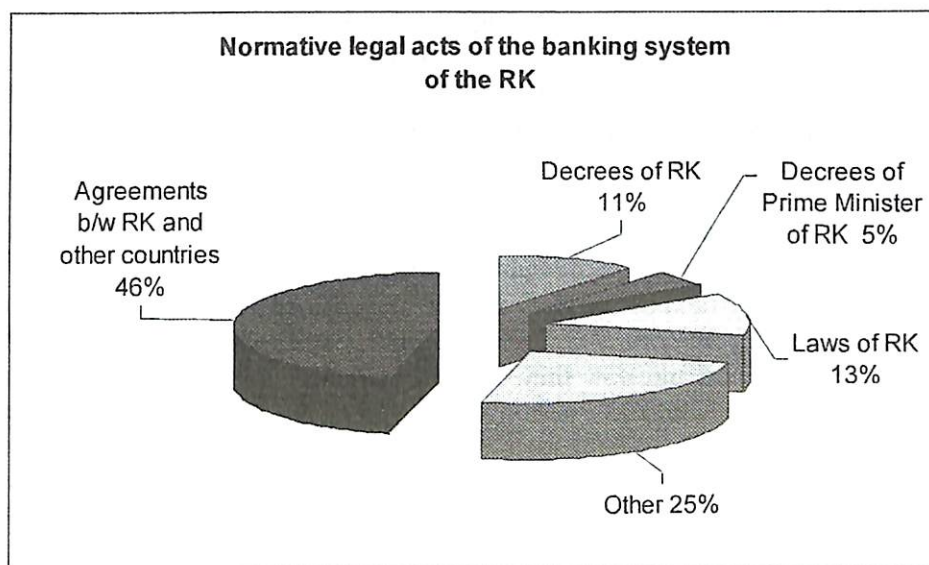


Banking industry in Kazakhstan strongly regulated by the government. It is shown in **Figure 2**:

Figure 2



By method of Kuatbaeva G.K

This figure shows as percent of each law from all normative legal acts. There are about 621 normative legal acts in banking system of RK. 286 of them are agreements between RK and other countries, 68 are decrees of RK, 31-decrees of Prime Minister of RK, 81-laws of RK, 155-others.

Despite on great achievement of banking sector in Republic of Kazakhstan, it has a problem in crediting sector. It constrained with rising of crediting new and riskier sectors, as: construction, real estate etc.

According to analyses of analytics, the solution of the problem can be the accuracy of the work of financial system.

Source:

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EXPECTATIONS AND THEIR ROLE IN ECONOMY

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People generally can not predict future with certainty. This fact forces people to make expectations and predictions about future. Expectations in economics refer to the forecasts that people and households make about future prices, sales, incomes, taxes, or other economic variables. Economists generally talk about people's beliefs in the context of their expectations about the future. Expectations influence every economic decision people and households make. For instance, when consumers make decisions about how much to spend and save, expectations play an important role. When making these decisions, people base their actions on both current income and future prospects. It means that actions today are influenced by people's beliefs in the future and their future expected earnings. Likewise, when people save for retirement, they base their decisions on how long they expect to be employed and their expected future annual income. Again, expectations about the future matter in an important way, as people's beliefs affect the steps people take today and the plans they make for tomorrow, aimed at achieving their economic and personal goals. Business decisions are similarly affected by firms' view of the future. In fact, their behavior is perhaps even more dependent on an assessment of

the years ahead. Companies thoroughly try to project future gains that can be derived from current investments. When making a decision to invest in a specific project today, businesses compare the project's expected future flow of revenues to its current cost. This is fundamental to capital budgeting. These cash flows are only expectations, because they are guaranteed exactly. They are derived from management's belief in the firm's value proposition, the marketing studies that support the project, and the firm's assessment of its own capability. Expectations even affect economic decisions about foreign activity. Decisions about whether to import or export or whether to make a foreign direct investment or a foreign financial investment are all tied to the future relative expected value of the currencies involved. Results of public policies, implemented by government also depend on expectations of people. The main goals of government policies can not be achieved, because of people's beliefs and extent to which they believe to government.

So, expectations matter in every field of our lives and making right expectations about future can bring significant success and eliminate risk. So, in my work I've tried to disclosure the nature of expectations, how they're formed and how they can affect total outcome. I would like to reveal the role of expectations by dividing them in 3 sections: consumption and expectations, investment and expectations and role of expectations in implementing public policies (monetary and fiscal).

Consumption and Expectations

Expectations in the goods market generally connected with decision of how much to consume and how much to save. Consumption is very important part of GDP: in most of countries it is estimated to be more than 60%. So, consumption spending of people should be taken in serious consideration by all economists. Most early theories of consumption have assumed that consumption entirely depends on current income:

$$C = F(Y_D) = F(Y - T)$$

where Y_D -disposable income, Y -current income, T -taxes

This consumption function assumes that there is positive relationship between income and consumption. However it does not take into consideration the effect of expectations, but expectation is very important determinant of consumption decision. Consider such a situation, when person receives unexpected high income for short-run, but realizes that it is temporary income, rational person will save most of this temporary income.

Theories, which have taken expectations into account, were independently proposed in the 1950s by Milton Friedman (received the Nobel Prize in 1976) from the University of Chicago and Franco Modigliani (received the Nobel Prize in 1985) from MIT. Milton Friedman proposed permanent income theory of consumption. He argued that people prefer stable consumption, that's why they save in bad times and dissave in good times, thus maintaining stable level of consumption. In his point of view, consumers take into consideration permanent income, which is the sum of all future expected incomes discounted to the present. Franco Modigliani's life cycle theory of consumption stressed that people plan their consumption for their entire lifetime. Now new consumption function appears:

$$C = F(\text{Total wealth}, Y - T)$$

where total wealth is the sum of non-human wealth (financial assets, property) and human wealth (after tax labor income discounted to present).

Friedman in his original work assumed that expectations of future income are formed in mechanism, which he called adaptive expectations. This means that people readjust or adapt their estimations of permanent income each period, based on their previous estimations of permanent income and actual changes in it.

Friedman was the first, who implicitly has used concept of rational expectations in his work. It is implicit in much of his discussion. Rational expectations – expectations, which are formed by using all available information and, which exclude the possibility of making systematic errors in predictions of people. The first person to introduce the rational expectations in economics was John F. Muth of Indiana University in the 1960s. He used the term to describe many economic situations in which the outcome depends partly upon what people expect to happen. The price of an agricultural commodity, for example, depends on how many acres farmers plant, which in turn depends on the price that farmers expect to realize when they harvest and sell their crops. As another example, the value of a currency and its rate of depreciation depend partly on what people expect that rate of depreciation to be. That is because people rush to desert a currency that they expect to lose value, so contributing to its loss in value. Similarly, the price of a stock or bond depends partly on what prospective buyers and sellers believe it will be in the future.

In subsequent works John F. Muth and Robert E. Hall from Stanford University imposed rational expectations on versions of Friedman's model, with interesting results. In Hall's version, imposing rational expectations produces the result that consumption is a random walk: the best prediction of future consumption is the present level of consumption. This result proves the consumption-smoothing aspect of the permanent income model and reflects people's efforts to estimate their wealth and to allocate it over time. If consumption in each period is held at a level that is expected to leave wealth unchanged, it follows that wealth and consumption will each equal their values in the previous period plus an unforecastable or unforeseeable random shock—really a forecast error.

The rational expectations version of the permanent income hypothesis has changed the way economists think about short-term stabilization policies (such as temporary tax cuts) designed to stimulate the economy. Keynesian economists used to believe that tax cuts would boost disposable income and thus cause people to consume more. But according to the permanent income model, temporary tax cuts would have much less of an effect on consumption than Keynesians had thought. The reason is that people are basing their consumption decision on their wealth, not their current disposable income. Because temporary tax cuts are expected to be reversed, they have little or no effect on wealth, and therefore, they have little or no effect on consumption.

The concept of rational expectations asserts that outcomes do not differ systematically (i.e., regularly or predictably) from what people expected them to be. The concept is motivated by the same thinking that led Abraham Lincoln to assert, "You can fool some of the people all of the time, and all of the people some of the time, but you cannot fool all of the people all of the time." From the viewpoint of the rational expectations doctrine, Lincoln's statement gets things right. It does not deny that people often make forecasting errors, but it does suggest that errors will not persistently occur.

There are a lot of examples in recent history, when bad expectations lead to bad condition of economy. Example is 1990-1991 recession in USA. Many economists argue that the main reason of 1990-1991 recession was substantial drop in consumption, which in turn was due to large decrease in consumer confidence.

Here is the table, which shows what was happening in USA in 1990-1991:

Quarter	Change in Real GDP (bn.\$)	Forecast error for GDP	Forecast error for consumption independent from income (c_0)	Index of Consumer Confidence
1990: 2 nd quarter	19	-17	-23	105
1990: 3 rd quarter	-29	-57	-1	90
1990: 4 th quarter	-63	-88	-37	61
1991: 1 st quarter	-31	-27	-30	65
1991: 2 nd quarter	27	47	8	77

The first column shows the size and the timing of recession. It gives the change in GDP, in billions of 1992 dollars for each quarter. The third column gives the forecast error, the difference between the actual value of GDP and the value of GDP that had not been forecast by economists one quarter earlier. A positive forecast error indicates that that actual GDP turned out to be higher than was forecast; a negative forecast error indicates that the actual GDP turned out to be lower than was forecast. We can observe from this table that actual GDP was significantly lower than it was forecasted. It means that recession was unpredicted. Construction of GDP follows this way:

$$GDP=C+I+G+NX$$

where C – consumption, I – investments, G – government spending, NX – net export (exports-imports). Consumption is equal to:

$$C=c_0+c_1*(Y_D)=c_0+c_1*(Y-T)$$

The main reason of large drop in growth of GDP economists see in substantial decrease in consumption, given disposable income unchanged. The direct cause is shown in the fifth table, which gives value of consumer confidence. The index is computed from a monthly survey of 5000 households; the survey asks people how confident they are about both current and future economic conditions. We can observe from the table that there was a large decrease in the index in the fourth quarter of 1990. Consumers lost confidence, leading them to form bad expectations about future,

which has resulted in the decrease of consumption given disposable income. Economists agree that bad expectations about future were due to high probability of a war in the Middle East. People worried that US might get involved in prolonged and costly war. They also expected that a war could lead to a large decrease in oil prices and a recession.

So, we can draw a strong conclusion that expectations play very important role in economy.

Investment and Expectations

Investment is a term, which refers to purchase of new capital goods (machine, plants and office buildings). However, purchase of financial assets, such as stocks and bonds, is referred to financial investment.

A firm, deciding to invest, must make a simple comparison. Firm must first compute the present value of profits to the initial investments. If the present value exceeds the cost, the firm should invest, if the present value is less than the cost, the firm should not invest. It is the basic of theory of investment.

We formulate it in this way:

$$I = F(PV(\Pi^e))$$

where PV stands for Present value, Π^e – expected profit

It means that investment depends positively on the expected present value of future profits. The higher the expected profit discounted to present, the higher the level of investments.

Investment decision also depends on countless uncertain condition: technological, economical, political, which affect the production process. Investments typically require judgments about business conditions for many years in the future, not just for one period. Volatility and uncertainty of investment result from shifts in expectations about the future. These shifts in expectations may be strongly based on evidence about business conditions, including opinion surveys, observed shifts in technology, changes in demand. Famous economist John Maynard Keynes in his "General theory" stated that we rely mainly on the past in order to form our short-term expectations, and that we simply rely on our animal spirits in terms of forming our long-term expectations.

Investor considering buying financial asset, such as stocks or bonds, follows the same principle: finding the present value of all expected dividends and compare with cost of purchasing. There are several theories, which describe the assets prices are formed and how they're influenced by expectations of people.

One of the earliest and most striking applications of the concept of rational expectations is the efficient markets theory of asset prices. It states that the price of assets (such as daily stock prices) is said to follow a random walk if the current value gives the best possible prediction of future values. The efficient markets theory of stock prices uses the concept of rational expectations to reach the conclusion that, when properly adjusted for discounting and dividends, stock prices follow a random walk. In their efforts to forecast prices, investors use all sources of information, including patterns that they can spot in past price movements.

Investors buy stocks that they expect to have a higher-than-average return and sell those that they expect to have lower returns. When they do so, they bid up the prices of stocks expected to have higher-than-average returns and drive down the prices of those expected to have lower-than-average returns. The prices of the stocks adjust until the expected returns, adjusted for risk, are equal for all stocks. Equalization of expected returns means that investors' forecasts are reflected in the prices of stocks. More precisely, it means that stock prices change so that after an adjustment to reflect dividends, the time value of money, and differential risk, they equal the market's best forecast of the future price. Therefore, the only factors that can change stock prices are random factors that could not be known in advance. Thus, changes in stock prices follow a random walk.

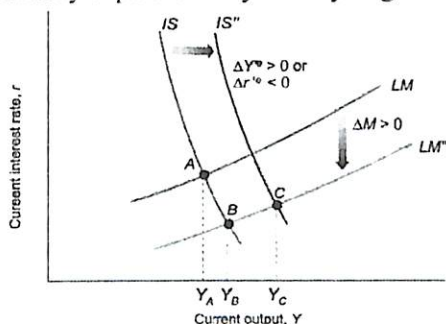
Many economists doubt that all movements in stock prices come from news about future dividends or interest rates. They argue that stock prices are not always equal to their fundamental value, defined as the present value of expected dividends. Stocks are sometimes underpriced or overpriced. This happens because investors are willing to buy every possible stock at high price, if they expect the price at which they can sell the stock later to be higher than in the present. This process suggests that stock prices may increase just because investors expect them to. Such movements in stock prices are called rational speculative bubbles. This principle applies also to other assets, such as housing, gold and painting. Investors, who behave in such a way, are rational people, since they are thinking at the margin, although it is very risky. Rational speculative bubbles are supposed to be the supplementary reason of such very high prices of real estate in Almaty and other cities of Kazakhstan.

As a conclusion, we can draw strong evidence that investments depend on expectations in very significant way.

Public policy and Expectations

Monetary Policy and Expectations

Expectation is supposed to be the crucial factor of success of policies implemented by the government. The effects of monetary policy on output depend very much on whether and how monetary policy affects expectations. We can analyze the effects of those policies using IS-LM model. If government implements expansionary monetary policy, output with certainty will increase and the interest rate will decrease. What we should consider is the size of this effect on output. If this monetary policy leads financial investors, firms and consumers to revise and adjust their expectations of future interest rates and output, then the effects of the monetary expansion may be very large. Both IS and LM curve will shift:



But if expectations remain unchanged, the effects of the monetary expansion on output will be small. Expectations in this situation are not arbitrary or random. All people give a lot of thought to what may happen in the future. They form expectations about the future results by assessing the likely outcome of future expected policy. They do so indirectly by watching TV, reading newspapers etc. Expectations, which are formed in this way, are called rational expectations. This kind of expectations are formulated using all available information and using it in an efficient and effective way. The effectiveness of monetary policy is determined by credibility of government, the extent to which people believe in programs of government. Credibility in turn depends on transparency and availability of right information in country. Many economists argue that policymakers can assist the market in its attempt to predict the future by greater transparency and more public disclosure. Any policy action can have very different effects, depending on what the private sector infers about policymakers' objectives, and about their likely future actions. Providing more certainty about the central bank's objectives and plans through greater transparency and disclosure will help avoid large fluctuations in public expectations about future changes in monetary policy. This can help stabilize the economy over the long run.

Fiscal Policy and Expectations

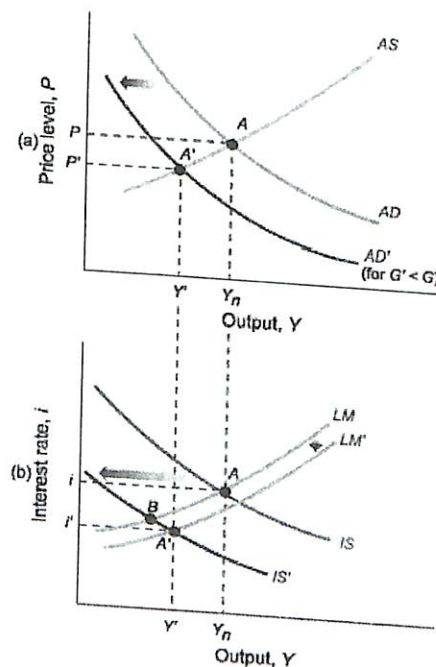
Fiscal policy has been used throughout the world to affect investment decisions. When investments and capital formation seemed to be insufficient in economy, policymakers have increased investment tax credit (tax reduction to firms, which reinvest profit in capital). This instrument was widely used in US in period between 1962 and 1986. A crucial distinction in successes of these policies is whether public anticipates them. In case of USA, the tax reform of 1986, directed on tax increases, was widely discussed by politicians and thus, anticipated by companies. Before the tax was imposed in 1986, there was significant increase in investments, but after tax imposition investment fell.

Another essential distinction should be made between policy changes that are supposed to be permanent and those supposed to be temporary. A temporary decrease in taxes, expected by firms, would result in large increases in investments, because tax reduction will be expected to be transitory. There are a lot of examples in history, when government fiscal policy was incredibly successful due to changes in expectations of people. The example is deficit reduction program in Ireland in 1981-1989. Ireland went through two major deficit reduction programs in the 1980s. The first program was started in 1982. In 1981 the budget deficit had reached a very high 13% of GDP, government debt was 77% of GDP. The government planned to decrease budget deficit in 3 years by increasing taxes. The program was very ambitious, but the results were bad. As shown in table, output growth was low in

1982, negative in 1983. As a result, tax revenues, which depend on the level of activity, were lower than anticipated. The second program was proposed in 1987. At this time things were still bad. The 1986 deficit was 10.7% of GDP, debt stood at 116% of GDP. The new program of deficit reduction was different from the first. The focus was more on reduction of government spending and the role of the government. The results were better than from the first program. The years 1987 to 1989 showed a strong growth. Deficit was reduced by nearly 9% of GDP. The difference of two programs is due to different expectations formed by people. The reason can be observed in the table.

Years	1981	1982	1983	1984	1986	1987	1988	1989
Budget deficit (% of GDP)	-13	-13,4	-11,4	-9,5	-10,7	-8,6	-4,5	-1,8
Output growth rate (%)	3,3	2,3	-0,2	4,4	-0,4	4,7	5,2	5,8
Unemployment rate (%)	9,5	11	13,5	15	17,1	16,9	16,3	15,1
Household saving rate (% of disposable income)	17,9	19,6	18,1	18,4	15,7	12,9	11	12,6

Economists argue that first program created negative expectations about future, because it focused on tax increases and did not change what many people saw as too large a role of government in economy. The second program, focused on cuts in spending and on tax reform, has formed positive expectations about future and has led to significant improvements in economy and reduction of budget deficit. Using IS-LM model we would predict that output would decrease in the medium run, however positive effect of people's expectations has offset the effect of reduction in government spending and has not decreased, but rather increased the output:



Role of expectations in recovery of Irish economy can be verified through decreases in saving rate during the implementation of second program, which gives strong evidence that people have increased their consumption and thus, confidence about future.

From these historical examples we can conclude that forming positive expectations about future should be the main goal of policymakers, since it can improve the effectiveness of government programs and make the achieving of certain goals of government much easier.

Conclusion

Expectations are at the heart of every economic decision people make. The public's expectations about factors affecting the economy have a powerful impact on the economy's overall performance. From historical examples we can observe that bad expectations of people (USA case) have resulted in poor

activity of economy, although the state of economy was stable and good. Conversely, positive expectations about future (Ireland case) can improve bad state of economy, through strong consumption and high confidence level. The conclusion is that if people believe that the economy is healthy and strong, that belief helps to make it so. Their confidence will induce spending and increase demand, which will, in turn, promote investment spending, which creates jobs, and translates into economic growth. People's beliefs extend not just to the economy's state and structure but also to policymakers' behavior in their attempts to control both monetary and fiscal policy. As for monetary policy, its effectiveness depends on public confidence — people's belief — that the Central Bank has the commitment and the capacity to maintain stable prices and foster maximum sustainable economic growth. Establishing this confidence is not easy, particularly in a world where shifts in public expectations can themselves create episodes of economic instability. In my point of view, government should pursue three goals in its policy. Firstly, it should supply people with available and right information in order to make people use all information efficiently and effectively and, thus, forming rational expectations about future. It is connected with open-information society. Second, it should deserve high level of credibility — extent to which people believe that government will implement certain policies. High credibility of government will make those government programs more effective. Thirdly, government should form positive expectations of people about future. Increased consumer confidence can make great results as have seen from examples. From rational expectations principle, what people expect is becoming actual result, so with high positive expectations, improvement of economy can be achieved more easily and effectively.

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ЕЛ ЭКОНОМИКАСЫ МЕМЛЕКЕТТІК БАСҚАРУДЫҢ ОБЪЕКТИСІ РЕТІНДЕ

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Мемлекет болғандықтан, әр мемлекеттің мақсаты даму, өсу, халқының тұрмыстық жағдайының жақсы болуы, мемлекеттің аяғына нық тұрып, ешқандай сыртқы факторларға тәуелді болмау. Бұған жету үшін экономикалық, әлеуметтік, экологиялық және тағы басқа факторлардың өте жақсы жағдайда болуы абзал. Мемлекеттің экономикадағы ролі дамудың әр этапында әр түрлі болды. Мемлекеттің экономикаға араласпау керектігі жайлы ой қалыптасты, ол нарық шектеулі ресурстарды өзі тиімді реттей алады деп санады. Қоғамның алға жеделдете дамуы мемлекеттің араласуын қажетсінетін жағдайларды көптеп туғызды. Енді қазір ХХІ ғасырда дүние экономиканы мемлекеттік реттеудің міндетті түрде керек екендігіне және ұлттық шеңберде мемлекеттің экономикалық саясатының қырылуы керектігіне көз жеткізді.

Экономикалық саясат — бұл экономикалық жүйені бір даму жағдайынан келесі жеделдете даму жағдайына ауыстыру үшін оған мақсаттыбағытталған түрде субъективті әсер ету. Бұндай ауыстыруды мемлекет белгілі қалыптасқан бағдарлама бойынша жүргізеді.

Экономикалық саясаттың сапалы, тиімді болған-болмағандығын бағалау үшін келесі үш индикаторларды қолданамыз:

1. экономикалық индикаторлар, өндірістің тиімділігін көрсетеді.
2. әлеуметтік индикатор, экономикалық саясаттың тиімділігінің нақты көрсеткіші. өмір сүру ұзақтылығы, еңбек ақы, тағы сол сияқты.
3. қаржылық индикатор, ақша, айырбас құны мықты ма, экспорт, импорт, сыртқы сауда балансы.