



Kazakhstan's economy expanded by 4.2% in 1H17, supported by growth in mining, manufacturing, construction and transportation sectors

Review of 1H17 GDP growth

Kazakhstan's economy maintained its strong growth momentum in the first six months of 2017, with 1H17 GDP growth of 4.2%. Mining, manufacturing, construction and transportation have been the largest growth contributors, while overall industrial production rose by 7.8%, with the growth rate remaining at the same level as in 5M17. Meanwhile, the short-term economic indicator, which is a gauge for change in production indices of basic industries, increased by 5.8% YoY over the same period.

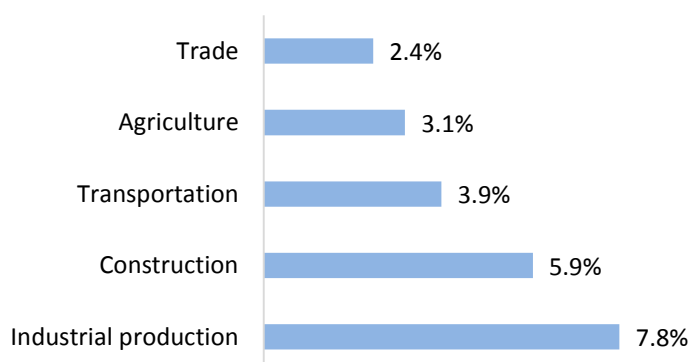
In particular, the mining sector grew by 9.4% YoY, attributable to the rise in coal and lignite (16.5%), non-ferrous metal ores (11.9%), natural gas (10.5%) and oil production (9.7%), while iron ore and other mining output demonstrated 8.5% and 7.8% growth respectively.

The manufacturing sector maintained a growth rate of 6.5% in 1H17, with pharmaceuticals (34.6%), light industry (15.4%) and ferrous metals production (9.1%) being the major contributors to this output increase. Meanwhile, production of coke and petroleum products and non-ferrous metals rose by 7.2% and 7.3% respectively. Machinery output growth stood at 3.8% in 1H17, compared to 4.1% in 5M17, driven by increase in other vehicle manufacturing (33.6%), electronics (28.9%), and car manufacturing (20.1%). However, manufacturing sector was undermined by decrease in tobacco (-21.9%) and moderate rates of growth in chemicals (1.1%), clothing (1.4%) and rubber and plastics (1.8%).

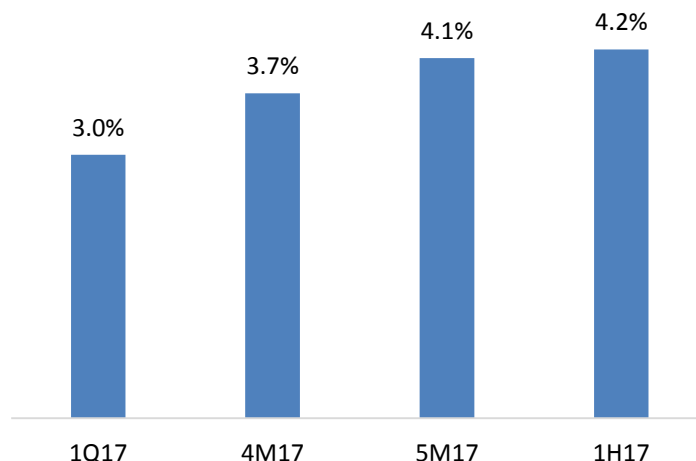
Over 1H17, agriculture output amounted to KZT887.5bln, growing by 3.1% YoY. Crops production gained 2.2% while livestock growth rate stood at 3.1% over the same period. Agriculture-related services sub-sector remained relatively unchanged.

The services sector demonstrated moderate performance, with information & communication and trade growing by 2.5% and 2.4% respectively. Retail trade increased by 5.9%, while the growth of wholesale trade moderated to 0.6% YoY in 1H17 from 0.7%, recorded in 5M17.

YoY growth by sectors, % (1H17)



GDP growth, YoY % (1Q17-1H17)



Source: Ministry of National Economy, Samruk-Kazyna

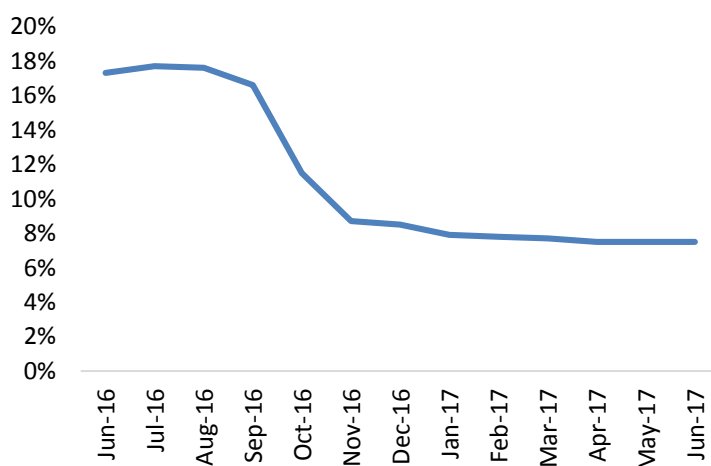
Construction sector expanded by 5.9% in 1H17, supported by the implementation of Nurly Zhol and Nurly Zher state infrastructure projects. Concurrently, transportation industry recorded a growth rate of 3.9%, while passenger and freight turnover rose by 3.1% and 6.9% respectively.

Over 1H17, oil production growth accelerated to 9.7%, compared to 5M17 growth of 9.5%. The increase in crude production was supported by rising output from the Kashagan oil field and decreased volatility of oil prices. Meanwhile, natural gas output rose by 10.5%. Electricity, gas steam and air conditioning gained 5.1% while electricity production alone rose by 5.7%, partially attributable to industrial production growth.

Inflation environment

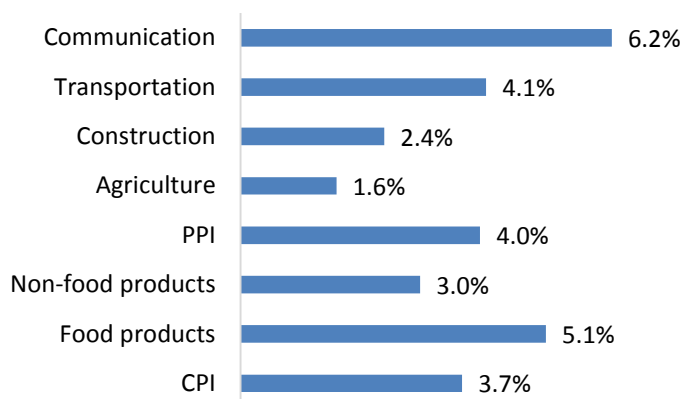
On inflation front, CPI rose by 3.7% in 1H17, compared to 4.6% increase year earlier. On annual basis, YoY CPI growth remained at a moderate 7.5% level, within the official target range of 6.0%-8.0%. Construction prices gained 4.2% while producer prices rose by 9.6%, compared to 15.3% YoY growth in May. Meanwhile, freight transportation and communication tariffs rose by 4.9% and 3.5% respectively.

Inflation rate, % YoY (June 2016 – June 2017)



Source: Ministry of National Economy, Samruk-Kazyna

Inflation rate across categories, % (1H17)



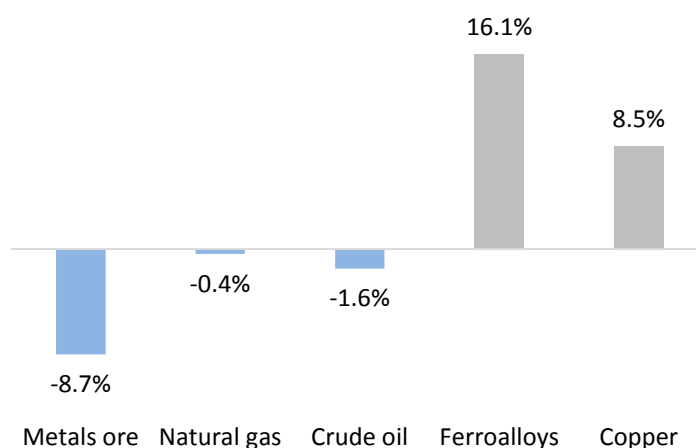
Source: Ministry of National Economy, Samruk-Kazyna

Over 1H17, food product prices increased by 5.1%, while non-food products and services recorded growth of 3% and 2.8% respectively. In particular, prices rose for potatoes (77.3%), fresh vegetables (15.6%), mutton (10.7%), beef (9%), butter (5.6%), fresh fruit (7.9%) and canned milk (6.4%). Meanwhile, cucumbers (-58.7%), tomatoes (-28.7%), eggs (-27%) and sunflower oil (-6.6%) registered decline in prices.

On non-food product front, car prices increased by 4.7%, while prices of glass and ceramics, pharmaceutical products and personal goods rose by 4.6%, 2.8% and 2.9% respectively. Gasoline prices grew by 5.4% while diesel fuel gained 6.6%. Meanwhile, prices for legal services increased by 7%, with vehicle insurance, healthcare, and entertainment rising by 6.8%, 4.8% and 2.6% respectively. Intercity bus (4%) and air transportation (2.4%) demonstrated a moderate growth in prices while rail transportation tariffs declined by 1.4%. Electricity tariffs rose by 3.2% while gas prices gained 4.2%, remaining relatively unchanged from the previous month.

On producer prices front, over 1H17, mining sector prices gained 4.2%, compared to 6.3% growth in 5M17. Meanwhile, manufacturing sector tariffs increased by 3.9%, accelerating from 5M17 reading of 2%. In June, metals ores (-8.7%), crude oil (-1.6%), natural gas (-0.4%) and gasoline (-0.4%) demonstrated moderate decline in prices, while ferroalloys and copper producer prices gained 16.1% and 8.5% respectively.

Producer prices growth composition, % (June 2017)

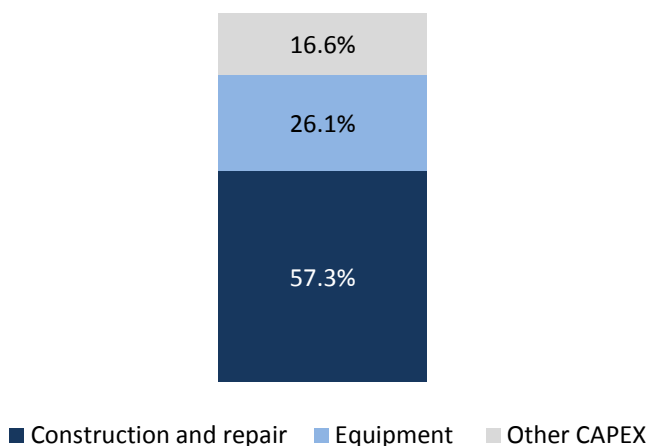


Source: Ministry of National Economy, Samruk-Kazyna

Fixed asset investments continue positive growth momentum

Over 1H17, fixed asset investments rose by 3.7% YoY, reaching KZT3,284bln and compared to 5.2% increase in 5M17. Construction and repair represented 57.3% of overall investments, while acquisition of equipment and other capital expenditures constituted 26.1% and 16.6% respectively.

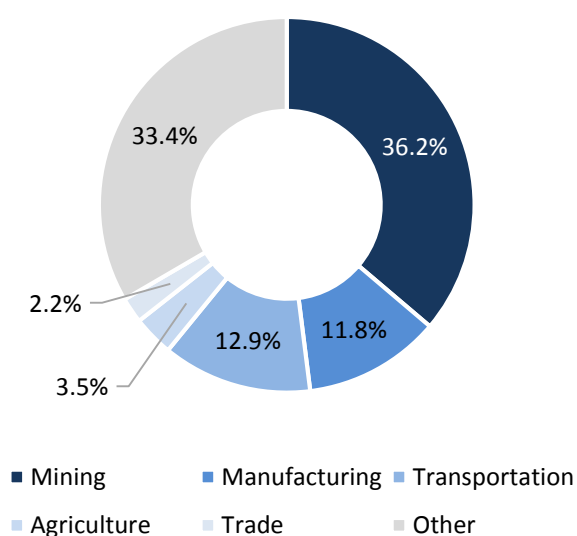
Fixed asset investments composition (1H17)



Source: Ministry of National Economy, Samruk-Kazyna

Private sector's funds accounted for 69.2% of total fixed asset investments, providing approximately KZT2,274bln in financing. Meanwhile, commercial bank loans and state funding contributed another 8.2% and 13.2% respectively. Other funding sources represented 9.4%.

Main recipients of fixed asset investments (1H17)



Source: Ministry of National Economy, Samruk-Kazyna

Sectorial composition indicates that mining (36.2%), manufacturing (11.8%) and transportation (12.9%) have been the largest investment recipients, with agriculture and trade representing only 3.5% and 2.2% respectively.

Regional growth review

Russia

Russia's economic growth momentum started to accelerate as higher oil prices this year supported consumer confidence and reduced fiscal pressure. For 2Q17, Russia's GDP growth is estimated at 1.1%, accelerating from 0.5% YoY growth observed in 1Q17. Inflation is close to the central bank's target of 4%, allowing the regulator to continue its accommodative monetary policy, which is expected to further boost consumption and aggregate demand. Following 0.2% contraction in 2016, full year GDP growth is forecasted at 1.3%-1.8% in 2017, implying average Urals oil price of USD50pb. Meanwhile, Russia's unemployment rate declined to 5.2% in May, the lowest jobless rate since September 2016.

Macroeconomic indicators of Kazakhstan's main partners

Indicator	Eurozone	Russia	China	Kazakhstan
Unemployment rate, May 17	9.3%	5.2%	3.97%	4.8%
Inflation, June 17, YoY	1.3%	4.4%	1.5%	7.5%
Benchmark interest rate	0%	9%	4.35%	10.5%
PMI Manufacturing	57.4	50.3	50.4	N/A
PMI Services	55.4	55.5	51.6	N/A

Source: Bloomberg, Samruk-Kazyna

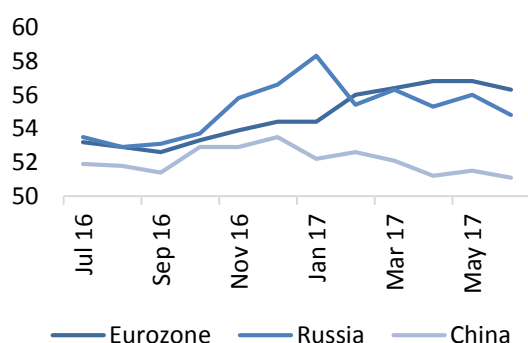
China

China's economy expanded by 6.9% YoY in 2Q17, outperforming median expectations of 6.8% and in line with 1Q17 growth. For 2017, official GDP growth is expected at 6.5%, slightly lower than last year's 6.7%, which was the weakest pace in 26 years. Market players anticipate that the world's second-largest economy will experience a decelerating momentum in 2H17, partially attributable to restrictive fiscal policy and deleveraging. Meanwhile, the country's manufacturing PMI unexpectedly rose to 50.4 in June, compared to 49.6 in May, while services PMI declined to 51.6 in June vs. 52.9 in May. On external trade front, exports and imports grew by 11.3% YoY and 17.2% YoY respectively.

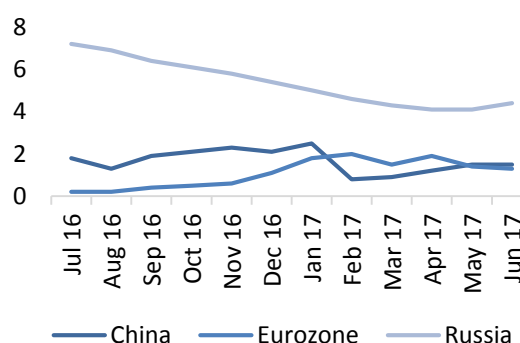
Eurozone

Preliminary estimates indicated that Eurozone is benefiting from rising growth momentum. The region's 2Q17 average composite PMI stood at 56.6, compared to 55.6 recorded in the previous quarter. For 2Q17, Eurozone's GDP growth is anticipated at 1.8% YoY, driven by accommodative monetary policy and improved business confidence. Meanwhile, CPI in the Euro Area increased by 1.3% YoY in June of 2017, easing slightly from 1.4% in May and marking the lowest inflation rate so far this year, mainly due to a decrease in energy prices, while unemployment rate stood at 9.3% in May, providing additional monetary policy flexibility to ECB.

Composite PMI



CPI, % YoY



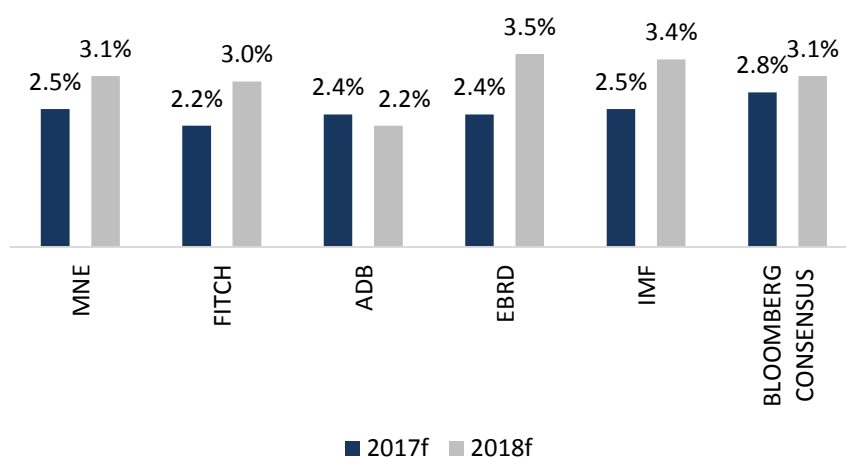
Source: Bloomberg, Samruk-Kazyna

Market expectations indicate continuation of positive growth dynamics in 2017

The USD-KZT exchange rate averaged at 318.67 in 1H17, compared to 318.62 average exchange rate in 5M17. As at end-June 2017, the average exchange rate stood at 318.91, stronger than 330.85 in January 2017. However, compared to the previous month (313.44), USD-KZT exchange rate rose by 1.7%, reflecting recent short-term correction in oil prices. **For 2017, we expect USD-KZT exchange rate to average at 330** (2016: 342.2 average), driven by accelerating GDP growth and higher global oil prices.

On monetary policy front, over the last two weeks of June, overnight repo rates (TONIA) were stable, fluctuating in the range of 9.49-9.62%, near the lower band of the base rate corridor. Meanwhile, overnight swap rates and 2-day swap rates were steady at 9%, after sliding down from 9.5% on 5 June. Trading volumes in overnight swaps were mostly low, remaining in the range of USD0.2 – 93.8mln with a spike of USD1,726mln on 29 June, indicating the increase in demand for FX currency, while trading volumes in 2-day swaps were high, fluctuating in the range of USD1,456-1,581mln. The volume of liquidity withdrawn by NBK stood at KZT2.4tln, including other operations (currency interest rate swap with banks, loans to banks), and at KZT3.7tln, excluding other operations as of 29 June, while the amount of loans provided by NBK to banks stood at KZT800bln on 31 May, with some banks continuing to experience liquidity shortage on the back of customer deposits outflows in the recent months. NBK is finalizing the revision of its program aimed at providing subordinated loans to banks, which is expected to strengthen banks' balance sheets, with the funds being distributed to banks that are of major importance to the industry and with more than KZT45bln in capital. However, shareholders will be required to inject more capital based on a set timetable.

GDP forecasts (2017f-2018f)



Source: Ministry of National Economy, Bloomberg, Samruk-Kazyna

The strong growth momentum observed in 1H17 is expected to continue into the second half. Consequently, Kazakhstan's GDP growth is on track to meet **our in-house conservative target of 2.5%-2.6% for 2017**, reflecting our expectations of **USD50-52pb average Brent crude oil price**, increase in oil production, continuous fiscal pump priming (Nurly Zhol) as well as improved economic performance in key trading partners. China's investments under the One Belt & One Road program will also lead to steady improvement in infrastructure and cross border connectivity, boosting economic activity in Kazakhstan. Nonetheless, we will continue to monitor closely economic developments on the regional and global fronts with uncertainties emanating from the US economic and monetary policies as well as from economic performance of key trade partners.

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