

Banking System of Kazakhstan in the Aspect of the World Development

¹Amina Mussina, ²Rymkul Ismailova, ³Gulzhan Alina, ¹Almagul Jumabekova and ⁴Nurgul Esmagulova

¹Kazakh University of Economic, Finance and International Trade, Astana, Kazakhstan

²Department of Finance, Kazakh Agrotechnical University, Astana, Kazakhstan

³Department of Banking, Kazakh University of Economic,
Finance and International Trade, Astana, Kazakhstan

⁴L.N. Gumilyov Eurasian University, Astana, Kazakhstan

Abstract: The study examines the state of banking activities in the Republic of Kazakhstan, the Russian Federation and the Republic of Belarus, due to similarity of their economic development levels compared to the situation emerging in the world. The statistical materials of these countries illustrate common problems and trends as well as existing possibilities and undertaken measures in the development of banks. The assessed outcome regarding current state of the banking systems in these countries has also made conclusions about the role of the banks in economic system. Emphasis of the research is directed at issues related to the credit and deposit operations of banks. The world bank's achievements substantiate the need of consolidation and specialization of the establishment of banks in Kazakhstan and the improvement of banking regulation based on the leading countries' experiences in the banking business.

Key words: Banking, integration, financial intermediaries, emerging markets, republic

INTRODUCTION

The emergence of financial intermediation is a process that passed through several historical stages. In addition, the importance of formulation and development of financial intermediation was necessary in regard to the economic and social realities which are connected with solving contradictions in the cost of different types of economic systems. This means that without financial intermediaries the existence of the economy is impossible as there will always be conflicts between the interests of separate entities in the form of accumulated temporary free funds and other subjects of additional funding. The modern system of intermediary institutions is quite diverse so that, different countries have their own characteristics and ways of development. The common sign of financial intermediation systems is commercial banks. As the major institutions, they play a leading role in institutional aspect. However, the banking business in various countries differs depending on significance and development pace as well as varies by degree and efficiency of regulation. There are different banking systems in the world practice caused by traditional and national peculiarities. Nevertheless, the banking systems of industrialized countries stand out, having extensive practical experience in the banking business attaining a high level of development in banking industry. In the developing countries of post-soviet space banks

practically started a new period in transition to a market economy. Today these institutions with relatively little experience completely cope with the tasks within the country, ensuring the functioning of monetary and credit systems. However, there are a number of difficulties that banks face in entering the world market because they can't compete at a sufficient level with foreign institutions. Insufficient development level of banks, scope of their activities, infrastructure and management are major obstacles for successful cooperation. What kind of trends and legitimacies are characteristics to the most developed and developing economies in banking business? What could affect the competitiveness of banks and their role in economy? It is necessary to explore the trends of development of different banking systems to get answers to these questions. In this regard, it is worth considering achievements and issues of banks in the post-Soviet space in comparison to the leading banks of developed countries. This study is devoted to the comparative analysis of bank's activities in Kazakhstan within the context of the world banking business. The purpose of this study is to identify opportunities and perspectives of banks in Kazakhstan in representing the global competitiveness and overviewing their achievements.

Formation of the two-tier banking system: The traditional theory of financial intermediation has given the answer to the question about the reasons for the existence of banks

as well as their economic role in the economy. Banks carry out the transformation of non-liquid assets into liquid liabilities, by monitoring credit contracts and reducing transaction costs. The so-called “triple” transformation is performed under the transformation of capital, time and risk. Image of modern commercial bank was formed during the historic and economic development. Analyzing changes and major shifts in the banking industry which contributed to the emergence of current type of modern bank, should be started from the process of legislative reform of 1960's that took place in most countries with developed market economies. The main directions of those reforms brought us to:

- Deregulation of the financial market
- Strengthening competition in banking business
- Computerization and financial innovations
- Financial globalization

By the 1990's the period of profound changes in organization and management of banks was started in the banking system of industrially developed countries of the world. This period in literature is called “financial revolution”. At the same time, the banking systems of socialist countries began to break down. This period is generally acknowledged as the transition to the market principles of economy. These countries in a short period of time had to learn the principles of market and create an adequate financial and banking sector in economy. The factors that determined the root changes in depth (transformation) in the CIS countries are of different characteristics. First of all, the crucial role was played by the political and economic transformations, exacerbating such conditions as:

- Transition to market economy and commercialization of banking activities
- Creating a two-tier banking system with allocation of the emission center and business banks (second-tier banks-STB)
- Computerization and introduction of new technologies
- Transition to the international standards of accounting, regulation and banking supervision
- Development of the currency market and securities market (Parusimova, 2008)

Important step for banks in Kazakhstan was an enactment of two laws in 1995 “About the National Bank of Kazakhstan” (31 March 1995) and “About Banks and Banking Activities in the Republic of Kazakhstan” (30 August 1995). These two laws have defined the

further development of the banking system in the country and nowadays continue to operate as a legal basis. Certainly, in the following years, they had made a number of amendments and changes related to the demands of the economy (Law of the Republic of Kazakhstan, 1995a, b). The National Bank as the Central Bank plays the role of emission center and lender in the reserve system of the country. In this regard, there are not sufficient differences from developed countries in the world. However, the Central Bank of Kazakhstan is responsible for regulation and supervision of financial and credit institutions. It is known that in many countries of the world, these functions are carried out by special organizations. Banking systems of the CIS countries were formed under similar conditions. For example, in Russia after the adoption of following laws in 1990: “About the State Bank”, “About banks and banking activities” and “About banks and banking activities of the Russian Federation” was established the two-tier banking system in the form of the Bank of Russia and commercial banks (National Bank of the Republic of Belarus, 1990ab). In Belarus “About the National Bank of the republic of Belarus” and “About banks and banking activities in the republic of Belarus” laws have been adopted in December, 1990. The National Bank of the Republic of Belarus was created on the basis of the republic bank of the State Bank of the USSR as it was in Kazakhstan. The specialized state banks have been transformed into joint-stock commercial banks (Law of the Republic of Belarus, 2008; Law of the Republic of Kazakhstan, 2006).

MATERIALS AND METHODS

Analysis of the role of banks in the economy: The fact about the generality of bank's operations is undoubted because the essence of banks as intermediaries remains unchanged, regardless the country they are functioning. As for the quantity and scope of banking transactions, it is quite clear that they are determined by the characteristics of the various countries and their economies. Based on this statement, we consider the structural composition of the Kazakhstan banks and compare them with other countries. During the establishment and development period of market relations (since 1993) the institutional structure of the second-tier banks of Kazakhstan went through significant quantitative reductions (Yutish *et al.*, 2007). As it is shown in Table 1, in 1994 the optimization process was started in the number of banks and continued into the significant reduction in their numbers until 2005. During these 10 years, the number of banks decreased from 184-36 which is >5 times. During this period, the

Table 1: Information about the second-tier banks of Kazakhstan (by end of the year)

Indicators	1994	2004
The total number of banks of the second level, of which	184	36
State	4	1
With the participation of foreign capital, including subsidiaries	85	1510
Branches	1042	385
On the territory of the Republic of Kazakhstan	1042	384
Foreign	-	1
Withdrawn licenses for the year	33	-

Table 2: The Kazakhstan banking sector's structure

Types of banks	2007	2012	2013
Number of banks including	35	38	38
Banks with 100% share owned by state	1	1	1
Banks with foreign participation		19	17
Representation of banks-nonresidents	26	-	-
Subsidiaries of banks	16	14	
Number of branches of banks	352	362	378

Table 3: Number of banks in Russia, Belarus and Kazakhstan

States	2007	2012	2013
The Russian Federation	1136	956	923
The Republic of Belarus	27	32	31
The Republic of Kazakhstan	35	38	38

annual reduction in the number of banks in different years varied from 4-6 up to 50 institutions. Subsequently, during 2005-2014, the quantitative indicators on the subjects of banking system have not changed (Table 2). Nowadays, the banking sector of Kazakhstan is represented by 38 second-tier banks where 17 banks are with foreign participation, including 14 subsidiaries of banks. Moreover if we consider the list of banks, we can notice that it includes the majority of banks that operate as successful and developed institutions. These banks are top ten banks such as "Kazkommertsbank" JSC, "BTA Bank" JSC, Halyk Savings Bank of Kazakhstan JSC (HSBK), "Bank Center Credit" JSC (CCBN), "ATF bank" JSC, etc.

Second-tier banks in Kazakhstan are universal commercial banks which conduct all banking transactions for economic entities, including legal entities and population. There are no specialized institutions in the country serving only individuals or implementing investment transactions. If we compare the dynamics of banks in Russia and Belarus, it may be noted that in recent years in the Russian banking system the number of banks is reducing. A number of experts and analysts consider that Russia has too many banks and their number will be reduced sooner or later by three times (Table 3).

The situation in the republic of Belarus is more stable and the tendency towards reducing or increasing the bank's quantity is not observed. The raised question is whether there are many or few banks in Kazakhstan? Some experts hold an opinion that the number of banks in

Table 4: Grouping of banks in Kazakhstan by the volume of assets

Volume of assets (bln. KZT)	Number of banks at 01.03.2014
From 1000-2000	6
From 500-1000	4
From 200-500	8
From 45-200	12
From 5-25	8

Kazakhstan should be reduced. They propose to conduct an amalgamation process of banks through merging and uniting. Moreover, formal steps have been taken in this direction which is reflected in the Concept of development of the financial sector until 2030 (Halyk Bank, 2011). These conclusions are of common sense considering the competitiveness of banks both in the domestic and foreign markets. If we consider banks in Kazakhstan in terms of their own equity assets and liabilities, there is a leader's group including 6 banks, followed by 12 middle-tier banks. The remaining 20 banks are fairly small banks that are not able to withstand the competition in many areas. It should be noted that 8 banks are at the bottom part of the list and their assets between 5 and 25 billion tenge. That is 200 times less than the assets of leader banks (Table 4). According to the introduced standards Bazel III, the country has adopted a policy aiming at consolidating the banks. Henceforth, the requirements were increased to the minimum ownership of capital within the financial institutions. The minimum size of ownership capitals in Kazakhstan's banks will be increased by 10 times since 2019 and it must be at least 100 billion tenge. The decision was adopted on amalgamation of major banks: "Halyk Bank" JSC and HSBC, "Kazkommertsbank" JSC and "BTA bank" JSC, "Alliance" JSC, "Temir" JSC and Forte bank. The results of such integration will bring into the emergence of three giants in the banking sector. The combined share of the three new structures will have 46% of all branch network and 57% of ATM parks (Federal Law, 2002). Besides, a number of mergers have been planned, especially for small banks. In this way the number of banks in Kazakhstan will be reduced twice until 2020.

The question of how many banks must be in the country should be decided not only from the perspective of the quantitative reductions but also taking into account the qualitative growth of banks. It would be rational to fulfill requirements of the position in terms of the quality of capital, the quality of risk management in conjunction with the system of internal control and the ability to allocate resources and manage liquidity, attract customers and to keep them.

We believe that the consolidation of the market should improve the structure of the banking sector in conditions of limited growth. Larger banks should become more resistant to economic cycles, introduction of Basel

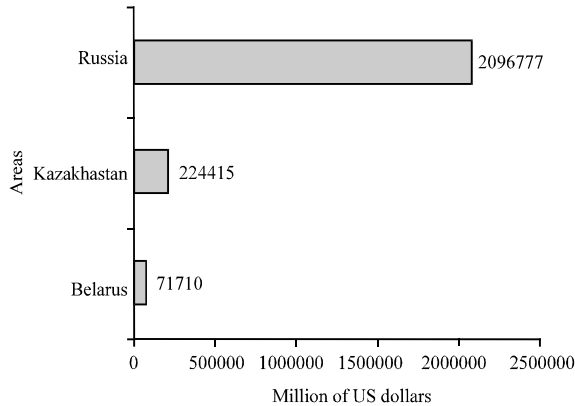


Fig. 1: The GDP of 2013

Table 5: Banking assets to GDP (%)

Countries	2009	2010	2011	2012
Kazakhstan	67.9	55.2	46.5	47.4
Russia	75.8	74.8	76.3	79.4
Belarus	60.6	77.5	94.6	60.9

3 standards and also to the changes in the competitive environment as a result of the financial integration of Kazakhstan, Belarus and Russia in the framework of the Eurasian Economic Union (the EEU). The selected vector of development trend, defined in the project of the financial sector development concept until 2030 can be considered as a positive factor in the consolidation of banks. It is noteworthy that the Government and the National Bank of Kazakhstan focused on consolidation of mainly middle-tier banks but not the largest banks in the country. Another aspect of the consolidation of banks, in our point of view is the unification according to the work principle that is in compliance with the specialization in selected areas. For example, the specialization in retail credit, mortgage lending sector, operations with securities and so on. If banks will be consolidated in regard to the specialization, their competitiveness and stress resistance will increase. Specialization does not mean denying the universality of banking activities. The banks have the right to decide what direction is a foreground way for the business and on what client they should be targeted.

RESULTS AND DISCUSSION

Analysis of macroeconomic indicators: Figure 1 shows the GDP size of 2013 in comparison to three countries: Belarus, Kazakhstan and Russia. The leader among these countries is the Russian Federation which takes 8th place in the World Bank ranking, whereas Kazakhstan is 45th and Belarus the 68th. Apart from the difference in absolute values there is a great difference in relative indexes which confirm the position of Kazakhstan, Belarus and Russia as countries with a developing market economy. Index rates of Kazakhstan and other CIS

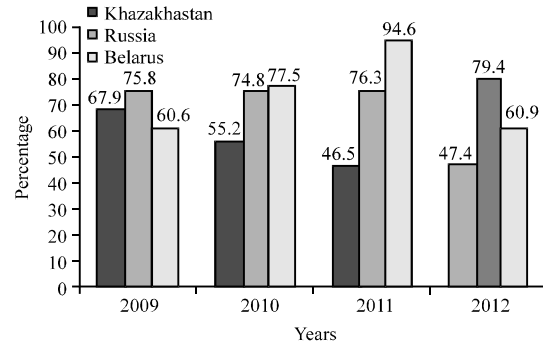


Fig. 2: Kazakhstan, Russia and Belarus banking assets to GDP

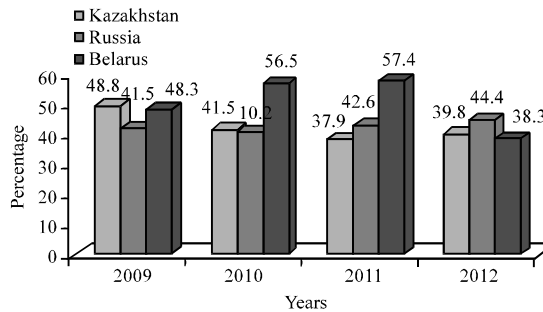


Fig. 3: Bank loans to GDP (%)

Table 6: Bank assets (USD bln.)

Countries	2008	2009	2010	2011	2012
Kazakhstan	98.4	77.9	81.600	86.300	92.300
Russia	987	980	1.107	1.296	1.620
Belarus	28.8	29.1	42.500	30.900	37.500

Table 7: The comparison of bank loans to GDP (%)

Countries	2009	2010	2011	2012
Kazakhstan	48.8	41.5	37.9	39.8
Russia	41.5	40.2	42.6	44.4
Belarus	48.3	56.5	57.4	38.3

countries are very low (Table 5). In 2011 Belarus had the highest rate (94.6%) while in Kazakhstan it was the lowest number (46.5). Table 5 and Fig. 2 show that the ratio of Kazakhstan’s bank assets to GDP has a tendency to decline because bank assets in the post-crisis period (between 2008 and 2011) declined from USD 98,4 bln. to USD 86.3 bln. Kazakhstan has the lowest ratios of bank assets to GDP if we compare it to others. However, the banking system of Kazakhstan is 10 times smaller than Russian by the volume of assets (Table 6).

The banks asset’s volume of Kazakhstan and Belarus is immeasurably small compared to similar indices of Russia and Switzerland. This is due to many reasons, including historical, geographical and economic factors. If we compare another important indicator of bank activity, the ratio of credits and GDP, the highest level of credit to GDP was in Belarus (in 2011) and it was 57.4%. The lowest rate belongs to Kazakhstan (37.9%) (These data are shown in Table 7 and Fig. 3). Fairly low indices of

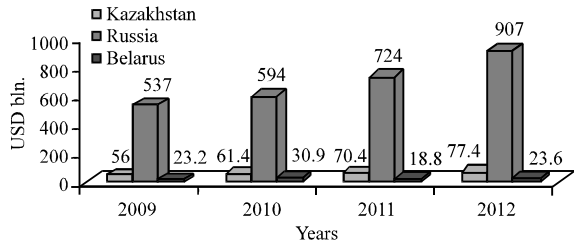


Fig. 4: The volume of bank loans

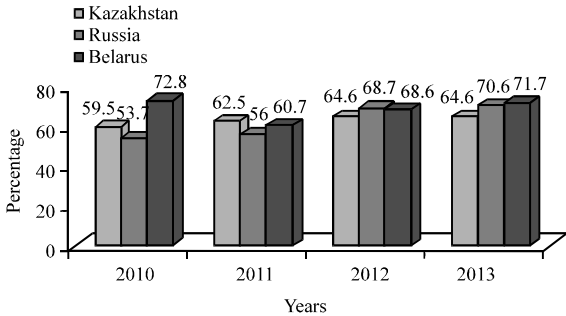


Fig. 5: The share of loans in bank assets of Kazakhstan, Russia, Belarus

Table 8: Bank loans (USD bln.)

Countries	2009	2010	2011	2012
Kazakhstan	56.0	61.4	70.4	77.4
Russia	537.0	594.0	724.0	907.0
Belarus	23.2	30.9	18.8	23.6

Table 9: The structure of assets in the Kazakhstan's banking sector (as of end of year, percentage share of total)

Assets	2010	2011	2012	2013
Cash refined precious metals and correspondent accounts-liquid assets	5.6	8.3	8.2	9.5
Deposits placed with other banks	6.6	3.6	2.9	2.3
Securities	14.5	11.1	10.6	9.2
Bank loans and "reverse REPO" operations	59.5	62.5	64.6	64.6
Investment in capital	2.5	2.3	1.8	1.7
Other assets	11.3	12.2	11.9	12.7
Total assets (without reserves (provisions))	100	100	100	100

credits to GDP ratio in the three focus countries compared to developed countries show a general problem associated with the low role of banks in the economy. There is the fact that banks are not completely crediting the economy, despite the fact that these financial institutions are credit leading institutions in these countries. Analysis of bank credit volume in these countries shows that the least of all credits provided by banks of Belarus is due to its conservative lending policy (Table 8 and Fig. 4).

Analysis of loans: Loans are the predominant assets for banks of Kazakhstan as well as in Russia and Belarus. For the banks of Kazakhstan credits remain predominant, their share reaches more than two-thirds of assets up to 64.6% (Table 9). Thus, banks are mostly crediting the economy

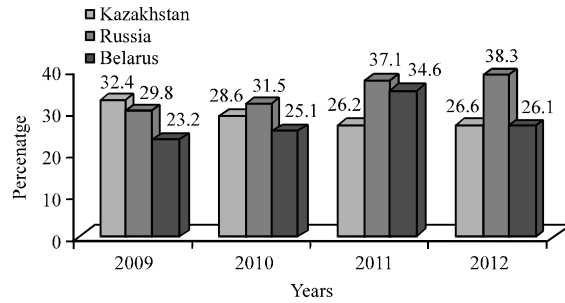


Fig. 6: Bank deposits (as % to GDP)

Table 10: The share of loans in assets (end of year, percentage share of total)

Countries	2010	2011	2012	2013
Kazakhstan	59.5	62.5	64.6	64.6
Russia	53.7	56.0	68.7	70.6
Belarus	72.8	60.7	68.6	71.7

and the population, despite the relatively high risks. The risks are a limiting factor in increasing the credit investments. The advantage of credits in assets as a characteristic has been a feature for banks of Kazakhstan during the whole period of operation. The similar situation is developing in Russia and Belarus; evidences are provided in Table 10 and Fig. 5. The predominance of credits as the main type of asset is typical for commercial banks which is intended to serve the needs of the real sector of the economy. This issue is highly relevant for developing countries where alternative credit market as a source of resources is not sufficiently developed. As we know such alternative could be the securities market. However, there are certain problems in its formation in the countries of the former Soviet Union and Kazakhstan. One of the tasks that is needed to be addressed is the extension of a financial investment instrument's list as well as creating additional opportunities and forms of investments and savings for the population. Today the opportunities of population and economic agents for choosing the financial instruments for the investment are limited. Hence, the main type and way of investing the free funds for population and businesses are still deposits in banks. Further, we will consider the situation in the deposit market.

Analysis of deposits: In the analyzed countries the situation on deposits is similar to the situation on credits. In the three countries, the level of this index was around 40% over the past 4 year (in Kazakhstan 32.4%, in Russia 38.3%, in Belarus-34.6%) (Fig. 6). The Russian banks have the largest volume of deposits (Table 11, Fig. 7). Bank deposits are the main traditional source of attracted funds in banks. Here is a characteristic that is typical for the all analyzed countries Kazakhstan, Russia and Belarus. It could be compared in percentage for the ratio of client's total funds to obligations of banks (Table 12, Fig. 8). Deposit policy of banks is the main

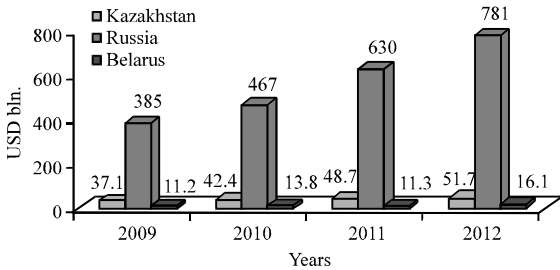


Fig. 7: Dynamic of bank deposits in Kazakhstan, Russia, Belarus

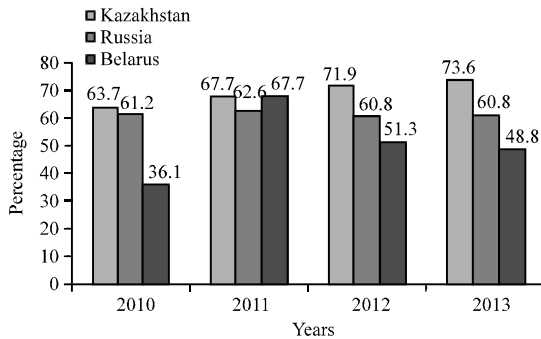


Fig. 8: Dynamic of the share of client deposits in liabilities of the banking sector

Table 11: Bank deposits in Kazakhstan, Russia, Belarus (USD bln.)

Countries	2009	2010	2011	2012
Kazakhstan	37.1	42.4	48.7	51.7
Russia	385.0	467.0	630.0	781.0
Belarus	11.2	13.8	11.3	16.1

Table 12: The share of client deposits in liabilities of the banking sector (%)

Countries	2010	2011	2012	2013
Kazakhstan	63.7	67.7	71.9	73.6
Russia	61.2	62.6	60.8	60.8
Belarus	36.1	67.7	51.3	48.8

component of banking policy. By the virtue of the successful deposit policy it becomes possible to increase the resource base which is in turn provides opportunities for active work. That is why banks pay much attention to the deposit policy, customer attraction and creating the maximum favorable conditions for them. The main problems of banks in Kazakhstan, Russia and Belarus in attracting deposits include:

- Low incomes of population
- Low level of confidence in banks that has been destroyed by a number of negative events of past years (reforms, crises)
- Low yield deposits, eaten up by inflation

At the same time the lack of alternative investment opportunities for the population and economic agents

allows banks to build up this kind of resources. According to experts, reserves of deposit's growth are high enough. However, the large potential customers-depositors prefer foreign banks than domestic banks because nowadays in Kazakhstan risks are high for savers. The state guarantees the safety of the deposits of individuals within the limits of 5 million tenge (from January 1, 2012) that amounts to approximately 27 thousand USD. Compensation of deposits in the Russian banks is less than in Kazakhstan and in the insured case, the depositor will receive the deposit amount but not more than 700 000 rub (about USD 19,000). (Note: The official exchange rate of the dollar to the ruble of the Bank of Russia from 26 August 2014 is 36.1201 rub.) Unlike Kazakhstan and Russia, 100% guarantees to savings exist in Belarus, regardless of the amount of the deposit according to the Law of Belarus". About guaranteed compensation of bank deposits of physical person" from July 8, 2008. It should be noted that, today few countries in the world guarantee full refund of deposits. For example, in the United States deposits are refundable up to USD 100 thousand dollars per depositor, in most EU countries it varies between 15 and 20 thousand euro. Starting recently, 100% guarantee of deposit's security exists in Austria, Germany, Greece and Ireland among several other countries. Now a days deposit guarantee systems in Russia and Kazakhstan are aimed at protecting the interests of small and medium-sized investors. Besides, for the banks of Kazakhstan and Russian the attracting a big capital in the form of deposits is difficult due to the owner's absence of ability to manage his assets on his own. In this way, the information asymmetry risk is increasing. In this regard, the global private banking system experiences from year to year the development and expansion of their customer's bases due to large deposits.

Having examined the specific problems of banking activities in Kazakhstan and comparing the situation in CIS countries with whom Kazakhstan bound by the agreement on Eurasian Economic Union we can try to formulate a number of conclusions:

- Analysis of Kazakhstan's banking system in the aspect of the world development has shown that Kazakhstan has certain achievements and trends
- Positive developments in activity, despite the effects of the global financial crisis which appears in the stability of the banking system indicators
- Declining trend in the number of banks through their consolidation
- Rational diversification of assets and liabilities
- Meanwhile, Kazakh banks are experiencing definite problems in the development of the banking sector

- Low roles of banks in the economy, reflected in the low level of the ratio of loans assets and deposits to GDP
- Narrow range of financial instruments for public investments

Kazakhstan as Russia and Belarus has a certain desire to standards and regulations of developed countries as the consolidation of banks and improvement of their competitiveness which is dictated by the need of integration development within the EEU and globalizing world. Countries with a developing market economy have great interest in the vast experience and high achievements of the world banking sector, in particular, the experience of private banks in attracting major investors in order to hold money in the country and circulate them through banks.

CONCLUSION

The study on the problems of the banking activities in Kazakhstan aims to further exploration of the experience and achievements of the global banking practices. Identified trends and characteristics in the development of banks of different countries, namely Russia and Belarus, showed that Kazakhstan's banks today have the objectives of consolidation and concentration of the banking business, dictated by the global integration processes and globalization. Consolidation and specialization of banks to work with customers on the principle of asset management as well as the development of financial instruments for investment would help banks to expand and improve national and international competitiveness. Important factor in this direction is the improvement of the bank regulation system, namely, the adoption of appropriate rules and regulations of functioning specialized banks and deposit guaranteeing systems in the light of the current experience of the countries-leaders in the banking business.

REFERENCES

- Federal Law, 2002. On the Central Bank of the Russian Federation. Bank of Russia, Russia.
- Halyk Bank, 2011. On the banking market of the Republic of Kazakhstan will be a tendency of consolidation of its players. Business Week (Almaty), Halyk Bank, Kazakhstan. <http://www.halykbank.kz/ru/press-center/media-publications/2011/2697>.
- Law of the Republic of Belarus, 2008. On deposit guarantee (deposits) of individuals. Law of the Republic of Belarus, Belarus. <http://infobank.by/1497/default.aspx>.
- Law of the Republic of Kazakhstan, 1995a. On Banks and Banking Activity. National Bank, Kazakhstan.
- Law of the Republic of Kazakhstan, 1995b. On the National Bank of the Republic of Kazakhstan. National Bank of Kazakhstan, Kazakhstan, Pages: 32.
- Law of the Republic of Kazakhstan, 2006. On Mandatory Insurance of Deposits Placed in Banks of the Republic of Kazakhstan. Law of the Republic of Kazakhstan Publisher, Kazakhstan.
- National Bank of the Republic of Belarus, 1990a. Law of the Republic of Belarus of the Supreme Soviet of the Byelorussian Soviet Socialist. National Bank of the Republic Of Belarus, Belarus, Lyeninski Rayon.
- National Bank of the Republic of Belarus, 1990b. On Banks and Banking Activities in the Republic of Belarus. National Bank of the Republic of Belarus, Belarus, Lyeninski Rayon.
- Parusimova, N.I., 2008. Banking: Model of Development. Moscow Academy of Entrepreneurship, Moscow, Russia, Pages: 495.
- Yutish, V.M., B.S. Tadzhiyakov and V.K. Nazarov, 2007. Kazakh banks at the Turn of the Century. Monograph Publishing Company, Almaty, Kazakhstan, Pages: 832.