

# ECONOMIC POLICY REFORMS: GOING FOR GROWTH COUNTRY NOTE

## KAZAKHSTAN

After two decades of relatively strong economic growth Kazakhstan's GDP per capita is now at levels similar to that of some of OECD member countries, such as Turkey, Greece or Chile (PPP adjusted). Consequently, GDP per capita is now some 50% below the level in the upper half of OECD countries.

Labour productivity has significantly increased in Kazakhstan since 2000. However, it is still low in comparison with the best performing OECD countries with considerable resources employed in low-productivity activities, such as agriculture. Over the past decade, investment has been stable relative to GDP at levels similar to the OECD average. Most investment is taking place in industry and mining, while in some other areas, for example infrastructure, capital stock appears less developed. Total factor productivity growth has been on a trend decline since 2000 and has even been negative in the recent years. R&D spending, in particular government spending, is significantly lower than the OECD average.

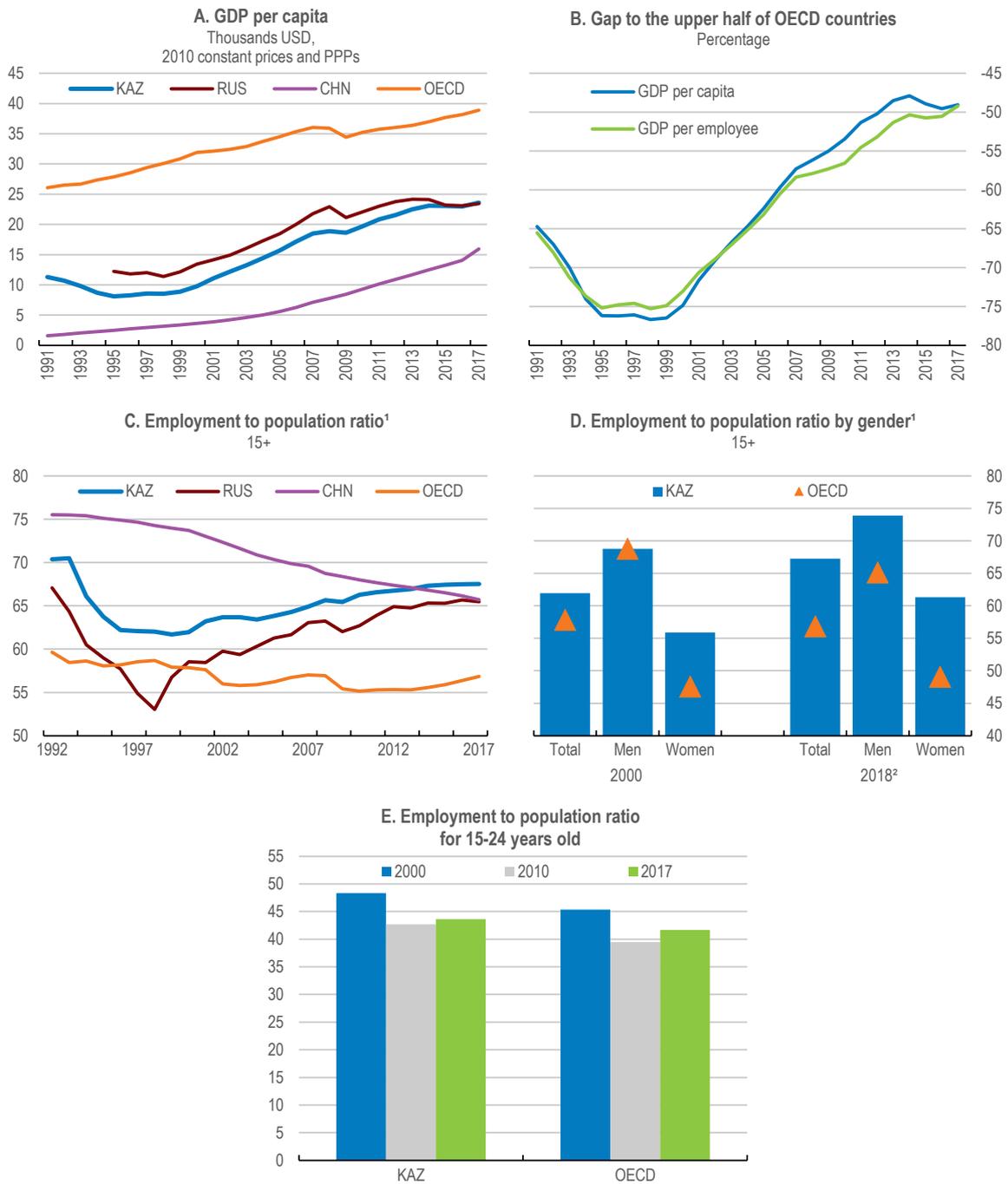
The employment to population ratio has been growing since the beginning of the 2000s. Employment rates among men and women are now well above the OECD average and higher than in Russia and China. The population is relatively young, and employment rates of young people are well above the OECD average. Unemployment is low in international comparison. Informality is significantly higher than in advanced economies, but has been decreasing according to estimates.

Inequality as measured by the Gini coefficient (World Bank estimate) has been on a decline in the past two decades and is now close to the level of OECD member countries with the lowest inequality. Consistently, the share of income held by the poorest 20% households has been increasing in the past two decades, and is just below 10%, well above the OECD average.

Greenhouse gas emissions per capita are significantly higher than the OECD average, China and Russia. More than 90% of total Kazakh population is exposed to a level of fine particulates above WHO Air Quality Guideline thresholds, a higher share than in advanced countries.

The economy is heavily reliant on natural resource exports, in particular oil. Sustained improvements in wellbeing will require the transition to an innovative, flexible economy with high quality jobs and low emissions. Reviving productivity growth and boosting innovation are key challenges in the face of globalisation and digitalisation and require a more pro-competitive approach to regulation, in particular of State Owned Enterprises and network sectors. Improving the incentives for and capacity to innovate and invest in skills via the education system are crucial to global challenges and sustain high employment levels in the future. Finally, a broad and stable tax system will be both crucial for steering the transition as well as for ensuring sustainable revenues in the face of global challenges, in particular that of curbing climate change.

Figure 1. Growth performance indicators

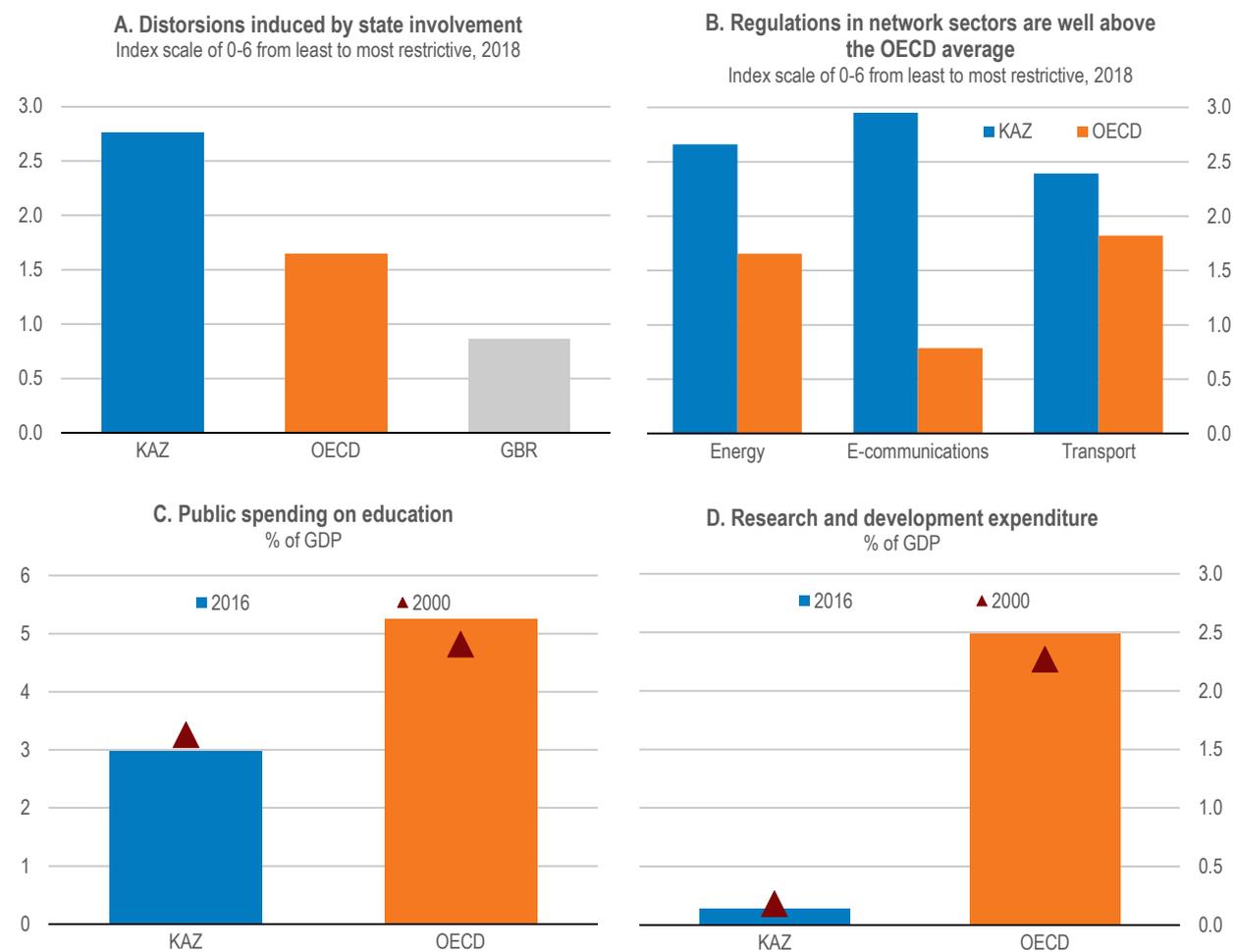


1. For China, Russia and the OECD average, data refer to total ages.

2. For the OECD average, the last available year is 2017.

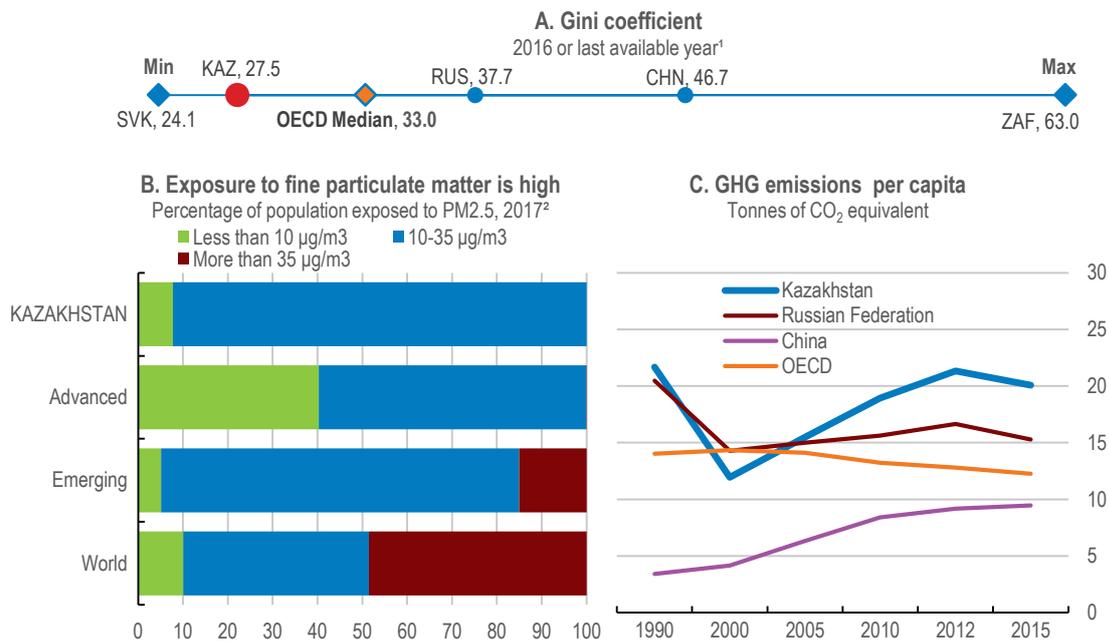
Source: Panels A and B: OECD, Economic Outlook Database, International Labour Organisation (ILO), Key Indicators of the Labour Market (KILM) Database and World Bank, World Development Indicators (WDI) Database; Panels C,D,E: World Bank, World Development Indicators Database and OECD, Labour Force Statistics Database.

Figure 2. Policy indicators



Source: Panels A and B: OECD, Product Market Regulation Database (as of April 2019); Panels C and D: World Bank, World Development Indicators Database.

Figure 3. Beyond GDP per capita



1. The last available year is 2016 except for CHL DNK DEU ISL IRL JPN KOR CHE TUR BRA RUS for which the last year refers to 2015 & 2017 for CHN, CRI and KAZ.

2. According to the World Health Organisation (WHO), exposure to fine particulate matter (PM2.5) has significant adverse effects on health compared to other pollutants. Inhaled PM2.5 cause serious health problems (respiratory and cardiovascular diseases), having most serious effects on children and elderly persons. The estimates of chronic outdoor exposure to PM2.5 (from both anthropogenic and natural sources, in µg/m<sup>3</sup>) are derived from satellite observations, chemical transport models and ground monitoring stations. Population exposure to air pollution is calculated by weighting concentrations with populations in each cell of the underlying gridded data.

Source: Panel A: OECD, Income Distribution Database; World Bank, World Development Indicators; China National Bureau of Statistics; Panels B and C: International Energy Agency (IEA) and OECD, Environment Databases.

The OECD's Going for Growth framework builds on a wide set of OECD and external indicators of outcomes and policies. A crucial set of policy indicators is the OECD's Product Market Regulation (PMR) indicators. The PMR indicators are key OECD policy tools, allowing cross-country comparisons and identification of best practices to achieve a business-friendly environment, improve the openness and conduct of business, ensure a level playing field and facilitate quality job creation. In this respect, they represent an instrument for the governments to identify which regulatory areas could become more competition-friendly and provide examples of alternative and best practice regulatory set-up from other OECD and non-OECD countries. The PMR indicators build on an extensive questionnaire filled in by the national authorities with OECD support. The 2018-19 PMR was the first time for Kazakhstan to participate in the full cycle of consultations and results are used to identify Kazakhstan's scores in both economy-wide and sectoral PMR indicator relative to OECD average. Two out of the Top 5 Going for Growth priorities for Kazakhstan are identified thanks to PMR indicators and the full report on Kazakhstan's performance in the PMR indicators is presented in the in depth PMR Chapter.

## Going for Growth priorities

**Improve the governance of State Owned Enterprises and reconsider the role of the state in the economy.** SOEs play a crucial role in the Kazakh economy, spanning most of goods and services sectors. The high share of SOEs strengthens the role of SOE governance, which is weak in international comparison. While some significant steps have been taken in the recent years to reduce and clarify the role of the state in the economy, reforms are needed to ensure that the remaining SOEs compete on a level playing field with private companies in order to strengthen the incentives for the development of a dynamic, innovative private sector and a more productive allocation of resources.

**Table 1. Potential areas for improvements in SOE governance and the role of the state in the economy**

	Areas for improvement as derived from the OECD PMR indicators
Scale down the role of the state in the economy by:	<p>Advancing with the privatisation plans laid out by the government. Reducing government involvement in the economy, especially in manufacturing and service sectors</p> <p>Facilitating the procedures for partial or entire SOEs sale by the state</p> <p>Re-evaluating the necessity of golden shares in privatised SOEs</p>
Improve the governance of SOEs by:	<p>Simplifying and clarifying the ownership structure of SOEs</p> <p>Ensuring the ownership and regulation of SOEs in separate public bodies. Ensuring arms-length regulation of SOEs. A common approach in OECD is a strong and independent competition authority and sectoral regulators</p> <p>Ensuring a level playing field for SOEs and private companies they compete (or potentially compete) with, e.g. vis-a-vis laws and regulations (i.e. competition law, procurement law).</p> <p>Reviewing and reconsidering state aid to SOEs. Removing implicit state guarantees to SOEs and improving transparency and tendering of universal service obligations. Making state aid rules and actions transparent</p> <p>Changing the procedures of appointing top management of SOEs to appointment by the board of directors and not by the government</p> <p>Facilitating the procedure of restructuring, bankruptcy and mergers of SOEs</p> <p>The adoption of the OECD Guidelines on Corporate Governance of SOEs could be an important step in improving the functioning of the SOEs</p>
Improve public procurement by:	<p>Using tenders as main method for public procurement of goods, services and public works</p> <p>Ensuring the time allocated for bidders is proportional to the size and complexity of the tender</p> <p>Reconsidering whether the contracting authority should continue to provide the reference price in the tender documentation for the goods, services or public works</p>

**Open the network sectors to competition to seize their full productive potential.** Network sectors are the backbone of an economy. However, in Kazakhstan, they are dominated by state presence and heavily regulated. Underinvestment in infrastructure, its roll out and innovation is a resulting problem hampering business dynamism in downstream sectors and regional development.

Table 2. Potential areas for improvement in network sector regulation

	Areas for improvement as derived from the OECD PMR indicators
<b>Entry regulation by:</b>	Introducing regulated third party access to electricity transmission grid and distribution network Replacing the obligation of getting the license to establish a national road freight business by simple notification of relevant authorities Conducting and making public the evaluations of market power held by the fixed and mobile telephony operators
<b>Regulation of network sectors and competition by:</b>	Strengthening the independence of regulators, for example by moving them outside government ministries
<b>Retail price regulation by:</b>	Basing the regulated retail tariff for electricity and gas on the tariffs or cost of the most efficient supplier As competition improves, moving from the system where the electricity and gas retail tariffs are regulated by the government to the only for vulnerable consumers or not regulated at all Considering liberalising the retail tariffs charged by domestic air carriers. Identifying routes, services or consumers eligible for universal/public service obligation and design a transparent, competitive pricing mechanism for pricing them Introducing an independent regulatory ex-ante or ex-post supervision in the airports on the level of their charges or revenues Legally requiring the mobile operators to provide appropriate and timely information about billing of roaming services to their customers
<b>Vertical separation by:</b>	Progressively moving to stronger separation of activities in the various segments of the electricity, gas and water transport sectors
<b>Barriers to foreign entry by:</b>	Reducing the barriers to foreign entry in air transportation  Liner-conferences (private arrangements between shipping lines to utilise common rates) in the water freight transport sector should not be exempt from the application of antitrust rules

**Reform the education system to better deliver skills and employability.** The education system needs to be ready to respond to the demand for skills of the future. However, public spending on education has not kept up with GDP growth, resulting relatively low teacher salaries and poor education outcomes in the past. Recent reforms aim at improving various aspects of the curricula (e.g. language teaching and transition to relevant education programs) but a thorough review of the education system, coupled with an increase in investment is warranted.

**Set up a robust, stable tax base.** Oil revenues are over a third of budgetary revenues, making budgets heavily dependent on oil prices and volatile. While oil production and exports have backed economic growth in the past, energy and emission intensity is high. Moreover, recent tax reforms have aimed at encouraging oil exploration. In the longer-term, under global climate mitigation targets, such a revenue base will not be sustainable and a broad, reliable tax base should be developed. In particular, the tax system appears as rich in tax expenditures, which can erode the tax base and result in complex incentives and should be subject to a complex evaluation.

**Improve market openness and reduce barriers to foreign trade and investment to create more incentives for an innovative, competitive and flexible economy.** The economy is still heavily dependent on extractive and heavy industries. Multi-factor productivity growth is sluggish and innovation expenditure, in particular of the private sector, is very low in international comparison. While, thanks to reforms, administrative burdens to new entry are low, a number of barriers limit the flexibility and hinder the restructuring of the economy. For example, behind-the-border trade barriers are high, with burdensome, bureaucratic and non-transparent procedures and weak governance. The foreign entry to a number of sectors is limited. What is more, perceptions of corruption and an inefficient judicial system hamper investment and FDI incentives. As regards competition, the 2017 reforms of competition laws and authorities are a welcome step, but it will take time to evaluate to what extent the adopted measures are effective in assuring a level playing field.

**Table 3. Potential areas for improvement of the barriers to trade and investment**

	<b>Areas for improvement as derived from the OECD PMR indicators</b>
<b>Differential treatment of foreign suppliers by:</b>	Reducing the barriers to foreign entry (i.e in air transportation, mining, professional services and public procurement)
<b>Barriers to trade facilitation by:</b>	<p>Improving the availability of information on the agreement with the other countries as well as the information on procedural rules for appeal</p> <p>Reducing the number of documents necessary for import and export and the time necessary for its preparation.</p> <p>Improving the share of import and export declarations cleared electronically as well as enabling the availability of full-time automated processing for Customs</p> <p>Simplifying trade procedures in terms of time, cost and improving availability and flexibility of Single Window and Customs</p>

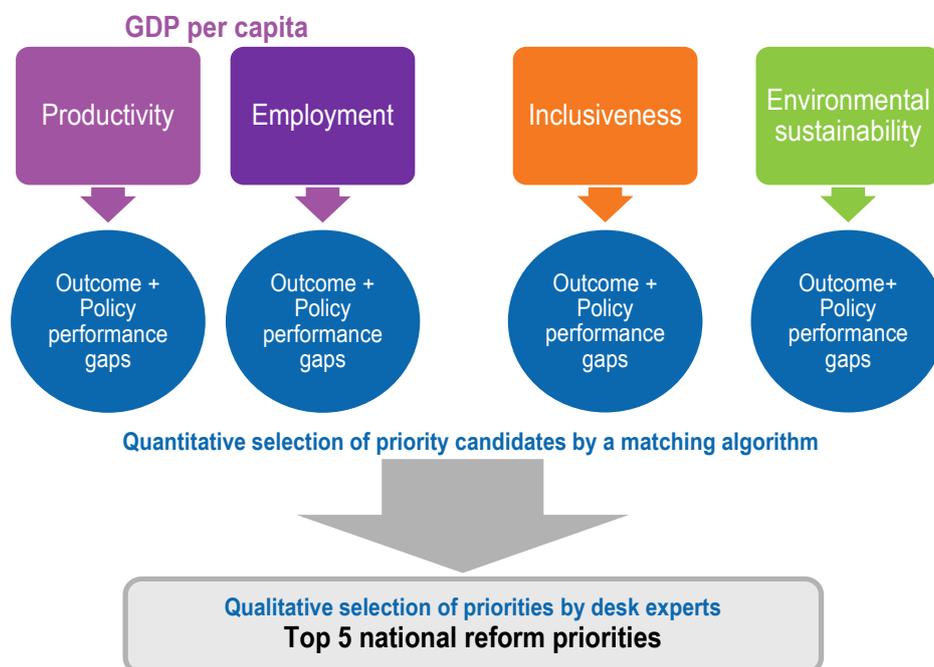
### The OECD Going for Growth framework

Since 2005 the OECD's Going for Growth framework identifies the Top 5 priority challenges for policymakers to address in order to boost longer-term living standards and to ensure that the gains are broadly shared across populations. The Top 5 priorities are identified for OECD member states and, since 2011 for key non-member economies. For each country, they take into account domestic circumstances.

A combination of quantitative and qualitative tools is used to identify the policy priorities (see Figure 4). In the first, quantitative step, indicators of policies and outcomes they affect are matched into pairs based on empirical evidence. For example, multifactor productivity growth (an outcome indicator) is matched with product market regulation indicators such as administrative burdens on start-ups or barriers to entry in professional services (policy indicators). Similarly, the aggregate employment rate (an outcome indicator) is matched with the level of the labour tax wedge (policy indicator), while the employment rate of women (performance indicator) is matched with childcare related costs embedded in tax and benefits systems (policy indicator).

Each outcome-policy pair is then compared to the benchmark of the OECD average in order to identify poor performance on both outcome and policy jointly. The pair becomes a candidate for a priority in a given country, if both the outcome and matching policy rank poorer than the OECD average.

Figure 4. The Going for Growth framework for identifying reform priorities



In the second, qualitative step, OECD expert assessment is used to select the actual Top 5 priorities. The priority candidates identified in the first step serve as a starting point, but the set of potential priorities is supplemented with areas relevant for growth, which may not have been well measured or not straightforward to compare. In collaboration with OECD experts, the Top 5 reform priorities for each country are identified, taking into account the local context. For each of these priorities, detailed reform recommendations are formulated and past reform actions are reported.

The Going for Growth framework is centred around the decomposition of growth in GDP per capita into labour productivity and labour utilisation (hours worked per capita) growth. Since 2017, inclusiveness is an additional dimension of the *Going for Growth* exercise. The integration of inclusiveness relies on a dashboard of indicators of income and non-income dimensions such as inequality and poverty, job quantity and job quality, labour market inclusion of vulnerable groups, gender gaps and equity in education. Along similar principles, in the 2019 *Going for Growth* edition, environmental sustainability considerations have been integrated, so as to address the issue assuring the longer term gains in growth and wellbeing.

For Kazakhstan, as for most non-member economies, the set of available outcome, and in particular policy, indicators is limited due to data availability. This restricts the nature of priority candidates that can be evaluated quantitatively. Still, the data availability is improving, including in the case of some major tools used in the Going for Growth framework. An important example is the inclusion of Kazakhstan in the 2018-9 vintage of the OECD's Product Market Regulation indicators. This has led directly to the identification of two of the five priorities (*Improve the governance of State Owned Enterprises and reconsider the role of the state in the economy* and *Open the network sectors to competition to seize their full productive potential*) and contributed to the identification of a third one (*Improve market openness and reduce barriers to foreign trade and investment to create more incentives for an innovative, competitive and flexible economy*). Another, forthcoming milestone is the participation of Kazakhstan in the 2018-9 OECD Programme for International Student Assessment, which will contribute to the refinement of the priority on education and skills.