

State and Prospects of the Securities Market in the Developing Economy (on the Example of Kazakhstan)

Nurasheva Kulyanda KULBOSYNOVNA
Business and Commercialization Department,
M. Auezov South Kazakhstan State University, Kazakhstan
concelyaria@mail.runurasheva@mail.ru

Kulanova Darikul ASKARBEKOVNA
M. Auezov South Kazakhstan State University, Kazakhstan
k_dana_a@mail.ru

Abdikirimova Gulzhanar IMANBAEVNA
M. Auezov South Kazakhstan State University, Kazakhstan
abdikirimova71@mail.ru

Mergenbayeva Aziza TOIMAKHAMBETOVNA
M. Auezov South Kazakhstan State University, Kazakhstan
aziza.mer.69@mail.ru

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Abstract:

The purpose of the research is to study the economic environment and determine the possibilities of issuing and circulating municipal bonds. The methods used were information sampling, its grouping, system and statistical analysis, comparison of indicators and logical conclusions. It has been determined that the large quasi-public sector, the feebleness of development institutions, the instability of the banking sector, and the uneven development of regions impede the formation of the stock market. Low household incomes, inflation and depreciation of the national currency reduce investment opportunities. The risks of buying securities by the population are not calculated, there are no clear guarantees for the rights of ordinary shareholders, the return of funds causes problems due to imperfect legislation.

In order to substantiate the true opportunities and desires of people to spend money on the purchase of securities, questionnaires and interviews were conducted among representatives of various social groups. The study showed that citizens are willing to buy bonds, but first it is needed to create an innovative economy and implement attractive projects in the regions for the population in order to fully launch the stock market. In the current scheme for issuing municipal bonds, only the quasi-public sector is involved. To attract the investments from pension funds, insurance companies, small investors (population), the authors recommend a scheme of business processes for issuing and circulating bonds. The problems and proposals discussed are of interest to post-Soviet countries, which are facing with the need to develop the stock market.

Keywords: household income; municipal bonds; public opinion; real sector; securities market; stock exchange.

JEL Classification: D53; E65; G11; G14.

Introduction

Securities play a key role in the economy. In difficult situations, they have proven their benefit by providing access to capital when other financing channels were difficult of access or unattractive. Securities are necessary for attracting investments in socially important projects. For the regions of Kazakhstan, we see the market for municipal

bonds (MB) to be promising. It is known that many large projects were implemented with their help, hundreds of hospitals, athletic fields, dormitories, civilian objects have been built (O'Hara 2012; Thomas 2019). In Kazakhstan, there is some experience in circulation of municipal securities (MS). In 1999 discounted bonds with a nominal value of \$100 in the amount of 399.7 million KZT were first issued in Mangystauskaya region. The region Akimat (Mayor) was the first executive body in Central Asia to receive a credit rating from the Fitch rating agency (Makhmutova 2008; Fitch Rating Agency 2001). The coupon rate was 10.99%. Following Mangystauskaya region, the municipalities of Almaty, Astana and Atyrauskaya region placed their loans on the Kazakhstan Stock Exchange. The authors have been studying financial levers for managing the regions of Kazakhstan for a long time and have developed an economic mechanism to motivate the economy of the territory using stock market instruments. To justify the expedience of organizing the MB market, the regional stock market was studied. As a result, the possibilities of using free cash flow of the population to invest in the MS were identified.

1. Research Method and Methodology

The idea of issuing bonds is that payments are made at the expense of income from the maintenance of public facilities.

For example, in Japan, strategic bonds for innovative projects are attractive. Their main goal is to finance agriculture, education, construction, disaster management (Ryan 2019). They are issued by prefectures, cities and municipalities to finance definite investment projects, usually for 10 years, the interest rate practically does not differ from the rate on government bonds.

In Germany, the securities market is effectively organized thanks to the clear interaction of federal and regional governments. Decentralization of power allows local governments to act quickly and efficiently. The bulk of MB is represented by short-term and medium-term securities, the coupon value is 5-10% per annum (Furness 2019; Davies 2019).

In Russia, bonds are issued to receive funds for projects, social programs, construction of schools, kindergartens, dormitories. Housing loans are an example. Redistribution of funds is also carried out in favor of sectors with insufficient profitability (for example, local agriculture). Borrowed funds cover the lack of budgetary funds in a specific city, region, and republic. Municipal bonds have a high yield: in August of 2018y. coupon interest ranged from 6% per annum (Moscow) to 15% (Magadan Region). The main reason for this is the absence of taxation on coupon payments and a higher annual rate (Nittayagasetwat 2018).

Unfortunately, about 20 years have passed since the first municipal bonds appeared, however, this market has not received proper development. Brief statistics is presented (Official site KASE 2018). On August 01, 2018, securities of 383 names of 151 emitters were available for trading on the Kazakhstan Stock Exchange (KASE). Trading volume in the primary market reached 165.8 billion KZT (one dollar = 344.19 KZT), at that the share of municipal bonds amounted to only 0.02%. In world practice their share is much higher: the volume of the US MB market is about \$1.5 trillion or 11.5%, in France - 6.6%, in Japan - 6%, Russia - 6% (Thomas 2019, Chuklin 2019).

Today, attempts to promote the stock market in Kazakhstan are made through IPO. In this case, problems and difficulties arise; since there is no experience, this market is riskier than, for example, investing money in deposits. Lack of liquidity and a small list of instruments on KASE are a constraining factor for the development of the MS. Meanwhile, in the regional sector, stock assets in the near future may be in demand. So, in connection with the implementation of the 'Affordable Housing' and 'Credit Housing' programs, local executive bodies of Kazakhstan issued bonds in 2016y. to the amount of 36,505 million KZT, in 2017 – 38,214 million KZT (On approval of the 'Affordable Housing 2014, State Program of Housing Construction 2016). However, the population of the country does not participate in the purchase and sale of MS, although in the Central Depository as of August 1, 2018y. there were 110 thousand personal accounts of individuals (mainly IPO), i.e. some citizens have experience in purchasing securities and can participate in the purchase of municipal bonds.

Banks, financial organizations and business structures of the region also have resources to participate in the formation of the stock market. This situation makes the development of the regional stock market urgent. To bring the matter to its logical conclusion, we have chosen projects that are profitable and socially significant for the region and recommended the local authorities to finance them through MS. We believe that our experience will be useful for the countries with developing economies (Nurasheva *et al.* 2018).

As part of the study the world literature on securities market, legislative and regulatory acts of Kazakhstan (Beisbekova *et al.* 2019; The Law of Kazakhstan 2003; Rules of issuing securities 2009); KASE reports (Official site KASE 2018); documents on the organization of the Astana International Financial Centre (AIFC) (About the Astana 2015), statistics, Internet resources have been examined. The projects that are being implemented according to

the State Program for Industrial and Innovative Development for 2015-2019yrs. (SP IID), the Industrialization Map-2020 and the Business Roadmap-2020 were studied.

Analyzing the data of the National Chamber of Entrepreneurs 'Atameken', we found out projects for the financing of which there are no funds, but they can be implemented if the securities market is launched. The Concept of territorial specialization was used, the economic meaning of which was to emphasize specialization branches in the regions of Kazakhstan, which allowed for the south of the country to suggest projects in the field of tourism, textile cluster, processing of agricultural products. But in order to substantiate the true possibilities and desires of the population to spend money for purchase of securities, the authors decided to conduct a survey and interviewing of representatives of various social groups, visited institutions and enterprises, interviewed entrepreneurs, because official statistics data do not reflect the real situation.

The fact is that there is no universal declaration of income and expenses in the country, survey of household budget is made on the basis of selection of 12 thousand families. However, according to the authors' data there are approximately 5.6 million families (coefficient of domesticity 3.4) (Aydapkelov 2018), which suggests that survey is done within 0.22% of the total families. The Max Lorenz curve and the Corrado Gini coefficient are also determined on the basis of this sample, therefore, from the point of view of reliability, one cannot fully rely on statistics.

Authors decided to examine the most prepared part of the population by random sampling. Processing of the answers showed that all respondents had higher and postgraduate education, i.e. quite competent people responded to the questionnaire and gave interviews. In some attended institutions the sample was more than 50% (banks, insurance companies, pension funds, micro credit organizations, departments of the city mayor, etc.). The range of opinions on the prospects for the securities market development in the country, including MB, was quite large. Some answers were not typical, and so the use of computer processing of the data was not advisable. In our opinion, the main task of obtaining high-qualitative and objective information first-hand, rather than from official sources, has been achieved. The authors intend to further make more in-depth study of the problems formulated in the article; perhaps the community study will be improved.

2. Research Results

The Situation in the Economy and Regions of Kazakhstan, Problems and Difficulties

The modern economy of the country is undergoing significant changes caused by the globalization of the world economy, high tech development and commercialization of innovations. However, there are internal problems:

- (1) large quasi-public sector. Thus, the assets of the National Fund 'Samruk-Kazyna' comprise more than 40% of the Gross Domestic Market. In recent years, the fund has been actively working to clear companies from unprofitable and outward activities, as a result of which the number of companies has been reduced from 768 to 560 (Abdymanapov *et al.* 2018, Isayev 2017). It is assumed that after privatization and transformation, the fund will represent a compact and mobile industrial holding that manages assets;
- (2) the banking sector runs a fever. The National Bank controls only 40% of the total currency in cash from the general volume. Deposits of enterprises by 60% are in foreign currency, and deposits of the population – by 80%. Although the external debt of the banking sector was not very large - \$ 8.5 billion, large banks (Qazkom, Qazaq Bank, RBK) had problems in 2018y. By the end of the year Qazkom joined Halyk Bank (Ranking of Kazakhstan banks 2017);
- (3) the share of foreign capital in large domestic enterprises is high (Matrekov 2016). Direct investments in the external assets of Kazakhstan account for \$ 32 billion or 19%, and the reserve assets of the National Bank of the country - \$ 28 billion or 17% of foreign investments. Since independence, foreign investment has amounted to \$ 197 billion, a significant part of which the investors have provided in the form of loans to their daughter companies, operating in Kazakhstan (Osmanbayev 2018). Currently, more than 140 large investors are registered and operate in the primary industry of Kazakhstan.

Table 1. Some key indicators of Kazakhstan for 2000-2017yrs

Indicators	2000	2005	2010	2011	2012	2013	2014	2015	2016	2017
Nominal GDP, billion \$	18.3	57.1	148.0	192.6	208.0	236.6	221.4	184.4	123.2	126.3
Money supply: billion \$ -%	2.8	34.8	57.6	66.5	70.6	76.2	71.5	92.5	59.2	59.6
to GDP	15.2	61.0	38.9	34.5	33.9	32.2	32.3	50.2	48.0	47.2

Indicators	2000	2005	2010	2011	2012	2013	2014	2015	2016	2017
State budget:- billion \$	4.1	21.7	29.2	3.6	39.0	42.0	40.9	41.0	27.6	28.7
-% to GDP	22.6	38.1	19.7	19.0	18.7	17.7	18.5	22.3	22.4	22.7
Tax revenue:- billion \$ -%	4.8	17.7	19.9	27.2	27.5	31.4	28.6	26.3	17.9	14.9
to GDP	26.0	31.1	13.5	14.1	13.2	13.3	12.9	14.2	14.5	11.8
For reference: KZT to USD rate	142.1	132.9	147.4	146.6	149.1	152.1	179.2	186.0	336.8	332.9

Source: Kazakhstan GDP (2019); Main social-economic (2018).

Kazakhstan's GDP peaked in 2013 due to high prices for oil, metals and other raw materials (Table 1) (Kazakhstan GDP 2019). The fall in prices caused a sharp decline in gross domestic product. Despite this, the money supply in KZT was growing all the time, reaching 19,825 billion KZT in 2017y.; in dollars it was declining: for example, in 2015y. it was \$ 92.5 billion, and in 2017y. - \$59.6 billion. This was because of a 1.81 fold increase in the dollar to-KZT exchange rate, i.e. currency depreciated (Main social-economic 2018) (For reference: KZT to dollar exchange rate in July of 2018 already exceeded 345 KZT).

In 2017 in comparison with 2000y. GDP has grown by 6 times, and money supply by 21 times! The whole external debt of Kazakhstan in July of 2017 was estimated at \$167.9 billion, which is more than GDP (External debt of Kazakhstan...2018, Perepelitsa 2018). It is known that in targeted developed countries such figures reach 90-100%. However, it is incorrect to compare, because the question is about the countries where industry and services predominate in GDP. For resource countries, the situation is different. So, for Norway the external debt is 32.2%, in Russia it is 13.7%, in Iran- 11.9%, in Chile- 18.5%, in Indonesia -29.4% (Pettinger 2017).

Budget deficit in 2017 amounted to 1.2% of GDP. The dynamics of the state budget change corresponded to GDP growth; however, KZT devaluation depreciated budget revenues. Taxes are one of the indicators of economic efficiency. In our case, tax revenues in KZT remained at approximately the same level, but in dollar estimation, they fell significantly over the past two years.

Social sphere suffers from the economic instability. The unemployment level for many years is at an acceptable level of 5%, and the number of unemployed is a little less than half a million. For a country with a small population like Kazakhstan, there are rather much unemployed. At the same time the share of the self-employed population is large: 2.4 million people, part of which is hidden unemployment (Self-employment rate 2018). The subsistence level in 2018 was 28,284 KZT (\$ 83), which experts consider low relative to the average salary of 165 thousand KZT. According to the data, almost 69% of all incomings of the population are wages. The second largest source of wealth is pension, which accounts for 13.7%. Self-employment and entrepreneurship account for only 11% of income (Isabayeva 2018).

After the WEF Global Competitiveness Index has been harmonized with the UN Human Development Index in 2018, the task set by Kazakhstan to become one of the 30 developed countries in the next few year's remains unrealizable. The fact is that the primary economy does not create demand for human capital, as a result of which it does not accumulate investments, does not form intellect to achieve the country's competitiveness. Many problems in the economy of developing countries, such as Kazakhstan, are determined by the insufficient level of development of the regions. In this case, a large territory with a small population experiences difficulties in managing the regions, especially when the infrastructure is weak and logistics is underdeveloped.

As seen from Table 2, the regions of Kazakhstan are different in terms of development level (Aydapkelov 2018; What regions replenish 2018):

- (1) the western regions (Atyrauskaya, Mangystauskaya, West-Kazakhstan regions) live off the extraction and refining of oil and gas, most of the revenue is deposited in the republican budget;
- (2) the eastern regions (East-Kazakhstan region) stand apart from the rest ones, the heavy industry sectors are preserved, the influence of the Russia (borders on the Altai Territory) is strong, the influence of China is also felt;
- (3) the northern regions incline toward the Russia, not without reason many cities and towns have Russian names: Pavlodar, Petropavlovsk, Mikhailovka, Smirnov, Ruzayevka, Olginka, etc.; the infrastructure is weak in the region, real incomings are low;
- (4) the southern regions (South-Kazakhstan, Almatinskaya, Zhambylskaya regions) are characterized by a low-income level, influence of Uzbekistan, Kyrgyzstan, China is felt, the population is prone to entrepreneurship, the share of small business is significant.

Table 2. Indicators of development of Kazakhstan regions in 2017y.

Regions	Share of population, %	Share of regions in GDP, %	Share of investments, %	Share of industry, %	Share of local budget, %	Share of innovative production, %	GRP per capita \$	Real household income per month, \$
Kazakhstan	100	100	100	100	100	9.6	7,715	219,6
Akmolinskaya	4.1	2.8	2.9	2.4	4.4	7.5	5,210	182.9
Aktubinskaya	4.7	4.2	4.8	6.8	4.2	10.1	6,937	190.5
Almatinskaya	11.1	4.7	6.8	3.6	9.1	8.1	3,316	172.5
Atyrauskaya	3.4	10.8	26.2	23.6	6.0	8.0	24,879	415.5
West-Kazakhstan	3.6	4.3	5.2	8.2	3.9	5.3	9,291	212.6
Zhambylskaya	6.2	2.5	2.8	1.8	5.1	11.3	3,122	131.6
Karagandinskaya	7.7	7.9	4.1	10.2	5.5	11.1	7,900	206.7
Kostanaiskaya	4.9	3.3	2.3	3.2	4.3	11.3	5,155	186.6
Kyzylordinskaya	4.3	2.7	2.8	3.5	5.1	11.4	4,838	158.6
Mangystauskaya	3.6	5.0	5.2	9.9	4.0	3.5	10,867	334.0
South-Kazakhstan	16.1	6.1	4.9	4.1	12.8	6.5	2,938	121.7
Pavlodarskaya	4.3	4.1	5.7	7.2	3.8	8.7	7,541	221.5
North-Kazakhstan	3.2	2.1	2.2	1.1	3.9	11.2	5,034	180.6
East-Kazakhstan	7.9	6.1	5.6	7.9	6.7	15.1	6,022	186.0
Astana city	5.0	11.1	11.1	2.4	9.4	14.4	16,688	390.8
Almaty city	9.7	22.3	7.5	4.1	11.8	7.7	17,864	352.0

For reference: the data compiled from the calculation of one USD equal to 341.62 KZT as of July 3, 2018.

Source: Aydapkelov (2018); What regions replenish (2018).

The cities of Astana, Almaty, Atyrauskaya and Karagandinskaya regions are donors: their share in the country's GDP is large and they spend more investment for development. The lowest GRP per capita is in the South-Kazakhstan and Zhambylskaya regions, the difference between the highest rates of Atyrauskaya region, cities of Astana and Almaty is from 5.7 to 8.5 times. The uneven distribution of income between regions remains for many years. The difference between the maximum income in the Atyrauskaya region of \$ 415.5 and the minimum in the South-Kazakhstan region of \$ 121.7 is 3.4 times (Aydapkelov 2018).

The analysis shows that in Kazakhstan, many reforms do not work at the local level; decisions are made in a centralized way, without taking into account the opinions of the regional authorities and the public. The local authorities have not mastered all the instruments of market regulations of the region's economy. The economic levers provided for by the Law on Local Government and Self-Government in Kazakhstan are poorly used (The Law of Kazakhstan 'On local government 2001). Therefore, the authors consider it appropriate to improve the market regulations of the regional economy through stock market instruments, in particular the issue of municipal bonds.

Securities Market: Current Status, Problems of Legislation and Prospects

The current stage of development of Kazakhstan is characterized by the insufficient use of stock market instruments. In this area, there are a number of problems that are characteristic of countries with developing economies: mainly the money market and foreign exchange market prevail. The securities market takes only the third place, and these are mainly Government securities (GS) and corporate bonds; the share of municipal bonds

is so small that they are not always shown in the reports. So, the total volume of trading at KASE as of August 1, 2018y. amounted to 9.7 trillion KZT (Official site KASE 2018) (Table 3).

Positive dynamics is demonstrated by the stock market and the 'Securities of investment funds' sector. On August 01, 2018y. securities of 383 names of 151 emitters were available for trading at the stock exchange. At the Central Depository were opened 110 thousand personal accounts by individuals. The volume of trading in the primary market of GS reached 234.1 billion KZT, of which only 1.1 billion was attracted by local executive bodies. The remaining amount was attracted by the Ministry of Finance at 8.45% per annum.

Table 3. Structure of total amount of the trading of KASE, August, 2018

Type of operation	Volume, billion KZT	Share, %
Currency	1,002.0	10.33
Repo (repurchase agreement) GS	6,400.0	65.97
GS	234.1	2.42
Bonds	289.9	2.99
Shares	773.4	7.98
Others	1,000.6	10.31
Total	9,700.0	100.00

Source: Compiled on the basis of site data www.kase.kz.

As seen from Table 3, the share of trading in stocks in the total trading volume is only 8%, which is a fairly low indicator. Shares of some companies of KASE official list are not available on the market due to regulatory restrictions. Among them are securities of the largest companies, flagships of the Kazakhstan economy. About 7 thousand large and middle-size private companies and one thousand large state-owned companies operate in Kazakhstan. However, the listing of the stock exchange presents the shares of only 140 companies. Most of the transactions are handled with securities of a limited number of emitters (about 10), mainly in the banking and mining sectors (Official site KASE 2018).

The capitalization of the KASE shares market is constantly growing, which is linked with the extension of the list of companies whose shares are included in the calculation of capitalization. However, the KASE index often fluctuates under the influence of various factors. The publication of reports on operating activities of companies, market changes in the energy supply market, corporate events of companies became the determinative moment. In terms of the main categories of investors, individuals were the most active ones in trading (43.9%). Second-tier banks did not participate in the trading, the share of broker-dealers was 41.9%, and accounts of other institutional investors accounted for 14.2%. The secondary market share in the stock exchange's turnover is small and continues to decline (On the state of the financial market 2018). The main problem is the prevalence of negotiated transactions. The Agency for Regulation and Supervision of the Financial Market and Financial Organizations¹⁸ and KASE are taking measures to combat direct transactions, but their share in quantitative terms remains high (Beynoyeva 2019).

In general, when considering trading at any date, one can say that the capitalization indicators are characterized by high volatility because of the small size of the market. Any major transaction in size of our exchange stock affects the value of indicators. Taking into account that the capitalization of a developed stock market must exceed the GDP of the country by 2 times, it can be firmly stated that this indicator indicates the weak development of the Kazakhstani securities market and legislative imperfections (Demezhanova *et al.* 2019).

The total volumes of trading at KASE in comparison with the platforms of some countries are extremely small. Thus, the number of emitters on Chinese trading floors exceeds 6,000 companies, India - more than 4,000 companies; 3,500 companies and 3,552 companies correspondingly on international markets in London and New York (Hughes 2017; Kilp *et al.* 2019). The trading volume on shares of companies, included to the KASE index, is

¹⁸ On April of 2011, the Agency has been abolished by the Decree and its functions and powers were delegated to the National Bank. On May, 14 of 2019, Oleg Smolyakov, Vice Chairman of the National Bank informed that a decision was taken to establish again an independent body for check-out and monitoring the financial market and financial organizations.

2,375 times less than the volume of trading in shares, included in index FTSE 100. This does not allow bidders to independently determine fair prices for shares and makes KASE more dependent on more developed platforms.

It should be noted that Kazakhstani companies used the initial public offering (IPO) as the main instrument for capital rising. However, the picture does not look so optimistic due to the fact that our IPO market 'flows' outside the country. Most of the funds attracted by local companies come from share placing and global depository receipts in international markets of capital, but not in the domestic market (Nurasheva *et al.* 2019). In essence, the domestic market of initial placements has become an English one. Today, about 95% of the total turnover of the Kazakhstan share market and depository receipts falls on foreign exchanges, in particular on the London Stock Exchange (95%).

'Financial Times' experts believe that the securities of our companies carry large risks in case of change of ownership, privatization of electric power industry enterprises, uncertainties in the regulation of electricity tariffs, etc. (Batishcheva 2018; Charnavoki 2019). In Kazakhstan, where corporate governance is poorly developed, many decisions are made based on non-public information. The institution of pre-trial processing of claims is almost not developed. The situation can be changed by creation of a modern infrastructure of the securities market. Such a platform is only now being organized based on the Astana International Financial Centre (AIFC) (About the Astana 2015). A stock exchange, a mortgage company, insurance companies will be placed here, the main banks of Kazakhstan, microcredit organizations, Islamic finance institutions will also place their offices here. All documentation will be maintained in English to facilitate integration into the global stock market. The AIFC strategic goal is to create a competitive financial hub that meets international standards, and to join the group of 10 leading financial centres in Asia.

As a result of the reforms carried out in Kazakhstan, certain legal, economic and organizational foundations for the development of the domestic market of securities were formed. The Agency for Regulation of the Financial Market and Financial Organizations will be regenerated (Beynoyeva 2019). It should be noted that financial institutions are the first among all economic agents to respond to inflation processes, fluctuations in the exchange rate of the national currency; therefore, as a part of our research project, we have proposed some measures to develop the stock market:

- (1) to improve the quality of the information provided by the investors and to achieve transparency in the work of the company. Large Kazakhstani firms are not yet ready for this. In reality, it is practically impossible to obtain information about the shareholders and affiliates, data about the financial results or other information from the publicly available sources;
- (2) to give the company a public capacity. Publicity allows to interest people and to promote the investment culture, it can serve as a protective measure against the claims of the state;
- (3) to create a modern infrastructure of the securities market. As is known, foreign investors are accustomed to work in a favorable market environment, therefore, it is necessary to improve the settlements system, to stimulate the emergence of experienced brokerage-dealer companies, self-regulatory organizations.

Banking Sector: Instability Causes Concern

The key role in the whole system of money and securities circulation is played by banks. The activities of banks in Kazakhstan are at risk. Moreover, in 2020, under the terms of the WTO the transition period in the financial sector of Kazakhstan will end (Britskaya 2019). This means that foreign banks will be able to open branches in Kazakhstan, not subsidiaries, and thus use the entire capital of the parent companies to take risks. As a result of this, competition in the country's banking sector will increase.

Of course, the National Bank as a regulator pursues an active policy of preventing fluctuations in the banking sector. Weighing pros and cons of the decisions of the National Bank, it should be said that there are more positive effects of the current monetary policy. Today, in every region there is competition in the financial market, the range of banking products has extended, many banks work in partnership with the Western colleagues and attract syndicated loans.

However, by the 1st quarter of 2019y. household deposits decreased by 2.5% and amounted to \$ 22,325 million (Ranking of Kazakhstan banks 2017). Deposits of corporate clients decreased by 2% and amounted to \$ 21,593 million. The transfer by Tsesnabank of a part of the advances portfolio to the Problem Assets Fund was one of the reasons (Asylbek 2018). Among those who were able to reduce the volume of toxic loans, one should emphasize Eurasian Bank, ATF Bank, Tengri Bank. 12 out of 28 Kazakhstan banks since the beginning of 2019y. reduced the volumes of loans in arrears for more than three months (Aulbekova 2019; Musapirova 2019).

Banks' measures to support clients in difficult financial situations led to the increase of the advances portfolio. The share of loans in total bank assets over the past year increased by 9.3% and reached 86.1%. Currently, measures are being taken in all regions to reduce debts of the population on loans, write off penalties and fines. The government intends to restore public confidence in credit products and bank system as a whole.

Banks were overloaded by bad loans after the 2008-2009 yrs. crisis. The Government and the National Bank had a chance to clear off the bank balances from bad loans and restart lending of the economy. However, for various reasons, this was not done, the National Bank in its usual form carried out an unpopular adjustment of KZT rate. The 'Standard & Poor's' agency points out: 'We believe that industry risks in the banking system of Kazakhstan have increased due to the influence of the government, government agencies and related bank owners on the competitive environment' (S&P affirmed the ratings 2018).

Some believe that the National Bank pursues a policy in the interests of the financial oligarchy. It concerns both devaluation and clearing off small banks (Alekhova 2017). This also includes reserves requirements and the Presidential Decree on the allocation of a trillion KZT from the National Fund for strengthening the financial system. The question is about capitalization for the repurchase of toxic assets from the banks. At the same time, some banks have recently gone into oblivion, the campaign to merge the largest banks 'Halyk' and 'Qazkom' comes to an end.

In general, according to the estimates of foreign experts, the activity of the banking system of Kazakhstan is not sufficiently stable and is vulnerable to trends in the economy. According to Standard & Poor's, the weak level of transparency in the structure of banking capital casts doubt on an adequate assessment of risks. At that the experts of Moody's Investors and Standard & Poor's point out that the markets of developing countries, including Kazakhstan, are subject to economic, political, social, judicial and legislative risks, unlike the markets of developed countries. The laws and normative acts, governing the conduct of business in Kazakhstan can change rapidly; there is a possibility of their arbitrary interpretation. Because of the fact that Kazakhstan produces and exports large volumes of oil and gas, the country's economy is particularly sensitive to the changes of the world prices on power resources.

Based on the analysis of banks' activity, it can be said that they operate in the same operating environment, but the top-management strategy may differ, which affects the final indicators. All banks have debt securities on their balance sheets, which mean they can join the purchase of municipal bonds, thus supporting local executive bodies. Enterprises, business structures, etc., which can be active participants in the securities market, are important in the stock market besides the banks.

Real Sector of the Economy: State, Prospects, Opportunities for Participation in the Organization of the Market of Municipal Bonds

To justify the need for organizing the issue of municipal bonds, we evaluated the financial base of this process. In our opinion enterprises, people, banks, pension funds, insurance companies, micro-credit organizations, various business structures can be investors. Most of the companies operate at a profit, with their own funds they may well support socially significant projects implemented in the regions due to the acquisition of municipal bonds. Here are some data.

Significant growth of investments in 2018y. was observed in industry – 27.1%. The share of domestic investments was 69.6%, of external ones – 30.4% (The results of socio-economic 2018; Orynbet *et al.* 2019). The own assets of enterprises remain the main source of financing. The short-term economic indicator, including the development dynamics of 6 key industries, amounted to 104.7% in 2018y. According to the program of industrial-innovative development, new enterprises have appeared in a number of industries. In 2015 – 2017yrs. 378 projects to the amount of over \$8.2 billion were put into operation according to the Industrialization Map of the country, 31 thousand jobs were created. 12 free economic zones function with various stages of infrastructure completion (Main social-economic indicators 2018). The Chamber of Entrepreneurs, in collaboration with USAID, has assessed the current model of business incubators, industrial zones, and technological parks in Kazakhstan. An innovative Business Development Centre and a model business incubator are being created; trainings are held to educate entrepreneurs and to establish business contacts with business partners. The Program of development of mono towns has been successfully launched in the country.

Increased business activity in the real sector favorably affected the growth of enterprises' profits. However, enterprises in Kazakhstan vary widely in profitability. So, in 2018y. the mining and quarrying companies showed the best results in terms of production profitability - 76.9%. Information and communications industries also showed a favorable performance with an index number equal to 19.7% (In 2018 the profitability of production 2019; National

Bank named 2018). At the same time, companies in the field of art, entertainment and recreation still show negative profit: minus 18.2% in 2018y.

Despite the creation of conditions for import substitution, the share of products of local content over the past year decreased by 5%. In the real sector of the economy, there are a number of problems: depletion of the mineral resources base; high volumes of import of machinery and equipment; low competitiveness of local enterprises and lack of final semi-finished products in the value-added chain; weak involvement of the private sector in innovations. Among other reasons, we can name: weakness of the market economy, state regulation remains dominant. To eliminate these shortcomings, the 'Strategic Plan of the Ministry for Investments and Development of Kazakhstan for 2017–2021yrs' is being implemented. A package of incentives, providing for investment preferences, legislative stability, and improving the business climate in accordance with OECD standards is being introduced. The task was set to attract at least 10 multinational companies and create joint ventures with 'anchor investors' in priority sectors of the economy.

The Unified Accumulative Pension Fund (UAPF), insurance and micro-credit organizations have sufficiently large funds, part of which they can invest in municipal bonds. So, on January 1, 2019y. the pension accruals of Kazakhstan reached 9.5 trillion KZT, which were distributed as follows (Beynoyeva 2019):

- 43.3% were invested in government securities of Kazakhstan;
- 12.1%- in government securities of foreign countries;
- 13.9%- in bonds of quasi-public companies;
- 13.5%- in bonds of Kazakhstani banks;
- 3.7% -in deposits in foreign banks.

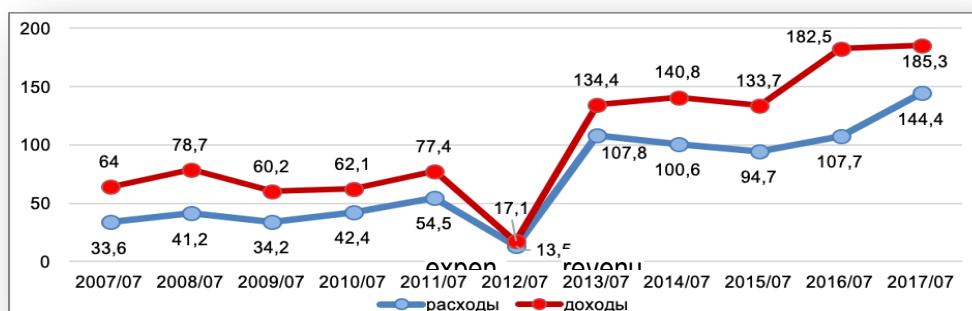
In 2018y. the return on assets of UAPF amounted to 7.9% per annum with inflation equal to 7.1% (Beynoyeva 2019). It is positively that the National Bank supports the Concept of the UAPF diversified portfolio. That is why the placement of IPOs of large companies, which is currently underway, is of interest.

In 2017y., the National Bank of Kazakhstan (regulator) adopted a new strategy for investing pension assets. It includes both independent management of the pension assets by the regulator and external management, involving foreign management companies. Moreover, the assets themselves remain on the accounts of the regulator. In addition, Kazakhstanis will be allowed to participate in the management of their pension accruals. Now, men who have accumulated 8 million KZT and women 10 million KZT have the right to choose a Pension Assets Management Company (PAMC) (Only those with more than 2019). The remaining savings remain in the UAPF under the management of the National Bank. This will allow investors to exercise their right to choose effective investment strategies and create a competitive environment in the services market.

In due course, PAMCs participated in the MS market. For example, 55.7% of the volume of placement of the loan in Astana and 10.8% of the loan of the Mangystauskaya region were made through their offices. In order to protect themselves from inflation, pension funds are ready to purchase low-risk securities, therefore they can be considered as potential clients of the MS market.

In 2017 Kazakhstan's insurance sector was represented by 32 companies, of which 25 were general insurance ones and seven were life insurance ones. Their total assets amounted to \$2.5 billion or 1.81% of GDP (Batishcheva et al 2019). At the end of the year, the total amount of insurance premiums was 6.5% more than in 2016y. As can be seen in Figure 1, insurers' income decreased in 2017y., while the expenses increased.

Figure 1. Revenue and expenses of insurance companies of Kazakhstan, 2017y., billion KZT



Source: Batishcheva *et al.* (2019).

Fitch Ratings Agency notes that Kazakhstan's insurance companies are as before exposed to a complex operating environment with volatile economic growth. As a result, it is not easy for insurance companies to set prices for insurance policies. Due to the high profitability, foreign companies are not allowed in the country's insurance sector due to legislation. However, insurance of such large facilities as an oil refinery is very risky and requires billions of capital, which the domestic insurers do not have. Therefore, they formally take risks upon themselves, but in fact attract foreigners. As can be seen from the analysis of the data, the possibilities of banks, business structures, enterprises, financial organizations for using free cash to buy MS are different.

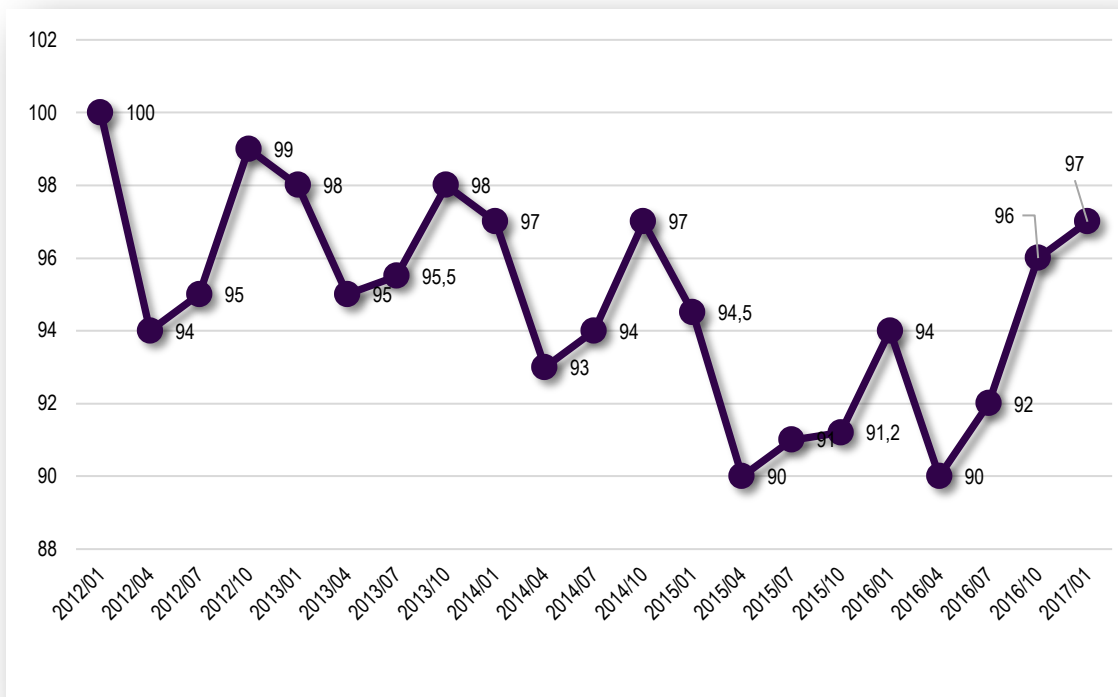
If to talk about enterprises, most likely, some will not buy MS, they themselves would like to issue securities; they do not have enough money for investments, circulating funds. Unlike enterprises, banks have securities in the portfolio, mainly state ones, the profitability of which is not high and long maturities. According to our survey, banks expressed the desire to buy municipal bonds, interest in which may be caused by dividends, the interest on them is higher than the bank interest and the repayment is guaranteed by the tax authority of the local government.

Household Income as a Source of Savings and Assets Acquisition

As can be seen in the above-mentioned Table 2, the main indicators of the economy do not have clear dynamics. The well-being of people depends on GDP, which, in its turn, depends on world prices for oil, gas, metals, uranium, gold, and wheat, i.e. what the country sells. As a result, such indicators as the minimum wage and the subsistence minimum established by the Government are growing annually in KZT and depreciating in dollars. In fact, the real content of the subsistence minimum, wage is determined by the dollar rate, since almost many everyday food and goods are imported. To support the most vulnerable segments of the population, the Government decided to increase the minimum wage by 50% from January 1, 2019y., approximately it will be \$112.4. For comparison: the minimum wage in 2018y. amounted to \$134 in Ukraine, in the Russian Federation it was \$164 (Yurin 2018).

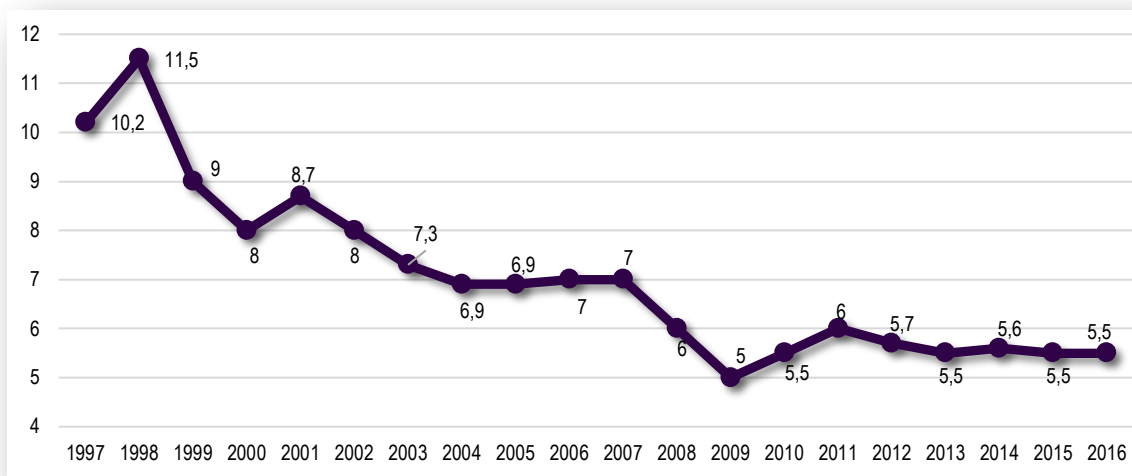
Analysts found out the level of money income of Kazakhstanis. The average per capita nominal cash income of the population in 2017y. amounted to \$258 (Shibutov 2018). At the same time, prices for consumer goods and services in 2017y. increased by 7.5%, while real cash incomes of the population decreased by 2.1%. Over the past five years, the propensity to consume has changed depending on consumer prices, but in general there is a tendency to decrease. Accordingly, the propensity to save increased, thereby reducing the multiplicative effect of costs (Figure 2).

Figure 2. Propensity of the population of Kazakhstan to consume, %



Source: Authors' calculations based on the data of the Statistics Committee of Kazakhstan.

Figure 3. Coefficient of funds, the number of times

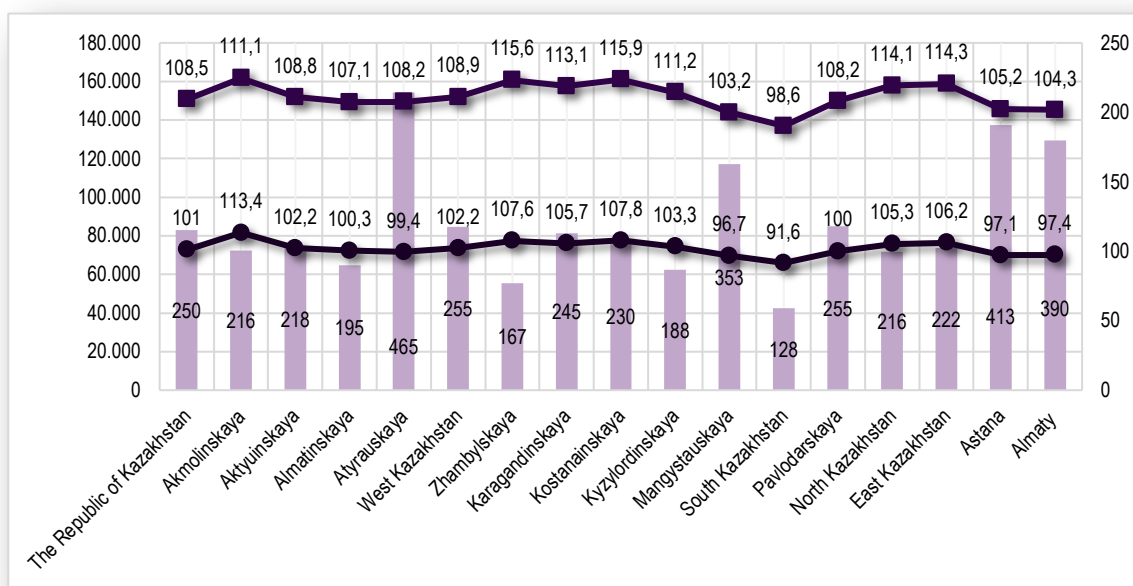


Source: Authors' calculations based on data (What regions replenish 2018; The results of socio-economic 2018).

It should be noted that income inequality is practically not decreasing. Thus, the total income of 10% of the country's wealthiest citizens according to the results of the 2nd quarter of 2017y. was 5.8 times more than the income of 10% of the poorest people (Figure 3). In 2015y. this ratio was 5.5 (What regions replenish 2018; The results of socio-economic 2018). Inequality in income persists also in the regions. The maximum value of per capita nominal cash income in 2017y. was in Atyrauskaya region, where this indicator exceeded the national average by 1.9 times (Figure 4).

South-Kazakhstan and Zhambylskaya regions are the regions with the lowest income: household income amounted to 51 – 67% of the republican level. According to the UN recommendations, the indicator of the coefficient of funds should not exceed 8 – 10, otherwise stratification in the society increases, which sharply increases the risk of social explosions. In general, in Kazakhstan, the safety threshold is respected.

Figure 4. Dynamics of household income in the regions in 2017y.



Source: Authors' calculations based on data (What regions replenish 2018; The results of socio-economic 2018).

It should be noted that income data are sometimes contradictory. So, in the country there is no universal declaration of income and expenses (so far only officials fill out the declaration), property can be registered on those relatives who do not submit the declaration. For the survey of income, a sample of less than 1% of all households from the number of pre-selected individuals is selected, which includes people with a solid income, that can reliably keep a record of the family budget. Given that there are approximately 2.5 million self-employed people in the country who mostly do not pay taxes and do not make contributions to the pension fund, income statistics do not reflect the real picture. Plus, there are unemployed, the number of which is practically kept at the level of 445-450 thousand (Aydapkelov 2018). Besides, the flat scale taxation – 10% individual income tax for everyone is the same, this allows to maintain the difference between high- and low-paid citizens.

Public Opinion: Problems and Ways of Development of the Stock Market

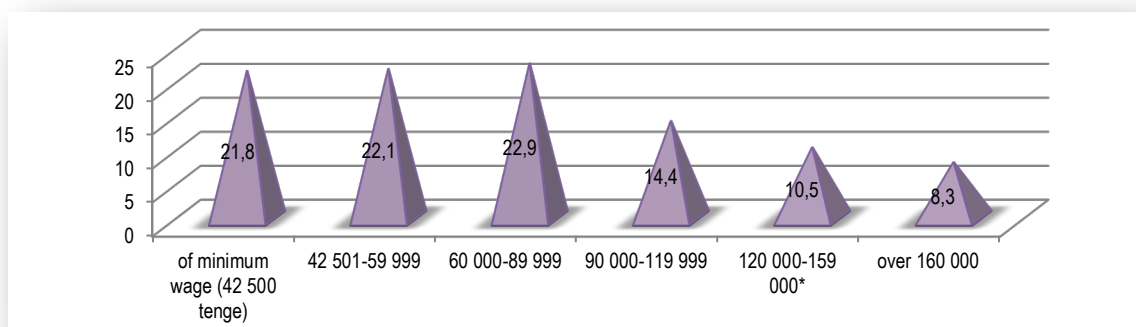
Through interviews and questionnaires, the most prepared part of the population was randomly sampled. (Levinson 2016; Guidelines for interviewers 2014). The sample size was determined based on the total number of the group (educationalists, scientists, service workers, entrepreneurs, government employees, specialists from bank and financial organizations, etc.).

All respondents had higher and postgraduate education, i.e. people, who were sufficiently competent, answered the questionnaire and gave interviews. Teachers of socio-economic and legal disciplines of HEIs represented a significant part of the respondents. It was necessary to find out - have the enterprises, organizations and the population money to buy securities, and are they willing to spend it on this?

Questioning Results

From the total number of respondents, men accounted for 37%, women for 63%. The age of the participants in the survey is mainly 43 – 58 years (60%), up to 42 years – 34%. 54% have higher education, the rest have postgraduate education – magistracy, doctorate – 46%. The family coefficient is 3.94, i.e. at average there are 4 people in a family, of which two works. The average salary per day for all respondents was \$11.8, and the average salary per 1 family member was distributed as follows (Figure 5). Average wage in the country in 2017y was 159,000 KZT. According to the survey data, 88% of respondents get income per family member below the average one.

Figure 5. Distribution of respondents according to the average income per family member, %



Source: Authors' research results.

The Information Bureau Agency according to the National Bank survey published approximate data: '... only 10% of Kazakhstani families have an average monthly income (total for the whole family) exceeding 300 thousand KZT. Less than 5% of families receive up to 40 thousand' (Gareyeva 2019). It should be noted that in the southern region of the country where the survey was conducted, traditionally the incomings are lower (see Figure 4). At that, 46% of respondents spend on food less than 30 thousand KZT, 34% of respondents spend from 30 thousand to 49 thousand KZT, 20% - over 50 thousand KZT.

When asked whether it is possible to save up in the current situation, 43% said that they were barely 'making ends meet.' Meanwhile, those who at least make some savings prefer a deposit (28.3%), keeping of money at home (11.4%), foreign currency purchase (8.6%), investing in business (5.7%), and only 3% buy securities. At that, 89% of respondents do not have experience of security purchase. Thus, the main body of the population has low money income and this does not allow making savings. At the same time, people have the desire and attempts are made to somehow save and make savings.

Interview Results

All respondents do no doubt the need to develop the stock market, but for this they propose to extend the domestic production of material goods and services and to improve the social status of people. The interview showed a critical attitude and some skepticism of people regarding the possibility of developing the municipal bond market. So, the risks are calculated insufficiently, the return of funds even in the presence of guarantees raises huge questions because of the legislation imperfection.

Among the negative reasons are distrust in the authorities' initiatives, corruption, and lack of well-defined guarantees of the rights of ordinary holders of securities. Corruption really hinders the economy: according to Transparency International, in 2018 Kazakhstan received 31 points and took the 124th position from among 180 countries in the Corruption Perception Index (CPI) (Selezneva 2019). The respondents pointed out another problem: this is the shortage of personnel with work experience, poor financial literacy of the population, mentality of people relying on the state, rather than taking the initiative themselves.

It should be noted that so far the population has not been involved in the domestic stock market as a shareholder or investor. It was just a consumer of services. Meanwhile in the developed countries, households are the widest and most active segment of the stock market. Today, the non-operating money of the population in the economy, according to experts, is about \$209 million, and it is necessary to make it cycle, bring income, to work for the country's economy (Ranking of Kazakhstan banks 2017).

In the course of interview, many expressed their willingness to buy securities and look at the problem deeper: there are large enterprises in the country that need to be extended, modernized, through this to create an innovative economy, which will give an impulse to the development of the stock market. In addition, in the regions many attractive projects were not implemented, because of the lack of funds. In 2018y. the authors of the article proposed several highly efficient projects of the businessmen to the regional authorities, these projects have a social significance for the population of the region and can be invested by issuing MS.

Using Stock Market Instruments to Increase the Investment Attractiveness of the Region

To create a stable financial basis for the development of the regions, we consider it appropriate to form a new approach to the policy of loan rising in the local market. In fact, there are not so many sources of financial resources in the region, today we consider investments through municipal bonds to be the most important among them. Using the example of the largest region of Kazakhstan – South-Kazakhstan (since 2018y. Turkestan region), we have considered the option of issuing these securities for projects that are socially significant for the population. In Kazakhstan, the MS market began to develop in the early 2000yrs. Although bonds have proven to be effective, for various reasons, the initiative has not been continued. So, the yield on bonds of the Mangystauskaya region was 14.71%, Almaty – 13.00%, Astana – 10.90%. The yield of GS with the same circulation period at that time was 18.01%, and the bank loan rate was 19-24% per annum. MS turned out to be a cheaper way to raise funds for the needs of the region (Makhmutova, 2008, Fitch Rating Agency 2001).

MB allows achieving better market conditions in comparison with government securities, leading to the improvement of the financial system of the region. The size of the loan depends on the needs of the region in investment resources. In the Atyrauskaya region, funds were raised for the reconstruction and repair of roads, infrastructure development. The local government executive body is the emitter of MS. At that, local authorities take upon themselves the liabilities, pledging to pay the owners of securities from the local budget. The sum of these obligations should not exceed 10 – 15% of the budget, as is customary in Western countries. It is much more profitable for the municipalities to issue their own securities than to take loans from banks. Noncash options for repayment of the MS, for example, using land or real estate, can be envisaged.

There are all competitive advantages for issuing MS in Kazakhstan: the main investor is the region's largest population in the republic (16.7%); the country has experience in MS circulation; development institutes have been formed; according to the industrialization program numerous enterprises, that generate income, are launched. With that, there are sufficiently many ideas and projects that could be implemented, however, due to lack of funds, remain unclaimed. It is this niche that the MS market is intended to close. We have recommended nominating the municipal securities in national currency; the income that the investors receive should be 3-4% higher than the banks offer.

Insurance companies, banks, microcredit organizations, etc. are interested to work in the primary market, therefore they will buy up the MS and hold them until they are fully repaid, since the investors are attracted more by the reliability of stock instruments (local taxes are the guarantee is) than by the profitability. It is to be wished that, after all, the population (small investors) would be the main investor, rather than banks that are interested in covering their liquidity. This is well understood by local authorities. That is why regional mayors (Akimat) acted as

emitters and placed securities on KASE to raise funds for the construction of credit and rental housing for a period of 2 years (On approval of the 'Affordable Housing 2014; State Program of Housing Construction 2016).

At present, one of the conditions for the development of the MS sector is to assign a credit rating to the region, which increases the liquidity of municipal liabilities. In developed stock markets, all liabilities are rated. Assigning a rating would solve many problems locally. Investors' confidence is much higher if they know what exactly their money will go for and where the funds will come from to repay. Akimat becomes an active player in the stock market with marketable securities, its role in the eyes of the population increases.

In the draft of the program of issue we suggest: an interest rate equal to 0.40%; the circulation period of 2 years; pay out of par value at the end of the circulation period with the right of prepayment; coupon payment must be biannually. In order to build an effective mechanism for MS functioning, it is proposed to carry out the following work in stages (Table 4). Based on the established sequence, a business process chart of the organization of issue and trading of municipal bonds is drawn up (Figure 6).

Table 4. Work stages on organization of the issue and circulation of municipal bonds

Work stages	Content of the processes	Time outlays, weeks
1	Negotiations of the emitter (Local Executive Agencies - LEA) and the leading underwriter	7
2	Assessment of market conditions and investment attractiveness of projects suggested for investment	8
3	Preparation of business plan draft. Conclusion of a service contract with the leading underwriter	12
4	Legal assessment of the issue of MS. Working out of a package of legal documents	5
5	Work of the evaluating, audit companies, negotiations of the LEA representatives with these organizations	10
6	Drawing up the Concept of issue and circulation of securities. Design of bonds by the issue initiator	7
7	Search and negotiations with potential investors, warrantors, guarantors. Marketing company to promote bonds on the market. Work with the public through market-makers	7
8	Determination of the subject of pledge, coordination of the issue of municipal securities with the taxation bodies. Making of the issue prospectus and listing for the exchange.	5
9	Obtaining permission from the Government to issue bonds. Preparation of documents and state registration of the MS.	2

Source: Authors' analysis.

Conclusions

- (1) The current stage of development of Kazakhstan is distinguished by insufficient use of economic methods of management, which is proved by a large share of the quasi-public sector; instability of the operation of the banking sector; national currency devaluation; growth of the share of foreign capital, which is not interested in developing the domestic economy. The experience of the development of the securities market of the leading countries is indicative as a standard, but in these countries the stock market developed in a purely market environment. Kazakhstan is affected by the former planned system, development institutions are weak, bureaucracy and elements of corruption take place. Companies do not use the stock market to raise capita;
- (2) The study of public opinion showed that the income level of the population is insufficient as a source of savings and acquisition of securities, although common people have a desire to participate in trading on the stock exchange. The risks of buying securities by the population are not calculated, there are no clear guarantees of the rights of ordinary shareholders, return of funds raises major questions due to the imperfection of the legislation. There is a shortage of personnel with work experience and poor financial literacy of the population is present. It is proposed to solve the problem of the stock market by issuing municipal bonds for projects that are socially significant for the region;
- (3) There is a number of problems on the stock market of Kazakhstan, they are also encountered in some countries with developing economies: the money market and the market of foreign currencies prevail. Government and corporate securities are in circulation, the share of municipal bonds is so small that it is not always shown in the reporting. It is proposed to improve the legislation in terms of protecting the

rights of shareholders, transparency of activity of companies, development of the stock market towards broad participation of the population.

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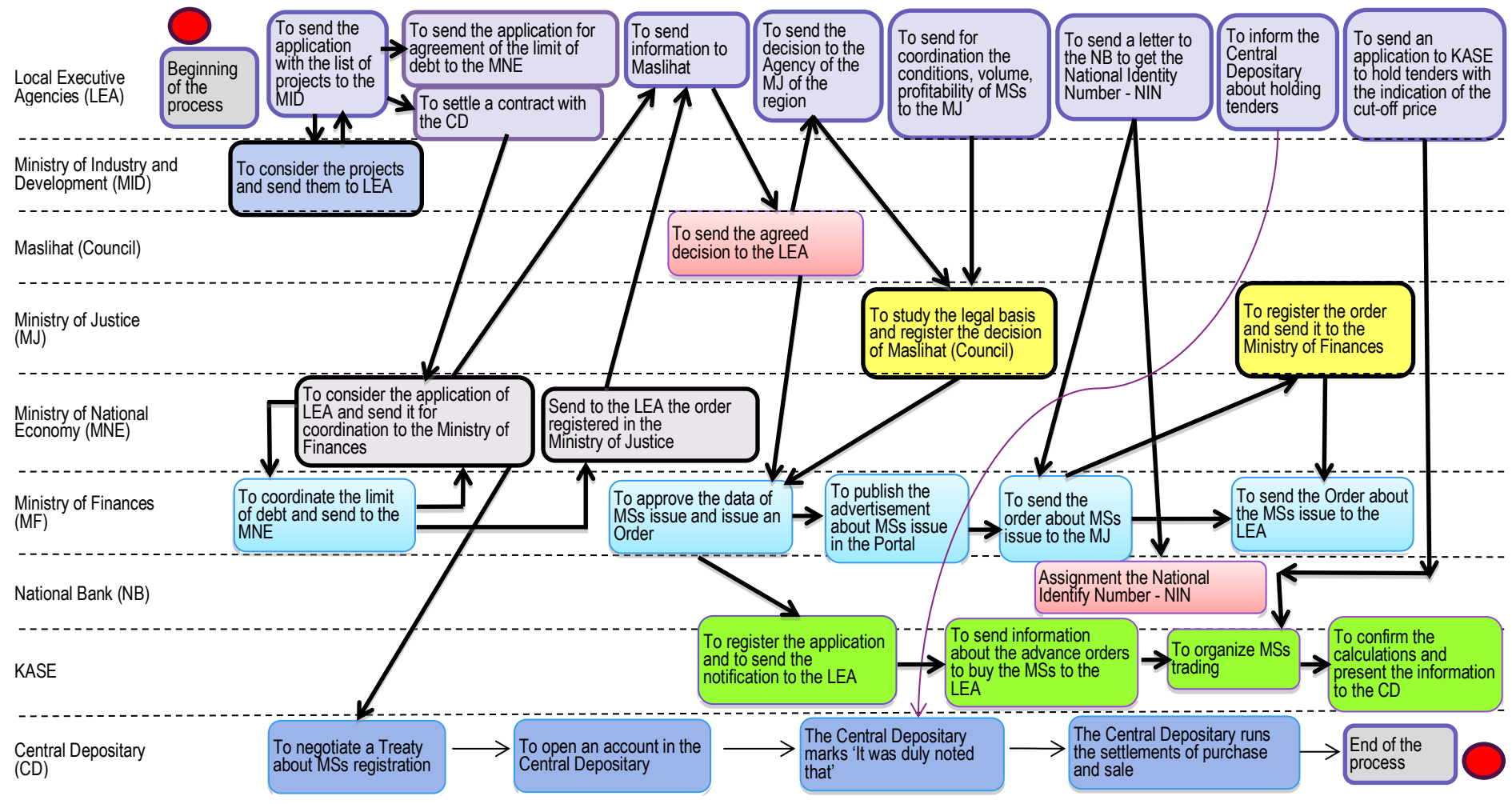


Figure 6. Scheme of business-process of preparation, registration, Municipal Bond placement

Source: Authors' research results.

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