

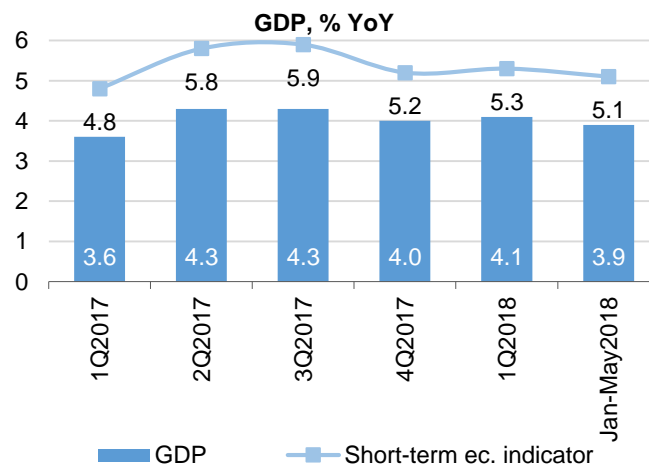
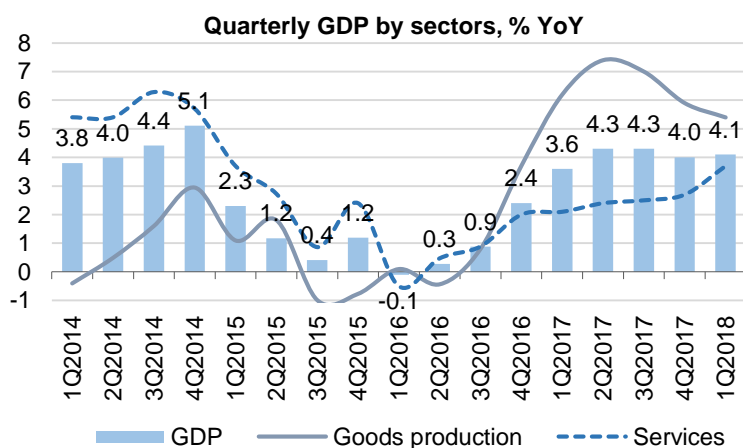
Macroeconomic updates – GDP growth

Key highlights:

- Economic growth moderated marginally in Jan-May to 3.9% YoY vs 4.1% YoY in the first quarter.
- There was stronger growth in the trade sector (+5.8% YoY), while the slowest being the construction sector (+0.3% YoY).
- Investment activity touched two digits at 30% on average in the first five months of the year.
- Employment slipped by 0.8% YoY in May, the biggest decline in two years.
- Real wages were down by 0.9% YoY in May.
- Compared to the end of 1Q18, tenge weakened by 2% against USD, but strengthened by 6.6% vs. ruble as at end-May.
- NBK once again cut the base rate at the beginning of June, but sees limit to further rate cuts this year, due to increasing inflation expectations.

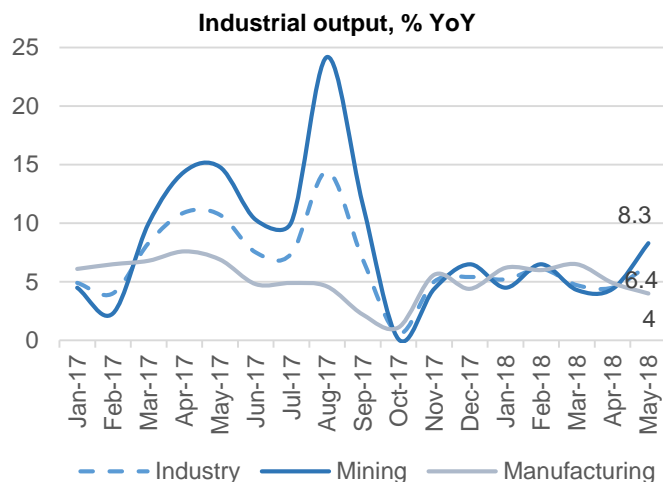
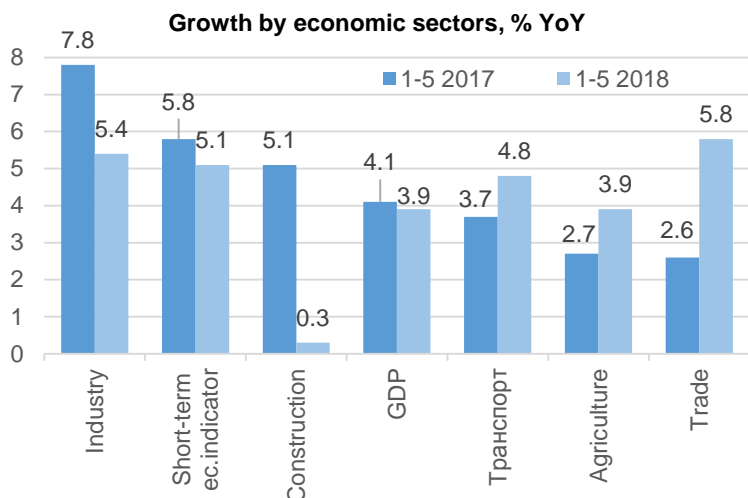
After rising by 4.1% in the first quarter of 2018, the economy moderated slightly to 3.8% YoY in January-April and 3.9% YoY in the first five months. Short-term economic indicator (covering 60% of GDP) also slowed to 5.1% YoY in January-May compared with 5.3% YoY in the first quarter of this year.

Growth in the first five months of the year was driven by broad-based expansion across economic sectors, with the exception of the construction industry. The weak dynamics in construction industry was due to high base in the first half of last year when growth was underpinned by the construction of EXPO 2017 projects. Nevertheless, positive dynamics were observed in the housing construction segment, which grew by 30% YoY, boosted by "Nurly Zhol" and "Nurly Zher" programs. Under the "Nurly Zhol" program, KZT475bln of spending was allocated in the current year State budget, and KZT8bln for the "Nurly Zher" program with a significant increase in expenditure in relation to the April amendments to the State budget and commissioning of "7-20-25" mortgage program.



Among economic sectors, the highest growth was recorded in trade at 5.8% YoY in January-May. The main contribution to the growth of trade was wholesale trade, which grew by 6.2% YoY due to the growth of oil products trade.

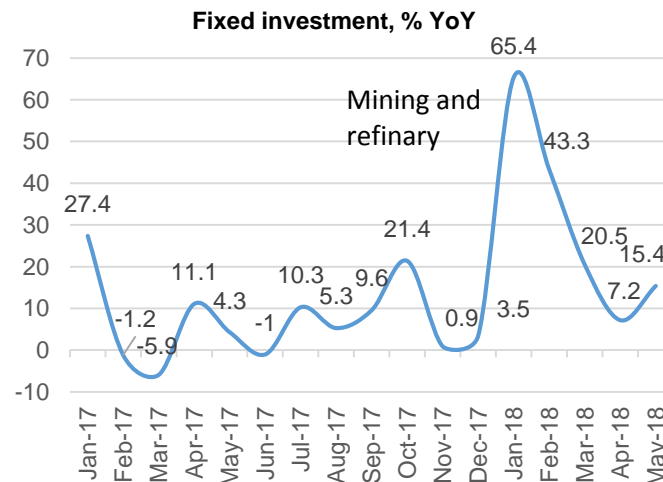
Meanwhile, industrial sector expanded by 5.4% YoY, where the mining industry showed a growth rate of 5.6% YoY. Oil production increased by 6.4% YoY and mining of metal ores rose by 3.6% YoY. The manufacturing industry increased by 5.5% YoY, with a 4.3% YoY growth in oil refining, 4% YoY growth in metallurgy, and other smaller industries such as engineering, food, engineering showing stronger growth.



Source: Statistics Committee, Ministry of National Economy, Samruk-Kazyna

Employment growth slowed in April and fell by 0.8% YoY in May. Wages in the first quarter of 2018 increased by 2% YoY in real terms, but decreased by 0.9% YoY, by our assessment in May. In contrast, retail trade turnover showed healthy growth close to 6% YoY.

Investments witnessed double-digit growth rate of 25.3% YoY in the first five months of the year. The main increase was associated with the expansion of investment in increasing oil production capacity at Tengiz and the modernization of the oil refinery in the South of the country. Robust growth rates were also observed in the investment for transport (+36.1% YoY) and real estate (+41.4% YoY) sectors in the first five months of 2018.

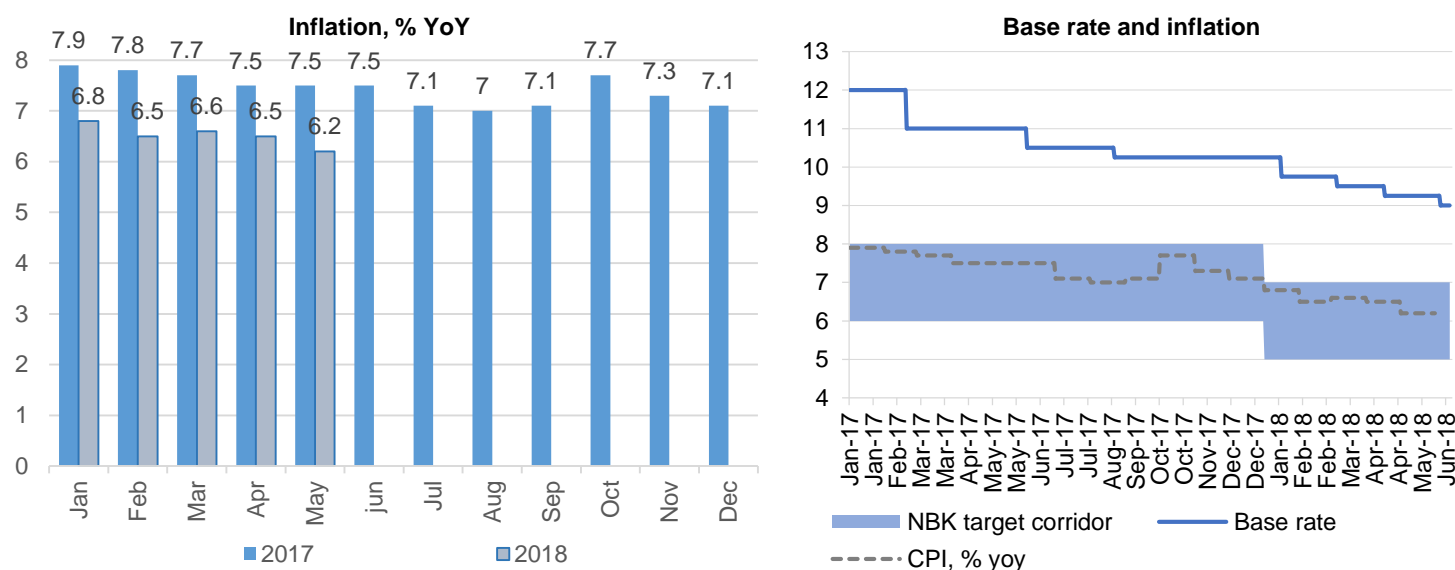


Source: Statistics Committee, Ministry of National Economy, Samruk-Kazyna

On inflation, it slowed significantly in May, amounted to 0.2% mom compared to 0.4% mom in April and 0.6% mom on average in the first quarter. Annual inflation slowed sharply to 6.2% YoY in May, compared with 7.1% YoY as at end-2017 and 6.6% as at end-1Q18.

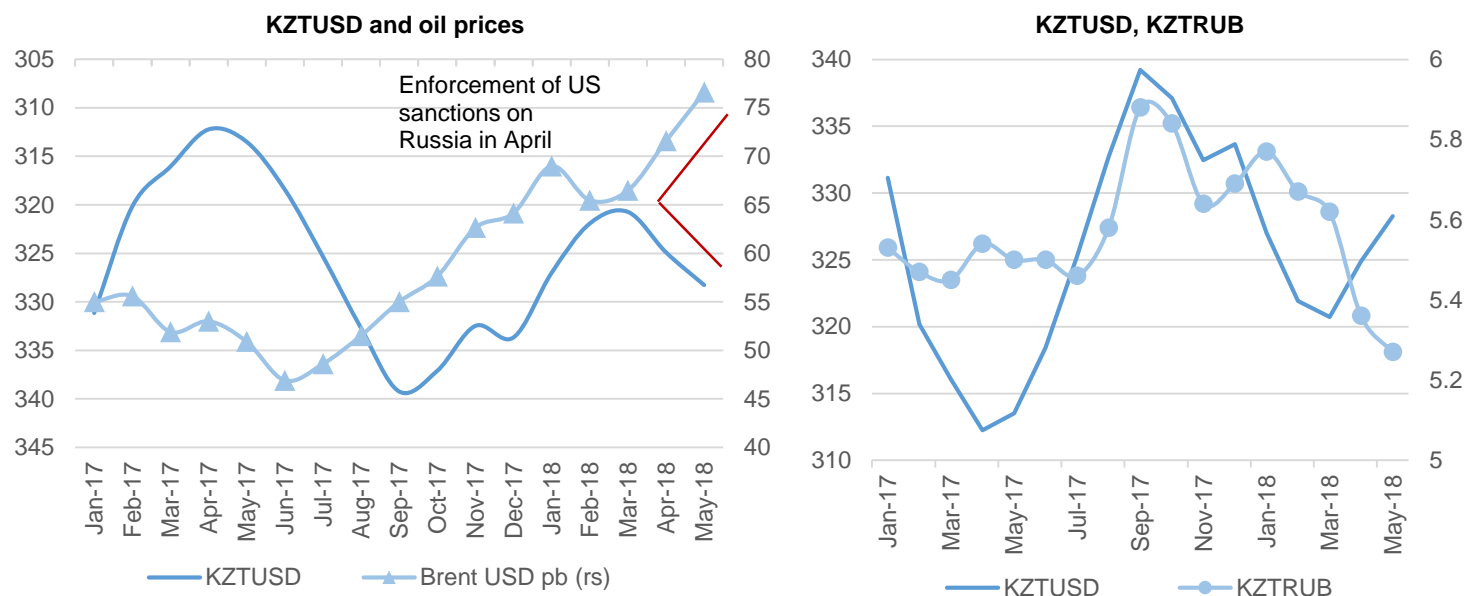
In a recent published report of the NBK, inflation expectations have increased slightly, however, the projected rate of inflation is anticipated to remain within the target corridor of 5-7%, while medium-term inflation target is unchanged at 4% by 2020. The risks to higher inflationary pressures may come from a rise in motor fuel prices, volatility in FX market and strengthened inflation expectations of the population.

In view of moderating actual inflation and positive growth dynamics, NBK decided to cut the base rate by 0.25pp to 9% in early June, with the preservation of corridor +/-1%. At the same time, the regulator highlighted that further potential reduction to the base rate in the current year is limited as there is some rise in inflation expectations. Since the beginning of last year, the base rate was cut by 3pp in total i.e. 1.75pp in 2017 and 1.25pp this year. Assuming that inflation maintains at the current level for the remaining of 2018, the base rate could potentially be reduced by a further 0.25pp due to the need to stimulate economic activity.



Source: Statistics Committee, Ministry of National Economy, Samruk-Kazyna

As the US sanctions on Russia were enforced in early April, there was a break in correlation of the tenge with US dollar and oil price. Starting March, the average price of Brent oil rose by 15% to USD77pb, while the national currency weakened against USD by 2% and the USDRUB exchange rate dropped more significantly by 8%. At the same time, tenge gained 6.6% against the ruble from 5.6 to 5.3 per ruble. It should be noted that in addition to US sanctions against Russia, emerging markets currencies have weakened since the beginning of this year due to consistent rise in the US key interest rate, making the US dollar more attractive relative to other currencies.



Source: Statistics Committee, Ministry of National Economy, Samruk-Kazyna

The official forecast for GDP growth is at 3.8% for 2018, with upside potential according to our view. This is because the annual growth of oil production in the first five months of the year has already exceeded 6%, way above the Ministry of National Economy's forecast of 1%. Combined with higher oil prices on average for the year, we think GDP growth this year could potentially be higher than 4.0%.

At this time, the risks to the economic growth may pose the construction sector and agriculture, but since these sectors account for only 10% of the overall GDP, the risks are marginal.

The overall positive growth dynamics should result in positive impact on the labor market and growth in wages that are currently lagging behind the improvement observed in the domestic economy.

Key Macroeconomic Indicators

Key Indicators	2013	2014	2015	2016	2017	2018f
GDP, USD bln	236.6	221.4	184.4	137.3	159.4	168.3
GDP, % YoY	6.0	4.2	1.2	1.1	4.0	3.8
Industrial output, % YoY	2.5	0.3	-1.6	-1.1	7.1	3.3
Retail trade, % YoY	16.0	7.9	-2.5	2.0	6.3	3.9*
Inflation, % YoY	4.8	7.4	13.6	8.5	7.1	5-7
Current account, % of GDP	0.5	2.8	-2.8	-6.5	-3.4	-2.2
State budget deficit, % of GDP	-1.9	-2.7	-2.2	-1.6	-2.8	-1.5
Brent, USD per barrel	108.9	98.9	52.4	44.0	54.4	65.0
KZTUSD year average	152.1	179.2	221.7	342.2	326.0	325.0

*including wholesale Source: Statistics Committee, Ministry of National Economy, Samruk-Kazyna

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