

EY's attractiveness survey

Kazakhstan 2014

The brand paves the way



Building a better
working world

Attractiveness

EY's attractiveness surveys

EY's attractiveness surveys are widely recognized by our clients, the media and major public stakeholders as a key source of insight on foreign direct investment (FDI). Examining the attractiveness of a particular region or country as an investment destination, the surveys are designed to help businesses to make investment decisions and governments to remove barriers to future growth. A two-step methodology analyzes both the reality and perception of FDI in the respective country or region. Findings are based on the views of representative panels of international and local opinion leaders and decision-makers.*

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Cover: Left coast of Ishym river in Astana, Kazakhstan.

* EY's 2014 Kazakhstan attractiveness survey focuses solely on the perception of international investors, based on a survey of 211 international business leaders. For more on the survey's methodology, please go to page 44.

EY's attractiveness survey – Kazakhstan 2014

Perception

Kazakhstan's strengths, weaknesses and main competitors



Future

Kazakhstan's medium-term attractiveness, the sectors expected to drive foreign investment in the next three years, and Kazakhstan in 2030



Actions

Where Kazakhstan should focus to develop as an investment destination



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Foreword

Ready for action



Jay Nibbe
Chair of Global
Accounts
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**Erlan
Dosymbekov**
Managing Partner,
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This year's *Kazakhstan attractiveness survey* reveals how the country's international integration and innovation agenda are poised to enable growth. These developments are expected to enhance Kazakhstan's appeal among investors. In addition, the Government's efforts to position the country among the 30 most competitive nations worldwide by 2050 offer significant opportunities to companies in many different sectors.

This survey reveals that Kazakhstan's "brand perception" is at its strongest compared with previous years. Investor awareness, among both established and non-established investors, has increased. More players are likely to enter the economy, which will intensify competition in the market.

Investor confidence in Kazakhstan's future prospects is also high – 47.3% of our respondents believe that the country's attractiveness will improve in the next three years. Kazakhstan's stable macroeconomic and sociopolitical environment has continued to increase its appeal.

However, over 50% of the investors surveyed still do not have any immediate plans to invest in the country. And the plans of investors already established in Kazakhstan vary significantly from those not yet established. Existing investors are far more likely to have immediate investment plans than those investors who are not yet operating in Kazakhstan.

The survey also reveals that the long-term success rate of companies in Kazakhstan is high, particularly in the case of large enterprises in the industrial and automotive sectors. Investors feel that the traditional energy sector will be the most attractive in the next three years. But we also believe that high-tech, telecommunication infrastructure and the business services sector can offer



significant potential. As diversification is undertaken at a larger scale, these industries are set to gain popularity.

Despite the improved World Bank Doing Business rankings, the main challenges cited over the years have not changed. In addition, 16.6% of respondents feel that Kazakhstan will be surpassed by more dynamic countries by 2030, up from 6.2% in last year's survey. This means that prospects in other rapid-growth markets (RGMs) will intensify Kazakhstan's competition for FDI.

This survey was conducted prior to the devaluation of the local currency by nearly 20% in February 2014, as well as before the geopolitical tensions emerging from the situation in Ukraine. The outcomes of these events and their impact on Kazakhstan's economic development are yet to be seen.

To encourage further investments in the country, Kazakhstan needs to enhance the consistency of its business environment, invest substantially in infrastructure, develop human capital, and ensure judicial independence.

We would like to thank the investors who have taken the time to share their thoughts with us.

We hope the report makes a positive contribution to the development of Kazakhstan's investment climate, and provides useful insights for companies as they prepare their future investment plans.

"Kazakhstan's 'brand perception' is at its strongest compared with previous years."

Viewpoint

Kazakhstan's potential as a regional investment hub



Aset Isekeshev

Deputy Prime Minister of the Republic of Kazakhstan, Minister for Industry and New Technologies

Kazakhstan's macroeconomic, social and political stability have become key factors in attracting investment to the country. Kazakhstan today presents lots of new opportunities and huge potential for both major players and mid-sized businesses.

The World Economic Forum's (WEF) *Global Competitiveness Report 2013–2014* ranks Kazakhstan as the 50th most competitive country of the 148 it surveys. Kazakhstan also moved up three positions on the World Bank's Doing Business index this year – the best result among the members of the Customs Union (Belarus, 63rd, and Russia, 92nd). Meanwhile, the United Nations Conference on Trade and Development (UNCTAD) placed Kazakhstan in the top 20 world leaders

for FDI inflow in 2012 – behind only Russia in the Commonwealth of Independent States (CIS) region.

More than half of foreign investment to Kazakhstan since 2005 (about US\$96b) has been attracted since the launch of the State Program for Accelerated Industrial and Innovative Development (SPAIID) in 2010. Since SPAIID was initiated, about 70% of FDI inflow has been in the processing industry (around US\$19.9b). All of this only became possible thanks to the improving investment climate in the country. But we are hoping for more.

Since the launch of our new industrial policy, we have been focusing on attracting more FDI. To achieve this, we have developed a tripartite

system. The first stage is our foreign mission, mainly via our embassies, which seeks to attract prospective foreign investors; the second stage is the administration at a national level, particularly the Ministry of Industry and New Technologies (MINT), which provides centralized support to foreign investors; and finally, our regional administrations, to which we direct investors who have serious and specific interest in investing in Kazakhstan.

After assessing prospective industries, we have defined our priority countries as Germany, France, the USA, Japan, South Korea and the UK. We have also identified priority projects and intensified the work in the regions, including establishing Investors Service Centers.

“Today, Kazakhstan is primarily interested in innovation projects that use cutting-edge knowledge and technology.”

The Government of Kazakhstan provides a variety of benefits to investors, from tax and customs incentives to land plots and facilities. But all these benefits are for investors in priority sectors of the processing industry.

Today, Kazakhstan is primarily interested in innovation projects that use cutting-edge knowledge and technology. The country has the required financial and institutional infrastructure to support the implementation of such projects, and can act not only as a recipient of FDI, but also as an active partner, working in collaboration with investors.

In 2015, Kazakhstan will launch the second five-year phase of SPAIID. As President Nazarbayev has noted, investment policy will be instrumental to its success. The Government is working on attracting a new wave of investments, particularly from transnational companies. This will require a lot of effort, taking into consideration global economic challenges and the fierce international competition for FDI.

Currently, we are revisiting the National Investment Plan. In particular, we are working on improving the entry requirements for foreign investors, making it easier for them to visit and stay in Kazakhstan. For

example, we are considering the implementation of a visa-free regime for Organisation for Economic Co-operation and Development (OECD) member countries, and simplified entry procedures for highly qualified talent in the processing industry. We will also provide the stability of legislation and develop a new stimulus package for major investment projects. We will also be focusing on special economic zones (SEZs), which are important for attracting FDI.

Enhanced engagement with national companies, which act as key drivers for attracting transnational corporations, is another priority for us at the moment. For example, Kazakhstan Temir Zholy (the national railway company) has already attracted Talgo, Alstom and General Electric. Meanwhile, Kazatomprom (the national nuclear company) has attracted Areva, CEIS, Marubeni and Cameco.

It is worth noting that, unlike the first phase, the second phase of SPAIID will be concentrated on a finite number of priorities. These include metallurgy, oil processing, petrochemicals, the chemicals industry, food processing, machinery engineering and construction materials. Cluster development is also on our agenda. Depending on the scale, we will develop national,

territorial and innovation clusters.

It is important to note that, if businesses are interested in investing in other sectors, they are free to do so. But if businesses wish to receive the state support within the framework of SPAIID, then their investment needs to go into the processing industry.

Currently, the Government is working on more than 300 investment projects with the participation of foreign companies. So far, 110 projects, at a value of US\$20.6b, have been implemented. Ninety-eight projects worth US\$44.7b are currently in implementation and another 131 projects are in the pipeline.

In 2011-13, KAZNEX INVEST, which operates under the MINT, supported the attraction of 35 investment decisions, worth US\$1b.

It is also worth noting that when we talk about investments, we mean not only finance, but also the arrival of new technology, knowledge and production. This is why the President has identified the attraction of foreign investment as one of the top priorities of Kazakhstan's economic policy. And we will make every effort to achieve the objectives set out by the President in order to transform Kazakhstan into a regional investment hub.

Executive summary

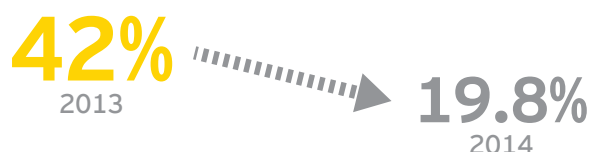


"Brand Kazakhstan" strengthening in the FDI market

This year's survey results reveal that investors' awareness of Kazakhstan's potential has increased, as evidenced by the decline in the "can't say" responses to our survey questions. This might be the result of various ongoing government efforts, such as the EXPO 2017 campaign, regular international visits, road shows and forums, and Kazakhstan's active involvement in regional and international integration processes, as well as strengthening relations with its key trade partners.

An improvement in brand Kazakhstan

Percentage of "can't say" responses to the question: "How do you see Kazakhstan in 2030?"

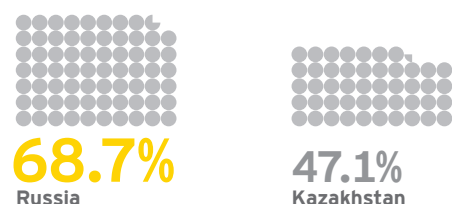


Sources: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211); EY's 2013 Kazakhstan attractiveness survey (total respondents: 206).

A stable position in the CIS region

Similar to our previous Kazakhstan attractiveness surveys, most respondents rank Russia as the leading CIS market for investment, followed by Kazakhstan. Many respondents established in Kazakhstan rank it first, while non-established investors rank it third.

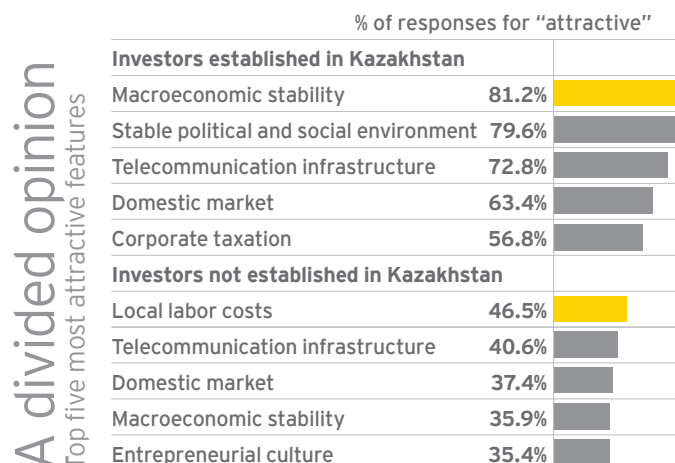
Most attractive CIS countries to establish operations?



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211).

Attractive features divide opinion

Both established and non-established investors are drawn to Kazakhstan's telecommunication infrastructure and domestic market, which presents larger opportunities to connect to the Eurasian Economic Union (EEU). However, non-established investors overlook some of its main advantages, such as its macroeconomic and political stability and its low level of corporate taxation, while they value the country's local labor costs and entrepreneurial culture.

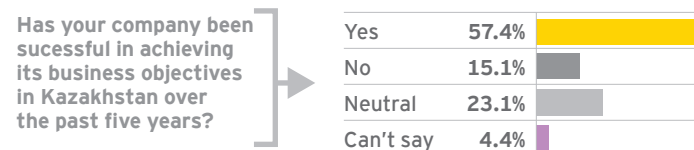


Sources: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211; established in Kazakhstan: 78; and not established: 133).

Investors report success

Among established investors, 57.4% say they have met their business objectives in the past five years. Industry and automotive respondents are the most likely to report such success, with 70.4% noting so.

Business objectives



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211, established in Kazakhstan: 78).











Bright prospects for present and future investors

Investor confidence in Kazakhstan's potential is at an all-time high compared with previous years. In this year's survey, 47.3% of respondents said that its attractiveness will increase over the next three years, compared with 41.4% who thought so in 2013, and 43% in 2012. In contrast with divided opinions on other survey questions, both established and non-established investors responded positively to this question.

Levels of attractiveness

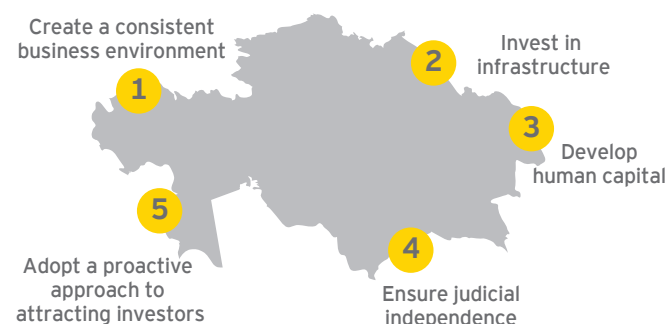
How Kazakhstan's levels of attractiveness are expected to change over the next three years.

	Established in Kazakhstan	Not established in Kazakhstan
Improve	55.2% 	42.6% 
Deteriorate	13.1% 	18.7% 
Neither improve nor deteriorate	21.7% 	31.8% 
Can't say	10.0% 	6.9% 

Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211; established in Kazakhstan: 78 and not established: 133).

Five areas for reform

Needed improvements



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211).

Investors continue to point out the need for improvements in Kazakhstan's business environment, infrastructure and human capital. They also draw attention to the necessity of strengthening the country's judicial structure and adopting a proactive investment policy.

A likely energy leader in 2030

Although some anticipate stiff competition from other growing markets, many business leaders expect Kazakhstan to be a leading energy producer by 2030.

Kazakhstan in 2030?

12.8%
A highly diversified economy

40.3%
A leader in energy

14.9%
A leader in agribusiness

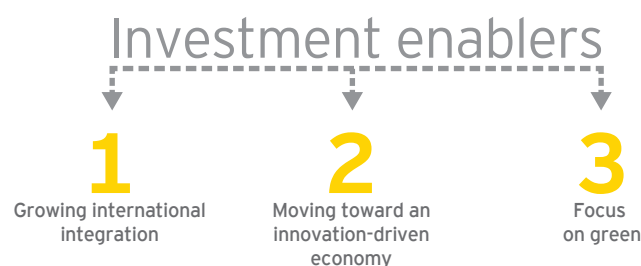
7.8%
A leader in green economy

16.6%
Surpassed by competition from more dynamic countries

Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211).

Three investment enablers

Increasing links with the global economy, a higher innovation capacity and a greater focus on green energy will have a positive impact on Kazakhstan's investment appeal. The country serves as an important link in what has been called the "new silk route," which connects the East to the West and positions Kazakhstan as a potential transportation hub for Europe and Asia.



Kazakhstan's path to sustainable growth

“Improving the business climate and competitiveness will unleash Kazakhstan's economic and employment potential.”



Antonio Somma

Head, OECD Eurasia Competitiveness Programme

Driven by its vast natural resources, more people are viewing Kazakhstan as a frontier of economic opportunity for global investors. It is one of the world's fastest-growing economies and attracts more FDI than all other Central Asian countries together. Poverty rates have fallen dramatically, income inequality has narrowed, and education and health outcomes have improved significantly.

However, in 2011, Kazakhstan ranked as the 12th most restrictive economy for FDI of the 51 countries included in the OECD FDI Regulatory Restrictiveness Index. The Index is a reference in the 46 countries (34 OECD members and 12 non-members) that have subscribed to the OECD Declaration on Investment and Multinational Enterprises. Signatories to the Declaration held 79% of Kazakhstan's investment stocks at the end of 2011, and 73% of investment inflows into Kazakhstan in 2012.

Kazakhstan has also taken steps to strengthen its relationships with international organizations. In the past five years, Kazakhstan has consistently expressed interest in scaling up its relations with the OECD, mainly in the priority policy areas of the National Development Strategy reform agenda, adopted in 2013. This is a strong signal to the investment community of Kazakhstan's willingness to position itself as a leading emerging economy in Central Asia, a premier destination for trade and FDI, and a leader in regional integration.

Given the limited size of its internal market, external integration through increased trade and FDI will remain the driving force behind Kazakhstan's growth over the coming decade. China and Russia are the main trading partners. China accounts for 21% of total exports and 26% of imports, while Russia is responsible for 10% of exports and 31% of imports. OECD member

countries ranked among Kazakhstan's top trading partners are France (9.3% of exports in 2012), Germany (6.9% of exports and 6% of imports), Italy (5% of exports) and Canada (4.8% of exports). This pattern is set to continue.

Kazakhstan is now accelerating policy work to achieve a more diverse and sophisticated export offering. Exports in high value-added sectors such as electrical products, machinery and complex processed goods have not increased significantly in the last 15 years. However, this could change with the promotion of new knowledge-intensive sources of growth and upgraded R&D capacity.

Kazakhstan aims to establish a business-friendly investment climate, both in the traditional extractive sectors and in new value-added sectors. It participates in a wide range of international initiatives. However, according to the OECD's 2012 *Investment Policy Review*, improvements



are still needed in general investment policy, investment climate issues and responsible business conduct. In addition, planned strengthening of cooperation with the OECD and further alignment with OECD standards will help Kazakhstan secure an inclusive and sustainable growth path, while mitigating the macroeconomic volatility associated with fluctuations in global commodity prices.

There are four key areas for reform:

► **Good governance.** Accountability and corruption pressures in public administration remain issues, despite significant recent efforts. Improving governance is a fundamental condition for sustainable development.

► **Environment.** In May 2013, Kazakhstan approved a Green Economy Concept policy paper. This paper sets an ambitious reform agenda in six areas: water, agriculture, energy efficiency in

specific sectors, energy production, air pollution and waste, and ecosystems and human resource development.

► **Fiscal affairs.** Kazakhstan is simplifying its tax and customs administration and reporting. It should continue to stimulate internal growth and exports, and encourage savings and investment by individuals.

► **Private sector diversification.** Kazakhstan should step up efforts to diversify its economy. Improving the business climate and competitiveness will unleash Kazakhstan's economic and employment potential. Significant barriers to diversification remain in the areas of trading across borders, access to electricity and construction permits. The rail and road transport system is insufficient for adequate domestic and international connectivity.

Kazakhstan plays a leading role in the OECD Eurasia Competitiveness

Programme and is the Co-Chair, together with the European Union, of the OECD Central Asia Initiative. Over the past five years, the program has built on OECD good practices and instruments, and developed a platform for peer review and knowledge exchange. This has helped Kazakhstan to boost competitiveness, improve its investment climate and strengthen entrepreneurship. The program has established strong regional policy networks at the highest political levels. It has undertaken a series of ambitious projects and reviews at the regional, national and sub-national levels.

Kazakhstan in context



Growth expected, but it will remain fragile

Real GDP growth rate

	2012	2013	2014E*
US	2.8	1.9	2.8
Eurozone	-0.6	-0.5	0.9
RGMs	4.6	4.4	4.7
CIS	3.4	2.1	2.6
Kazakhstan	5.0	5.5	6.3

*E=Estimate

Sources: *World Economic Outlook*, International Monetary Fund (IMF), April 2014; *EY Rapid-Growth Markets Forecast*, February 2014; *EY Eurozone Forecast*, December 2013; *EY Eurozone Forecast*, March 2014.

In 2013, growth picked up in the advanced economies, but it slowed in a number of emerging markets. Globally, the second half of 2013 was a growth period, with further improvements expected thanks to the recovery in advanced economies. Global economic activity is projected to expand by 3.7% in 2014 and by 3.9% in 2015. However, low inflation in advanced economies as well as capital flow volatility in emerging economies continue to pose threats.

► The US is regaining momentum.

The US economy continued to grow modestly in 2013 amid strong fiscal consolidation. Recovery is set to accelerate in 2014. US GDP is projected to grow by 2.8% in 2014, supported by a pickup in domestic demand.

► The Eurozone is moving out of recession, but risks remain.

The Eurozone economy grew by 0.3% in the second quarter of 2013, after six consecutive quarters of negative growth. However, the Eurozone economy shrank in the year overall. Growth is expected to return in 2014, but the recovery will be uneven. Exports will drive growth, but high public and private debt and financial fragmentation may deter domestic demand.

► Opportunities and challenges ahead for RGMs.

After the slight slowdown in 2013, we expect the RGMs to grow by 4.7% this year, and 5.1% by 2015. However, if the global monetary tightening anticipated in 2014 does not fare well for the markets, capital flight and weakening currencies could limit growth to 3.7% this year and 2.8% in 2015.

Viewpoint

Looking beyond oil and gas

“We want to help the country to diversify its economy and support industries outside the oil and gas sector.”

The European Bank for Reconstruction and Development (EBRD) is the largest investor in Kazakhstan outside the extractive industries. In total, we have invested US\$6.5b in the country. Last year, we invested approximately US\$550m in various sectors, including energy efficiency, urban transport, infrastructure, agribusiness, micro-credit and small and medium enterprises (SME) lending.

Furthermore, the Government of Kazakhstan provided €2.9m for the next three years to help us extend our Small Business Services (SBS) program. SBS operates from Almaty, Astana and five regional offices. It has provided consulting services to over 1,000 companies in Kazakhstan. The Government also committed US\$6m to the EBRD-Kazakhstan Joint Technical Cooperation Fund. The fund will support various policy advisory projects. For example, it will help to establish legislation for green energy projects, strengthen corporate governance and fund a study on economic diversification.

The Government has stressed the EBRD's vital role in upgrading Almaty's urban infrastructure and supporting the growth of the green economy. The EBRD has invested US\$120m in the urban transport sector. It has, for example, provided 400 green buses and 195 trolleybuses. As a result of our work, nearly 60% of the public transport fleet in Almaty is now carbon-friendly. EBRD



Janet Heckman

Country Director, European Bank for Reconstruction and Development

is now replicating this work in other administrative areas in Kazakhstan.

The EBRD's Strategy for Kazakhstan, which was approved by the Government of Kazakhstan and the EBRD Board of Directors in December 2013, includes three main priorities. First, we want to help the country to diversify its economy and support industries outside the oil and gas sector. Kazakhstan's GDP amounts to three times the value of the country's extracted oil. In Russia, this ratio is five to one. Increasing this factor will help the country to achieve its goal of becoming one of the world's top 30 developed countries. Diversification is also possible beyond this ratio of five to one. Russia's policies, for example, focus exactly on that objective.

We will continue to help develop the other, non-oil and gas sectors in Kazakhstan by financing projects that enhance productivity in the corporate sector; improve the business environment; promote modernization of the agribusiness sector along the entire value chain; and support growth of the SME sector. We will also work to develop further the banking and non-banking financial sectors.

The second priority is to try to assist the Kazakh authorities with the task of balancing the roles of the state and the market, by supporting growth of private sector enterprises. As part of this, the EBRD will support policies aimed at commercializing public enterprises and making them more efficient. We will also continue to help upgrade the country's infrastructure, while ensuring appropriate sharing of risks between the private and public sectors.

Third, we will continue to promote low-carbon growth and energy efficiency. The Government's recently announced Green Economy Strategy is a top national priority. We will aid the implementation of key aspects of the strategy through projects in energy, renewables, agriculture, water, waste management, transport and other sectors.

We are working with the Government of Kazakhstan on a number of policy initiatives, including: tariff reform and regulation; local currency and capital markets development; banking sector support; development of SMEs and the micro credit sector; the green economy and energy efficiency; corporate governance; and reform of public-private partnerships (PPP).

Kazakhstan today and tomorrow

Kazakhstan in the world economy

Kazakhstan's economy grew by 5.5% in 2013, supported by strong domestic demand, increased oil output and recovered crop production.¹ But the economy currently faces headwinds, as is the case with most RGMs. Many emerging markets have experienced currency depreciation in recent years, and Kazakhstan is no different. In February 2014, the central bank devalued the currency (the tenge), by nearly 20%, which received a negative

feedback from consumers and some businesses. However, according to the central bank, this decision will preserve macroeconomic stability and have a medium- and long-term positive impact on increasing the competitiveness of Kazakhstan's goods and services. It will also be beneficial to exporters.

While investors continue to feel strong about the country's appeal as its macroeconomic outlook is stable, external challenges, including geopolitical tensions in the region, could pose a threat to this

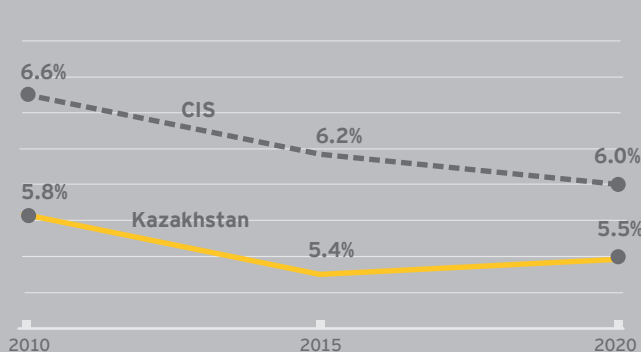
growth. The economy could safeguard itself against external shocks by successfully diversifying. And Kazakhstan's economy may also be cushioned by the US\$70b stored away in a sovereign wealth fund that is not counted as part of reserves.² At the same time, expansion in credit is expected to drive investment. But investors and the Government will need to come together for a collaborative growth agenda.

1. EY Rapid-Growth Markets Forecast, February 2014.

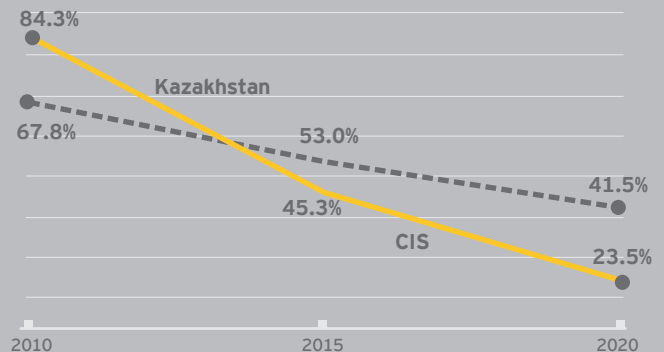
2. "Feeling Economic Pressure, Kazakhstan Takes Sudden Action," *The New York Times* website, www.nytimes.com, accessed 15 February 2014.

Kazakhstan's macroeconomic indicators are robust

Low unemployment rate (%)



Reduced debt (external debt-to-GDP ratio)



Growing incomes (GDP per capita US\$)

	2010	2015	2020
Kazakhstan	11,124	14,433	18,499
CIS	10,143	11,872	14,370

Increasing urbanization (% of total population)



Sources: Oxford Economics; "Kazakhstan Overview," *The World Bank* website, www.worldbank.org, accessed 2 February 2014.

Note: for the purpose of calculations, median data has been used for select CIS countries that include Azerbaijan, Belarus, Kazakhstan, Kyrgyzstan, Russia and Ukraine.

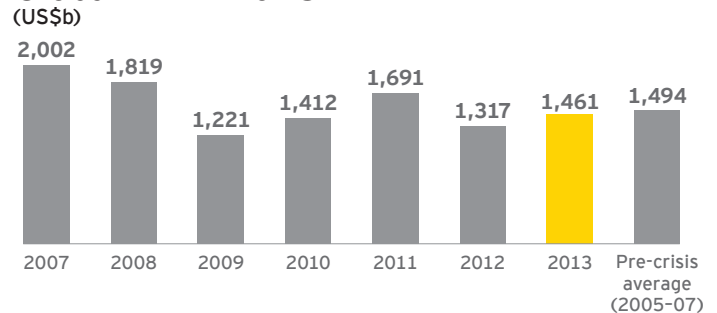
Bouncing back

Global FDI increased by **11%** in 2013.

Global FDI was up 10.9% in 2013 from 2012. However, this growth was not evenly spread. The shift in FDI patterns seen in 2012 continued in 2013, with developing economies drawing a greater share of investors' attention.

Advanced economies recorded a mere 39% global share of investment – a historical low. On the other hand, developing economies commanded an impressive 52% of inflows. Latin America and the Caribbean led the way, while foreign investment in Africa also grew at a healthy pace. Transition economies also enjoyed a significant rise in FDI inflows. UNCTAD remains optimistic about FDI prospects and predicts that global FDI inflows will reach an estimated US\$1.6t in 2014 and US\$1.8t in 2015.

Global FDI inflows



Source: *Global Investment Trends Monitor*, UNCTAD, January 2014.



KazMunayGas, the national oil and gas company of Kazakhstan in Astana, Kazakhstan.

Growing awareness

Kazakhstan's strengths, weaknesses and main competitors



The Bayterek monument and observation tower at the center of Astana, Kazakhstan.

Perception

47% consider Kazakhstan the most attractive of the CIS countries.

47% consider Astana the most attractive city in Kazakhstan.

57% of established investors report being successful in Kazakhstan.

30% plan to invest in Kazakhstan in the next year.

Kazakhstan's strengthening position in the CIS

The CIS countries are in the midst of currency devaluations and regional tension, as well as the speculation about growth

Kazakhstan remains the second most attractive CIS country.

prospects resulting from these concerns. In this changing economic climate, businesses need to reassess the opportunities and challenges of doing business in the region.

This year's attractiveness survey results show that Russia's lead in the CIS region has increased. Accession to the World

Trade Organization (WTO) and a significant improvement in the World Bank's 2014 Doing Business rankings (up to 92nd in 2014 from 111th in 2013) have added to the country's appeal.³ Other positive factors include infrastructure development, and the focus on innovation and diversification.

Kazakhstan remains the second most attractive CIS country, and its lead over Ukraine in third place has increased since last year's survey. However, investors remain divided in their outlook for Kazakhstan. Investors who are already established in the country rate Kazakhstan as the most attractive CIS destination, but non-established investors rank it third, after Russia and Ukraine.

Ukraine's favorable geographic location, its domestic market of 45 million people and its skilled, competitive human capital contribute to the country's investment appeal.

But we must note that the survey was conducted prior to Ukraine's change in leadership and recent geopolitical developments, the impact of which, on the CIS countries' investment appeal, is yet to be assessed.

3. *Doing Business 2014: Russian Federation*, The World Bank, 28 October 2013, p. 5.

Most attractive CIS countries

Which do you think is the most attractive CIS country to establish operations in?

	2012	2013	2014
Russia	55.7%	52.5%	68.7%
Kazakhstan	38.5%	36.4%	47.1%
Ukraine	37.5%	34.1%	38.6%
Azerbaijan	9.2%	9.1%	17.0%
Belarus	6.0%	11.8%	15.6%
Georgia*	6.9%	6.0%	12.2%
Uzbekistan	-	4.8%	10.8%
Moldova	0.9%	1.7%	4.2%
Turkmenistan	3.6%	1.8%	4.2%
Can't say	30.0%	32.4%	15.2%

Sources: EY's 2012 Kazakhstan attractiveness survey (total respondents: 211); EY's 2013 Kazakhstan attractiveness survey (total respondents: 206); EY's 2014 Kazakhstan attractiveness survey (total respondents: 211). Respondents were requested to select three countries.

* Georgia is not a CIS member, but has been included in the reference group for the purpose of this survey.

A stronger brand in the FDI market

This year's survey results showed that investors are becoming increasingly aware of Kazakhstan. In previous surveys, a relatively high proportion of respondents have not been able to express an opinion on Kazakhstan as an FDI destination. In 2014, the number of respondents who said that they "can't say" has gone down considerably. For example, this year, only 21.8% of non-established investors did not have an opinion about Kazakhstan's economic position in 2030, compared with 54.6% in our 2013 survey.

This increase in awareness can be partly attributed to a number of ongoing government efforts. These include its focus on increasing international integration, its diversification initiatives and its investment promotion activities. For example, the Ministry of Industry and New Technologies set up the National Export and Investment Agency KAZNEX INVEST in 2010 to attract foreign investment in priority sectors and to improve the country's investment climate.⁴ In 2017, Astana will host EXPO 2017, which will secure developments in physical and social infrastructure.

The Government's foreign embassies have also actively engaged in brand building, by organizing investment forums and road shows.⁵ As a result, investors are now tracking the economy to identify potential opportunities emerging from the WTO accession and EEU talks, and they are now more aware of specific investment opportunities, and of how to invest in the country.



Nevertheless, Kazakhstan needs to continue its efforts to increase awareness among investors. One way it can do this is by publicizing the success stories of corporations operating in the country. Investment agencies can also play an important role by proactively arranging partnerships between investors who are not yet established in the country and local manufacturers and suppliers. This would help new investors to get acquainted with the local environment.

4. "KAZNEX INVEST summed up the efforts to attract foreign investment in Kazakhstan for 2012," *Kaznex invest website*, www.kaznexinvest.kz/en/news, accessed 1 March 2014.

5. "Kazakhstan-US Investment Forum," *Embassy of the Republic of Kazakhstan in the US website*, www.kazakhembus.com, accessed 25 February 2014.

Narrowing awareness gap

Percentage of "can't say" responses for parameters on Kazakhstan's attractiveness

	2013	2014
Most attractive cities or locations in Kazakhstan for investors	57.3%	42.7%
Sectors that will get most foreign investment over the next three years	27.6%	23.0%
Perception of Kazakhstan in 2030	42.0%	19.8%

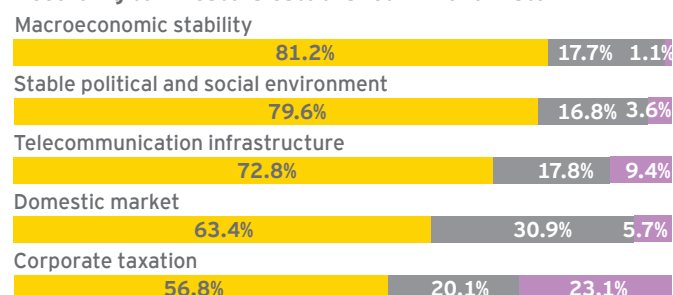
Sources: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211); EY's 2013 Kazakhstan attractiveness survey (total respondents: 206).

Key advantages vary for established and non-established investors

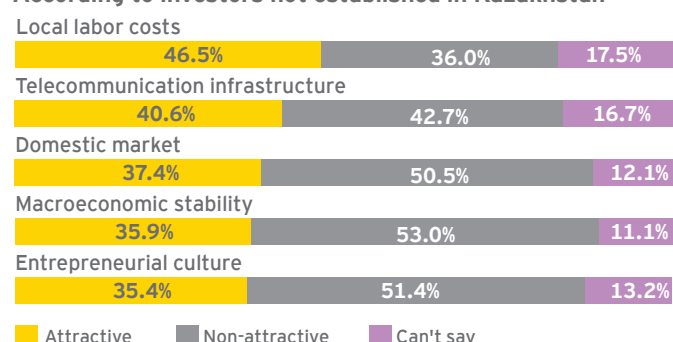
Our survey results show that there is a significant difference between the views of those who are yet to invest in Kazakhstan and those who already have. Established investors place great value on the country's high level of economic, political and social stability and its competitive corporate tax rate. Those not present in the country seem to be less aware of these factors. However, both groups place the country's telecommunication infrastructure and the size of its domestic market, due to integration initiatives, as two of Kazakhstan's five most attractive features.

Top five most attractive features

According to investors established in Kazakhstan



According to investors not established in Kazakhstan



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211; established in Kazakhstan: 78 and not established: 133).

► **Macroeconomic stability.** In the *Global Competitiveness Report 2013-2014*, produced by the WEF, Kazakhstan is ranked 23rd out of 148 countries for its macroeconomic stability. This places Kazakhstan ahead of many other emerging markets, including Ukraine (107th), Turkey (76th) and Brazil (75th), though it does fall behind Russia (19th). Established investors have benefited from the country's stability-oriented macroeconomic policies. These policies are based on a robust framework that mobilizes resource earnings. However, the currency devaluation and volatility caused by the country's high level of dependence on the oil and gas sector are concerns for some of the corporations operating in the country.

► **A stable political and social environment.** Kazakhstan's political system is considered highly stable. This has been reflected consistently in the business environment, which has worked well for investors established in Kazakhstan. The Government's long-term strategies, such as the Kazakhstan 2050 program, have helped to build investor confidence by articulating the country's priorities.

► **Telecommunication infrastructure.** Kazakhstan has a booming telecommunication market, which had achieved nearly 100% mobile penetration by early 2010. The country came in 43rd on the WEF's Network Readiness Index, ahead of Russia (54th), Azerbaijan (56th) and Ukraine (73rd).⁶ Kazakhtelecom, the largest telecommunication company in Kazakhstan, has deployed a fully digital national telecommunication network, which uses local and long-distance switches and fiber-optic lines to ensure connectivity across all of the major cities. The country is also working toward increasing the number of fixed-line subscribers, digitalizing telecommunication exchanges and improving international connectivity.⁷

6. *The Global Information Technology Report 2013*, World Economic Forum, March 2013.

7. "Research and Markets: Kazakhstan – Telecoms, Mobile, Broadband and Forecasts – 2012," *Reuters website*, www.reuters.com, accessed 1 March 2014.



Kazakhstan's reform agenda has remained fairly consistent, with some improvements over time. Investors continue to see the country's regulatory and administrative environment, its trade and labor policy, as well as infrastructure, as key areas for improvement.

► **Domestic market.** About 67% of Kazakhstan's population is in the working-age range (15-64 years), which is the group that contributes most both to consumption and the workforce.⁸ This, along with the high level of purchasing power, makes the domestic market attractive to investors. Kazakhstan's GDP per capita is US\$13,952.6, substantially higher than the CIS average of US\$10,262.6.⁹ Although its population of 16.7 million is relatively small, it does provide investors access to the multiple surrounding markets.¹⁰ Kazakhstan also benefits significantly from its location between the key commodity markets of Europe and Asia. With the introduction of the Customs Union between Belarus, Kazakhstan and Russia, the common market covers almost 170 million consumers.

► **Corporate taxation.** While the level of corporate taxation is regarded as an attractive feature by 56.8% of established investors, only 21.6% of non-established investors find it favorable. A positive feature of Kazakhstan's tax system is its low corporate as well as individual income tax rates, at 20% and 10% respectively. However, foreign investors complain about arbitrary and frequent inspections by local and national financial authorities.¹¹ And some business leaders have raised concerns about the country's transfer pricing legislation.¹²

8. "Global Economic Databank," *Oxford Economics database*, accessed 25 February 2014.

9. *EY Rapid-Growth Markets Forecast*, February 2014; "Global Economic Databank," *Oxford economics database*, accessed 25 February 2014.

10. *EY Rapid-Growth Markets Forecast*, February 2014.

11. "Doing Business in Kazakhstan," *United States Diplomatic Mission to Kazakhstan website*, www.kazakhstan.usembassy.gov, accessed 10 March 2014; "2013 Investment Climate Statement – Kazakhstan," *US Department of State website*, www.state.gov, accessed 10 March 2014.

12. "Foreign Investment Climate: Reforms and progress" *Consulate General of the Republic of Kazakhstan in the United Arab Emirates website*, www.kazconsulate.ae, accessed 10 March 2014.

Wanted: more improvement in infrastructure and business environment

Percentage of respondents who rate the following parameters as "attractive"

	2011	2012	2013	2014
Transport and logistics infrastructure	25.5%	27.4%	18.6%	33.7%
Open trade policies (introduced in 2013)			25.7%	32.6%
Labor law flexibility regarding hiring, termination and duration of work*	19.1%	28.6%	23.2%	29.9%
Visa and work permits regime – ease of bringing in qualified talent** (introduced in 2012)		18.2%	17.5%	28.1%
The transparency and stability of the regulatory and administrative environment***	14.2%	20.6%	17.6%	25.7%
Tax administration system (introduced in 2012)		16.8%	19.7%	24.7%
R&D availability and quality	14.2%	15.6%	10.1%	24.6%

*Until 2012: "Flexibility of labor regulations." **Until 2012: "Visa and work permits regime." ***Until 2012: "Transparency and stability of legal and regulatory environment." Sources: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211); EY's 2013 Kazakhstan attractiveness survey (total respondents: 206); EY's 2012 Kazakhstan attractiveness survey (total respondents: 211); EY's 2011 Kazakhstan attractiveness survey (total respondents: 204).

► **Transport and logistics infrastructure.** Both established and non-established investors want to see improvements in the country's transport and logistics infrastructure. The WEF's *Global Competitiveness Report 2013-2014* ranks Kazakhstan's overall infrastructure quality 62nd out of 148 economies.¹³ A vast territory, landlocked geography and uneven distribution of population clusters drives up the country's transportation cost. In Kazakhstan, transportation costs account for 8% (railways) and 11% (automotive traffic) of the final cost of goods. This is much higher than the 4%-4.5% level in developed economies. Kazakhstan also needs to shift toward models adopted in the European Union countries to handle its cargo intensity.¹⁴ This could significantly reduce the cost of operating in the country.

► **Open and flexible trade policy.** Kazakhstan's strategic location between Europe and Asia gives it great transit and trade potential. But it needs a more open trade policy to reach its full potential. The World Bank's *Doing Business Report 2014* ranks Kazakhstan 186th out of 189 economies on the "trading across borders" parameter. Companies operating in Kazakhstan need to comply with a lengthy process for exporting and importing goods. For instance, a company needs to spend US\$4,885 and wait for 81 days to export a standard container of goods from Kazakhstan. In contrast, it takes an average of only 25 days and US\$2,109 to export a standard container from Europe and Central Asia.¹⁵

► **Administrative environment.** Even with its stable political system, the country suffers from governance issues, such as corruption and bureaucracy. Investors from developed economies (North America and Western Europe) have negative views about Kazakhstan's administrative environment. On the other hand, those from Central and Eastern Europe (CEE) and Brazil, Russia, India and China (BRIC) are more accustomed to operating in these conditions, as such challenges are typical for many emerging markets. The country has substantially improved its business environment over the past few years, but further development is expected, particularly in combating corruption. Transparency International's Corruption Perception Index 2013 places Kazakhstan in the category of the most corrupt countries, ranking it 140th out of 177 economies.¹⁶

► **Labor law flexibility and a more favorable work permit regime.** Many investors want Kazakhstan to make it easier to bring foreign talent into the country, and they would like more flexibility regarding the hiring and dismissal of employees and the duration of their work. This is something that is highlighted most by North American investors, whereas CEE and BRIC respondents are relatively satisfied with the country's labor regulations. The Government limits the issuance of work permits to boost local employment based on the area of specialization and geographic region. This makes the work permit system difficult and time-consuming. Nevertheless, there has been some improvement in this regard. For instance, the foreign labor quota (ratio of foreigners to number of local hires) has increased from 0.14% of the active labor force in 2003 to 1% in 2012.¹⁷

13. *The Global Competitiveness Report 2013-2014*, World Economic Forum, August 2013.

14. "Transport and communications," *The Embassy of Republic of Kazakhstan in the United Kingdom website*, www.kazembassy.org.uk, accessed 26 February 2014.

15. *Doing Business 2014*, The World Bank, 28 October 2013.

16. "Corruption Perceptions Index 2013," *Transparency International website*, www.transparency.org/cpi2013, accessed 14 February 2014.

17. "2013 Investment Climate Statement – Kazakhstan," *US Department of State website*, www.state.gov, accessed 3 March 2014.

Viewpoint

Resources remain key, but diversification offers promise

“We see potential benefits from the Government’s efforts to diversify the economy.”



Gordon Haskins

Chairman of the Management Board, RBS Kazakhstan

While RBS Kazakhstan expects the local economy to grow at a healthy pace, certain short- and medium-term headwinds remain in emerging markets, including Kazakhstan. The realignment of global liquidity triggered by the shift in monetary policy in the US has resulted in increased volatility in emerging markets. In response to some of these threats, the National Bank of Kazakhstan has announced the devaluation of the tenge. And most recently, we have seen events in Ukraine result in sanctions being imposed by the US and the European Union, which could have spillover

effects for Kazakhstan. Unfortunately, some of these headwinds could also further impact the local banking market in Kazakhstan, which has yet to recover fully from the effects of the financial crisis.

For RBS Kazakhstan, our strategy remains as it has been over the last couple of years: to focus on our large corporate and institutional clients – both local and global – that have operations in Kazakhstan. In particular, this includes our core UK clients. From a sector perspective, oil and gas, energy and other natural resources will remain the key sectors driving the local economy.

However, we see potential benefits from the Government’s efforts to diversify the economy. We will continue to diversify our client portfolio in the same way. For example, we are pursuing opportunities in the transportation and telecommunication sector.

We also think that local efforts to improve the foreign investment climate, and to enhance the ease of doing business, need to continue. These efforts remain crucial if the Kazakhstan economy is to continue attracting significant investment from abroad.

The appeal of Kazakhstan's cities

This year's survey shows that our respondents' overall awareness of the investment potential of Kazakhstan's cities has improved, but there are regional variations. Compared with their BRIC and CEE counterparts, investors from the developed economies have less knowledge of the country's investment regions. This suggests that the Government needs to geographically align its investment-promotion initiatives.

Increasing city awareness

Percentage of "can't say" responses for most attractive cities for investment in Kazakhstan

	2013	2014
Established in Kazakhstan	18.9%	7.1%
Not established in Kazakhstan	74.6%	63.6%

Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211; established in Kazakhstan: 78 and not established: 133).

Most attractive cities in Kazakhstan for investors

What are the most attractive cities or locations in Kazakhstan for investors?

	2014
Astana	46.5%
Almaty	39.3%
Atyrau	12.8%
Aktau	8.5%
Karaganda	8.2%
Shymkent	7.1%
Pavlodar	4.0%
Aktobe	3.6%
Usk Kamenogorsk	1.4%
Can't say	42.7%

Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211). Respondents were requested to provide three cities.

Astana accounts for 9.4% of the country's total GDP.¹⁸ Astana is home to the headquarters of national companies and holdings, including the sovereign wealth fund Samruk-Kazyna and the Baiterek national holding. The Astana New City SEZ offers tax and customs preferences, land plots and access to engineering infrastructure. Over the last few years, a number of projects have been launched, with the participation of major international investors:

- ▶ **Airbus Helicopters (France):** helicopters
- ▶ **Alstom (France):** electric locomotives
- ▶ **Astana Solar (France):** photovoltaic modules
- ▶ **GE (US):** locomotives
- ▶ **Talgo (Spain):** passenger cars

Astana's strategic position at the heart of Eurasia contributes to its transport and logistics potential. More than 96% of freight traffic passing into Astana is in transit. The city infrastructure is developing rapidly. For several years, the construction sector has been an engine of economic growth. It has attracted investment and jobs. Annually, the volume of commissioned housing exceeds one million square meters. The city aims to join the top 50 global intelligent communities and, since 2012, has been implementing the Smart Astana project. In 2017, Astana will host the international exhibition Expo 2017, which will focus on the topic of "future energy." The city is working on three other projects:

- ▶ **Astana Green City** (solutions in energy efficiency and renewable energy).
- ▶ **Astana Mobility** (renovation and improvement of transport infrastructure and logistics systems).
- ▶ **Welcome to Astana!** (upgrading hotels and hospitality to the best international standards).¹⁹

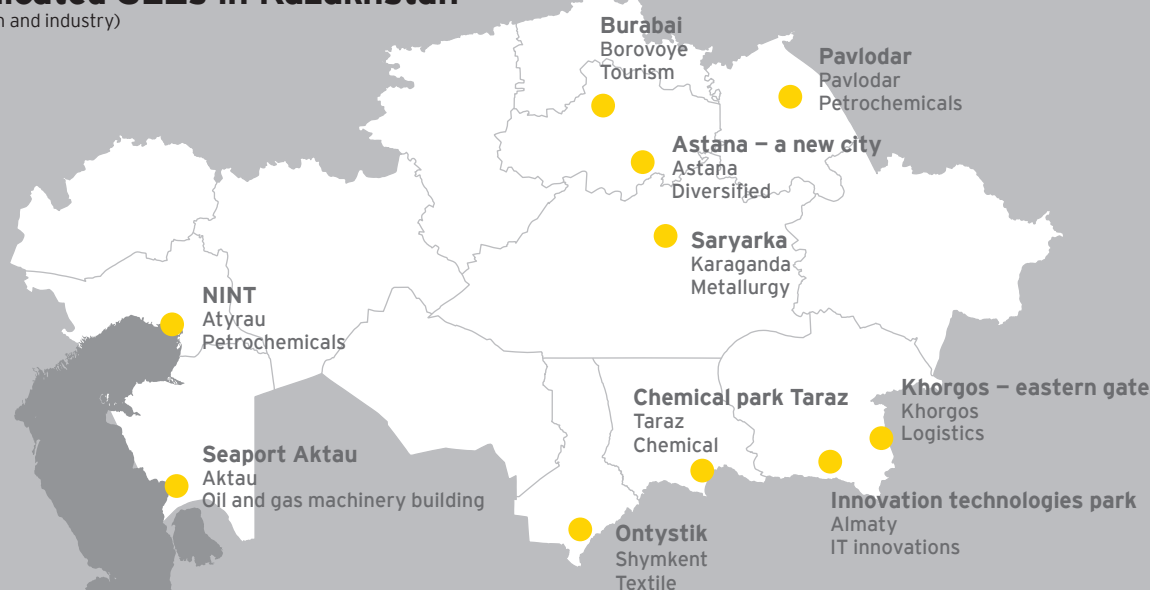
Almaty is the largest city in Kazakhstan, with a population of over 1.5 million people. The city accounts for around 20% of the country's GDP. Almaty is one of the major transportation hubs in the region. It has a developed infrastructure that helps investors to export goods to neighboring markets. Almaty plans to invest in innovation, tourism and hospitality, and urban infrastructure. Alatau IT City, an innovative technology park, hosts 150 companies. This number has increased fourfold over the past two years.

18. Statement of Mayor of Astana, *Akimat of Astana website*, astana.gov.kz accessed 3 May 2014.

19. *Invest in Astana website*, investinastana.kz, accessed 8 May 2014.

Ten dedicated SEZs in Kazakhstan

(Name, location and industry)



Source: Ministry of Industry and New Technologies of the Republic of Kazakhstan website, mint.gov.kz, accessed 8 May 2014.

The Greater Almaty Ring Road (BACAD)

BACAD is Kazakhstan's visible PPP in road construction, and capitalizes on the country's transit potential. EBRD and International Finance Corporation (IFC) are facilitating the project.

Project highlights:

- ▶ Four- to six-lane road with a total length of 66km, 8 road interchanges and 21 bridges
- ▶ Construction: 2016–2020, operation: 2020–2046
- ▶ Estimated cost: KZT124b

Source: Ministry of Transport and Communications of Kazakhstan.

Almaty is an important tourist destination, given its location at the foot of the famous Tien-Shan mountain range. The city has world-class skiing facilities and will develop a new ski resort. The 2017 Winter Universiade, an international sporting and cultural festival, will contribute to the development of tourism and hospitality.

Almaty plans further urban transformation through investment in its public transportation network, the development of an intelligent transport system and increased energy efficiency. These factors will all help to improve the quality of life for the city's inhabitants.²⁰

Atyrau is the energy capital of Kazakhstan. The Atyrau region's share of the country's total GDP reached 10.6% in 2013, the second-largest share after Almaty.²¹ Its gross regional product (GRP) per capita is the country's largest. The oil and gas industry is the main sector in the region. Atyrau accounts for 73% of the country's hydrocarbon reserves, 47% of oil and 36% of gas

production.²² The city is located near the world's largest oil and gas fields – Karachaganak, Kashagan and Tengiz. Other developed industries include petrochemicals and machinery building.

Aktau is located in the Mangystau region and is the country's biggest seaport. The region's share of the country's GDP reached 5.5% in 2013 and its GRP per capita is the fourth-largest after the Atyrau region, Astana and Almaty.²³ The oil and gas industry – including a range of related sub-sectors such as oil field services, offshore construction, shipbuilding, and oil and gas machinery manufacturing – is set to be the main driver of region's future growth. Cross-border trade, transportation and logistics hubs, and tourism are other factors in the region's development.²⁴

In 2002, the Government set up the Aktau Seaport SEZ to encourage foreign and domestic investment in the country's logistics and transport industry. A hub for transporting goods to foreign markets via the Caspian Sea, many believe that the port is still not being used to its full potential.

Karaganda is located in central Kazakhstan and is among its largest industrial centers. The Karaganda region has considerable wealth in natural resources, including 100% of Kazakhstan's manganese reserves (9.7% of the world's reserves), 80% of the country's wolframite (55.1% of the world's reserves), 54% of Kazakhstan's lead, and significant shares of other natural resources. The major industries are mining and metals, machinery building, heavy machinery and chemicals. Karaganda is one of the major cities in Kazakhstan with more than 450,000 people.²⁵

22. "Economy of Atyrau region," Atyrau region governance website, www.atyrau-ds.kz, accessed 13 May 2014.

23. The Agency on Statistics of Kazakhstan, May 2014.

24. "Economy of Mangystau region," Mangystau region governance website, www.mangystau.gov.kz, accessed 13 May 2014.

25. Karaganda region governance website, www.karaganda-region.gov.kz, accessed 13 May 2014.

20. Statement of Mayor of Almaty, Almaty Invest forum, 3 December 2013.

21. The Agency on Statistics of Kazakhstan, May 2014.

Investors report success

To a large extent, investors in Kazakhstan have created successful businesses in the country. Survey results indicate that large businesses – those with revenue of US\$2b (€1.5b) or more – are more successful in the country than smaller companies.

However, some decline in confidence can be seen in this year’s survey. Only 57.4% of the established investors surveyed said that their companies have been achieving their business objectives in the past five years. This figure is down from 66.7% in last year’s survey. This fall can be partly explained by delays in investment projects, which have affected some companies’ short-term profitability.

Our survey reveals that industry and automotive respondents are the most upbeat about their achievements over the past five years.

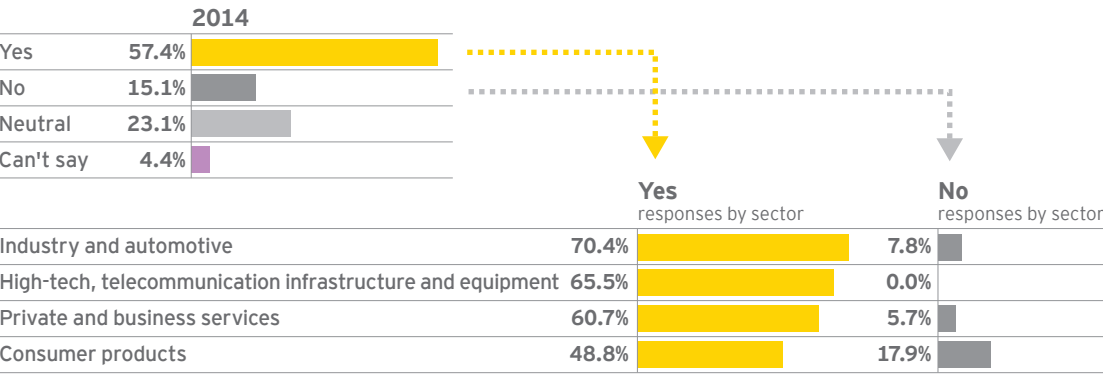
ArcelorMittal

ArcelorMittal has been present in Kazakhstan since 1995. The company has built a vertically integrated operation including a steel plant, a pipe plant, a laboratory, a testing complex and a pipe yard. The company is currently implementing a comprehensive modernization program to expand its crude steel production capacity to six million tons by 2015-16. To achieve this, it plans to invest up to US\$1b to expand capacity, overhaul its blast furnace and construct a more efficient oxygen unit.

Source: Success stories: foreign investors in Kazakhstan, Kazakhstan Foreign Investors' Council Association, 2011.

Evaluating investor success

Has your company been successful in achieving its business objectives in Kazakhstan over the past five years?



Source: EY's 2014 Kazakhstan attractiveness survey 2014 (total respondents: 211, established in Kazakhstan: 78; 15 were private and business services; 12 were high-tech and telecommunication infrastructure and equipments; 13 were consumer products; 12 were industry and automotive). Question only asked to investors established in Kazakhstan.

Industry and automotive includes heavy industry; automotive; infrastructure (roads and highways and ports); real estate and construction; and logistics. **High-tech and telecommunication infrastructure and equipment** includes electronic and electrical equipment; aerospace and defense; software and IT services; telecommunication; and information and telecommunication. **Private and business services** includes financial services; business services; media and entertainment; hotels and tourism; and human capital. **Consumer products** includes consumer products and retail.

Newcomers hesitate, established companies invest further

Responses to this survey suggest that investors are now more certain than they were last year about their investment plans in the short term. The 2014 survey shows that the percentage of respondents planning to set up or expand operations in Kazakhstan has increased to 30.3%, from 25.4% in 2013 and 17.2% in 2012. At the same time, however, the proportion of investors who expect that they will not invest has also increased.

Investors are now more familiar with and have greater confidence in Kazakhstan's investment climate. Tesco, the UK's biggest retailer, is among recent entrants; it opened a showroom in Astana in June 2013.²⁶

Around 65% of established investors have immediate plans for investment in Kazakhstan, compared with just 10% of non-established investors. This is similar to the trend that we saw in our 2013 Russia attractiveness survey, where 68% of established investors had immediate investment plans compared with 6.2% of non-established investors.

Mode of investment

Among those planning to make further investments, established investors are most likely to be looking to expand their facilities and increase their labor forces. New investors, on the other hand, are most likely to be planning to set up a JV or to make an acquisition. New investors often prefer to form partnerships with local firms, because it allows them to reduce their operational risk by accessing local expertise and knowledge.

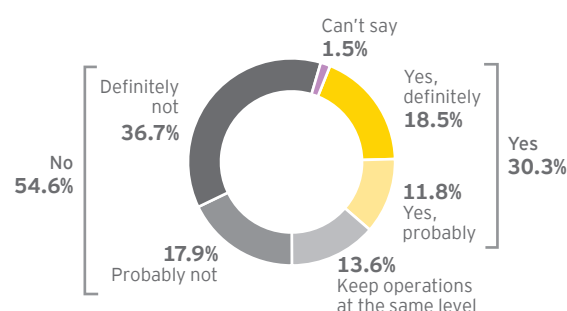
In June 2013, France's PSA Peugeot Citroen signed an agreement with Russia's Agromash Holding for assembly and distribution of Peugeot cars and Light Strike Vehicles (LSVs) in Kazakhstan. The project is designed to provide employment to approximately 150 people, with a production capacity target of 4,000 units per year in its initial years.²⁷

26. "F&F announces international expansion plans," Tesco press release, www.tescopl.com, 19 May 2013.

27. "PSA Peugeot Citroën will begin local assembly in Kazakhstan," PSA Peugeot Citroën press release, www.psa-peugeot-citroen.com/en/media/press-releases, 3 July 2013.

Immediate investor plans

Is your group considering establishing or developing activities in Kazakhstan over the next year?



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211).

Expansion of facility and increase in labor force are preferred

How are you planning to invest?

	2014
Expansion of facility or increase in labor force	51.3%
JV or alliance	27.8%
Acquisition	16.5%
Greenfield investments	15.0%
Franchise or licensee agreement	3.3%
Other	1.3%
Can't say	12.8%

Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211; planning to invest in Kazakhstan: 64). Respondents were requested to select from several possible answers.

Future

47% believe that Kazakhstan's attractiveness will improve in the next three years.

49% expect energy to be the top growth sector for FDI.

37% identify industry and automotive as the key FDI sectors.

40% believe that Kazakhstan will be a leading country in energy by 2030.

17% expect Kazakhstan to be surpassed by competition.



The Kazakhstan Central Concert Hall in Astana, Kazakhstan.

Rising expectations

Kazakhstan's medium-term attractiveness, the sectors expected to drive foreign investment in the next three years and Kazakhstan in 2030



Spreading confidence

Spreading confidence

Over the next three years, do you think the attractiveness of Kazakhstan as a place for companies to establish and develop activities will improve or deteriorate?

	2012	2013	2014
Improve	43.0%	41.4%	47.3%
Deteriorate	8.9%	9.4%	16.6%
Neither improve nor deteriorate	32.9%	29.5%	28.0%
Can't say	15.2%	19.7%	8.1%

Sources: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211); EY's 2013 Kazakhstan attractiveness survey (total respondents: 206); EY's 2012 Kazakhstan attractiveness survey (total respondents:211).

Investors' confidence in Kazakhstan's future prospects is at an all-time high compared with previous surveys. Almost half of this year's survey respondents expect Kazakhstan to become increasingly attractive over the near term. Interestingly, established and non-established investors hold similar views about the country's investment potential, in contrast with their responses to other survey questions. Around 55% of those who have already invested in Kazakhstan believe that its investment attractiveness will increase over the next three years, compared with 42.6% of investors not yet established in the country.

The improvement in investors' perceptions of the country could, in part, be the result of the country's long-term vision and its commitment to sustainable development. Kazakhstan has adopted a strategy that aims to position the country among the

30 most developed nations in the world by 2050. To achieve this, Kazakhstan is proactively defining new markets, building its innovation capacity, promoting sustainable private sector business development and creating a favorable investment climate. Kazakhstan's imminent WTO accession, and its improving links with China, Russia, as well as other Asian and European countries, will also enhance its trade potential and the opportunities for investment. The country's development prospects depend on its success in diversifying its economy, developing its infrastructure, investing in human capital and reforming its institutions.

Viewpoint

Bringing government and industry together

“Technological progress will be fastest when there are good communications between all of the oil and gas industry’s stakeholders.”

Oil and gas is among the most capital- and technology-intensive of all industries. The role technological innovation plays in aiding the discovery of economically viable new reserves and improving the efficiency of resource extraction is critical.

Investments in technology and R&D aimed at supporting vital oil and gas projects in Kazakhstan will also help to realize the country’s broader industrial and economic potential.

The Upstream Technology and R&D Roadmap was developed collectively by the Kazakhstan oil and gas industry, with facilitation and support from Shell Kazakhstan. Shell’s global Project & Technology organization formulated the technology and research priorities that are essential to ensuring that common industry challenges are addressed effectively.

If appropriate solutions can be put in place in the required time frame, the prime technology target areas identified in the road map have a significant value associated with them. It will be important for academia, local industry, the operators, service companies and the Government to form a genuine partnership. They should work together to plan ahead and drive the technology development vision of the Kazakhstan upstream oil and gas sector.

The vision is of an industry that maximizes the value of its oil and gas resources through world-class R&D; and strong local companies that are capable of delivering high-quality materials, equipment, services and innovative

solutions to the international standards demanded by major resource holders and field operators in Kazakhstan.

Technological progress will be fastest when there are good communications between all of the oil and gas industry’s stakeholders. The Roadmap, which is now fully supported and endorsed by the Government of Kazakhstan, is designed to promote purposeful collaboration and knowledge sharing across the industry, aligning the Government’s innovation agenda with real business needs.



Campbell Keir

Kazakhstan Country Chair, Shell

Co-Chair of Joint Innovative-Technologies and Economy Diversification Working Group of Foreign Investors’ Council, chaired by the President of the Republic of Kazakhstan

Moving forward: energy and beyond

Energy: Kazakhstan's winning card

The energy sector provides attractive business opportunities in Kazakhstan. The oil and gas industry's share in national GDP increased from 11% in 2001 to 25% in 2012.²⁸ International players, including the US energy giants Chevron and ExxonMobil, the UK's BG Group and Royal Dutch Shell, Italy's ENI, France's Total and China's CNPC, have long been involved in the country. Future industry trends look positive. The Organization of Petroleum Exporting Countries (OPEC) expects the country's oil production to increase by 90,000 barrels per day (bpd) to average at 1.73m bpd in 2014.²⁹ However, energy opportunities are not limited to just oil and gas. Driven by the country's 2050 targets, Kazakhstan is committed to diversifying its energy production and developing environmentally sustainable energy sources.

28. Kazakhstan oil and gas tax guide 2014, EY.

29. "OPEC says Kazakhstan's oil supply to jump in 2014," OPEC news today website, www.opec.einnews.com, accessed 1 April 2014.

Chevron

Chevron set up its operations in Kazakhstan in 1993 through a JV with the Government of Kazakhstan. The JV, Tengizchevroil (TCO), was set up to explore the Tengiz oilfield. Currently, it is Kazakhstan's largest private oil producer, with high participation in oil projects operating in the Tengiz and Karachaganak oil fields. It also has significant ownership in the Caspian Pipeline Consortium, which provides an important export route to transport oil from Kazakhstan's major oil fields. It has also undertaken community initiatives, such as the development of social infrastructure. Since 1998, Chevron and its partners have invested more than US\$240m in social infrastructure projects in western Kazakhstan.

Source: "Kazakhstan Fact Sheet," Chevron, April 2013.

Energy all the way

Which business sectors will attract the most foreign investment projects in Kazakhstan over the next three years?

	2013	2014	2014 Established	2014 Not established
Energy	41.5%	48.5%	70.1%	35.8%
Industry and automotive	22.5%	37.3%	62.3%	22.7%
Mining and metals	28.8%	18.5%	25.2%	14.6%
High-tech and telecommunication infrastructure and equipment	6.2%	14.9%	20.1%	11.8%
Private and business services	14.0%	13.9%	22.4%	8.8%
Agriculture	10.2%	10.9%	11.2%	10.8%
Consumer products	5.6%	9.2%	10.3%	8.6%
Life sciences	11.9%	8.1%	11.4%	6.1%

Sources: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211; established in Kazakhstan: 78 and not established: 133); EY's 2013 Kazakhstan attractiveness survey (total respondents: 206). Respondents were requested to provide up to three answers.

Energy includes oil and gas; power and utilities; alternative and renewable energy; and cleantech. **Industry and automotive** includes heavy industry; automotive; infrastructure (roads and highways and ports); real estate and construction; and logistics. **High-tech and telecommunication infrastructure and equipment** includes electronic and electrical equipment; aerospace and defense; software and IT services; telecommunication; and information and telecommunication. **Private and business services** includes financial services; business services; media and entertainment; hotels and tourism; and human capital. **Consumer products** includes consumer products and retail. **Life sciences** includes chemicals and allied products; health care; chemical and pharmaceutical industry; and pharmaceutical and manufacturing of medical equipment.



Industry and automotive are catching up

This year's survey has shown that investors are feeling increasingly positive about Kazakhstan's heavy industry and automotive sectors. This sentiment is justified by the ongoing growth across both of these sectors.

Industrial activity is getting a boost from the uptick in the heavy industry, infrastructure, real estate and construction sectors. Industrial output in the period from January to October 2013 increased by 2.3% compared with the same period in 2012.³⁰ Growth and opportunity is being driven primarily by two factors: diversification efforts and urbanization. The diversification drive is creating opportunities across a range of industrial product industries. In addition, the share of the population residing in urban centers is expected to rise to around 60% by 2030.³¹ As people move to cities, Kazakhstan will need to increase investment in infrastructure, including in public utilities and transport, and businesses will have to rethink their strategies according to the changing requirements of urban customers.

Automotive vehicle sales grew by 120% in 2012 to 98,231 units, exceeding the growth rates in most other geographies worldwide.³² Sales are expected to more than double again by 2017, to over 240,000 units.³³ This suggests that there are significant opportunities for automotive companies to tap into new segments and income groups. Opportunities for investors exist in both the domestic market and in exports. Foreign producers – including Russia's AvtoVAZ, France's PSA Peugeot Citroen and Japan's Toyota Motors – have indicated that they intend to increase their production in the country in 2014 and beyond.³⁴

30. Kazakhstan Results selection, *IHS Global Insights*, 14 January 2014, p. 2.

31. "Global Economic Database," *Oxford Economics database*, accessed 1 March 2014.

32. *Kazakhstan & Uzbekistan Autos Report 2014*, Business Monitor International, 13 November 2013, p. 8.

33. *Kazakhstan & Uzbekistan Autos Report 2014*, p. 8.

34. *Kazakhstan & Uzbekistan Autos Report 2014*, p. 8.

Toyota

Japanese car manufacturer Toyota Motors established operations in Kazakhstan in 2008 and has gradually enhanced its market share. The sale of Toyota cars in Kazakhstan reached 13,400 units in 2013, an increase of 45% from 2012. In February 2013, the company signed a Memorandum of Understanding with the Government and started manufacturing sport-utility vehicles at its existing plant in Kostanay. The production is expected to start soon, with a target of 3,000 units in 2014.

Source: Toyota Fortuner assembled in Kazakhstan to meet Japanese standards – Toyota Motor Corporation, "KazInform News Agency website, www.inform.kz, accessed 25 March 2014.

What should investors watch out for?

To ensure that their operations are successful, apart from complying with the general statutory legislation, investors also need to understand the specific industry regulations. The oil and gas sector, being a part of the extractive industry, is regulated by the Subsurface Use Law. Under this law, investors conducting exploration or production activities are required to conclude a relevant contract with the Government, which is normally referred to as a "subsurface use contract." The Government, represented by the competent authority, has the power to amend or terminate a subsurface use contract on the grounds provided by the Subsurface Use Law. Furthermore, there are a number of fields that are considered to be of strategic significance, to which certain additional requirements may apply. These strategic fields include, among others, the three largest projects in the industry, commonly referred to as Karachaganak, Kashagan and Tengiz.

Export duties apply to crude oil exports at the rate of US\$80 per ton (the rate is subject to periodic change) unless the exporter has special provisions in its subsurface use contract that would allow it not to pay the duty.

A mixed picture for mining and metals

The mining and metals industry accounts for 30% of Kazakhstan's total export earnings, and it is therefore considered a priority sector.³⁵ The country is blessed with abundant deposits of minerals and metal ores: it boasts of 30% of the world's chrome deposits, 25% of its manganese ore and 10% of its iron ore.³⁶

Kazakhstan's metal industry is expected to benefit from the country's developing logistics infrastructure and its location between major metal markets, such as China and Europe. The shift of global metallurgical production toward Asia will also work to its advantage.

The Government aims to attract US\$13b in investment into the sector and has set a target for doubling metal production between 2015 and 2019. This will require substantial foreign participation and an increased use of modern technology to improve productivity.³⁷

However, in this year's survey, investor confidence in the sector has declined. Mining companies in Kazakhstan express concern about bureaucratic hurdles when attempting to secure mining exploration licenses and tenders.³⁸

High-tech, telecommunication infrastructure and business services demonstrate potential

In order to flourish, technology and telecommunication infrastructure companies, as well as business services, require highly skilled and innovative staff. Kazakhstan has made little progress in this regard. The country ranks low (87th) on its business sophistication and innovation in the WEF's *Global Competitiveness Report 2013-2014*. And there is insufficient public-private dialogue on the skills required by these sectors. The skills gap could be addressed by better cooperation between the Government and industry, and by multinationals.

Nevertheless, these sectors do have growth potential, and they can become an important source of revenue and jobs in the country. Kazakhstan has the potential to become a good base for business services companies in Central Asia.

35. "Metal industry," KAZNEX INVEST, November 2013, p. 8.

36. "Metal industry," KAZNEX INVEST, November 2013, p. 7.

37. "Mining to Kazakhstan," Australian Trade Commission website, www.austrade.gov.au, accessed 17 April 2014.

38. "Miners urge Kazakhstan to remove investment barriers," Reuters website, www.reuters.com, accessed 17 April 2014.

Cameco

Cameco, a Canadian uranium producer, has been present in Kazakhstan since 1996, and it currently employs more than 500 people there. It operates in the country through Inkai, a JV with Kazatomprom. The JV holds two uranium production areas and one exploration area. Inkai has become an important production center for Cameco. The company aims to double its overall uranium production by 2018, and Inkai is expected to account for a large proportion of this increase. It is worth noting that the Inkai facility was recognized as the company's top site in its internal safety evaluation in 2007 and 2009.

Source: *Success stories: foreign investors in Kazakhstan*, Kazakhstan Foreign Investors' Council Association, 2011.

TeliaSonera

TeliaSonera, a leading European telecommunication services operator, has been present in Kazakhstan since 1998. It operates through its subsidiary Kcell (GSM Kazakhstan) and provides voice mobile communication as well as value-added services (VAS). Currently, it is the leader in Kazakhstan's mobile market in terms of sales volume. It has a total subscriber base of 14.3 million. It seeks to strengthen its position in Kazakhstan's mobile internet industry and improve competitiveness. In view of this, it acquired the WiMax division of local player Alem Communications for US\$170m in January 2013.

Sources: *TeliaSonera 2013 annual report*, available at www.teliasonera.com, p. 27; "TeliaSonera boosts presence in Kazakhstan," *Telecoms website*, www.telecoms.com, accessed 25 March 2014.

Viewpoint

A growing appetite for communications

“The young population of Kazakhstan ... and the high level of education will drive demand for more data services.”



Johan Dannelind

President and CEO, TeliaSonera

With 14.3 million subscribers, TeliaSonera's Kazakh operators Kcell and Activ are the undisputed market leaders in a country with a population of 17.2 million. According to the Statistics Agency of the Republic of Kazakhstan, there were 1,800 mobile subscribers per 1,000 people in 2012. Internet, however, lags behind, with only 96 subscriptions per 1,000 inhabitants.

As in Europe, we can expect major changes over the coming years. Smartphones, which are basically small computers, will undoubtedly become the norm. In Kazakhstan, as elsewhere, we will see more and more smart devices online. During 2013, we saw data revenue rise by nearly 40%. Data income now constitutes 14% of total revenue, 4% more than in 2012, and the share will continue to rise.

We can safely assume that many, if not most, will watch films on the web. The need to invest more in our networks no longer emerges from phone calls, but from a higher demand for moving images on mobile phones, tablets or TV.

Our customers want more and more from us, which, of course, is encouraging. They rely on us to provide them with the communications of the future. New business models are being developed in the digital revolution that we are going through, there are new ways to communicate, and even new lifestyles.

Within a short space of time, we have seen the establishment of new, exciting industries and new customer behavior. The demand for data capacity is growing dramatically. During the last quarter, data traffic in TeliaSonera's networks

grew by a staggering 60%. In Europe, more than half of today's internet traffic is composed of videos watched via such services as online TV and YouTube. The young population of Kazakhstan – with a median age under 30 – and the high level of education will drive a similar demand for more data services.

Kcell has, to date, invested more than US\$2b in Kazakhstan. Investments on a high level will continue, with a focus on strengthening our leadership in the data segment by ensuring high-quality telecommunication services.

The future will reflect today's strengths



Respondents to this year’s survey have a far more definite view of Kazakhstan’s opportunities and challenges in the years up to 2030, compared with last year’s survey. They are also more optimistic about Kazakhstan’s ability to emerge as a leading energy and agricultural producer, but they do recognize that the country faces stiff competition from other growing markets.

Energy continues to be the best long-term bet

Kazakhstan’s energy reserves will be the foundation for its development. Already strong in oil and gas, the energy sector is broadening its scope to include nuclear power and green energy. When asked about their vision of Kazakhstan in 2030, 4 out of 10 respondents said that they expect the country will be a leader in energy. Increased production volume and the good development prospects for the country’s giant fields – Karachaganak, Kashagan

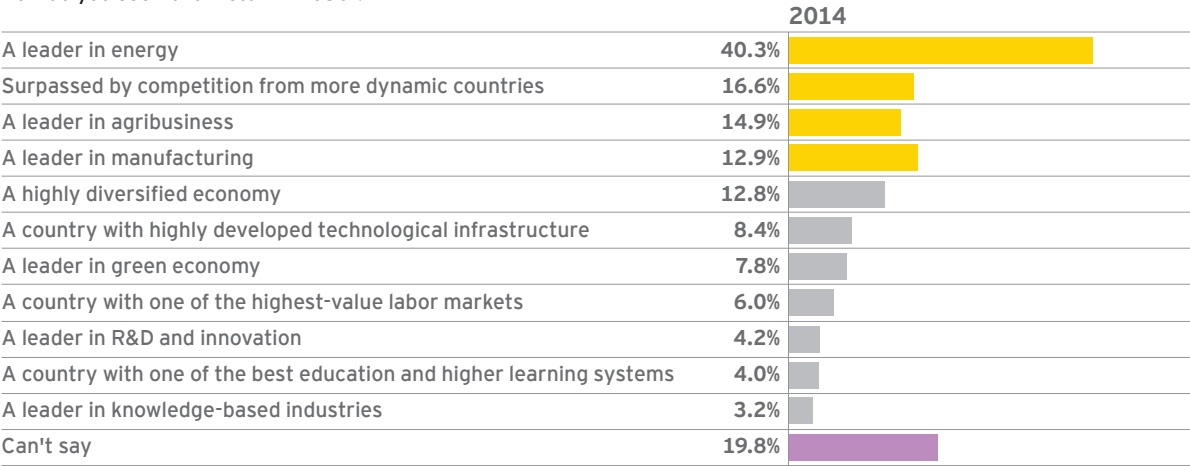
and Tengiz – hold the promise of a more prosperous future for the country. The International Energy Agency agrees, predicting that Kazakhstan will be among the top 10 oil and gas exporters by 2020.³⁹

However, dependence on a single sector carries intrinsic risks for the economy and for investors alike. Along with volatility issues inherent in energy pricing, the environmental and technical risks must also be considered. Production at Kashagan (one of the world’s largest oil discoveries in decades) was halted in October 2013 after a toxic gas leak. Nevertheless, Kazakhstan is likely to be able to work through these challenges and to continue increasing its export levels.

39. Kazakhstan oil and gas tax guide 2014, EY.

Kazakhstan – a likely energy leader in 2030

How do you see Kazakhstan in 2030 ?



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211). Respondents were requested to select two answers.



Competition at its most intense

Investors are not shy to state how the competition facing Kazakhstan has intensified. Other dynamic countries, especially among the other RGMs, are set for a period of high growth – there are expected to be nearly 200 million households in the RGMs with an annual in excess of US\$35,000 by 2022.⁴⁰ Investors are likely to target mainly consumers in the BRICs and other emerging economies, such as Turkey. In such a scenario, Kazakhstan needs to look to its domestic market to drive demand and to create a more robust middle class. Businesses need to anticipate what goods the growing middle class will want to buy tomorrow and then produce them at affordable prices.

A greater push in agribusiness

Agribusiness in Kazakhstan is poised for growth. The country is among the top 10 grain exporters in the world, and its export destinations cover over 70 countries. Its major grain importers are the other CIS countries, the Middle East, North Africa and the European Union.⁴¹ The sector benefits from high domestic demand and high export potential. Recognizing this, the Government has adopted the Agribusiness-2020 Program, by which it plans to increase the support subsidies to agriculture 4.5 times by 2020.⁴² Kazakhstan is also expected to pursue growing agricultural export opportunities in Central Asia and China.

Still time to become a leader in innovation

Our survey respondents do not expect Kazakhstan to become a leader in innovation or a knowledge-based economy by 2030. According to the United Nations Economic Commission for Europe's Innovation Policy Review, Kazakhstan lacks in terms of research-related institutional capacity and connectivity among important innovation stakeholders.⁴³ Therefore, to become a knowledge-intensive economy, the country must strengthen its industry-science linkages and upgrade its science and technology institutes. It should work toward providing an environment conducive for innovative entrepreneurs.

40. EY Rapid-Growth Markets Forecast, EY, February 2014.

41. "Agricultural sector," *Invest in Kazakhstan* website, www.invest.gov.kz, accessed 6 March 2014.

42. *Agricultural Development Program 2013-2020*, U.S. Agency for International Development, 12 June 2013.

43. "Innovation Performance Review: Kazakhstan," *United Nations Economic Commission for Europe*, 2 April 2012.

The food processing industry is set to grow

From 2006 to 2011, the value of the food processing sector's output increased by 73%. The most rapidly developing subindustries are meat, fat and oil, and flour milling. Continued development in these areas will require investments in modern technologies. Investors will gain the opportunity to serve the growing markets in large cities and to capitalize on exports. The potential for exporting beef is particularly significant. In 2011, the Ministry of Agriculture announced a two-phase plan to support beef exports. The first phase, from 2011 to 2015, will focus on quickly expanding the population of high-yielding breeding cattle. The focus in the second phase, between 2016 and 2020, will be on rapidly increasing the amount of beef exported.

Sources: *Promoting investments in Kazakhstan's agribusiness value chain*, OECD, 29 January 2013, p. 19; BMI Agribusiness Industry View – Kazakhstan – Q2 2014, Business Monitor International, February 2014; "Agricultural Sector," *Invest in Kazakhstan* website, www.invest.gov.kz, accessed 6 March 2014.

Facilitating success

Where Kazakhstan should focus to develop as an investment destination



Round Square in Astana, Kazakhstan.

Actions

44% of investors want to see improvement in the regulatory environment.

31% think that Kazakhstan should focus on physical and social infrastructure.

38% believe that the success of the EEU depends on the unification of administrative processes.

41% call for advancement in training and education in new technologies.

3 enablers of future investment in Kazakhstan: international integration, innovation-driven economy and green technologies.

Action plan: focus on business environment, infrastructure and talent

Investors' views about Kazakhstan's reform priorities remain consistent. Investors continue to want improvements in the business environment, infrastructure and human capital. One noticeable change from last year's survey is the decline in "can't say" responses, which suggests that investors are more certain of what the country needs to improve.

1 Create a consistent business environment

Corruption and bureaucracy are among the key issues deterring business in Kazakhstan.⁴⁴ Business leaders, particularly those with established operations in the country, are expecting a more transparent and stable regulatory environment. This need is highlighted by respondents across many sectors – which calls for the Government to address this challenge effectively, given the country's drive toward a knowledge-based economy. The Government needs to make efforts to reduce administrative barriers, ensure the consistent application of law and reduce its involvement in the economy. The authorities have been working in this direction. As a result of such efforts, the country consistently improves its ranking and, last year, moved up three positions to 50th place in the World Bank's *Doing Business* report.⁴⁵

44. *The Global Competitiveness Report 2013-14*, World Economic Forum, 8 September 2013.

45. *Doing Business 2014*, The World Bank, 28 October 2014.

2 Invest in infrastructure

To accommodate the needs of industries and to drive growth, the Government needs to develop infrastructure at a faster pace. This will require an investment of more than US\$25b by 2030, of which 40% will be needed for the railway system, 23% for the roads, 25% for telecommunication and 12% for air and water transport systems.⁴⁶ The scale of investment presents opportunities for PPP. In November 2013, the Government launched the State Program for Development and Integration of Transportation System to 2020.⁴⁷ The program involves the modernization of 30,000km of roads, over 8,200km of railway lines and 302 railway stations, as well as most of the airports and bus stations across Kazakhstan. This is expected to double the volume of transit by 2020. At the same time, new rail lines are being constructed – Zhezkazgan-Beyneu (east-west), Arkalyk-Shubarkol (north-south) and Zhetygen-Kazybek-Bek. Upon completion, which is expected by 2016-17, these will speed up cargo transportation between China and the Caspian Sea.⁴⁸

46. "Transport and communications," *The Embassy of the Republic of Kazakhstan in the UK website*, www.kazembassy.org.uk, accessed 26 February 2014.

47. *Report List (Kazakhstan)*, IHS Global Insight, 14 January 2014, p. 3; "Kazakhstan's 2020 Transit Plan Helps Connect Europe and Asia," *Astana Times website*, www.astanatimes.com, accessed 12 March 2014.

48. "Kazakhstan's 2020 Transit Plan Helps Connect Europe and Asia," *Astana Times website*, www.astanatimes.com, accessed 4 December 2013; *Report List (Kazakhstan)*, IHS Global Insight, 14 January 2014.

Action areas to improve investment climate

In your opinion, where should Kazakhstan concentrate its efforts to improve its investment climate?

	2012	2013	2014	
Develop a transparent and predictable regulatory regime	47.3%	32.2%	43.7%	Consistent business environment
Increase consistency of policy implementation*			28.0%	
Invest in physical and social infrastructure	30.8%	29.7%	30.6%	
Develop highly skilled human capital with a focus on economic needs	27.8%	26.4%	30.2%	
Ensure the court system's independence	24.1%	17.9%	28.0%	
Adopt a proactive approach to attracting investors	22.8%	15.2%	25.3%	
Stimulate entrepreneurship and innovation**		9.3%	21.1%	
Increase flexibility of labor regulations for skilled foreign specialists**		15.5%	17.7%	
Can't say	24.3%	29.8%	9.9%	

* Question introduced in 2014. ** Question introduced in 2013.

Sources: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211); EY's 2013 Kazakhstan attractiveness survey (total respondents: 206); EY's 2012 Kazakhstan attractiveness survey (total respondents: 211). Respondents were requested to select three answers.

3 Develop human capital

The third area of focus is the development of human capital to match the growing demands of businesses. The WEF's *Global Competitiveness Report 2013-2014* highlights the "inadequately educated workforce" as the second most problematic factor for businesses in Kazakhstan.⁴⁹ The country also ranks low on the quality of management education (96th), which suggests that there is a gap in managerial talent. The Government of Kazakhstan recognizes the need to upgrade its educational infrastructure. This can be done by setting up new-generation schools and colleges, and by modernizing teaching methods. For example, the Government has set up several Nazarbayev Intellectual Schools as part of the ongoing educational reform. These schools, which are equipped with the latest technology, focus on mathematics, science and foreign languages.⁵⁰

4 Ensure judicial independence

Our survey highlights the importance of ensuring judicial independence to improve the investment climate. President Nazarbayev acknowledged this in his speech at the Eurasian Forum of Emerging Markets in September 2013. He stated that Kazakhstan needs to improve the rule of law to become a developed, knowledge-based economy.⁵¹ This can be achieved by guaranteeing good governance and judicial transparency, and by creating legal literacy in the country. Under the Kazakhstan 2050 strategy, the Government plans to modernize the national legal system, to bring it in line with the international legal environment.⁵²

49. *The Global Competitiveness Report 2013-14*, World Economic Forum, 8 September 2013.

50. "Kazakhstan: Elite Schools May Limit Opportunities," *Eurasianet website*, www.eurasianet.org, accessed 3 March 2014; "Support Education Reform in Kazakhstan," *Embassy of the Republic of Kazakhstan in the US website*, www.kazakhembus.com, accessed 2 March 2014.

51. *Kazakhstan: Solid Growth, Unsettled Global Environment*, The World Bank, 13 November 2013.

52. "Strategy Kazakhstan 2050 new political course of the established state," Address by the President of the Republic of Kazakhstan, Leader of the Nation, N.A. Nazarbayev, December 2012.

5 Adopt a proactive approach to attracting investors

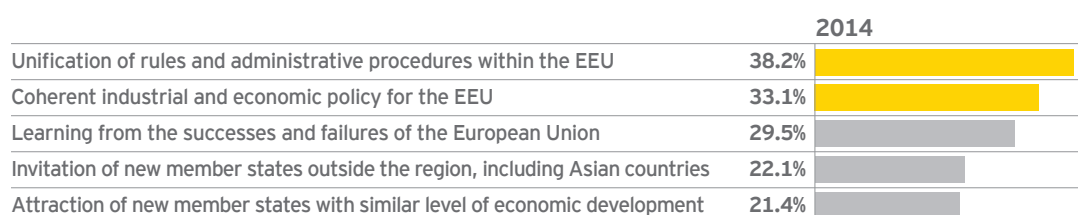
Improvements in the state governance system should encourage the consistent implementation of strategic initiatives. Investors expect legislation to be implemented transparently, and want to see its impact on the business community taken into account prior to enactment. Special effort should be made to attract FDI to the regions. There should be dedicated solutions for small and medium-sized foreign investors. Currently, the Government is working on a package of measures to improve the institutional environment and provide incentives for investors. These include stability of legislation and tariffs, guaranteed long-term state procurement, partial reimbursement of infrastructure costs after the project is commissioned, and simplification of the visa and work permits regime. All these efforts will support the innovative and industrial development of the country.⁵³

53. Press briefing of A. Iseshev, Deputy Prime Minister and Minister of Industry and New Technologies; E. Dosayev, Minister of Economy and Budget Planning, 29 April 2014, *Kaznex Invest website*, www.kaznexinvest.kz, accessed, 9 May 2014.

Investment enablers

Success factors for the EEU

Which are the key factors for the successful and sustainable development of the EEU?



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211). Respondents were requested to select two answers.

1 International integration

Kazakhstan is making significant progress in its effort to integrate with the global economy. The country has balanced trade and economic relations. While Kazakhstan is part of the EEU, it is also expanding its cooperation with other major trade partners, such as the European Union and China.

As it integrates into the regional economy, Kazakhstan is capitalizing on its transit potential. The country serves as an important link in the "new silk route," which connects the East to the West, allowing for the transport of goods from China to Europe through Central Asia. The construction of the Western Europe-Western China transportation corridor – a series of intercontinental highways – and of a number of large-capacity railway lines is also underway. Kazakhstan is set to become the transportation hub of Europe and Asia. In addition, as a transit route, it will gain from the increasing trade volume between the countries.

Kazakhstan has defined six priority countries for inward FDI aligned to its innovative industrial agenda: France, Germany, Japan, South Korea, the UK and the US. For example, in July 2013, Kazakhstan signed a strategic partnership agreement with the UK. The deal will boost bilateral trade and investment, and deepen economic links between the countries in sectors such as renewable energy, mining, chemicals and telecommunication. The UK also included Kazakhstan

The EEU

The EEU promises to deliver the free trade of goods, services, capital and workforce, as well as some coordination on regulatory policies. It offers Kazakhstan benefits such as access to a larger market and greater foreign investment. It is managed by the Eurasian Economic Commission (EEC), which is based in Moscow and is jointly controlled by Belarus, Kazakhstan and Russia.

Survey respondents believe that the EEU's success will depend upon how it frames policies and administrative procedures to ensure efficient regulation. It will need to come up with an unbiased policy that is beneficial for all of the participating countries. It is also important that the EEU learns from the successes and failures of other major economic blocs. Some respondents believe that the union would be more attractive if it had more member states, including Asian countries.

in its list of 14 preferred countries for activation of trade. Such cooperation treaties represent new opportunities for companies to showcase their potential on the international arena.⁵⁴

⁵⁴. "Kazakhstan signs strategic partnership agreement with Great Britain," *Tengri News website*, www.en.tengrinews.kz, accessed 25 April 2014; "Joint statement on Strategic Partnership between the United Kingdom and Kazakhstan," *The Government of the UK website*, www.gov.uk, accessed 25 April 2014.



2 A call for innovation-driven economy

The World Economic Forum notes that Kazakhstan is making the transition from an efficiency-driven to an innovation-driven economy. Innovation is expected to be an important driver of diversified economic development in Kazakhstan. The Government developed its State Program of Accelerated Industrial and Innovative Development 2010-2014 to drive economic diversification by placing a greater emphasis on knowledge-intensive and innovative industries. Within the framework of this program, Kazakhstan has managed to attract US\$14.1b of FDI into its industrial sector.⁵⁵ The program focuses on “new generation” integrated industrial economic clusters, including an integrated energy cluster, a metallurgy and machinery cluster, an agriculture and food processing cluster, and an integrated chemicals cluster.

Many of our survey respondents said that, to enhance Kazakhstan's innovation capacity, education and training in new technologies needs to be improved. They also highlighted the importance of vocational courses. The Government also recognizes these requirements and, under the Kazakhstan 2050 strategy, it has made the system for training engineers and other technical specialties a priority.⁵⁶ State-owned nuclear holding company Kazatomprom and a number of oil companies have agreed to participate in the

55. Press briefing of A. Isekeshev, Deputy Prime Minister and Minister of Industry and New Technologies, and E. Dosayev, Minister of Economy and Budget Planning, 29 April 2014, KAZNEX INVEST website, www.kazninvest.kz, accessed, 9 May 2014.
56. “Kyzyl-Orda region's oil companies to participate in vocational training colleges' establishment,” *Kazakhstan strategy 2050 website*, www.strategy2050.kz, accessed 10 March 2014.

SPAID 2015-19

State Program of Accelerated Industrial and Innovative Development (SPAID)

The new SPAID 2015-19 is expected to be rolled out in the near future. The second five-year plan is set to accelerate industrial development by building on the new opportunities created by SPAID 2010-14. The objectives of SPAID 2015-19 are to increase added value and effectiveness in the natural resources processing industries; accelerate manufacturing development; improve the business climate; establish the basis for the “sectors of the future” by creating innovation clusters and other infrastructure; attracting foreign investment; support entrepreneurship; and developing innovative SMEs.

Sources: Ministry of Industry and New Technologies of the Republic of Kazakhstan website, www.mint.gov.kz, accessed 25 March 2014; Kazakhstan industry development institute website, www.kidi.kz, accessed 25 March 2014.

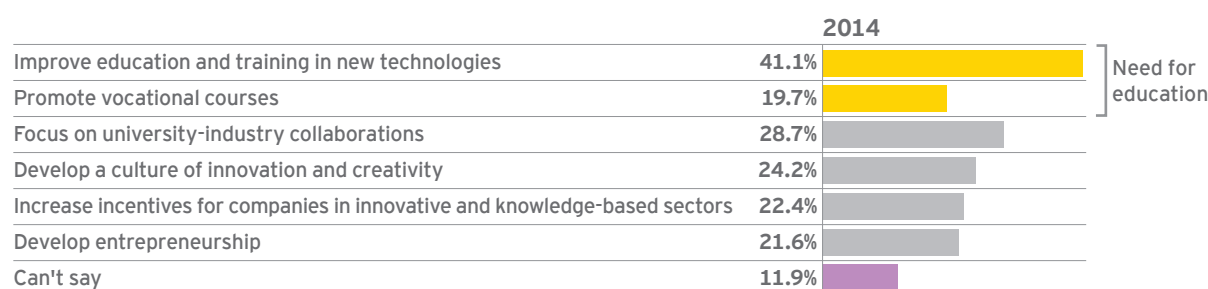
creation of vocational training colleges. In April 2013, the President of Kazakhstan announced the formation of an innovation cluster at the Nazarbayev University.⁵⁷ The university has already signed agreements with multinational companies, including HP, Microsoft and Samsung, to open high-tech research centers.⁵⁸

57. “Innovation cluster to be formed at Nazarbayev University,” *Interfax: Kazakhstan General Newswire*, 18 April 2013, via Dow Jones Factiva, ©2013 Interfax Information Services.

58. “Microsoft, Samsung and HP team with Nazarbayev University to open research centers,” *Interfax: Kazakhstan General Newswire*, 11 November 2013, via Dow Jones Factiva, ©2013 Interfax Information Services.

Improving innovation

What are the main areas of reform needed to improve Kazakhstan's innovation capacity?



Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211). Respondents were requested to select two answers.

3
Focus on green technologies:
green signals for a sustainable economy

Kazakhstan ratified the Kyoto Protocol in 2009. And, in 2010, the country initiated a program to reduce its greenhouse gas emissions by 15% from levels seen in 1992 by 2020. This set the basis for the country’s new policy initiatives that should foster “green growth,” chiefly through supporting renewable energy.

The country has set itself an ambitious target: generating 3% of its total electricity supply from renewable energy sources by 2020, and 30% by 2050.⁵⁹ Recognizing the importance of private investment for reaching these targets, Kazakhstan has passed legislation designed to create transparent and stable conditions that will facilitate capital inflow into the development of renewable energy.

In July 2013, Kazakhstan introduced changes to the Law on Support to Renewable Energy Sources, which establishes the mechanism of feed-in tariffs for “clean” energy investors.



And now, in addition to its impressive resource potential, Kazakhstan can offer investors a reliable investment-return mechanism, which should allow the country to establish itself among others that are developing renewable energy.

59. “Energy sector,” Prime Minister of Kazakhstan Karim Massimov official website, www.primeminister.kz/strategy2050, accessed 9 April 2014.

Becoming a regional leader in green energy

Overall, the new regulatory framework proposed by the Government of Kazakhstan has been welcomed as an important step toward developing the renewable energy sector. As might be expected for a new sector and regulatory environment, there are a number of open issues that require continued attention:

- ▶ Bankability issues
- ▶ Tariff levels and indexation formulae
- ▶ Institutional setup issues

In December 2013, the Renewable Energy Investment Forum, organized by the IFC with support from EY and other key stakeholders, discussed these areas in direct dialogue with Kazakhstan’s Ministry of Environment and Water Resources to provide a further set of recommendations. Our attractiveness survey suggests that investors believe more emphasis should

Ecosystem approach for developing green energy

What measures should Kazakhstan focus on for becoming one of the major regional players in green energy?

		2014
Provide incentives to entrepreneurs for investing in green energy	28.9%	
Focus on infrastructure development	28.7%	
Strengthen institutional capacity for creating renewable energy policies	23.3%	
Encourage PPP in renewable energy projects	23.2%	
Increase incentives for R&D and innovation or patent filing	23.1%	
Fund innovative energy research programs	21.7%	
Can't say	15.9%	

Source: EY's 2014 Kazakhstan attractiveness survey (total respondents: 211). Respondents were requested to select two answers.

be given to the development of a green energy framework, including incentives to invest in green energy and the creation of a supportive infrastructure. This will require strengthening institutional capacity and inviting private sector participation. The efficient production

of green energy will create employment opportunities and will benefit resource-deficient regions, such as southeastern Kazakhstan. On the demand side, both the public and private sectors need to promote energy efficiency and the culture of eco-friendly consumer behavior.

What it means for business

Businesses that are interested in investing in Kazakhstan should keep track of the following factors:

► Growth and international integration

By 2015, Kazakhstan is set to have one of the highest GDP growth rates among the 25 leading RGMs. This will provide attractive opportunities for foreign investors to serve the growing domestic and export markets. Eurasian integration of Belarus, Kazakhstan and Russia provides free access to 170 million consumers. At the same time, Kazakhstan has strong relations with other key trade partners, such as China and the European Union. Kazakhstan's position on the "new silk route" is also critical to its growth story. Because the country can serve as a bridge between Asia and Europe, it could become a transit point for regional exports. However, exporters need to assess the processes involved. Companies also need to plan for contingencies, including currency fluctuations and rapidly changing oil prices.

► Diversification

The current diversification drive requires investment from private players in industrial and infrastructure industries. These include heavy machinery, automotive, construction materials, chemicals and food processing. The state encourages foreign investors with knowledge, expertise and technologies to launch projects.

► Expanding the green energy sector

Green energy is likely to be one of the sectors driving FDI and the local economy, enabling the creation of high-tech jobs, innovation and cooperation between the public and private sectors. Kazakhstan is targeting a 30% share from alternative sources in its total energy mix by 2050. Strong international players in green energy need to get involved if the country is to capitalize on its vast potential in wind, hydro and solar energy.

► Increased awareness

Both established and non-established investors are showing greater awareness of Kazakhstan's potential. This suggests that more businesses will look to enter or expand in the country, which will increase competition in the market. We believe the way forward for investors may be to base their business models on strong local partnerships and consider the consumer base not only in Kazakhstan, but also in the EEU and Central Asian countries.

► Improving business conditions

Conditions for doing business are getting better in Kazakhstan, but challenges remain. Prudent macroeconomic policies are in place to encourage investment, but investors still experience inconsistencies in the application of the law, and inspections that are frequent and burdensome. Foreign investors that plan to bring their own staff into Kazakhstan have to take account of the country's work permit system, which can be time-consuming.

► Shortage of a skilled labor force

Investors often share concerns about the shortage of managerial talent and skilled personnel in the country. While the authorities have been taking steps to address this issue, progress will take time. Because of this, businesses should look to develop their own talent by setting up in-house training centers. They can also partner with the state to open up vocational centers for students in their industries. High-tech, telecommunication and business services companies are particularly affected by this skills shortage, because of the high demand for skilled personnel in their industries.

► Incentives and regulations

Business leaders should be on the lookout for sector-specific incentives in the 10 dedicated SEZs across the country. These incentives are dynamic – they can change with new policies or amendments. Companies need to be aware of any policy changes that affect their industries. State control in certain sectors, such as the extractive industries, is quite high. Businesses must build and maintain strong working relationships with the Government to ensure efficient operations.

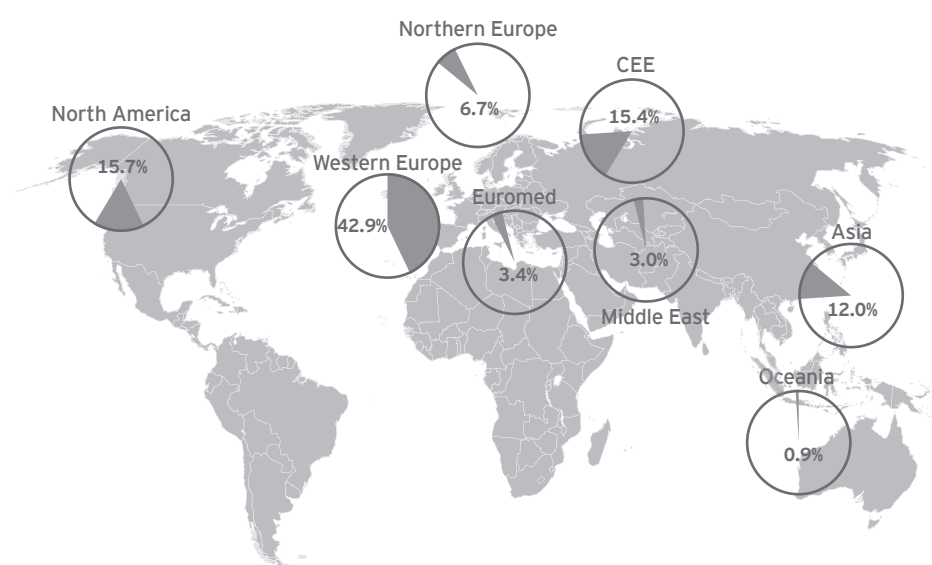
Methodology

EY's 2014 Kazakhstan attractiveness survey reflects the perceived attractiveness of Kazakhstan for foreign investors. We define the attractiveness of a location as a combination of the country's image, investors' confidence and their perception of the country's ability to provide the most competitive benefits for FDI. Our field

research was conducted by the CSA Institute and EY via telephone interviews, one-on-one meetings and an online survey. Overall, 211 international business leaders from 28 countries were interviewed between January and February 2014.

Profile of companies surveyed

Geography



Western Europe includes UK, Germany, France, Netherlands, Italy, Switzerland, Austria, Belgium and Spain. **North America** includes the USA and Canada. **CEE** includes Russia, Ukraine, Czech Republic, Poland and Lithuania. **Asia** includes India, Japan, Korea, China and Singapore; **Northern Europe** includes Sweden, Denmark and Norway. **Euromed** includes Turkey. **Middle East** includes UAE. **Oceania** includes Australia.

Size (sales turnover)



32.1%
More than US\$2b

18.6%
From US\$501m-2b

24.6%
From US\$201m-\$500m

24.7%
Less than US\$200m

Job title



27%
Financial director

26%
Director of development or sales and marketing director

12%
Chairman, President or CEO

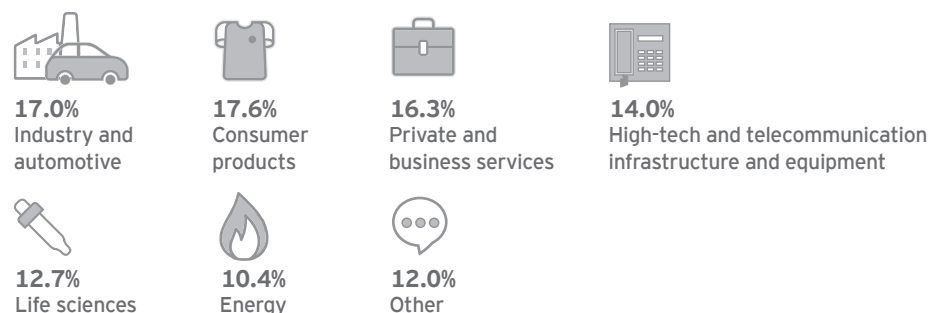
11%
Managing director, senior vice president or COO

9%
Director of investments or director of strategy

7%
Manager for investor relations, international affairs or communications

8%
Other

Sector of activity



Consumer products includes consumer products and retail. **Industry and automotive** includes heavy industry; automotive; infrastructure (roads and highways and ports); real estate and construction; transport industry; ceramic industry; paper and packaging industry; and logistics. **Private and business services** includes financial services; business services; media and entertainment; and hotels and tourism. **High-tech and telecommunication infrastructure and equipment** includes electronic and electrical equipment; aerospace and defense; software and IT services; telecommunication; information and telecommunication. **Life sciences** includes chemicals and allied products; pharmaceutical and manufacturing of medical equipment (life sciences); and health care. **Energy** includes oil and gas; power and utilities; alternative and renewable energy and cleantech. **Other** includes mining and metals; education; engineering; agriculture; manufacturing; and private equity.



EY in Kazakhstan



In 1992, EY was the first professional services organization to open an office in Kazakhstan. Our member firm in Kazakhstan is part of our EMEIA practice, encompassing Europe, the Middle East, India and Africa. EY has three offices in Kazakhstan: in Astana, Almaty and Atyrau.

Commitment to employee development

Ninety-seven percent of our employees in the country are Kazakh citizens. EY has established an effective professional training system that is not only supported by EY's practice in Kazakhstan, but also by its offices worldwide. Each of EY's four service lines – Advisory, Assurance, Tax and Transactions – supports milestone learning programs and more than 10 international qualifications programs.

EY supports hiring young specialists and providing training, professional development and career growth opportunities. Each year, we employ around 100 students and provide them with training and international professional qualifications. We also bring students into the job market by hiring around 40 interns annually.

Supporting entrepreneurship

We launched Entrepreneur Of The Year™ (EOY) in Kazakhstan in 2007. EOY is an EY program that runs in 60 countries around the world to recognize and honor the outstanding achievements of entrepreneurs in developing local and global economies. Since its inception, the Kazakhstan program recognized about 60 finalists, representing diverse industry sectors and regions. The national winners represent Kazakhstan at the annual World Entrepreneur Of The Year™ awards in Monte Carlo.

Encouraging investment

EY is committed to enhancing the business and investment environment in Kazakhstan. We organize a variety of professional events and knowledge-sharing sessions in order to promote international best practices and industry expertise, as well as to advise the investment community on the most recent or anticipated changes to the regulatory environment.

EY is involved in the work of the Foreign Investors' Council, chaired by the President of the Republic of Kazakhstan, and co-chairs its working group on investment policy. EY is also actively involved in a number of business, professional and industrial associations in Kazakhstan.

Supporting our clients in the dynamic landscape

At EY, we know that businesses in emerging markets need innovative thinking and practical advice in order to succeed. We support our clients by facilitating their sustainable development strategy and creating new growth opportunities in today's dynamic economic environment.

EY's major services:

- Assurance
- Tax and Law
- Transactions
- Advisory
- Academy of Business



Publications

Doing business in Kazakhstan 2014



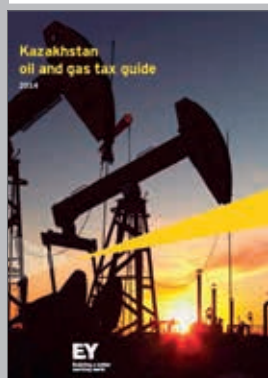
This practical guide provides advice on the legal and tax issues that investors face when they are building businesses in Kazakhstan. It helps investors to plan so that they can avoid common pitfalls.

EY Rapid-Growth Markets Forecast – February 2014



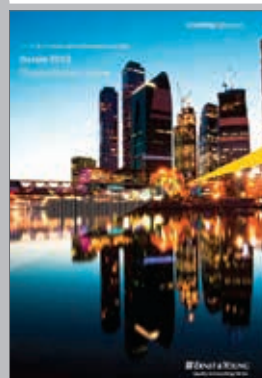
Explore trends, opportunities and the latest market conditions in the world's fastest-growing economies. Read the latest *EY Rapid-Growth Markets forecast* and find out how surging middle classes in rapid-growth markets are changing the global economy and offering more opportunities to business around the world.

Kazakhstan oil and gas tax guide 2014



The oil and gas industry plays an important role in the economy of Kazakhstan. The guide provides useful information on the taxation in the industry.

2013 Russia attractiveness survey: shaping Russia's future



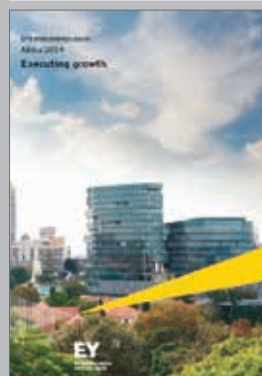
Russia's growing consumer market, rising disposable income, expanding middle class, vast resource reserves and highly skilled workforce continue to attract investors from all corners of the world. Our respondents rank it as the sixth most attractive country in the world for FDI. Find out more in our *2013 Russia attractiveness survey*, which combines an analysis of FDI in the country with a survey of over 200 international business leaders.

Kazakhstan Compensation and Benefits Survey 2013/14



This publication contains information on pay levels across 14 Kazakhstan regions and the cities of Astana and Almaty. It also includes details on pay for performance, benefits package structures, allowances and other compensation. In addition, industry-specific reports cover oil and gas, mining, financial services and consumer products sectors.

2014 Africa attractiveness survey: executing growth



Despite a decline in the number of new FDI projects into Africa in 2013, largely caused by a significant decline in North Africa, the continent's share of global FDI projects reached the highest level in a decade, with the number of new projects in sub-Saharan Africa continuing to grow. Africa's perceived attractiveness relative to other regions has also exhibited remarkable progress, moving to second place, up from eighth, only four years ago, showcasing how the image of Africa has begun to change. Go beyond the headlines in *EY's 2014 Africa attractiveness survey*.





About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

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