The 2013 guide to
Kazakhstan

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Eurasian Bank on the rise

Fast-growing lender Eurasian Bank is exceeding even its own expectations, expanding its asset base by 25% last year, with profits up over 50%.

It has been another robust year for Eurasian Bank, and for its forward-thinking management team. The fast-growing lender, based in the leafy southern Kazakh city of Almaty, has in recent years shrugged off with seeming ease the financial concerns that continue to dog many Western countries.

Raw data highlights Eurasian Bank’s seemingly unstoppable rise. Net income surged by more than 60% year on year in the full year 2012, while total loans jumped 38.5%, to T355 billion ($2.2 billion). Net interest margins rose a full 1.6 percentage points, to 7.7%. Assets and capital expanded at a record pace, while the key metric of net interest income also climbed sharply in 2012 to T27 billion, from T18.6 billion the previous year.

Rapid rise

Eurasian Bank’s continued rise – this, remember, is a lender that didn’t exist two decades ago, and only really began its precipitous ascent around the time of the financial crisis – has raised eyebrows in Central Asia and beyond.

Yet not everyone has been surprised by Eurasian Bank’s upward trajectory. The lender’s senior management team, led by chief executive officer (CEO) and chairman of the management board Michael Eggleton, who joined in October 2009, leave nothing to chance. Regular credit meetings keep management and board members apprised of internal events; weekly board meetings corral thinking about the bank, the nation and the global economy.

Eggleton, a US native, is upbeat about future prospects, as well he should. Few lenders in Kazakhstan – or anywhere in Central Asia – can touch Eurasian Bank at the moment. Poring over final consolidated IFRS data from 2012, he picks out several key metrics that underscore the bank’s record year.

“Three figures in particular stand out from the last year,” he says. “We increased our asset base by more than 25% in 2012. Profits rose to T9.8 billion, which is an increase of more than 50%. We also opened just under 50 new, mostly full-service points around the country – and we plan to open another 50 during the current year.”

Even these impressive figures outperformed original expectations. Eurasian Bank expected to open just 30 service outlets across the country in 2013, and targeted profits of around T9 billion: that it managed to surpass initial targets says much about both the bank and Kazakhstan’s resurgent economy. “Last year we actually achieved more than we expected,” adds Eggleton. “We increased
the footprint of the bank, processed more transactions, and brought in more clients.”

**Bright prospects**

Indeed, the prospects look good all round. Kazakhstan remains a paragon of political, social and economic stability in an often-troubled region. Central Asia’s largest economy grew by 5% in 2012 and is on track to expand by 6% this year, according to forecasts from the National Bank of Kazakhstan.

The peaceable state of Kazakhstan’s economy, and the financial stability that emanates from the president’s office, has not gone unnoticed, either domestically or beyond the country’s vast borders.

Consider two, unrelated, themes here, both of which have directly benefited Eurasian Bank.

Firstly, the stunning growth in the bank’s, and the country’s, retail sector. Consumer spending has been broadly on an upward path for three years, rising on an average annualized basis of 12.2% in the 18 months to end-March 2013, according to Kazakhstan’s central statistics agency. Eurasian Bank has benefited fully from this surge in spending, which has coincided with renewed bank lending and the return of robust domestic economic growth.

In this light, Eurasian Bank’s decision to buy Société Générale’s consumer finance division, ProstoCredit, in 2011, could turn out to be the most far-sighted investment the bank will ever make. SocGen’s loss, born out of necessity at a time when the French bank was desperate to shore up capital at home, has quickly turned into Eurasian Bank’s gain.

Eggleton describes ProstoCredit as an “inspired” purchase. An outstanding 2011 saw retail lending jump by 67.7%. That theme continued in 2012, during which new lending to retail customers expanded by just shy of 70%.

Much of that startling growth comprised uncollateralized consumer loans, which doubled last year to nearly T90 billion, and auto loans, which more than tripled year on year in 2012, to T29 billion, pushing total loans to retail customers to T170 billion. Indeed, Eurasian Bank financed the sale of 2,000 new cars every month in 2012, 50% more than the previous year. That startling rise means that Eurasian Bank now finances the sale of 15 out of every 100 new cars sold each year in Kazakhstan.

**Growth from retail**

“Across the board, retail has been the big provider of growth,” Eggleton says, who notes that while 2011 provided “considerable growth”, the real step-change came in 2012, the first year in which Eurasian Bank had ProstoCredit, working atop the bank’s brand-new IT platform, at its full disposal.

Bertrand Gossart, the French-born head of retail banking, joined Eurasian Bank in spring 2011 from SocGen, where he...
supervised consumer finance in four key emerging economies: China, India, Kazakhstan and Vietnam. He points to the depth of the market: new retail lending isn’t being pushed just to Kazakhstan’s wealthier citizens, but to an increasingly broad demographic across the country, from miners and IT engineers to bus drivers and entrepreneurs.

“People’s lives are changing in a positive way across the country,” Gossart notes. “There is a huge chance for our retail division to grow even further and faster, and not just in the likes of Almaty and [the capital] Astana but across the country, from Shymkent to Caspian cities like Aktau and Atyrau.”

Steady and stable
Then there is the second clear benefit of investing in, banking in and placing your wealth in such a steady and stable country. Kazakhstan was once viewed with either ignorance or suspicion by outsiders, partly due to its isolation, partly as a result of the last syllable in its name (people connected it with the less stable ‘-stan’ nations to the south).

No more. For nearly 20 years, this has been a haven of stability, offering investors personal financial surety. Even at the height of the financial crisis, a period that led to the nationalization of several local lenders, the deposits of Kazakh savers were insured by the state and its financial regulators.

This matters. Recent events in Cyprus, an island state buffeted by economic crisis after customers of all sizes took a huge haircut on their savings, shocked depositors everywhere. Across the region – from Russia to Ukraine to the rest of Central Asia – depositors who squirreled away savings in the European Union are now considering their options. If their deposits can be whisked away from them in Cyprus, after all, their thinking goes, it could happen in other peripheral, and even core, European states.

This has led to a rush in deposits held by high-net-worth individuals (HNWIs) being wrenched from Europe, and placed in secure locations, notably in the likes of Kazakhstan. And safer-than-houses Eurasian Bank, boasting a ‘B+’ long-term credit rating with a ‘stable’ outlook from Standard & Poor’s, and a ‘B1’ long-term foreign currency deposit rating from Moody’s Investors Service, has benefited more than most.

Notes CEO Eggleton: “Because of Cyprus and fears that the Cypriot solution is now the official new solution across the eurozone, we are getting Russians and Kazakhs contacting us to place their savings here, in Almaty. We expect to gain significant depositors from the Eurozone crisis. The end result in Cyprus was bad, but the process was even worse, and it had HNWIs thinking about the end-game: how the crisis could come to affect them.”

Ayaz Bakasov, deputy chairman and head of private banking at Eurasian Bank, points to solid reasons for this step-change. “Kazakhstan is really very blessed,’ he says. “We are politically, economically and financially very stable, a fact that is drawing in lots of wealthy individuals from across the region. Plus, there is the added attraction of Eurasian Bank, which has absorbed so many best practices in recent years, making it so well run and managed.”
Building corporate business
And there’s more. Eurasian Bank has in recent times become an increasingly integral part of the corporate banking world in Kazakhstan and beyond. Even the largest multinationals doing business in Kazakhstan are gravitating to the lender. Many start by testing the waters – channelling payroll solutions through Eurasian Bank – but then stay for the service and the surety offered by one of the region’s most secure banks.

Lending to all corporates rose 20% in 2012 year on year, to T214 billion, with loans to large corporates jumping by 22%, to T177 billion. Lending to small and medium-sized corporates – a noticeable trend in a country seeking to diversify and support smaller, privately-run enterprises – also ticked up. The number of client accounts jumped even more sharply, by 42% in 2012 to more than 825,000, a further sign that corporates of all shapes and sizes trust Eurasian Bank with their business.

“Corporate clients bank with us because they know we can help finance their operations by providing them with clear lines of working capital,” says Eggleton, who points to other benefits of banking with Eurasian Bank: “We offer a full range of services and products. We are Kazakh but we employ the best professionals from all over the world, so lots of our staff are English-speaking. And we offer financial stability: we have never been downgraded once during the financial crisis, and in fact we have been upgraded. Moreover, we continue to profit, to invest, to expand and, first and foremost, to look after our clients.”

Looking ahead, the economic outlook looks rosy both for Kazakhstan and for its best-run lender. “The country has never stopped growing, even during the financial crisis, and it looks set to continue growing, across all sectors,” says Seitzhan Yermekbayev, deputy CEO and head of corporate and SME business at Eurasian Bank.

Risks do exist – notably fears of slowdown in neighbouring countries. But as the past year has shown, there seems little that can halt Eurasian Bank’s onward march. More than 200,000 Kazakhs now use a Eurasian Bank debit or credit card. Private banking custom is booming as HNWIs transfer their capital east, from the instability pervading Europe.

Corporate clients are increasingly drawn to an economy driven by rising earnings from commodities, and by resurgent earnings from key sectors like real estate, manufacturing and retail. But corporates of all sizes, from SMEs right up to the largest global corporates, are also flocking to the country’s most ambitious and stable lender. “We have full-service banking, we have the best IT platform around, we have great ratings, and all the awards and accolades we have earned offer even the biggest corporate clients comfort about banking with us,” says CEO Eggleton. “The outlook for us, and for Kazakhstan, is very good indeed.”
Little ever seems to ruffle Kazakhstan’s economic feathers. This vast Central Asian nation, a key global producer of everything from oil and natural gas to zinc and yellowcake uranium, has bounced back strongly from the financial crisis.

Its economy, following a few lean years, is again powering ahead. GDP growth hit 5% last year, and is on track to inch up to 6% in 2013, according to data from the National Bank of Kazakhstan (NBK). The more troubled financial sector is also returning from the wilderness, thanks to the recent creation by NBK chairman Grigoriy Marchenko of a distressed asset fund designed to help the financial sector shed the worst of its bad loans.

Not everyone is going begging, of course. Kazakhstan’s banking troubles, leading from excessive leveraged lending and external borrowing prior to the financial crisis, created distress at some banks and opportunities at others. At some, things have never been better. Net income at Almaty-based Eurasian Bank surged by more than 60% year on year in 2012, with total loans and net interest margins rising to record levels as the lender attracted new corporate and wealthy individual clients.

Look everywhere and positive indicators abound. Oil production, which underpins the economy, is set to rise to 82 million tonnes this year, up from 79.2 million tonnes in 2012. Most is exported west to Europe, south to the Indian subcontinent and east to energy-hungry China.

And that in turn helped boost national coffers: at end-2012, according to the NBK, gross foreign currency and gold reserves hit $28.3 billion. Ayaz Bakasov, deputy chairman and head of private banking at Eurasian Bank, is hardly alone when he describes a “flourishing economy” with very few weak points.

Mapping the future
Kazakhstan’s economy is becoming more meritocratic as wealth trickles down to a growing middle class. The economy remains skewed toward, and dependent on, energy-related earnings. But diversification is now starting to shift from theory to reality, with information technology, pharmaceutical and engineering firms starting to cluster around first- and second-tier cities.

The goal of the government’s much-heralded ‘Business Roadmap 2020’ is to
boost industrial diversification and channel new funding into high-tech industries over the next several years, creating thousands of higher-earning jobs. And then there is Kashagan, one of the world’s largest untapped oilfields, set to come on stream in the next few years, an event that will promote this vast, peaceable, investment-friendly nation into Big Oil’s big leagues.

In short, there’s little not to like. And looking ahead, the future appears even brighter. Jean-Christophe Lermusiaux, head of research at Almaty-based Visor Capital, tips Kazakhstan’s economy to “outperform many countries this year”. He sees inflation picking up but remaining at a “reasonable” level through 2013 of around 8%, driven by higher incomes and a new surge of bank lending, a slight rise on last year’s average of around 6%.

Few seem overly concerned: in a regular monthly economic briefing issued on 22 March, Russian investment bank Renaissance Capital said it saw “no reason to worry” about rising prices. Besides, Kazakhstan has a net cash pile in excess of $80 billion, comprising the national oil fund and national reserves, in which to dip in case of emergency.

**Investors committed**

It’s hard to overstate how solid and stable Kazakhstan has become. Yes, the financial crisis hit many here, notably in real estate and banking, but the global investor community has remained committed to the cause. Inward foreign direct investment (FDI) averaged $20 billion a year over the past six years, rising to a new record high of $22.5 billion in 2012.

Talk to any foreign executive working at a multinational in Kazakhstan and you hear little but praise about how the country is run. That has long translated into raw commercial strength: economic growth averaged 8.3% a year in the first decade of the century, a startling figure bettered by only one major emerging market: China. In 2012, Kazakhstan’s President
Nursultan Nazarbayev set a long-term annual GDP growth target of around 7%, a target that most economists believe is eminently achievable.

Nor does topline data conceal much economic frailty. Not for nothing is Kazakhstan considered the most structurally, politically and economically stable nation anywhere in the region. In 2012, the country boasted a better economic and employment outlook, healthier government finances and a sounder currency and monetary policy than any other member of the 12-nation Commonwealth of Independent States, an area encompassing Russia, Central Asia and much of the Caucasus, according to statistics from Euromoney Country Risk (ECR).

Across the board, data underscores how robust Kazakhstan’s increasingly diversified economy has become. The latest regional ECR survey, completed in December 2012, places Kazakhstan second to Russia in terms of overall economic performance, with a score of 45.8.

The nation’s measure of ‘economic risk’ has remained stable for nearly two years, again placing Kazakhstan second behind Russia. And in terms of economic gross national product, a measure of the country’s overall output that includes foreign earnings, Kazakhstan leapfrogs Russia into first place.

Across the board, experts point to a bright future. “Everything is improving here, from the economy to the banking sector,” says Michael Eggleton, chief executive officer (CEO) and chairman of the management board at Eurasian Bank. “Industrially, Kazakhstan is good and getting better. The energy and mining sectors are doing as well as ever, and the services sector is also growing in strength across the board.”

Janet Heckman, Kazakhstan director at the European Bank for Reconstruction and Development (EBRD), arrived in Almaty as recently as summer 2012, following long stints in the financial sector across the emerging world. Yet she’s been pleasantly surprised by what she has seen. “They are doing all the right things: focusing on industries where there is a natural advantage, like oil and gas, while boosting diversification in new industries,” she says.

**Building diversity**

For sure, there are a few spots of gloom amid the sunshine. Perhaps the main current concern domestically is whether the country can wean itself off a dependence on oil and gas and build a truly diversified and self-sustaining economy. Politicians in Astana are working hard to inject more private sector vibrancy and entrepreneurialism, and the benefits are already being seen.

Of more immediate concern is the possibility of external shocks. Europe, a
major buyer of Kazakh metals and energy, and still a sizeable source of inward FDI, remains hobbled by debt and economic torpor. Russia and China have their own troubles connected to slowing and unbalanced economies.

Yet these concerns seem minor when compared to the strides the country is taking. Global investors remain firm believers in Kazakhstan’s economic story. FDI, as noted, continues to rise steadily, from an already high base. And Kazakhstan is returning to the international debt markets this year, for the first time in a decade, with plans to issue up to $1 billion in new Eurobonds.

Astana is taking advantage of surging global demand for higher-yielding debt issued by reliable emerging-market sovereigns, helping plug a budget deficit and, in the process, setting a benchmark for Kazakh corporates hoping to raise funds in 2013 and beyond. That process appears already to be working, with local corporate Eastcomtrans seeking to issue its first US dollar-denominated bond.

And there’s more. Fears about the effects of the visa-free single customs union spanning Kazakhstan, Russia and Belarus have proved unfounded. Far from simply leading to foreign corporates ‘dumping’ goods on the local economy, Kazakhstan has benefited enormously, with investment pouring into the auto and pharmaceutical sectors.

New rail tracks, built by local steel mills, are being laid across the country, linking Kazakhstan east and west and south-to-north, helping further boost trade and thus strengthening the underlying economy. New economic hubs, clustered around leading cities like Astana and modelled loosely on China’s special economic zones, are also boosting employment, economic output and exports.

“There are so many reasons to be positive about [Kazakhstan’s] economy,” notes Gennady Babenko, a senior analyst in RenCap’s equity research team. Adds Eurasian Bank’s Eggleton: “This year will be even better for Kazakhstan than the last, and last year was pretty good.” In short, Kazakhstan remains on the up, boasting an economy built on good fundamentals (energy and mining) and determined, as the decade progresses, to boost diversification and, in the process, raise all boats.
Kazakhstan’s story of development is unusual. It is an economy growing in leaps in bounds and a nation increasingly sure of its position in the world. Both consumer and investor confidence in the country was briefly knocked during and after the financial crisis, but has now returned.

The Kazakh people are buying again. Domestic markets for cars, white goods and property have all picked up, albeit without leveraging themselves too highly. And Kazakhs are investing in their futures, paying for education and investing in health insurance for their families.

The economy is still overwhelmingly dependent on earnings generated by exporting hydrocarbons, with exports of oil and gas and related industries comprising 56% of Kazakhstan’s economy in 2012, according to figures from the CIA World Factbook. Moreover, with the giant offshore Kashagan oilfield set to come on stream in stages over the next few years, the importance of oil and gas for Kazakhstan’s economy – from the way the country manages its budget to the means by which people live – is only set to rise.

Yet there is perhaps a more important story underlying daily events here. No longer is Kazakhstan an economic outpost, a hardship posting for brave foreign executives, as it was in the 1990s. Increasingly, this is a supremely self-assured nation, the beating heart of Central Asia, an economy that continues to drag in foreign investment even while it creates new opportunities for its highly educated and predominantly young population.

A new confident Kazakhstan
This new Kazakhstan is characterized by confidence, security and entrepreneurial spirit. It is a place where talent remains, rather than moves abroad, where young and upwardly mobile workers can genuinely and hopefully plan their future. And one industry epitomizes this new Kazakhstan: the car industry.

In the not-too-distant past, the streets of major Kazakh cities thrummed with two kinds of cars: shiny, new ones bought by the wealthy few or wheezing, old, dented ones bought by everyone else. But now in cities like Almaty and the capital Astana, or even in provincial towns such as Shymkent, Karaganda or Pavlodar, car dealerships are springing up everywhere.

Kazakhstan’s car market was the fastest growing in the world in 2012, posting a 115% year-on-year rise in sales.
It remains only the world’s 50th largest car market, but figures like this are getting noticed. Automobile sales in December 2012 alone totalled 10,029, an annualized increase of 150% and a five-fold rise from the same period two years ago.

There are three good reasons for this growth in car sales. Kazakhstan’s economy is roaring ahead, growing by 5% last year and on track to expand by 6% in 2013. The government wants that figure to settle at around the 7% mark in the longer term. This supercharged wealth generation process is creating a middle class that wants to spend, and this often involves the purchase of one or more cars.

“The auto sector is exciting,” says Michael Eggleton, CEO and chairman of the management board at Eurasian Bank. “We aren’t just seeing growth in terms of the sale of high-end cars; the growth is being seen across the board.”

**New car assembly plants**

Investment in domestic car plants - notably in the north of the country - has spiked over the past 18 months despite difficulties in building cars here from scratch due to the country’s isolation. Assembly plants are slotting together semi-formed automobiles to be sold both domestically and into Russia, thanks to a three-year-old visa-free single customs union. In April 2013, minister of industry and new technology Albert Rau forecast that Kazakhstan would be churning out up to 300,000 cars a year by the end of the decade.

Most successful factories construct a number of different brands on one assembly line. For example, Azia Avto’s vast plant in the far eastern city Ust-Kamenogorsk assembles cars made by Kia, Lada, Skoda and Chevrolet. In the first half of 2012, Azia Avto churned out more than 6,500 cars, a threefold increase over the previous year. The Lada remains the most popular auto brand in Kazakhstan, but Russian rival Gaz along with South Korean makes Kia and Hyundai all saw their market share increase in 2012.

The increasing ease of accessing consumer credit in Kazakhstan has been a factor behind the growth of car sales. Kazakh banks that have invested heavily in retail are reaping the rewards. Eurasian Bank is one of the biggest players. Thanks to its far-sighted 2011 acquisition of Société Générale’s consumer finance division, ProstoCredit, the Almaty-based lender now finances the sale of around 2,000 new cars every month, or around 15% of all cars sold in Kazakhstan. Total auto loans extended in 2012 by Eurasian Bank more than tripled, to T29 billion ($192 million).

The next step for Eurasian Bank will be a car-leasing service. “If you’re a big multinational here, you need 200 or 300 cars,” says Eggleton. “We will provide the entire package: fleet finance, maintenance at the service centre, insurance, the whole works.”

**Retailing back with a flourish**

While the auto industry has come into its own, another sector has seen its fortunes
The return of retail has really surprised on the upside. It has come back with a flourish.”

To a large extent, the return of retail has been driven by two factors: the previously mentioned availability of consumer credit and the public’s willingness to access those credit lines. The former is available increasingly through consumer finance platforms like Eurasian Bank’s ProstoCredit, offered at point of sale via most major local retailers.

“When I joined two years ago, our retail portfolio was around T40 billion,” notes Bertrand Gossart, the France-born head of retail banking. “Now, our loan portfolio is more than four times that size, and our number of clients has also more than quadrupled. That’s a big change.”

Within just a few years retail has come to make up nearly half the lender’s entire loan book: further evidence that Eurasian Bank is rapidly becoming a full-service universal bank.

Access to consumer lending improves
But availability would mean nothing if people weren’t willing to spend. Clearly, they are. You only need to look around cities like Almaty and Astana to see stark evidence of consumers making good use of their wallets. On evenings and weekends, Esentai Mall, a new shopping centre funded by regional property development firm Capital Partners and anchored by Saks Fifth Avenue, is extremely busy.

Then there are the Mega-branded malls, incorporating supermarkets, single-brand chains and multiplexes, springing up everywhere from Almaty and Astana to second-tier cities Akto and Shymkent. Mega, owned by the investment holding firm Astana Group, is planning further malls across the country as it rides the retail wave.

And there’s the surprising success of standalone brands: further evidence that small can be beautiful here, too. Janet Heckman, Kazakhstan director at the European Bank for Reconstruction and Development (EBRD), highlights the rise of Marwin, a toys-to-paperbacks chain of stores in Almaty that slots into the market somewhere between Barnes & Noble and Toys R Us.

Kazakhstan used to be a dour place to shop - one of the reasons why most well-heeled Kazakhs spend their money in Dubai or London. But even this is changing now. Seitzhan Yermekbayev, head of corporate and SME business at Eurasian Bank, remembers launching a pilot staff-loan programme 13 years ago, when working for a previous employer.

“Months after it was launched, we had zero takers, even at very low rates of interest,” he remembers. “I was the first to borrow in the end - I bought a car. People were very conservative, very cautious. Now look at it. This is a country that has changed beyond belief over the past decade.”
Kazakhstan has been a haven of political and economic stability almost since announcing independence 22 years ago. Aside from a few scattered, mostly localized riots - the most recent of which occurred in the western province of Mangystau in December 2011 - the political stability of the Central Asia's largest economy has resulted in substantial foreign investment in its natural resources sector.

Jean-Christophe Lermusiaux, head of research at Almaty-based Visor Capital, says: "The country has proven more stable politically and more open to foreign investors than its neighbours." This includes more turbulent states to the south and west - Turkmenistan and Ukraine - as well as Kazakhstan's often prickly northern neighbour, Russia.

Ayaz Bakasov, deputy chairman and head of private banking at Eurasian Bank, reckons that the country is "a little like Norway: another well-balanced, politically stable and resource-rich country that never really changes."

Stability draws in investment

It is this political stability, allied to a mostly stable taxation and regulatory structure, that continues to draw in foreign direct investment (FDI). Between 2006 and 2012 inward FDI averaged $20 billion a year. Most of this investment came from Western Europe and the US. According to figures from the National Bank of Kazakhstan, FDI rose to a record $22.5 billion in 2012 and, even at the height of the financial crisis, foreign capital continued to flow into the country.

Euromoney Country Risk data underlines this enduring stability. Kazakhstan ranks third among all of the Commonwealth of Independent States in its political risk weighting in December 2012. The area for this analysis includes Russia, Central Asia and non-EU emerging Europe. In terms of the key measure of government stability, it slots in fourth.

This stability could be due - at least in part - to Kazakhstan’s political leaders being flexible and able to listen, as was evident after the 2011 riots which broke out following the sacking of oil industry workers who had gone on strike over a pay dispute. President Nursultan Nazarbayev said the workers had been treated unfairly following the demonstrations.

In many countries, this sort of uprising would have heralded a crackdown. That it happened in late 2011, at the height of the Arab Spring, and yet yielded positive repercussions, was all the more
remarkable. Again, it attests to the stability of the Kazakh state – an insecure government would have reacted with belligerence to any perceived provocation to its rule.

To their credit, political leaders in the capital Astana opted to view events as a wake-up call, rather than a call to arms. Like many fast-growing emerging economies, Kazakhstan boasts a relatively young population, with a median age of less than 30 years in 2010, according to the CIA World Factbook.

This type of demography can create problems. Kazakhstan’s workforce tends to be highly educated, thanks to the country’s large number of excellent technical colleges. And now the government is under pressure to create thousands of new highly skilled jobs in engineering, information technology and chemistry to meet the newly raised expectations of young professionals.

**Political reform**
The Kazakhstan government is not afraid to reform political structures to make the country a better environment to conduct business. For example the akims or mayors who head the country’s 16 municipalities were until recently powerful figures. But following the 2011 demonstrations the role of the akim has been transformed. They are now graded by the central government on a weighting system that gauges their performance against their peers. Each is graded on 10 measures, including the number of jobs generated each year in their municipality and the number of new companies created. Now akims are seeking to foster business links. Executives describe akims calling them up and asking them how the local government can help them - something that rarely occurred before.

And this has had three knock-on effects. First, it has created new sources of employment essential to keeping a young, ambitious, highly educated and mobile workforce motivated and happy. “The key is to create jobs in general and productive jobs in particular, in order to keep young workers happy, and to create a thriving middle class. In all these ways, the government is doing all the right things,” says Janet Heckman, Kazakhstan director at the European Bank for Reconstruction and Development.
Second, this process helps accelerate economic diversification. Government knows that its energy and mineral reserves, while vast, are finite. Politicians, bank chiefs and business leaders are working together to channel money into new industries – helping expand burgeoning industries like car production, pharmaceuticals and information technology. Anyone creating a new company, particularly a privately run enterprise, now enjoys generous subsidies from local and central authorities, and low-interest start-up capital from lenders.

Driving diversification

This in turn is creating a new generation of fast-growing small- and medium-sized enterprises (SMEs), which further hastens diversification. “One of the government’s key ambitions is to expand the SME sector,” says Seitzhan Yermekbayev, deputy CEO and head of corporate and SME business at Eurasian Bank. “This is the right path to take for everyone, and it is directly helping secure Kazakhstan’s economic future.” The results are mirrored in Kazakhstan’s Euromoney Country Risk employment ranking, where it scores 6.4 points, the highest mark of any country in the region.

Last but not least, this process is helping further promote political stability. With regional political leaders being held more accountable to both the business sector and to private individuals, everyone benefits. The events of late 2011 have not been repeated; employment is on the rise across the country, and Kazakhstan is rolling out new engineering and technical colleges to feed the factories and offices of the future.

And this in turn aids the country in commercial terms: nothing promotes inward FDI better than the assumed knowledge, among global corporate and institutional investors, that a country boasts solid political, economic and social foundations. And Kazakhstan has all of this in spades. “Every time I come back here, I’m impressed,” says Eurasian Bank’s Yermekbayev, a native of the leafy southern city of Almaty. “Kazakhstan is very quiet, which is great from a commercial standpoint. There are new roads, people are employed, and the country has the sort of stability that is rarely seen here or elsewhere.”
Like an elephant, sovereign structural stability is hard to describe or define – but you know it when you see it. That’s certainly the case with Kazakhstan, one of the most intrinsically stable countries anywhere in the Commonwealth of Independent States (CIS), a confederacy of former Soviet nations that covers Russia, Central Asia and most of the Caucasus.

Indeed, Kazakhstan is one of the most fundamentally secure nations anywhere in our troubled world. Throughout the Arab Spring it remained largely unruffled, avoiding the turbulence that spread through the Middle East and North Africa and caused shivers as far afield as Moscow and Beijing.

Kazakhstan, though, is different. This is a country being fastidiously planned and built by a far-sighted group of business and political leaders based mostly in the country’s financial and economic heart of Almaty, and in the official and political capital of Astana.

The work is not yet done, and there remains a long way to go. But like South Korea and Singapore, nations that have successfully moulded a group of leading state-linked corporates around a strong, sovereign core, Kazakhstan is certainly heading in the right direction.

In the top 10

It’s hard to argue with the raw data. Over the past decade, Kazakhstan has been one of the world’s 10 fastest-growing economies. Growth in gross domestic product hit 5% in 2012 and is on track to rise to 6% this year.

Rankings also speak volumes about the country’s core stability. According to the latest Euromoney Country Risk (ECR) data, compiled in December 2012, Kazakhstan ranks second in terms of overall structural risk in the CIS, three places above Russia. A young and highly educated workforce, and the absence of a talent-sapping brain drain, help it rank number one demographically. In terms of the country’s ‘hard’ (transport) and ‘soft’ (education, health services) infrastructure, the country ranks second and fourth respectively.

For now, Kazakhstan’s copious reserves of energy remain the biggest show in town. The huge Tengiz and Kashagan oilfields, bearing as many as 100 billion recoverable barrels of oil, have helped the country “live up to expectations”, Renaissance Capital (RenCap) said in an April 2013 report titled: ‘The new Middle East’. The investment bank noted approvingly that Kazakhstan had secured more inbound foreign direct investment (FDI) over the past decade than Russia, a country with far greater reserves of energy.
Investment has also continued to flood into metals and mining extraction: Kazakhstan boasts the second-largest reserves of uranium, lead and zinc, and significant reserves of iron ore, coal, and gold. “We see the country’s economy, based on energy and metals and mining, remaining strong for years to come, driven by rising demand from countries like China,” says Gennady Babenko, a senior analyst in RenCap’s equity research team.

**Improving connections**

But Kazakhstan is far from a mere one- or two-trick pony. Slowly but surely, almost like a giant jigsaw, this vast nation is being pieced together. As Janet Heckman, Kazakhstan director at the European Bank for Reconstruction and Development (EBRD) in Almaty, notes: “This is a big country with a small population, so there is a real need to improve connectivity and infrastructure.”

This is happening right now, and it’s fascinating to watch. Having created a strong economic bedrock – steady inflows of energy-generated wealth and a rising tax-take – Kazakhstan is now building out its hard and soft infrastructure.

“Transport is improving across the country,” notes Michael Eggleton, chief executive officer (CEO) and chairman of the management board at Almaty-based Eurasian Bank. “Railways and highways are being laid and connected; ports are being built to connect municipal energy hubs such as Aktau and Atyrau] across the Caspian Sea.”

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**We see the country’s economy, based on energy and metals and mining, remaining strong for years to come, driven by rising demand from countries like China”**
Nor is transport and infrastructure investment limited to major cities like Almaty and Astana. A four-lane blacktop highway, now under construction, will link Kazakhstan east to China, south to Uzbekistan and Turkmenistan, and north and west to Russia and beyond. This ‘Western Europe-Western China’ corridor is being built by South Korea’s Posco and financed by a consortium of multilateral institutions including the EBRD, the World Bank and the Islamic Development Bank.

Ultimately, the road will become just one, vital segment of a national transport network designed to boost trade internally, and with neighbours near and far. Other highways are being planned in the north of the country, connecting Astana with the Russian cities of Chelyabinsk and Omsk, and the Kazakh city Aktove with the faraway lights of Moscow. This process of boosting trade north and west is also benefiting from the single customs union covering Russia, Belarus and Kazakhstan, signed in 2010.

Transport investment is gearing up wherever you look. Kazakhstan’s national carrier, Air Astana, has recently secured new routes to Asian cities including Bangkok, Hong Kong, and Saigon. Next up, analysts say, are flights to Tokyo and Singapore, building on flourishing air links to the UAE and Western Europe. “Day by day, month by month, you can see the country becoming more and more connected,” notes Seitzhan Yermekbayev, deputy CEO and head of corporate and SME business at Eurasian Bank.

Moreover, the country is becoming more intrinsically and structurally linked on a micro-level. Almaty has recently introduced 600 new ‘green’ buses powered by natural gas, along with 400 new trams and trolleybuses. An eco-friendly public transport push is planned in Astana as well as the southern cities of Shymkent and Kysylorda.

Almaty recently opened its first underground rail route, and is busy promoting the use of bicycles rather than automobiles, in an effort to reduce congestion. Astana meanwhile is building out its transport links ahead of the 2017 World Expo, to be proudly hosted in the Kazakh capital. Astana is also introducing car parking schemes, and a railway line connecting the airport with the Expo site.

Another high-speed rail link, set for completion by 2019, will reduce overland journey times between Astana and Almaty to five hours from 12. The new line, stretching 1,000 kilometres and set to be part of a high-speed regional rail grid, is being built by US contractor G E Logistics (no relation to GE), and a privately-run Kazakh freight operator, Eastcomtrans.

Spreading the wealth
Structural changes are visible elsewhere. Infrastructure is helping join the dots, but this is a country also determined to build a fully diversified economy benefiting all its population. For sure, like the rest of the region (and reflecting the nature of all emerging economies rich in natural resources) this is a country where wealth remains concentrated. But the Gini coefficient, a measure of relative economic equality, has been steadily falling in recent years, a sign that wealth generation continues to spread. Kazakhstan is building a middle class, not just in the major urban centres but across the country.
The big change here has been a concerted government push to diversify the economy by encouraging the creation and expansion of private enterprise, notably in key sectors such as auto construction, information technology, retail, and agricultural processing.

“This is all part of a major structural shift across the economy,” notes Eurasian Bank’s Yermekbayev. “We have to diversify away from a dependence on natural resources, and that’s what is happening, thanks to the government pouring investment into new industries. It will take time – the natural resources sector will continue growing, which is good for everyone. But over the next five or 10 years, you will see real changes taking place.”

It’s here that you can see the combined interplay of hard and soft infrastructure at work. Take Petropavlovsk on the Russian border, a dot of a town surrounded by vast, waving fields of wheat. This is the heart of Kazakh grain production, and Petropavlovsk is famous for its pasta and dumplings: food products that can now, thanks to improved rail links, be flash frozen and shipped across the region.

Thus, Kazakhstan has quickly ascended from being a regional seller of basic grains to a processor and exporter of finished foodstuffs, helping raise national earnings. This process is also under way in the dairy sector, with the government and private enterprises pumping billions of dollars into cattle breeding. Jean-Christophe Lermusiaux, head of research at Almaty-based Visor Capital, tips the dairy sector to grow at “double-digit rates” for at least the next five years.

Elsewhere, other sectors are being promoted: Astana and Shymkent focusing on the IT industry; Pavlodar and Oskemen as auto hubs; and Almaty as a Kazakh version of Singapore, home to banks, multilaterals and global corporates. Here, the government has a further long-term aim: to promote Kazakhstan as the heart of an enlarged Central Asia, a process that will accelerate if Iran is integrated into the global economy.

Working with everyone
And this is perhaps the last piece in the puzzle, and further evidence of how stable Kazakhstan is from a structural perspective. The country’s leaders have never played favourites with their sovereign business partners: they have long taken the eminently practical tack of encouraging trade with all nations, irrespective of their stripes. The US and Europe were early investors in an independent Kazakhstan; in recent years, the country has strengthened bilateral ties with nations in East and Southeast Asia while further improving links with Russia.

This ability to work with everyone and to plan for the future, which emanates from the heart of the country – the office of President Nursultan Nazarbayev – has long benefited the Kazakh economy.

But we are now entering a new age, in which an economy long dependent on hydrocarbon wealth is on its way to becoming a diversified, balanced economy creating wealth and employment across multiple sectors, and trading with a vast array of neighbours near and far. As Eurasian Bank CEO Eggleton notes: “From any standpoint, actual or theoretical, this is a very sound and stable environment. There’s little doubt that the future bodes well for Kazakhstan.”
When the Soviet Union broke up in 1991, few investors envisaged that the newly created republics would compete with their more westernized, democratic and reform-minded neighbours in central and eastern Europe. Two decades on, however, several – including Kazakhstan – are developing at a rapid pace.

Kazakhstan, the region’s second-safest country – at 74 in the ECR global rankings, ahead of Romania and just behind Hungary – has managed to halve its score differential with Russia in recent years.

In part, this is due to the country’s improved scores in the quantitative section of the survey. This section, which assesses a country’s external measures of creditworthiness (credit ratings, debt indicators and access to capital markets) has been a supportive element of its ranking following the country’s recovery from the global financial crisis in 2008.

In Euromoney Country Risk’s credit rating indicator, the sovereign receives a score of 5.4 points which is typical of investment grade status. Kazakhstan is rated BBB+ by Fitch and Standard & Poor’s and Baa2 by Moody’s, reflecting the great strides the economy has made over the past 10 years.

All rating agencies have placed Kazakhstan on a stable outlook, as of April 2013, which should firmly anchor the country’s investment grade allure. Fitch upgraded Kazakhstan to BBB+ in August 2012, citing strong public finances and favourable debt dynamics.

Kazakhstan won praise for the “continued strengthening of Kazakhstan’s sovereign external balance sheet, low level of government debt and healthy growth prospects, as well as tentative steps towards cleaning up the banking system”.

The country’s wealth fund, NFRK, is proving its worth as a key strategic asset. Sovereign assets saved in the national fund afford a growing cushion against economic shocks, and the country’s booming oil revenues have led Fitch to forecast sovereign net foreign assets will reach 45% of GDP by end-2014, up from 37% of GDP
at end-2011. The NFRK saved more than half of oil-related inflows in 2011.

Kazakhstan’s low debt-to-GDP ratio is also a strength. Government debt is just 11% of GDP, while the country is the second-strongest sovereign net external creditor in the ‘BBB’ category.

The country is expected to run a surplus of around 3% of GDP in 2013 at an average oil price of $100 a barrel. Fitch would expect the general government budget to remain in surplus even if the oil price falls to $80.

The Commonwealth of Independent States remains a high-risk area for investors, according to the results of the ECR survey. Encompassing Russia and the former Soviet satellites, the region has an average score of just 34.7 on ECR’s 100-point scale. Having fallen by 0.2 points since the start of the year and 3.7 points since 2010, the region still ranks below most other parts of the world, with the exceptions of Australasia, Africa and the Caribbean.

Yet, given a lower starting point and looser linkages to eurozone economies and banks, the CIS has escaped the more dramatic score declines seen in neighbouring regions. The eurozone fell by two points in 2012, central and eastern Europe (excluding the CIS) by 1.3 points and Asia (also excluding the CIS) by 0.4. Over a longer, two-year time-frame, the eurozone has shed 10.3 points, the CEE 7.2 points and Asia 4, narrowing their superior score differentials with the CIS.

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