks in accordance with the Law on Banks and Banking.	Number of banks which have violated three or more times over the preceding 12-month period any capital	3 (end 2020)	0 (end 2022)

PDO: Support institutional and policy changes for (i) a more competitive economy driven by a more vibrant private sector and accountable public sector and (ii) a more sustainable economic transition			
Prior actions	**Results**		
	adequacy ratios or liquidity coverage ratio.		
Prior Action #5. To reduce corruption and improve accountability in the public and quasi-public sector, the Borrower has: (a) Restricted all civil servants, persons subject to anti-corruption restrictions, and members of their families from accepting gifts, remuneration and services in exchange for actions or inactions within their official powers, and from opening and owning foreign bank accounts; (b) Expanded liability to all persons authorized to perform public functions, including the management of the quasi-public sector for corruption offenses; (c) Strengthened the enforcement of anti-corruption legislation by requiring the creation of anti-corruption compliance services across the quasi-public sector.	Annual National Anti-Corruption Report detailing progress of anti-corruption measures both across the public and the quasi-public sector.	Not published with such detailed progress (2020)	Published (2022)
Pillar 2: Support a more sustainable economic transition			
Prior Action # 6 To improve energy efficiency and reduce GHG emissions, the Borrower has submitted to Parliament amendments to the Energy Saving and Energy Efficiency Act of January 13, 2012 that: (a) Expand energy consumption reporting to include all state-owned and budget sector entities; (b) Update the reporting requirements to enable better tracking of energy consumption; (c) Require procurement of goods and services by all public entities to include energy efficiency requirements; and (d) Adopt a new certification system for individual energy auditors.	Heat consumption in budgetary organizations.	0.26 $GCal/m^2$ (2020)	0.24 $GCal/m^2$ (2022)
Prior Action #7. To strengthen the Emission Trading Scheme (ETS), a key instrument for meeting Kazakhstan's NDC commitment to reduce GHG emissions, the Borrower has: (a) Adopted a requirement to allocate emission allowances by benchmarking the emission intensity of production process for all enterprises under the ETS; (b) Strengthened the operation of the ETS with regard to the trade in carbon units and the operation of the carbon unit registry;	Accounts opened to register carbon offset projects in the carbon registry.	0 (2021)	10 (March 2023)
Prior Action #8. To increase the installed capacity of renewable energy generation, the Borrower has adopted amendments to the Renewable Energy legislation of July 4, 2009 (No. 165-IV) that: (a) Institute rules for determining the renewable energy surcharge in consumer billing, starting from July 1, 2021; (b) Strengthen state support to assure payment for renewable energy to renewable energy suppliers selected through competitive auctions; (c) Allow 20-year Power Purchase Agreements (PPAs) based on renewable auctions held	Renewable energy capacity	1635 MW (December 2020)	2400 MW (December 2022)

PDO: Support institutional and policy changes for (i) a more competitive economy driven by a more vibrant private sector and accountable public sector and (ii) a more sustainable economic transition			
Prior actions	**Results**		
after January 1, 2021; and (d) Establish waste-to-energy pricing methodology and standard PPA templates for waste-to-energy auctions.			
Prior Action #9. To protect, conserve, and restore the environment, the Borrower has adopted legislation that introduces: (a) Requirements for permits and reporting on emissions from facilities with a harmful impact on the environment, including flaring and venting of associated gas, with administrative penalties for misreporting and for exceeding permitted limits; (b) Requirements for a national standard on BATs to prevent pollution and minimize anthropogenic impacts on the environment in selected economic sectors; (c) Requirements for mandatory strategic environmental assessment (SEA) of government projects and the territorial development program; and (d) Requirements for climate vulnerability assessment and adaptation planning for agriculture, water management, forestry, and civil protection.	Reduction in flaring volume relative to 2014	25% (2019)	50% (December 2022)
	Green technology service operator established and staffed to provide business incubation services.	Not established (December 2020)	Established (2022)
	Strategic Environmental Assessment initiated for Government programs launched after July 1, 2021.	0 (2020)	10% of all government programs (2022)

ANNEX 2: LETTER OF DEVELOPMENT POLICY

**ҚАЗАҚСТАН РЕСПУБЛИКАСЫ
ҰЛТТЫҚ ЭКОНОМИКА
МИНИСТРЛІГІ**

**MINISTRY
OF NATIONAL ECONOMY
OF THE REPUBLIC OF KAZAKHSTAN**

010000, Нұр-Сұлтан қаласы, «Есіл» ауданы, Мәңгілік Ел даңғылы
8 ғимарат, тел.: +7(7172) 74-38-01, факс: +7(7172) 74-38-24
e-mail: info@economy.gov.kz

8 building, Mangilik El Avenue, Esil district, Nur-Sultan city
010000, tel.: +7(7172) 74-38-01, fax: +7(7172) 74-38-24
e-mail: info@economy.gov.kz

October 6, 2021 № 17-1/8171-И

Mr. David Malpass
President of the World Bank

Dear Mr. Malpass,

On behalf of the Government of the Republic of Kazakhstan (Government), we would like to express our appreciation to the World Bank Group for the continuous support in achieving our development goals. We value the collaboration through the Joint Economic Research Program, inputs through other analytical work and technical assistance, and lending operations financing our development projects. Today we are seeking the support of the World Bank Group as Kazakhstan embarks on a path of private-sector-led and more sustainable economic recovery.

The COVID-19 pandemic has had a significant impact on Kazakhstan. The registered positive COVID-19 cases in Kazakhstan reached 889 040 in October 2021, or 4.7 percent of the population. Earlier this year several surges have pushed some regions back into the red zones, but now we have softened the regime as the situation is getting better (less than 1.7 thousand cases a day). More than 35% of population are vaccinated now. The pandemic has also led to an economic contraction. The sharp drop in global demand and prices on oil and metals caused a 19.2 percent decline in our exports in 2020. Following the measures taken to limit the spread of the coronavirus pandemic, GDP growth rate declined by 2.5 percent. The increase in world food prices has led to an increased inflation up to 7.5 percent in 2020 compared to 5.4 percent in 2019.

In 2020, the Government has implemented large-scale measures to ensure employment and maintain the level of income of the population. Three packages of anti-crisis measures totaling $15 bln (9 percent of GDP) have been implemented: urgent measures to support the population and businesses, prompt measures to preserve socio-economic stability, and a comprehensive plan to restore economic growth. The measures are aimed at ensuring employment, monthly income loss payments, social payments, housing construction, compensation for the loss of tax revenues in the budget and other areas. These measures, and the weaker economy, widened the budget deficit to 3.1 percent of GDP from 1.9 percent in 2019 even after we boosted the transfers from the National Fund of the Republic of Kazakhstan by 2.1 trillion tenge.

We are committed to step up structural and institutional reforms to shift to a private sector led model of development that is more sustainable and greener. We realize the importance of the new economic model to significantly increase its citizens' well-being and secure the country's path to high-income status by 2025. We also recognize that the COVID-19 pandemic makes our task more challenging, and we cannot continue without change. In this regard, we have adopted several initiatives.

First, we adopted a National Action Plan for implementation of the 2020 President's Address to the Nation, that accelerates institutional and legislative changes for more inclusive and sustainable development. This Action Plan includes important reforms, such as the establishment of a new independent agency on competition. Second, we amended our medium-term development strategy, National Development Plan 2025, to incorporate the importance of transitioning to an inclusive society, with improved human capital, more efficient and sustainable use of our national resources, more opportunities for private citizens, more accountable and transparent public sector, and better resilience against climate change.

To this end, as part of the Government has committed to implement reforms on the following areas:

(1) Improving competition and reducing the role of the Government in the economy

We have undertaken important steps to level the playing field for all enterprises and encourage smooth functioning of markets. Specifically, a new and independent Competition Agency (the Agency for Protection and Development of Competition) was established in 2020. This new Agency, accountable directly to the President, is responsible for enforcing Kazakhstan's law and regulation in the field of protection and development of competition, including merger regulation contained therein (Chapter 14 of Entrepreneurial code), and also for carrying out an advocacy function by opening up markets to competition and identifying rules and regulations that may unnecessarily restrict competition.

Over the medium-term, we intend to deepen pro-competition reforms. First, by putting in place bylaws to implement the Presidential Decrees No. 407 and No. 428 to empower the new Competition Agency to execute its functions independently. Second, by adopting the strategic documents that will set Kazakhstan's vision to level the playing field for all enterprises and encourage the smooth functioning of markets: these are a separate part on competition development being elaborated within the Entrepreneurship Development National Project and the Competition Agency's Development Plan.

The Development Plan of the Agency for the Protection of Competition for 2021-2024 provides for target indicators such as Kazakhstan's position in the ranking of the Global Competitiveness Index of the World Economic Forum on the indicator "Competition in the service sector", the proportion of cases won in courts, on which decisions were made, reducing the number of state-owned enterprises and legal entities, whose more than fifty percent of shares (shares in the authorized capital) belong to the state, removing barriers to entry to commodity markets, ensuring the analysis of commodity markets.

(2) Strengthening the foundation for digital economy

To ensure the resilience of our economy to future shocks, we have undertaken a number of measures to enhance the legal and regulatory framework for the digital economy and the telecommunications sector as its infrastructure foundation, to increase the attractiveness of the sector to private investors, including for the provision of services in the most remote areas of our country.

To this aim, we have initiated the reform of the legal framework for digital technologies to provide investor certainty and enhance consumer trust in the deployment of new data-driven technologies, and further enhancements to the enabling environment for data protection are being planned.

We have also simplified the regulatory framework for licensing of high-speed wireless internet services, by introducing the technological neutrality principle, and have amended the Tax Code to reduce the cost of acquiring necessary radio spectrum licenses, as a way of incentivizing the deployment of high-quality internet services in currently unserved areas of the country, notably rural areas.

(3) Making public procurement more transparent and open for competition, and strengthening measures on anti-corruption

We are working hard to improve the public procurement system of the Government and of "Samruk-Kazyna" JSC. To improve open competition, transparency and accountability in public procurement, we are amending the Public Procurement Law to: (a) establish a requirement for a mandatory prioritized use of competitive procurement methods (tender, auction, request for quotation); (b) reduce the grounds for use of single sourcing, and clearly indicate the exceptional circumstances where single-sourcing could be permitted; (c) minimize preferences for state owned enterprises (SOEs). The Government has also been amending the legislation related to Samruk-Kazyna's procurement system in order to systematically align it with the public procurement system.

Finally, we intend to adopt a framework for citizens engagement for monitoring of procurement performance to improve governance. To enhance transparency and accountability of public spending, an appropriate provision needs to be incorporated in the legal framework that will facilitate engagement of citizens by giving them access to public procurement data, and reports on public procurement performance indicators.

To reduce corruption and strengthen accountability in the public and quasi-public sectors, the authorities introduced measures to restrict civil servants from accepting gifts and from opening and owning foreign bank accounts. The authorities also included persons performing public functions and managing the quasi-public sector for corruption offences, and requiring anti-corruption compliance services to be set-up across quasi-public sector.

The authorities have expanded the liability and accountability mechanism on public procurement to the quasi-public sector. This is done by amending the anti-corruption legal framework to include persons authorized to make decisions on the organization and conduct of procurement, including public procurement.

(4) Strengthening stability and improving the functioning of the financial sector

In the financial sector, Kazakhstan has implemented vital reforms to continue strengthening the framework for provision of financial services – particularly in banking, the dominant part of Kazakhstan's financial system. In January 2020, the presidential decree establishing the Financial Stability Council came into force. The Council's objective is to foster financial stability of the Republic of Kazakhstan, prevent and reduce systemic risks. In parallel, a new Agency for Regulation and Development of Financial Market (AFR) was established to take over the functions of public regulation, control and oversight of the financial market and financial organizations, which allowed the National Bank (NBK) to focus on monetary and macroprudential policy. Earlier, in January 2019, a new bank resolution framework entered into force – amended further in 2020 – to underpin the Government efforts to foster financial stability and proactively resolve problems at banks.

In response to the COVID-19 crisis, the government and financial sector authorities have enacted several financial support measures in early 2020. Most recently, in March 2021, an additional package of measures was introduced, including a deferral for the repayment of bank loans and microcredits by SMEs in affected industries. Also, the period of subsidizing the interest rates on loans to SMEs in affected sectors has been extended until July 1, 2021.

As a result of the Asset Quality Review (AQR) conducted by NBK/AFR and subsequent enforcement actions for banks published in the Final report in February 2020, several undercapitalized banks replenished capital, three banks fulfilled their recovery plans, one bank was acquired by a healthy bank with substantial public financial support and the licenses of three small banks have been withdrawn. As a result of the AQR, the banks are taking measures to improve the quality of assets, improve internal policies and procedures as well as risk management systems.

AFR is working to issue regulations obliging banks to report their capital adequacy ratio also on a consolidated basis with proper treatment of non-performing loans transferred to (affiliated) asset management companies. To create a civilized market for non-performing assets, AFR, together with government agencies, is working to assess and select the most appropriate development model, taking into account the best world practice. The Problem Loan Fund (PLF) board plans to adopt a bylaw on valuation for its purchases of distress assets that will exclude the possibility for PLF to buy distressed assets from banks or other financial institutions at nominal price or significantly above the market price determined by the PLF's valuation methodology.

The Government and its agencies are committed to continuing the reform momentum in the banking sector to correct incentives, foster financial stability, and boost lending to productive firms. Safeguards for deployment of state financial support to banks will be strengthened to both continue fostering financial stability and minimizing moral hazard of banks. Namely, the AFR is committed to enforce that the three midsize banks under recovery plans will recover according to the set milestones. The gaps in prudential regulation related to identification, provisioning, and transfers of NPLs shall be closed to ensure level playing field for banks and their adequate capitalization.

(5) Strengthening commitments to a greener and more environmentally sustainable development

The Government of Kazakhstan is committed to a greener, more inclusive and sustainable economy as outlined in Strategy Kazakhstan 2050. This is reinforced and implemented through the 2013 adoption of the Concept for Transition to a Green Economy by 2050, the National Development Plan 2025, Kazakhstan's pledge in the 2020 UN Climate Ambition Summit to reach carbon neutrality by 2060 and the adoption of a new Environment Code, which has entered into force from July 1, 2021. Work is underway to develop and adopt over 150 bylaws to implement the Code. The Supreme Council of Reforms is also expected to adopt a National Project on Green Kazakhstan which lays out a five-year program, aligned with the Code, to support a green transition.

The Government is finalizing its Doctrine for Achieving Carbon Neutrality by 2060.

We also have taken concrete steps to implement our commitments to reduce GHG emissions. First, a national Emission Trading Scheme (ETS) was established in 2013 to regulate GHG emissions, covering power and industrial facilities emitting more than 20,000 tons of CO2 per year. New bylaws are being issued to improve the functionality of ETS. We plan to further tighten the annual GHG emission caps under the ETS in forthcoming NAPs for the period 2022-2025 and 2026-30. The 5th NAP for 2022-2025 is expected to be approved by the end of 2021.

Second, parallel measures are also being taken to address climate change. The Environmental Code aims to strengthen adaptation capacity, accelerate the adoption of green technologies, and adopt standards to prevent pollution and mitigate anthropogenic impacts on the environment. The Code also includes provisions requiring owners of natural resources to report emissions to the regulators, including flaring and venting of associated gas, accurately and timely, with monetary penalties for misreporting. Reducing gas flaring and venting from oil and gas production has been identified as one of the most promising emission reduction opportunities in the country and the Kazakhstan Government, KazMunayGaz and KazPetrol Group have endorsed the World Bank's Zero Routine Flaring by 2030 initiative.

To systematically improve energy efficiency in Kazakhstan, we are also amending our legislations. We are proposing amendments to the Law "On Energy Saving and Energy Efficiency Improvement", which are currently with the Parliament for approval.

The amendments will bring more accurate and transparent reporting and monitoring of energy use by the largest enterprises and improve the capacity in energy use monitoring, real-sector digitalization and quality of energy audits and conservation plans.

Within the aforementioned framework of the Energy Efficiency act, it is planned to establish energy efficiency requirements for public procurement of household appliances and equipment by state institutions and quasi-public sector entities, as well as monitoring to ensure compliance with the requirements.

We also commit to increasing the volume of electricity produced from renewable energy sources. Kazakhstan has already met its target of 3% of its generation mix coming from renewable alternatives by the end of 2020. We expect the share of renewables in the power generation mix to be 10-20% by 2030 and 50% by 2050. To support this goal, we introduced legislative changes that have resulted in spurring investments in renewable energy from the private sector, setting the pricing benchmarks for renewables procured competitively, and then expanding them to include waste-to-energy methodologies. We plan to adopt new legislation to increase the maneuverability and flexibility of the electricity grid by adopting energy storage technologies and to competitively procure power from renewable sources as an alternative to coal-fired plants.

I also would like to take this opportunity to stress the commitment of The Government of Kazakhstan to the medium-term reform program. In the annual Address to the Nation in September 2021, H.E. President Tokayev reiterated seven areas of development focus, three of which are on economic development in the post-pandemic period, ensuring quality education, and, regional policy improvement. In this context, we intend to continue working on the following areas:

- **Improving the investment climate**

In an effort to reduce regulatory uncertainty and enhance investor confidence, we have already passed a package of legal amendments to help increase the transparency and inclusiveness of the law making process. The package includes a mandatory requirement to publish all legal acts affecting the investment climate at a draft stage and extends the mandatory consultation period to a minimum of three weeks.

Important next steps towards further enhancing investor confidence will include removing remaining barriers for foreign investors to participate in the consultative process for new legislation and, importantly, the full operationalization of an investor grievance management mechanism at the newly established Investment HQ. By enhancing the implementation of critical investment protections in practice, this mechanism will help reduce regulatory risk and therefore address a major concern voiced by the investment community. The grievance mechanism will act as an early warning and tracking mechanism to identify and resolve investor complaints and issues that arise from government conduct. It will ensure that the government responds to grievances in a timely and suitable manner and in accordance with the country's laws, regulations and international investment agreements.

In parallel, in order to reduce the SOE footprint and free-up space for private investment, we have approved the new Privatization Plan for 2021-2025, which lists 673 objects for privatization (including 8 republican and 448 communal facilities, 64 subsidiaries of national holding companies and 153 social entrepreneurial corporations. This is a follow up plan after the Government executed a similar one for 2016-2020 by more than 90 percent: 506 objects were sold/transferred into concession and generated privatization proceeds of almost 630 bln. tenge ($1.5 bln.), 301 objects were reorganized/liquidated. The ultimate goal is reducing the state's share of ownership to the level comparable with OECD countries.

We started to implement the privatization plan, especially for the entities that are subsidiaries of major holding companies. We also intend to strengthen governance of SOEs that will remain in state ownership. This includes streamlining the rationale for state ownership, adopting ownership policy, improving corporate governance and accountability, transforming and corporatizing SOEs with non-corporate legal form, and consolidating the state ownership function.

- **Improving economic management for resilient and sustainable growth and recovery**

We have taken steps to improve the management of fiscal policies. We revised the Budget Code to introduce the main principles of a counter-cyclical fiscal rules by to reduce the dependence of fiscal policy on the oil cycle by setting a limit on the size of the guaranteed transfer from the National Fund at a level not exceeding the amount of receipts to the National Fund from the oil sector at a cut-off price, as well as stabilizing public expenditures and limiting their growth rates at the level of long-term real GDP growth adjusted for the target inflation rate. However, further work is underway to implement and incorporate fiscal rules into the Budget Code by the end of 2021. Therefore, the mechanism of a counter-cyclical fiscal rule will be regulated by the Budget Code of the Republic of Kazakhstan and applied in 2022 when preparing the republican budget for 2023. To increase the efficiency in the use of public funds, we amended the Budget Code to require all agencies and line ministries to submit economic analysis on their new proposed budget for development programs.

We are committed to implementing further reforms in economic policies. To further the macroeconomic policy management, the Government will prepare and publish an extended sovereign balance sheet that includes assets and liabilities of the central and local governments, National Fund, all extra budgetary funds, and all government-owned enterprises, etc. We will also include an assessment of fiscal risks in our annual budget statement. We also plan to strengthen our public debt management strategy to help the Government make more weighted decisions on a planned debt issuance. In 2020, the NBK financed anti-crisis programs to overcome the recession and support demand in the economy. From 2023, as the goals of export diversification and reduction of import dependence are achieved, the NBK will start phasing out its participation in state programs. This process will be completed by 2025. We are also working to significantly improve the budgeting process of state programs to ensure they are properly coordinated, have appropriate results indicators and are accompanied with monitoring processes.

According to the recent Nation Address by the President, now the Government is developing a new Concept for Public Finance Management.

- **Promoting greener economic growth**

Kazakhstan also ratified the Paris agreement in December 2016 and its Nationally Determined Contribution (NDC) aims to achieve an unconditional economy-wide target of a 15 percent reduction in greenhouse gas emissions (GHG) by 2030 compared to 1990. Work on updating the NDC accompanied with a roadmap for the appropriate implementation has been completed. The updated NDC and its roadmap will be approved this year after consultation with all interested government agencies and organizations and will be presented at the 26th Conference of the Parties (COP-26) of the UNFCCC in October-November 2021.

Taking into account global trends aimed at achieving carbon neutrality and the commitments under the Paris Agreement, Kazakhstan began developing a Concept of Low-Carbon Development until 2050, with the aim of addressing transition risks. The concept is necessary for the further vision of the country's economic development, taking into account the need to transform the economy to achieve deep decarbonization. The Concept is expected to be approved by the end of 2021.

Under the National Project on Green Kazakhstan around two billion trees will be planted to increase forest cover by 500 thousand hectares by 2025 and support carbon sequestration among other things.

The Government also commits to promote more green investments, including upgrading energy, heating, water, and waste management infrastructure in urban areas. The Environmental Code will also support the adoption of green technologies by the public and private sectors. We also support the initiative to allow cities with strong administrative capability to issue long-term financing to implement green infrastructure projects. The Astana International Financial Center is partnering with International Finance Corporation to review legislative reforms that need to be enacted to enable cities with strong creditworthiness to issue financing for green infrastructure projects. The President also expressed support for providing better access to long-term financing to Almaty city, which needs to upgrade its infrastructure to sustain benefit from urbanization and agglomeration of economic activities.

- **Improving human capital for inclusive and sustainable development, and improving the social protection system**

The also Government intends to build a health care system that can improve the well-being of present and future generations. In this regard, the Government is taking the following key steps.

We have taken steps to strengthen the public health system to manage the COVID-19 crisis. The Government increased spending on the pandemic related health infrastructure, provided bonus payments for medical workers, allowed citizens to access regular health services under the mandatory social health insurance and introduced temporary deferred payment of insurance contributions. To reduce mortality and severe morbidity due to COVID-19, Kazakhstan has also developed and approved its national vaccination plan through the Decree of the Chief State Sanitary Physician No.3 dated January 27, 2021, and launched its COVID-19 vaccination campaign on February 1, 2021 with priority groups specified in the national vaccination plan. More than 3 million people have been vaccinated with the first component and about 2 million people with the second. It is already 16% of total population. In general, 100% access to vaccination will be provided.

The Government is also working to improve the accessibility and quality of health services. Kazakhstan in 2020 embarked in a major transition on its health system, from a government-funded health system to a compulsory medical health insurance system that purchases health services from public and private health providers. The Government commits to renewing healthcare infrastructure and equipment, particularly in underserved areas, as well as to inviting private investments in health infrastructure and services. We will continue to strengthen science-based medical practices and introduce innovative health technologies, further developing human resources for health, and create a digitally integrated health care system.

We also commit to strengthening policies on disease prevention and health promotion. Specifically, we intend to increase excise taxes on tobacco products to address the increasing burden of chronic non-communicable diseases that reduce the population's life expectancy, decrease labor productivity and result in disabilities. It will also help contain associated growing health expenditures and raise additional revenues that could be directed to health promotion measures, including health-strengthening innovations, opportunities for expanded physical activity, and others.

Second, we are systematically increasing access to qualitative education services to increase the capacity and productivity of human resources.

The Government is taking serious actions to address disruption in the learning process due to COVID-19 and improve equitable access to quality education. We have implemented measures to mitigate the negative impact of the pandemic on the learning process. To ensure access to education for primary and secondary school students, the Government substantially increased expenditures on education as a share of GDP by 1 percentage point; enacted legislation to deliver flexible teaching in a distance-learning format; providing synchronous and asynchronous learning platforms and data bank for teaching and learning resources for all students across the country; developing, recording and broadcasting TV lessons throughout the country in all subjects; distributing computer devices for students; and providing training for teachers to perform in emergency remote teaching.

The Educated Nation National project is currently being developed that will address disparities in the quality of education between different socio-economic groups and territories of Kazakhstan and thus broadly aim at increasing the global competitiveness of education in the country by 2025. The National Project would contribute to increasing education spending, building ICT infrastructure of schools, enriching digital educational materials, and upgrading the content and quality of teacher professional development programs. In the context of the COVID-19 crisis, all these measures will enable a shift in focus towards disadvantaged students while expediting the strategic priorities in the educational sphere to reduce inequalities to access in education services.

The Government realizes the importance of social protection policies as the line of defense to help prevent a rise in poverty, particularly during the economic recession. In this regard, the Government commits to improving further the effectiveness, adequacy, responsiveness, and coverage of the national social protection system. The main directions of the proposed reform include: revisiting on a systematic basis minimal living standards to ensure adequate support of the population through the social protection system; and promoting proactive approach to identifying and serving needs of the weak and vulnerable population through online monitoring of living conditions. The Government also intends to promote and strengthen social services delivery through additional efforts on digitalization of social services (through the National Social Services Portal) and increasing accessibility of the services for various categories of the population. We are also working to improve the mechanisms of social and economic inclusion for people with disabilities including their participation in the labor market.

The Government is firmly committed to continue implementing the above reforms and values the assistance from the World Bank Group. We need to address the emerging development challenges and adjust our policies to the new realities. In this light, we will be grateful for the positive response to our request and further cooperation in the framework of the proposed loans to support this economic transition to more inclusive and sustainable economic growth model.

Yours sincerely,

Aset Irgaliyev
Minister of National Economy
of the Republic of Kazakhstan

ANNEX 3: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior Actions	Significant positive or negative environment effects	Significant poverty, social or distributional effects positive or negative
Pillar 1: Support a more competitive economy driven by a more vibrant private sector and accountable public sector		
Prior Action #1	Yes, positive. Together with the enforcement of the Environmental Code, under PA #4, the introduction of more competition will result in efficiency gains that translate into environmental benefits through reduction in GHG emissions through fuel savings and BATs.	Yes, positive in the medium- and long-run. The promotion of a more competitive and private sector-led economy under PA#5 is expected to improve the quality and perhaps moderate the increase or lower the prices of some goods and services that will benefit consumers. In addition, it will likely create more and better paid jobs in the long run. Finally, all these actions should also create additional fiscal space for pro-poor spending, including through better social protection, which is expected to have a positive impact on poverty.
Prior Action #2	Yes, positive. Together with the enforcement of the Environmental Code, the strengthening of the digital economy will result in efficiency gains that translate into environmental benefits through GHG emissions through fuel savings and BATs.	Yes, positive. The strengthening of the telecommunication sector might help improve access to the internet for poor and vulnerable groups. In 2021, Kazakhstan ranks 50th out of 120 countries with available data on gender gaps in internet access, and 62nd in the Inclusive Internet Index.[65] Amendments to the legislation on digital technologies to simplify the requirements, promote investments, protect personal data, and reduce internet fees could not only extend internet coverage but also have internet access more affordable to low-income families and vulnerable groups, including women and girls.
Prior Action #3	None	Yes, positive in the long-run. More transparent, competitive, and efficient public procurement can reduce the burden on the budget and on businesses. It could also help providing better quality of goods and services to consumers. In addition, it could also create additional fiscal space for pro-poor spending, including through better social protection, which is expected to help reduce poverty.
Prior Action #4	None.	Yes, overall positive with some negligible negative impacts. A more competitive and stable financial sector can help economic growth and support poverty reduction in the long-run. Although the steps taken to withdraw the license of two small failing banks may translate into immediate unemployment

[65] https://theinclusiveinternet.eiu.com/explore/countries/KZ/performance/indicators/availability/usage/gender-gap-in-internet-access

		for some employees, the overall implication for poverty is expected to be negligible because of the very small number of workers affected. As of December 2019, there were fewer than 800 employees in both banks. There is a low probability that the affected workers are in a low-income group. In the medium- and long-term, these actions are envisioned to help strengthen the financial system and improve access to finance for all, including the most vulnerable.
Prior Action #5	None.	Yes, positive in the long-run. Anti-corruption measures supported under this prior action can reduce the burden on the budget, providing more resources for education, health, and social protection. In addition, these measures could significantly help boost the citizens' confidence in government; less than half of the population currently believe that the government does enough to fight corruption. In the short term, there could be negative social impacts. The engagement of civil society in oversight and accountability roles is still nascent in Kazakhstan. As a result, until systems have been developed, civil society groups and media may face challenges or scrutiny when providing oversight of the implementation of these reforms, whistleblowers may face negative social consequences, citizens may be unwilling to get involved in providing oversight, and there may be a lack of transparency and lack of access to justice for those prosecuted.
Pillar 2: Lay the foundation for a more sustainable economic transition		
Prior Action #6	Yes, positive. The achievement of the NDC will be a major accomplishment in energy efficiency. All SOE and budget sector public procurement will be subject to energy efficiency code compliance and new certification procedures are being adopted that will expand capacity across the country, not only for conducting energy audits, but also for suggesting quality and cost effective plans for making improvements. The tracking, monitoring, and reporting of energy use, a needed first step to have credible movement toward efficient energy use, will streamline reporting and monitoring across the country, with deeper and customized focus on the largest consumers. By focusing on energy efficient public procurement for all public enterprises, and setting up better norms, the government will lead in the purchase of energy efficient equipment and services. Expanded capacity for timely and better quality energy audits will	Yes, some positive impact in the long-term. The amendments to the Energy Efficiency Legislation in PA #6 provide stronger mechanisms to monitor enterprises' energy consumption and improve energy efficiency. Its requirement for annual reporting and the appointment of energy management specialists may increase operational costs for both public and private enterprises but this additional cost is unlikely to be substantial for firms to lay off workers or to pass the costs to customers. The expected reduction in GHG emissions and improvement in energy efficiency would be beneficial for both human health and productivity. These benefits will be important for the poor and vulnerable, whether they live near industrial sites or in rural areas, as they often have less voice and fewer means to cope with pollution or build

	further improve awareness of energy efficiency and help with implementing subsequent measures to economically reduce energy usage. In total, this will reduce uncertainty and improve transparency and accountability around GHG reductions and achievement of NDC and energy intensity targets.	resilience to climate change. There may be potential short-term negative social impacts if the monitoring leads social facilities including health clinics and schools to reduce heating or electricity. There is a need for careful monitoring by users and the government of these negative impacts.
Prior Action #7	Yes, positive. The new requirement and bylaws will align Kazakhstan's ETS with the EU ETS; consider the potential impact of the Carbon Border Adjustment Mechanism (CBAM) on Kazakhstan's economy; stress the need to improve Kazakhstan's MRV systems by updating methodological tools and enhancing existing verification processes; and recommends that the authorities tighten the annual emission caps to be covered under the 5th and 6th NAPs. The improved MRV will also drive an increase in the price of carbon units over time. The bylaws should help strengthen the ETS' operations to validate and verify GHG emissions and create, trade, and record offset units. The parallel draft update to the NDC and its implementation roadmap are expected to include: (a) a strengthened MRV system; (b) improvements in auctioning and domestic offsets for the ETS; (c) introduction of a carbon tax for non-ETS sectors; (d) application of BATs for bigger emitters; (e) increase of renewable energy sources and energy efficiency; (f) improvement of waste recycling; and (g) establishment of a decarbonization fund	The impact in 2021 is unlikely to be substantial. However, as the caps on emissions are tightened in the coming years through adoption of the next NAPs (NAP5 and NAP6), impacts on prices and employment may be more substantial.
Prior Action #8	Yes, positive. Reducing the overall carbon footprint will have positive effects on the environment as well as human health, particularly with the improvements in air quality expected with reduction and eventual elimination of coal fired power plants. The PPAs that enable renewable energy procurement through transparent auctions, allowing for longer terms, and inclusion of tariffs and auction methodology for waste-to-energy plans. Provisions also focus on promoting hydro power through auctions and include measures for land procurement for renewables as well as provisions to better assure payment for renewable power plants. More investment in renewable energy, including large scale plants, and the introduction of energy storage technologies are also expected. All of this will lead to the transformations necessary to achieve a carbon neutral economy by 2060.	Yes, positive in the long-term. Prior Action #8 aims to lower the economy's carbon footprint which can be beneficial for the health and productivity of citizens, especially poor and vulnerable populations who often inhabit areas near industrial sites and rural areas. Positive impacts may result from new jobs in renewable energy plants and associated constructions. However, in the short term, there are potential social impacts related to land acquisition and economic displacement. Potential impacts on current land use from investments in renewable power generation plants may not be avoidable but can be mitigated through compensatory measures.
Prior Action #9	Yes, positive. The Environmental Code and its related bylaws are a major step toward improving environmental management and governance and providing the regulatory and enforcement framework to protect, conserve, and restore the environment, and to help	Yes, overall positive but with some potentially negative impacts through prices and employment. Requirements for permits with emission standards, monetary penalties for violations, and compulsory environmental insurance may result in some cost

	Kazakhstan meet its climate commitments. The Green Kazakhstan National Project, aligned with the Environmental Code, will take action to reduce air pollution, support effective waste management and landscape restoration, enhance eco-education, and improve environmental culture. Implementing the Code will reduce gas flaring and venting significantly; toughen the legal regime, particularly for large facilities and heavily polluting industries; strengthen the polluter pays principles through licenses and, when necessary, penalties; require the development of SEAs for all governmental programs; and introduce BATs to prevent environmental pollution and minimize and control anthropogenic impacts on the environment. Results will also include better governance and a more leveled playing field for energy extraction, production, and polluting industries.	increase for firms that can fully or partially be transferred to customers through rising prices and/or cause firms to scale back their workforce. An Integrated Environment Permit is required for facilities with harmful environmental activities in Category I, which includes enterprises in several sectors of the economy, including energy, production and processing of metal, mineral industry, chemical industry, waste management, and food industry. An environmental impact permit is required for facilities in Category II, e.g. non-metallic mineral products, electricity, gas, steam, and others. These permits cover environmental conditions for carrying out activities and using best available techniques for certain technological processes. Data on the firms affected is unavailable (such as size of operations, number of employees, etc.) and additional costs to firms (such as costs of technological changes, strictness of the environmental permit, penalties for violator and compulsory environmental insurance). It is possible that the number of firms affected over the medium and long term could be large.

ANNEX 4: DEBT SUSTAINABILITY ANALYSIS TABLES

Baseline Scenario (in percent of GDP unless otherwise indicated)

Debt and Economic indicators

	Actual			Projections					
	2010-2018	2019	2020	2021	2022	2023	2024	2025	2026
Nominal gross public debt	16.8	19.6	24.5	26.7	29.4	30.1	31.0	31.2	31.7
Of which: guarantees	0.6	1.1	1.3	1.2	1.1	1.0	0.9	0.8	0.8
Foreign debt	6.9	6.8	8.1	11.9	13.0	13.4	13.5	13.4	13.7
Domestic debt	9.9	12.8	16.4	14.9	16.3	16.7	17.4	17.8	18.0
Real GDP growth (in percent)	4.5	4.5	-2.5	3.5	3.7	4.8	4.2	4.0	4.3
Inflation (GDP deflator, in percent)	10.7	7.6	4.3	5.3	5.6	6.3	4.5	4.7	3.8
Nominal GDP growth (in percent)	15.7	12.5	1.7	9.0	9.5	11.4	8.9	8.9	8.2
Effective interest rate (in percent)	5.4	5.7	5.9	6.1	6.1	6.3	6.4	6.5	6.5

Source: WB staff estimates and projections

Shock scenarios and projection of gross nominal public debt

Shock scenarios:	2021	2022	2023	2024	2025	2026
Real GDP growth (%)	3.5	0.9	2.0	4.2	4.0	4.3
Primary balance (% of GDP)	-5.0	-4.6	-3.4	-0.1	0.2	0.3
Effective interest rate: real interest rate shock (%)	6.1	6.1	6.8	7.3	7.7	7.9
Effective interest rate: real exchange rate shock (%)	6.1	8.0	5.7	5.9	6.3	6.4
Gross nominal public debt under different scenarios:	As percentage of GDP					
Baseline	26.7	29.4	30.1	31.0	31.2	31.7
Real GDP growth shock	26.7	31.0	34.3	35.2	35.5	36.1
Primary balance shock	26.7	31.9	35.2	36.0	36.3	36.9
Real interest rate shock	26.7	29.4	30.3	31.3	31.9	32.9
Real exchange rate shock	26.7	33.7	34.0	34.4	34.4	34.7
Combined shock	26.7	46.2	50.6	51.4	52.1	53.2

Source: WB staff estimates and projections