Key industries of the Kazakhstan economy showed stable development dynamics in 2006-2007.

Thus the highest rates of development were demonstrated in the construction and financial sectors. The high rates of construction development may be explained by, on one hand, the pre-existing low housing level of the Kazakhstan population, and on the other, as a response to the President’s Message to the people of Kazakhstan in 2004 and 2005, according to which housing construction became one of the main priorities of the state, in addressing the country’s social and economic problems.

Besides, factors supporting high rates of economic development were as follows:

- growing prices for raw materials which determine the level of economic development for the moment;
- investment projects on the development of services and production goods were financed in full;
- high income of the state budget, covering its expenses without using facilities from the National Fund;
- growing level of real incomes, pensions and benefits paid to disadvantaged groups of the population, allowing them to pay their obligations in due time;
- increasing import volumes due to growing domestic demand.

For 2007 the main macroeconomic indicators have maintained the positive dynamics observed in previous years. According to real-time data, rates of economic development are expected at 8.5-8.7 %. The liquidity crisis in the world in 2008 will result in decreased external capital inflows to the country. There will be structural changes in the financial, construction and trade sectors, as well as in the sphere of real estate operations. Incomes of the population, enterprises and the state will be stable. A non-payment crisis in the industrial sector and among households is not expected.

Mid-year inflation reached 10.8% compared to an estimated 7.3-8.3%. Based on 11-month results the positive trade balance of the country decreased by $721.1 million compared with the same period in 2006, totaling $2808.9 million.

Steady financing of the industrial sphere and consumer requirements of the population will be forthcoming, providing there is favorable development of the country’s macroeconomic indicators and external market conditions.
After the housing price increases of previous years, starting from the end of the first quarter of 2007, the Kazakhstan real estate market began to flatten and even decrease. Market movement to the bottom price will take place in fluctuations, with periodic variations both towards growth and towards decreases in the average price. Prices are most likely to “bottom out” in the second quarter of this year.

The home market shows the sustained solvency of the population and enterprises. There is no mass formation of debts to creditors by the population or by legal entities. As of January 1, 2008 default debts under the credits granted by second-tier banks for construction were 1.39%, including mortgage debts of only 0.33%.

**Financing of housing construction**

The total amount of investments into housing construction for the period January – December 2007 compared to the same period of the previous year has increased by 26.2%.

During the years of housing development program implementation the structure of investments into housing construction has considerably changed 2005 – 2007. As a result:

- the share of borrowings increased from practically zero in 2003 to 31.4% in 2007;
- the share of enterprises means decreased from 81% to 60%;
- the share of all level budgets decreased from 15.5 to 8.9%.

This is an important signal for the banking sphere, the reaction to which should be to strengthen repayment guarantees for the funds received.

A regional breakdown of all investments in housing construction shows that the greatest volume (55-60%) takes place in Almaty and Astana. Accordingly, the greatest number of incomplete construction sites is in these two cities.

The tendencies of housing construction finance in Kazakhstan shown by the analysis, especially structural ones, will occur long-term as well. As for the regions, we expect a shift of emphasis from Almaty and Astana to regional centers and other cities. High volumes of borrowing for housing construction will continue, though rates of growth will decrease considerably compared to current levels. This is connected with the outrunning growth in prices for contract works, land and construction materials. As for housing construction itself, the building of residential space intended for commercial use will develop.
Commissioning of housing

In 2007 the construction industry of Kazakhstan continued its boom, including housing construction, but with lower rates of growth. So, for the year construction work (services) volume, inclusive of appraisal, totaled 1307.5 billion tenge, exceeding the level of 2006 by 15.3% (against 26% growth in 2006).

Nationwide, the greatest activity is in construction work performed by private building organizations – 74.8%. Foreign contractors perform 24.6%, and state constructors just 0.6%.

The growth of housing construction volumes in Kazakhstan was caused by the following factors:

- strengthening of Kazakhstan’s investment rating, its banking system and liberalization of capital imports;
- growth of the population’s income and high, formerly pent-up demand for housing, especially in the largest cities;
- the priority position of housing construction in the economic policy of the Kazakhstan Government – creation of a system of mortgage credits, building savings and guaranteeing of mortgage credits, covering at least 50% of credit risks during the whole credit term;
- tightness of industrial activity financing frame for Kazakhstani investors, and a lack of effective investment projects;
- the availability of large illegal incomes for certain population groups (bribes, illegal business income, legal business income hidden from tax authorities etc.).

Cost of building and market prices for residential real estate

The average actual construction cost of floor area 1 sq. meter in apartment houses totaled 40,200 tenge in 2007, or increased by 3.8 % compared to the same period of the previous year. Such growth is not only due to increased prices for construction materials. According to the analysis, prices for real estate are just partially based on the cost component.
Since August 2007 the Almaty real estate market has suffered continuous reduction of housing prices for the first time in the last five years. This situation has been caused by the following factors:

- solvent demand decrease (housing availability index tends to decrease);
- psychological factor: consumers expecting maximum reduction of prices also contribute to reduction of demand on the market;
- revaluation of secondary housing against general boom in real estate market;
- toughening of second-tier banks’ conditions for mortgage crediting;

**Dynamics of prices in the real estate market**

The reduction of Almaty real estate prices has so far affected only the residential real estate market; demand for land remains high.

Kazakhstan still has considerable reserves for the development of mortgages, which will develop increasingly intensively as people’s incomes grow. One more argument in favor of mortgage is the mentality of the Kazakhstan population, which tends to prefer living in one’s own property rather than in rented housing.

It should be noted that mortgage crediting programs in Kazakhstan are considered inaccessible for the population and less risky for financial structures in comparison with the USA. This is due to the fact that an obligatory condition, besides requirements concerning income confirmation, is the availability of a liquid pledge, the mortgaging cost of which is discounted at least by 15–20% for existing apartments and by 50% for those under construction.

In connection with current liquidity, lack of credit volumes of the construction industry, from August till December 2007, have decreased by 38%.

As of January 1, 2008, according to National Bank data, II tier banks invested 6% less credits in the national economy than in the previous month. Meanwhile financing of construction industry increased by 18%. As of January 1, 2008 total mortgages amount totaled 684 billion tenge. Meanwhile defaulted debts under mortgage loans made up only 0.33% of the outstanding loans.
Current state Kazakhstan commercial real estate market

During the last 5–7 years growth of business activity in Kazakhstan has several times exceeded volumes of commercial real estate commissioning.

The principal causes of demand for high quality commercial real estate are as follows:

- program of small and medium business support;
- creation of financial center in Almaty;
- arrival of considerable numbers of foreign companies;
- branch network development in the banking sector.

During the last several years the volume of commercial real estate areas commissioned has been growing. A mismatch of supply and demand in the commercial real estate market has caused rents to be overpriced. Presently, Almaty along with London, Paris and Moscow is one of the most expensive cities in the world in which to rent an office.

Analysis of the pricing process has shown that the market for office premises may not be considered fully formed due to the absence of uniform qualifications for business-centers, an unstable market situation and the non-transparency of financial transactions. The quality of properties on offer does not match the high prices being charged.

In the immediate future expansion of the sector will continue and extend. Additional commissioning of various scale and location trading areas is expected on the market.

The hotel market is still insufficiently mastered. Hotel accommodation is often unduly expensive. Kazakhstan still suffers shortages of three-, four-, five-star hotels; however this situation may be changing, with the arrival of well-known international brands.

During the last two years investors became much more active in the market of warehouse premises. This will help reduce the double lag of supply in the commercial real estate segment. Currently the need for high-class warehouse premises in Almaty ranges from 350 to 500 thousand sq. m. According to participants of the market the average construction cost of class “A” warehouse 1 sq. m varies from 700 to 800 dollars, which exceeds the cost in Russia. Besides, about 50% of the total premises cost is made up of the land lot. This rather high cost is caused firstly by a larger share of imported materials and secondly by additional expenses on seismic strengthening works, and thirdly, by a shortage of companies erecting warehouses.
Residential real estate tendencies and forecast

The current situation on world financial markets does not allow highly confident predictions of these factors’ value. However, taking into account that increase in prices for real estate has stopped before the crisis in the USA mortgage market, we may expect segment by segment reduction of prices for real estate, at least, in Almaty. In its turn, the price dynamics of Almaty real estate influences prices for real estate in the regions. Increased interest rates and, accordingly, decreased housing availability will help reduce prices in the secondary market, especially for older properties; some correction in the market for secondary housing should be expected in the most prestigious areas of the city. As for the primary sector, here the situation will depend on whether the building companies can maintain more expensive credits; if this is not the situation then the supply of new housing will decrease and prices will rise. However some companies may reduce sales price of their objects to receive funds for credit settlement for the purpose of demand stimulation. Nevertheless, considerable correction of prices in the primary market is improbable.

Generally, currently we see a downward price correction and this situation will probably continue till the end of the second quarter of the current year.

Incomplete construction assessment and forecast

Taking into account the current situation in the financial sector related to the real estate and construction market of the republic (decrease in bank liquidity, toughening of loan conditions, increased interest rates, a slow down of housing price increases, reduction in demand for real estate), External Analysis department has made an assessment and forecast of incomplete construction volumes in terms of value. Here two variants have been considered:

1. the crisis in the West will be quickly overcome and building companies will be able to raise the additional funds (both at the expense of internal and external investors) necessary to complete existing construction projects.

2. volumes of investment from banks, enterprises, organizations and the population will further decline and the downward tendencies of real estate prices will continue until the end of 2007. This variant is con-
CONCLUSIONS AND PROPOSALS BASED ON HOUSING MARKET

Fundamentally, the Kazakhstan economy is stable, without obvious destabilizing factors;

Banks, despite restricted access to international debt markets, fulfill their obligations in full and in due time;

RK National Bank undertakes timely and adequate measures to manage the internal currency market and li-
quidity;

Rates of bank system growth will slow in the short-term, which will have a positive impact on the quality of bank assets in the longer term;

Taken as a whole, demand for housing is high and in the long-term housing construction will remain one of the state’s economic policy priorities;

Price levels on the housing market are experiencing some correction. Market movement to the bottom price will take place in fluctuations with periodic variations both towards growth and towards decrease in the average price. Changes in the commissioned housing structure towards more economy class apartments will smoothly occur;

Housing construction in Kazakhstan remains an attractive investment;

The liquidity crisis will prompt many banks to reconsider their approaches to business, to improve their risk man-
agement systems and to expand their sources of funding.

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