Macroeconomic Updates - Foreign Investments into Kazakhstan

Overview of 1H17
Kazakhstan’s investment attractiveness improved in 2H16 and 1H17, following the recovery in global commodity prices, as the country’s oil and gas sector is the main recipient of foreign investments. Gross inflow of FDI in 1H17 increased by 8.6% YoY to USD10.5bln, mostly attributable to reinvested incomes and increased inter-firm borrowing, while net inflow of FDI amounted to USD4.3bln growing by 20% YoY. Rising commodity prices drove Kazakhstan’s commodity exports and resulted in growth of investment profitability. Income on FDIs rose by almost 50% YoY to USD8.3bln in 1H17.

![Gross and net inflow of FDI, USD mln (1H13-1H17)](chart1.png)

As at June 2017, cumulative stock of foreign investments increased by 7.2% YoY and reached a historical high of USD224.8bln including USD160.9bln in FDIs, USD41bln in other investments and USD22.8bln in portfolio investments. Growth was primarily driven by FDIs (9.5% YoY) and portfolio investments (10.2% YoY), which expanded on the back of increased borrowing in foreign capital markets. Nevertheless, both portfolio and other investments stock remained below 2014 levels.

![Total stock of foreign investments, USD mln (1Q15-2Q17)](chart2.png)

Source: National Bank of Kazakhstan, Samruk-Kazyna
Sectoral breakdown

Gross FDI inflows in 1H17 were primarily directed into the mining (USD5.8bln vs. USD2.7bln in 1H16) as well as manufacturing (USD2.4bln vs. USD1.6bln in 1H16) sectors. Geological exploration was one of the primary recipients of foreign investments, recording an inflow of USD23.7bln between 2013 and 2016. However, in 1H17, investments into professional and technical activities, which include exploration, grew by a marginal USD151mln vs. an inflow of USD3.1bln in 1H16.

![Sectoral breakdown of gross FDI inflows, USD mln (2013-1H17)](image)

Source: National Bank of Kazakhstan, Samruk-Kazyna

Investments into mining were concentrated in the oil and gas subsector (USD5.3bln in 1H17 vs. USD2.2bln in 1H16), while metal mining subsector recorded an inflow of USD0.3bln over the same period. Growing inflow of FDI into oil and gas was mostly attributable to the TengizChevOil LLP’s expansion project, which will require approximately USD37bln in foreign investments in 2017-2022. Investments into this project are anticipated to increase further in 2018 as the company will start the construction of the main refinery plant.

In manufacturing, metallurgy was the primary recipient of FDI with USD2.1bln investments in 1H17. Other subsectors that registered growth include plastics (USD148mln), chemicals (USD52mln) and electronics (USD38mln).

![Sectoral breakdown of gross FDI inflows, % (1H17)](image)

Source: National Bank of Kazakhstan, Samruk-Kazyna

![Gross inflow of FDIs into mining, USD mln (1H13-1H17)](image)

Source: National Bank of Kazakhstan, Samruk-Kazyna

![Gross inflow of FDIs into manufacturing, USD mln (1H13-1H17)](image)
Largest investors

Netherlands was the largest source of incoming FDI with gross investments of USD3.1bln in 1H17. Gross FDI inflow from Netherlands reached USD57bln in 2013-1H17. The Netherlands’ cumulative stock investment portfolio in Kazakhstan (USD72.8bln) is concentrated in mining, manufacturing and technical activities. The US’ gross FDI in 1H17 amounted to USD2.3bln. Consequently, the US surpassed the UK as the second-largest investor into Kazakhstan with cumulative investment stock of USD29.3bln as at 1H17. Since 2013, the country has invested gross USD27.9bln, primarily into mining, professional and technical activities as well as finance.

Source: National Bank of Kazakhstan, Samruk-Kazyna

The UK invested gross FDIs of USD0.2bln into Kazakhstan in 1H17 and is currently the third-largest investor in the Kazakh economy with a total investment stock of USD27.7bln. The majority of UK investments into Kazakhstan is portfolio investments concentrated in technical activities, finance and public administration.

Source: National Bank of Kazakhstan, Samruk-Kazyna

As at 1H17, China holds USD14.8bln in stock investments including USD5.48bln in transportation, USD2.53bln in finance and USD2.47bln in mining as well as USD1.35bln in manufacturing. In 2Q17, China signed several agreements on investing USD980mln in Kazakhstan’s metals, energy and finance industries. These deals are expected to be finalized by end-2017. Moreover, Kazakhstan is expected to play a key role in the Chinese Belt and Road initiative, which should drive incoming FDI flows into transportation, finance and manufacturing industries.
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Outlook
Kazakhstan’s authorities are taking further steps to enhance investment climate in the country. Reflecting this, World Bank’s annual Doing Business 2018 report ranked Kazakhstan as the most attractive country globally in terms of protecting minority investors. The country improved its rating from 3rd place in 2017 as the Government increased shareholder rights and role in major corporate decisions, clarified ownership and control structures while requiring greater corporate transparency.

In addition, improvement in Kazakhstan’s economic growth prospects and strong macroeconomic fundamentals have been reflected in its sovereign ratings. On 8 September 2017, S&P raised the outlook on the country’s credit rating to stable while maintaining its BBB- rating, which makes Kazakhstan the best rated country in the region. The rating agency highlighted the improvement in monetary policy effectiveness and strong external positions, which facilitates investors’ confidence in Kazakhstan’s economy.

Sovereign Ratings Comparison, as at 6 November 2017

<table>
<thead>
<tr>
<th>Country</th>
<th>S&amp;P</th>
<th>Moody’s</th>
<th>Fitch</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kazakhstan</td>
<td>BBB-/Stable</td>
<td>Baa3/Stable</td>
<td>BBB/ Stable</td>
</tr>
<tr>
<td>Kyrgyzstan</td>
<td>N/A</td>
<td>B2/Stable</td>
<td>N/A</td>
</tr>
<tr>
<td>Russia</td>
<td>BB+/Positive</td>
<td>Ba1/Stable</td>
<td>BBB-/Positive</td>
</tr>
<tr>
<td>Tajikistan</td>
<td>B-/Stable</td>
<td>B3/Stable</td>
<td>N/A</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>BB+/Negative</td>
<td>Ba2/Stable</td>
<td>BB+/Negative</td>
</tr>
</tbody>
</table>

Source: S&P, Moody’s, Fitch

Kazakhstan’s policy on attracting foreign investors prioritizes investments into geological exploration to enhance the potential of the country’s extractive industries. Gross inflow of FDI into exploration has decreased to USD0.1bln in 1H17 vs. USD4.8bln in 2016. The Government plans to adopt a new code on subsoil use, which will provide tax preferences and other benefits to foreign investors in the oil and gas sector. Concurrently, the authorities also plan to implement international inventories reporting standards, eliminate excessive administrative barriers as well as reduce the number of procedures and waiting time. Elimination of administrative barriers and additional preferences for foreign investors should increase investments into geological exploration and facilitate technology transfer into the Kazakhstan’s extractive industries.

Gross inflow of FDI into geological exploration, USD mln (2005-1H17)

Source: National Bank of Kazakhstan, Samruk-Kazyna
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National Investment Strategy 2018-2022
To enhance the investment climate, the Government adopted a National Investment Strategy 2018-2022, which was developed in collaboration with the World Bank. The strategy identifies 11 key investor-countries (US, Russia, UK, Germany, France, Italy, China, Japan, South Korea, Turkey and UAE) as well as several key industries. Traditional industries include oil and gas, food processing and machinery manufacturing, while priority non-traditional industries include information and communication technologies, tourism and finance.

By 2022, implementation of the strategy should achieve several key performance indicators:

- Gross FDI to increase by 26% vs. 2016 levels (2016: USD21bln).
- Gross FDI-to-GDP ratio to reach 19% (2016: 15.2%).
- Gross FDI in productivity growth to increase by 50% vs. 2016 (2016: USD4.1bln).
- Fixed investments in non-primary sector (excluding government spending) to increase by 46% (2016: KZT834.1bln).
- Foreign fixed investments in non-primary sectors to increase by 1.5 times. (2016: KZT232.7bln).

Target gross FDI vs. FDI-to-GDP, USD bln (2016-2018f)

On the global economic front, continued recovery in the EU, Russia and sustainable growth in China should facilitate higher investments into the Kazakhstan’s economy. The country is expected to play a key role in the China’s One Belt One Road initiative due to its favorable geographic location between Europe and China. Chinese investors are anticipated to provide more than USD250bln to fund infrastructure projects in Asia region, with Kazakhstan being one of the primary beneficiaries. As at September 2017, direct financing from China’s investors into Kazakhstan’s infrastructure amounted to approximately USD1bln.

In particular, Khorgos Gateway, a dry port on the China-Kazakhstan border, currently represents a key logistics hub on the New Silk Road. In May 2017, as a part of B&R program implementation, China’s investors, COSCO Shipping and Lianyungang port, agreed to further develop Khorgos’ infrastructure base, acquiring a 49% stake in the terminal. In October 2017, Astana LRT, an entity established to develop Astana’s transport and logistics infrastructure, received approximately USD1.6bln from the China Development Bank to finance the construction of light rail system in the city, reinforcing China’s strong B&R commitment.

Based on investments dynamic in 1H17, full-year gross FDI flows are forecasted to marginally exceed 2016 total of USD21bln driven by investments into mining and manufacturing industries. Looking forward, foreign investment flows into Kazakhstan are expected to pick up supported by stronger growth in key trading partners, higher commodity prices and Government’s measures to stimulate investment activity. The Government’s privatization initiatives are expected to promote capital inflows into the country, especially through portfolio investments and derivative financial instruments (as at June 2017, portfolio and derivative investments provided 10.1% and 0.05% of cumulative investment stock respectively).
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