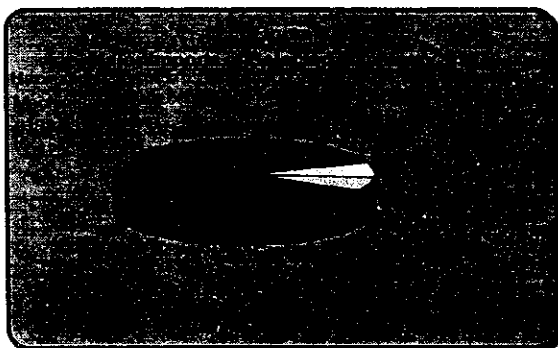

PART III INVESTMENT OPPORTUNITIES

A. Overview of the Industry

The growth of Kazakhstan's machinery and equipment output has generally followed that of overall industrial production. In the short run, however, changes in the level of production have differed from those of industrial output because of supply adjustments to support programs, production disturbances associated with interruptions of utility services, and shipment delays of raw material and intermediate inputs. At present, Kazakhstan's capacity to fulfill its machinery needs is limited, with local manufacturers supplying only about 15 percent of domestic requirements.

In agriculture, equipment inventory has also suffered. The number of operational tractors has declined dramatically, as has the number of harvesting combines and seeders. Given that excessive investments in equipment and machinery were typical for a command economy, the decline in numbers has been tolerable until recently. Machines have been broken up to provide spare parts, but this process is approaching a saturation level and there is an immediate need for new tractors and harvesting combines, as well as replacement parts.

Because of these conditions, end users have had to rely on foreign supplies of machinery and equipment. The leading imports are (i) harvesting or threshing machinery, (ii) pumps for liquids, (iii) machinery, plant or laboratory equipment for the treatment of materials by a process involving a change of temperature such as heating, cooking, roasting, distilling, rectifying, sterilizing, pasteurizing or steaming, (iv) parts suitable for use solely or principally with the machinery; and (v) parts of railway or tramway locomotives or rolling-stock. In contrast, exports are concentration on a much narrow group of products made up of tractors, ball or roller bearings, electric accumulators, and harvesting or thrashing machines.



Kazakhstan's trading partners are largely the CIS countries. The duty-free access offered by members of these preferential trade arrangements, and the importance of these partners to Kazakhstan, mean that about two-thirds of imports enter the country under preferential arrangements, with

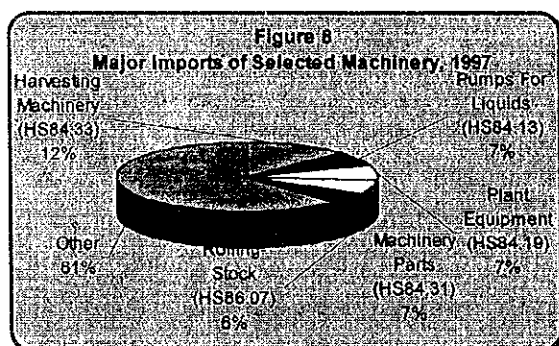
PART III INVESTMENT OPPORTUNITIES

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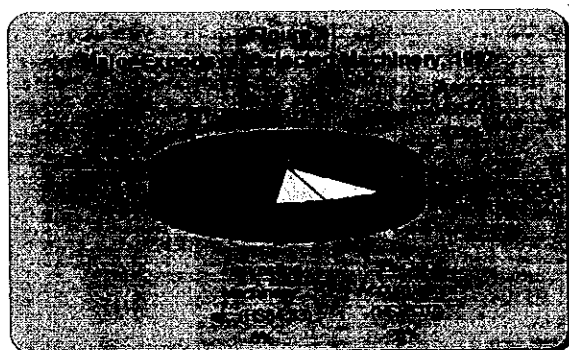
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nearly three-fourths of those imports originating from Russia. Similarly, one-half of Kazakhstan's exports are directed to markets that offer duty-free access, especially Russia, which absorbs about 40 percent of those exports. This pattern of trade has important implications for Kazakhstan as a member of the World Trade Organization (WTO). Since preferential trade accounts for a large share of the

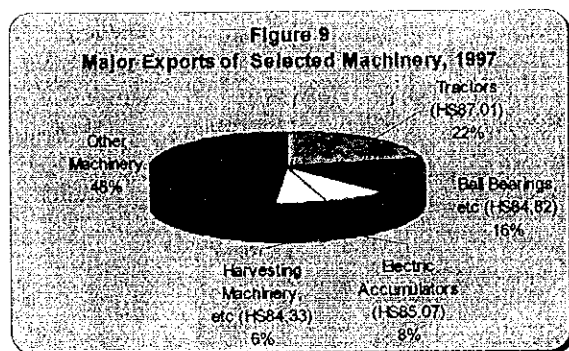
country's overall trade, much of the gains from trade will derive from redirecting trade patterns from less efficient to more efficient markets.

Kazakhstan belongs to the customs union formed between the Russian Federation and Belarus. After forming the customs union, Kazakhstan imposed high import tariffs on many goods at the urging of Russia, which wants protection for its heavy machinery and equipment sold in Kazakhstan. In addition to creating a common customs tariff, the members of the customs union intend to harmonize their legislation affecting foreign trade. Kazakhstan also has bilateral free trade agreements with Kyrgyzstan, Lithuania, Moldova, the Russian Federation, Ukraine, and Tadjikistan. A multilateral free trade agreement was also signed among Kazakhstan, Kyrgyzstan, and Uzbekistan establishing a unified economic area, and a multilateral agreement on the creation of a free trade area among all CIS countries has been signed. All of these agreements stipulate free trade based on exemptions from duties for all kinds of goods and services.

Table 6
Major Products of Machinery Industry-Related Activities

Sector	Major Products
Machine Building	Electromechanical machinery, machine tools, instruments, tractors, agricultural machinery and bulldozers.
Non-Ferrous Metallurgy	Bauxite, refined copper, lead, titanium and zinc.
Ferrous Metallurgy	Iron ore, manganese, chromate, cast iron, steel, rolled products of ferrous metals, sheet iron, tin and coke.
Food Industry	Processed meat, milk products, and confectioneries.
Agriculture	Barley, corn, cotton, eggs, fruit, meat, milk, millet, oat, oilseeds, potatoes, rice, rye, sugar beet, tobacco, vegetables, wheat, wool, cattle, sheep and goats, and pigs.
Light Industry	Fabric, knitted products, and footwear.
Wood Processing, pulp and paper	Timber, paper, lumber and cardboard.
Transport	Rail, maritime, internal waterways, air, road transport of passengers and freight.

Source: Ministry of Energy, Industry and Trade.



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Source: Ministry of Energy, Industry and Trade.

Table 7 Machinery Trade, 1997 (Quarters I-III) (thousands of US dollars)				
HS Code		Exports	Imports	Balance
84	Mechanical Appliances and Machinery, Nuclear Reactors and Boilers			
	<i>All Products</i>	86,031	688,229	-602,198
	<i>Products Covered by Master Plan</i>	84,049	348,329	-264,280
85	Electrical Machinery and Equipment			
	<i>All Products</i>	36,931	105,767	-68,836
	<i>Products Covered by Master Plan</i>	21,682	74,578	-52,897
86	Railway Locomotives, Rolling-Stock and Parts			
	<i>All Products</i>	3,368	453	2,915
	<i>Products Covered by Master Plan</i>	4,268	5,775	-1,507
87.01	Tractors			
	<i>All Products</i>	30,665	3,564	27,101
	<i>Products Covered by Master Plan</i>	30,665	3,564	27,101
84 to 87.01	Total of Machinery			
	<i>All Products</i>	156,994	798,012	-641,018
	<i>Products Covered by Master Plan</i>	140,663	432,246	-291,583

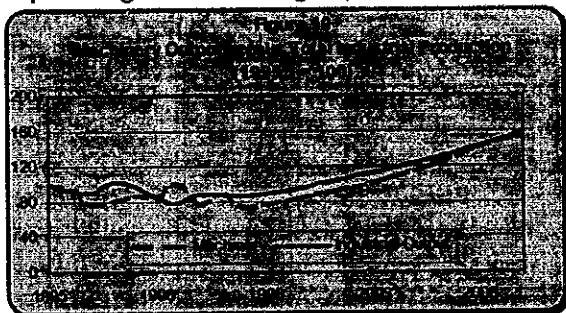
Source: Ministry of Energy, Industry and Trade

B. Investment Strategy

The rapid expansion of global production and markets in the last two decades has given rise to systemic changes in the world economy. For Kazakhstan, these changes could generate large volumes of international capital flows and transactions in the machinery industry, including the widespread diffusion of production technologies from corporate contracting arrangements. Kazakhstan's shift from import substitution policies to outward-oriented policies is likely to produce dynamic changes in the comparative advantage of the machinery industry. An improved trade and investment framework under the country's forthcoming membership in the WTO will permit Kazakhstan to export products that more closely conform to its factor endowments. It will also allow the country to more fully exploit its comparative advantage in the production of particular goods related to the machinery industry.

The introduction of new technologies through cross-border production networks and the dissemination of new skills in the workforce have now become as important to the specialization of production activities in countries such as Kazakhstan as their capital, labor and natural resource endowments. This

approach allows production costs to be reduced by exploiting economies of scale and expanding trade. A larger production area could, in turn, provide the basis with which



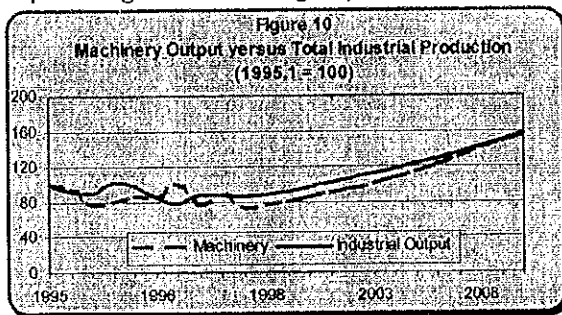
to develop intra-firm trade in machinery products, implement marketing processes that take advantage of vertical and horizontal product differentiation in markets, and bring in much needed domestic and foreign investments into Kazakhstan's machinery building industry.

For Kazakhstan to develop its own cross-national machinery production networks and compete in the global market, it will need to attract managerial, technological and financial support from the international business community. To this end, the sector is encouraging investment by foreign firms to attract technology and production know-how into the industry through complementary relationships with firms.

Table 8 Production of Major Types of Machinery, 95 (volume and value)		
	Unit	1995
Power transformers:	units	1,376
	'000 kWa	157
Power capacitors	'000 kVa	139
Storage batteries (lead)	tons of lead	16,749
	'000 amp-hrs	478,942
<i>of which:</i>		
Automobile batteries	units	470,210
Alkaline batteries	'000 amp-hrs	564
Metal-cutting machine tools	units	57
Press and forge machines	units	269
Centrifugal pumps	units	5,713
Rolling bearings	units	546,000
Excavators	units	-
Bulldozers	units	521
Tractors	units	1,803
Agricultural machines		
<i>of which:</i>		
Tractor plows	units	283
Tractor drills	units	349
Tractor cultivators	units	82
Tractor mower	units	2,030

Source: National Statistical Agency.

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Source: National Statistical Agency.

C. Priority Areas for Investment

The major sectors for machinery industry investments are those of agriculture, food processing, mining, and rolling stock.

1. The Agricultural Sector

In the immediate future, there are investment opportunities in spare parts and components of a number of key products that are already being produced in the country. For medium and large size tractors, the development of market information will be necessary, especially as it relates to the quality and design of machinery that is currently being imported. Combine harvesters that are currently being imported could also be supported by investment in the local production of components and special parts.

Eventually, investment opportunities are likely to arise in the final assembly of machinery, as well as the fabrication of machine parts and the progressive development of key machinery components. Foreign investors have a number of opportunities to introduce appropriate technologies for these activities.

2. Food Processing Sector

The major region for production of food processing machinery is the northern part of the country, where much of Kazakhstan's grain, milk and meats are produced. The meat processing and dairy processing industries have an especially large potential for growth, given the rapidly expanding demand for these types of products in the country. The demand for meats is strong, and Kazakhstan has a comparative advantage in livestock production because of its extensive pastureland. Local dairy processing business is also growing rapidly and one local company, Foodmaster, sells its dairy products throughout much of southern Kazakhstan. There is, nevertheless, considerable room for further growth, especially in the area of dairy processing equipment.

There are numerous vegetable and fruit juice processing opportunities in the south, near the production sites. At present only about one-tenth of domestic vegetable production and one-fifth of fruit production is processed by local industries. Instead, vegetable and fruit production tend to be preserved by individuals in their homes. Eight large enterprises account for most commercial production and most are canning operations. There is only one frozen food factory. The development of this industry will require large-size refrigeration and storage facilities, and demand for these types of facilities is expected to grow rapidly in the short and medium-term.

	1994	1995	1996
<i>Total</i>	100	100	100
Food Industry	32.4	38.0	48.1
Meat and Milk Industry	36.9	33.3	25.7
Cereals and Animal Feed Industries	23.4	20.9	16.9
Light Industry	5.1	5.7	7.3
Fish Industry	2.2	2.0	1.5

Source: National Statistical Agency.

3. Mining Sector

Mining equipment firms have a number of opportunities in the development of parts and components, since more than half of all mining, processing, and smelting enterprises in Kazakhstan use outdated equipment that is often in need of repair. The introduction of environmentally friendly technologies would also greatly benefit the industry. At present mining firms rely heavily on poor quality machinery imports from Russia, as there is only a small indigenous mining machinery industry.

Hydraulic pumps, engines and transmissions could possibly be produced locally. Over the longer term, a promising area of investment is in the production of surface wheel loaders. Manufacturing technologies already exist for underground wheel loaders, and the same components and parts could be used for the surface type of loaders. As mining methods shift from underground to surface mining, there will be an increased demand for these surface wheel loaders. Domestic firms will therefore require a widespread diffusion of production technologies from corporate contracting arrangements with overseas companies.

4. Rolling Stock

Overall modernization in the production and repair of rolling stock is needed to improve the production quality of passenger coaches and freight cars, especially in the areas of metal working for the repair and production of these components. Most components and parts of railway rolling stock are not currently manufactured in Kazakhstan and therefore need to be imported from abroad. There is therefore a considerable potential for investment in the manufacture of rolling stock parts and components in the country.

Electric railcars and freight cars could be produced in response to expanding demand if appropriate foreign production technologies can be effectively introduced into the country. Electric and diesel locomotives are in need of

replacement with more powerful engines. However, at present the lack of appropriate technology means that these locomotives need to be imported from Russia and the Ukraine. In addition, heavy repair is undertaken abroad for both electric and diesel locomotives. With appropriate foreign investment support, these repairs could instead be carried out domestically.

There appears to be sufficient capacity with the existing facilities and technologies for repair facilities of oil tank wagons. Nevertheless, investment in bogie repair and new bogie manufactures is needed since capacity is lacking in this area. There is also considerable investment potential for the manufacture of low and high-pressure oil tanks. Electric and diesel locomotives are in need of replacement with more powerful engines. Investors could profit from addressing the needs for a wide range of rolling stock parts and components, as well as supplying appropriate technologies and managerial know-how for the production of oil tanks, locomotive engines and a wide range of rolling stock components.

Table 10				
General-Purpose Rolling Stock at End-1995				
(units)				
	Total	Almaty Railway	W. Kazakhstan Railway	Tselinnaya Railway
Locomotives, total, <i>of which:</i>	3,045	1,060	805	1,180
Vapor locomotives	197	104	37	56
Electric locomotives	654	140	na	514
Diesel locomotives and special systems	2,194	816	768	610
<i>of which:</i>				
Diesel locomotives and special system locomotives over 260 kW	44	31	3	10
Railway motor car, total, <i>of which</i>	116	31	3	82
Diesel and special railway motor cars	44	31	3	10
Other	72	-	-	72
Coaches	2,353	1,105	377	871
Freight cars, total	80,242	33,788	27,872	36,642
<i>of which:</i>				
Closed cars, <i>of which</i>	80,242	33,788	27,872	36,642
Refrigerator cars	1,636	680	956	-
Open wagons	38,162	11,094	6,648	20,420
Flat cars	12,581	4,627	4,804	4,150
Other	27,863	17,387	15,464	12,072
Cars belonging to private companies	11,253	3,796	3,091	4,366

Source: National Statistical Agency.

D. Costs Related to the Machinery Industry

Utility rates are low compared with those of other countries. Since 1997 the electricity rate for industry has been \$0.053 a kilowatt hour. This rate is approximately equivalent to those in South East Asia, where rates have also been attractive for investors.

Kazakhstan's population is relatively well educated, and its literacy rate is almost 98 percent. An advanced scientific base consisting of 220 research institutes and regional agricultural stations has developed in Kazakhstan over the years. More than half a million students currently attend more than 300 institutions of specialized secondary and higher education. The country produces 125,000 specialists and 190,000 qualified workers each year.

	Industry	Agriculture	All Sectors
1995.1	113	28	66
1995.2	130	36	76
1995.3	146	48	91
1995.4	174	53	107
1996.1	165	40	102
1996.2	163	51	111
1996.3	173	66	118
1996.4	184	68	126
1997.1	164	50	112

Source: Government of Kazakhstan, Center for Economic Reform, based on information provided by the National Statistical Agency of Kazakhstan.

Labor costs are low. Since real wages have more than halved between 1991 and 1995, labor costs are low and generally make up a relatively low proportion of output costs.

The Land Code of 1991 established distinct land categories for agriculture, settlements, land under industrial enterprises, forestry, national reserves and recreation. According to the Constitution, all land in Kazakhstan is the property of the State and, as a consequence, all other forms of ownership are at the discretion of the state. Building from this base, early legislation did not intend to embrace the concept of private ownership and instead established the following categories: (i) permanent ownership, which was restricted to state enterprises; (ii) life inheritable tenure (LIT), which was granted for peasant farms, household plots, gardens, and

dachas; (iii) permanent use; (iv) temporary use; and (v) leasing. Since the State owns all land, the first category of permanent ownership remains a logical consequence of being a state enterprise. The concept of LIT appears to have been an attempt to bridge the gap between the concept of private ownership (non-state) and the constitutional status of land. The remaining categories of permanent and temporary use convey the possibility of termination of rights.

	Total Cost	Of which:			
		Materials		Labor	
		1995	1996	1995	1996
All Industries	100	52.9	50.4	13.9	20.4
Machine Building	100	50.7	52.7	24.8	34.1
Ferrous Metallurgy	100	61.8	58.0	13.1	28.3
Nonferrous Metallurgy	100	52.9	49.8	18.0	23.2
Forestry, Pulp And Paper	100	48.9	53.0	21.5	29.2
Light Industry	100	54.0	55.0	15.6	24.6
Food Industry	100	65.3	66.8	12.6	16.9
Chemicals And Petrochemicals	100	62.9	54.3	13.9	22.6
Electricity	100	41.6	39.8	10.2	12.7
Fuel	100	50.5	49.5	11.1	15.2

Source: National Statistical Agency

The introduction of the Civil Code in early 1995 with its acceptance into law of the concept of private ownership called for the reconciliation of land reform laws with its basic principles. As a consequence, the concept of private ownership of land was recognized in the December 1995 Law on Land. Private ownership can now be held over personal household plots, gardens and dachas and also under private industrial enterprises. However, land of agricultural designation cannot be granted a private ownership status, and foreign citizens and foreign legal entities can only lease land through a domestic partner for a period up to 99 years.

E. Export Processing Zones and Special Economic Zones

In 1996 the President issued the Decree on Special Economic Zones (SEZs) to accelerate the economic development of certain regions of Kazakhstan and to promote the integration of those regions into the world economy. According to the decree, development should be achieved, *inter alia*, through the creation of highly efficient export-oriented production, the attraction of investments, and the introduction of modern management methods and social norms. The SEZs enjoy special rights such as tax and duty-free status to encourage economic

development. If the SEZs do not achieve the purpose for which they were established, they can be abolished prematurely by a Presidential Decree. A second piece of legislation, Chapter 12 of the Customs Code on 'Free Customs Zones and Free Warehouses', provides for the creation of free customs zones and free warehouses within which any commercial operations, except retail trade, can be conducted, including the transshipment of goods.

The territories of free customs zones and warehouses are treated as being located outside the customs territory of Kazakhstan. However, legal entities in the special economic zones are subject to the taxation, registration, and licensing legislation of the Republic of Kazakhstan. Banking activities may also be carried out in special economic zones according to the banking legislation of Kazakhstan. The Customs Committee regulates and supervises the activities of free customs zones and free warehouses, while the Ministry of Justice is responsible for registering businesses within a SEZs. Only Kazakhstani legal entities and natural persons have the right to establish free warehouses. Kazakhstani legal entities can be fully or partially foreign-owned. The Foreign Investment Law of Kazakhstan governs foreign investment in special economic zones, and the national treatment stipulated under that law applies under this condition.

Currently, Kazakhstan has three operational SEZs in Lisakovsk, Kyzyl Orda and Astana. The Government plans to establish two more SEZs in Zhayrem-Atasuyskaya and Sary-Arka, where unemployment is high and industrial capacity is underutilized. These and other sites could be considered for the establishment of industrial export processing zones, depending on a number of economic, technical, physical and social characteristics determining the relative advantages and constraints of their locations. The suitability of these locations for industrial development generally, and export processing zones (EPZs) in particular, will greatly depend on the types of processing activities envisaged. Light manufacturing and assembly activities have different locational requirements than, for example, heavy machinery industry. Much of the variance arises from differences in the manufacturing cost structures of each type of activity.

Traditionally, a good location has been one that allows the minimization of these costs. For this reason, EPZs are traditionally located near transportation hubs; however, determination of a least-cost location varies greatly by the cost structure of the particular firm and its specific requirements for labor, materials, energy, utilities and other inputs. For most firms seeking a production base in an EPZ, the most important factor is the availability and cost of labor and access to materials and transportation. The development of Kazakhstan's free zones is increasingly being supported by ready access to telecommunications linkages and services that meet the requirements of foreign and domestic investors in the machinery industry.

PART IV INVESTMENT REGULATIONS

Kazakhstan is in the process of establishing a legal environment that is conducive to investment. The State Committee on Investment is invested with exclusive authority to co-ordinate the process of attracting inward investment from various sources. Since the Committee's stated objective is to provide the support of the state to investors, its directions have binding force for all government entities. The Committee provides a number of incentives for investors. These privileges consist of the following (a) grants of natural resources belonging to the State, (b) reductions of taxes on land and property, and (c) reductions or exemptions of customs duties on imports of equipment and material inputs for the investment project.

The main regulatory instruments affecting foreign investment in Kazakhstan are the Foreign Investment Law and the Law on State Support for Direct Investment. In addition, some of the key legislation affecting investment relates to taxes (Tax Code of 1995), customs procedures (Customs Code of 1995), insurance (Decree of President having the Force of Law On Insurance of 1995), competition policy (Law on Development of Competition and Restriction of Monopolistic Activity of 1991), land rights (President Decree having the Force of Law "On Land" of 1995), other currency and banking laws and regulations, and intellectual property legislation (Source: "The State Committee on Investment").

A. The Foreign Investment Law

The Foreign Investment Law provides for guarantees for national treatment and non-discrimination among foreign investors. Since Kazakhstan has a policy of free and open admission to foreign investments, it does not subject foreign investment to any prior authorization requirements. The law does not provide any investment incentives in the form of tax holidays or others either in general or with regard to a specific sector. The government plans to continue improving the legal and regulatory environment for foreign investment and to improve the conditions for stimulating the operations of credit, financial, investment, and insurance institutions servicing the small and medium-size enterprises.

B. Law on State Support for Direct Investment

In 1997 the Law on State Support for Direct Investment was enacted to stimulate domestic and foreign investment in the following priority sectors of the economy:

- Infrastructure (including electrical infrastructure and telecommunications);
- Light manufacturing;
- High-yield varieties of crops and livestock, fertilizers and pesticides;
- Social sector investments (including investments in the health, education, sports, and tourism); and
- Investments associated with the transfer of the capital to Astana.

As inducements to stimulate additional investments in these sectors, various forms of tax and customs exemptions, together with contributions of real property by the government, may be individually negotiated with the State Committee on Investments. Specific incentives include (a) up to 100 percent tax relief on the first five years of the investment, (b) up to 50 percent tax relief on the second five years of the investment, and (c) partial or full customs duty exemptions on equipment and raw materials needed for the investment.

Performance requirements generally refer to the investor's requirement to pay back wages, remodel factories and plants, and provide an agreed level of output. Rules on local content, hiring of nationals, and local source of financing vary from contract to contract. While investors are usually not required to purchase from local sources, such terms can be written into contracts (for example, the Petroleum Law requires that petroleum contractors give preferences to the purchase of local equipment, goods and services). There is no requirement in Kazakhstan that nationals own shares in foreign investments. In the banking sector, foreign investors have participated only through joint ventures with local entities, but this is no longer necessary. Likewise, there is no general requirement that the level of foreign equity be reduced over time. Technology transfers frequently occur and sometimes are written into contracts, but do not appear to be a necessary aspect of foreign investment.

C. Other Regulations

Land ownership is provided by Kazakhstan's constitution. Land and other natural resources can be owned or leased by physical persons according to conditions established by law. These conditions are: (i) permanent ownership is restricted to state enterprises; (ii) life inheritable tenure is granted for family farms, household plots, gardens, and dachas; and (iii) other land and natural resources may be leased up to 99 years. Agricultural land cannot be privately owned. Foreign citizens and foreign legal entities are only able to lease land for up to 99 years.

Patent and trademarks laws guarantee the right of inventors to the 'name' of their product, but financial rights of patent holders do not appear to be protected. In

addition, Kazakhstan lacks patent protection for certain types of products and processes, such as layout designs and plant varieties, and existing protection provided for trade secrets is rudimentary. Registration of trademarks also began in July 1992. Trademark violation is a crime, but enforcement appears to be rare and arbitrary. There are marked disparities in fees charged to domestic patent and trademark applicants, as compared with foreign applicants. The 'Law on Copyrights and Related Rights' was approved in June 1996.

Registration procedures and regulatory issues figure prominently in work being undertaken in the reform process, with a view toward assuring that the economic climate in Kazakhstan is attractive to both local and foreign investors. Private economic actors must know the "rules of the game" at the outset, and potential new investors have to be sure beforehand that they can confidently analyze risks involved in a new venture. Also, greater transparency is essential to counter corruption and ensure a level playing field for all private sector actors.

Licensing requirements remain a major problem. Under the April 1995 Law on the Registration of Legal Entities, the relevant agency must issue the registration license within one month of the submission of all required documents. The actual implementation of this decree has been grossly inadequate, and some foreign companies have complained that the process can take several months.

Customs clearances are a source of delay and can represent a significant cost in terms of foregone activities. Kazakhstan is taking steps to improve the functioning of its Customs Committee, including making the Customs Committee an independent body on an equal footing with other ministries. Moreover, membership in the WTO will require that Kazakhstan eliminate trade control measures and simplify its custom procedures.

Convertibility and transfer of currency no longer pose a problem for investors, although there appears to be an increase in bureaucratic obstacles to currency transactions. In 1996 the NBK allowed currency convertibility and restrictions on current account transactions were eliminated under Article 8 of the IMF Articles of Agreement. Money transfers in currency associated with foreign investments (whether inside or outside of the country) can take place without restriction. In addition, foreign investors can convert and repatriate tenge earnings made inside Kazakhstan. Notwithstanding the liberalization of transactions, anecdotal evidence from the Study Team's survey of machine building enterprises indicates that there has recently been an increase in the amount of paperwork involved in foreign exchange transactions. While there are fees associated with the paperwork, businessmen complained about the time wasted in processing the transactions rather than the fees. The time lost in business transactions represented a large cost in terms of delayed shipments leading to the cancellation of orders from buyers who are unable or unwilling to tolerate the procedural requirements.

D. Tax Matters

The Tax Code is considered by tax experts to be among the most comprehensive in the NIS. In general, taxes are applied universally within the code, allowing only a limited set of exemptions. The code essentially applies the international model of taxation, based on the principles of equity, economic neutrality and simplicity. The Tax Code is the only vehicle employed by the government of Kazakhstan to specify compulsory nationwide and local taxes. The Code provides for three major central government taxes: income tax for both businesses and individuals; value-added tax (VAT); and excise duty.

Income tax is assessed on a residency basis rather than citizenship (normal residency rules apply). There are no preferences given to foreign nationals or foreign owned or joint ventures. Business income is taxed at 30 percent (20 percent in special economic zones) except for income derived principally from land for which the rate is 10 percent. Dividends and interest are subject to a 15 percent withholding tax, and tax credit provisions effectively exempt dividends and interest received by businesses from withholding tax.

The Code provides for a 20 percent VAT that applies to the value added through the various stages of production and distribution up to final sale for consumption or use. It is charged on both goods and services consumed in the country whether domestically produced or imported. The tax is paid at each point in the chain of sales but a system of tax crediting avoids any cascading effect. The tax is comprehensive with very few exemptions. Exports are assessed at a zero rate with credit for all input taxes except for export to CIS countries. There are a few imported goods exempted from the VAT but the most important exemption is on goods originating in and imported from CIS countries.

The issue of double taxation of traded goods from Russia has recently been resolved. In the past, Russia levied a VAT of approximately 20 percent on exports, while Kazakhstan levied a similar VAT on imports. A solution to the so-called double VAT problem between the two countries was reached in 1998. Both countries initially charged a VAT only on exports, to give Russia time to draft new VAT legislation but in 1999 both Russia and Kazakhstan drafted legislation that would allow each country to charge a VAT on imports.

The Tax Code lists the goods that are subject to excise tax and subsequent resolutions specify the various rates for excise taxes. In general these taxes apply to luxury items such as alcoholic beverages, tobacco, automobiles and lorries, jewelry, and clothes. It also applies to diesel fuel and gasoline. Exemptions apply to goods imported or exported on a temporary basis, goods originated in and imported from CIS countries, and alcohol intended for use in production of liqueurs, vodka products, fortified drinks and juice, wine, and balsam. Two other nationwide taxes are collected, one a securities transaction tax, the other a special taxes and payments imposed upon mineral resource users. There are also local taxes, a

land tax, property tax and a tax on vehicles. Under the February 1997 changes to the tax law, accelerated depreciation is allowed and companies can deduct their expenses on construction and purchases of technological equipment.

PART V SOURCES OF FINANCING

A. Domestic Sources

The banking system in Kazakhstan is currently in a state of transition towards the establishment of Western banking standards. The system is made up of a central bank, domestic and foreign-owned commercial banks and government-owned banks. Nearly 95 percent of the assets of the banking system are in Almaty-based banks. As a result of more stringent reserve requirements, the number of Kazakh banks dropped from over 200 banks in 1995 to less than half that number by 1997. There have also been several mergers and acquisitions in the banking sector. The development of the stock market, which has only been in operation since 1993, and more competitive pressure to increase capital is leading to more effective control and better corporate governance.

The National Bank of Kazakhstan (NBK) is charged with the overall supervision and regulation of all banking activities in the country, and performs standard central bank functions. It has the responsibility for protecting the stability of the monetary-credit system and the interest of creditors, depositors, and other bank clients. More specifically, the NBK determines the criteria for entering into the banking system and the procedures for licensing of banking activities. The NBK implements its supervisory policies through prudential normative requirements with which all banks must comply. These requirements include minimum capital requirements, limitations on loans to a single borrower, a minimum liquidity ratio, and the limits of the bank's open currency position.

The NBK allows the national currency to float. In 1996 Kazakhstan joined Article 8 of the International Monetary Fund Charter, stipulating that the country would not restrict current account transactions such as currency conversions or the repatriation of investment profits. Money transfers in currency associated with foreign investments, whether inside or outside of Kazakhstan can take place without restrictions. For example, foreign investors are permitted to settle their obligations, including the payment of wages to their resident and non-resident employees, in foreign currency. In addition, foreign investors can convert and repatriate tenge earnings made inside Kazakhstan.

Apart from the NBK, there are four main segments that make up the rest of the banking system: (a) nine large domestic banks with branches located throughout

Kazakhstan; (b) 13 foreign banks; (c) four fully government-owned banks (the Kazakhstan Eximbank, the Housing Construction Bank, the Rehabilitation Bank, and the Turan Alem Bank); and (d) approximately 35 small Almaty-based banks and 35 regional banks. Foreign banks have been active in Kazakhstan since 1993. Under existing legislation, foreign banks are not permitted to operate branches in Kazakhstan, but can establish subsidiaries, joint ventures and representative offices. Foreign investors are treated equally with Kazakh nationals, but their overall share of Kazakhstan's banking system capital must not exceed 25 percent (excluding portfolio investments), unless the NBK permits this limitation to be exceeded. If a bank is not a subsidiary of another bank, no person can own more than 25 percent of its shares without special permission from the NBK.

Article 10 of the Foreign Investment Law provides that foreign investors can open and maintain foreign currency accounts at any bank in Kazakhstan. Non-residents can open special 'Type I' accounts for conducting investment activities in the country. Transactions from these accounts related to privatization activities can be carried out by any non-resident legal entities, except non-resident legal entities having Kazakh shareholders owning more than 25 percent of the charter fund. Transactions related to other types of investment activities can be carried out from 'Type I' accounts by all non-residents, excluding individuals who do not have authorization to carry out economic activity in their home country. Non-resident individuals cannot open joint accounts in tenge or make payments in tenge for expenses related to investment operations (including privatization). 'Type C' accounts in tenge can be maintained by non-residents for the purpose of financing export and import operations, excluding certain operations related to exports from Kazakhstan to which non-tariff provisions apply.

The main sources of financing for trade and investment transactions and projects are commercial banks, a company's own retained earnings, foreign government-assisted loan funds and loans from international and bilateral donor programs. For small and medium size companies in Kazakhstan, most financing is obtained through commercial banks and a company's retained earnings. Limited financing is available for export development, and there are no commercial banking institutions in Kazakhstan that provide financing for sector-specific activities, such as agriculture. Given the limitations of financing within Kazakhstan, most funding for projects is done through international financial institutions or from funds generated within companies. However, financing offered by international institutions is often limited to certain trade and investment projects, and enterprises often find that requesting a loan is cumbersome in terms of paperwork and time and that the loan approval process is lengthy. Moreover, this type of financing is usually offered within a limited timeframe, which does not often correspond to the needs of manufacturers.

B. International and Bilateral Sources

- ◆ **Asian Development Bank (ADB):** The ADB focuses its efforts largely on the energy sector, followed by social infrastructure, transport and communications, agriculture and agro-industry, finance, and industry and non-fuel minerals. The ADB's medium-term strategy centers on poverty reduction, improving the status of women, population planning, and environmental protection. While most of its projects are undertaken directly with the government, the ADB recently financed a US\$400 million loan for food processing equipment to be purchased by private companies.
- ◆ **Central Asian-American Enterprise Fund (CAAEF):** The CAAEF has offices in all five Central Asian republics, and makes loans to small enterprises for private sector development. The U.S. government-sponsored US\$150 million fund makes equity investments, loans, and offers technical assistance to new private companies and entrepreneurs in the Central Asian republics. Emphasis is placed on small and medium-sized enterprises. The CAAEF also offers assistance to Kazakhstani entrepreneurs for business plan development.
- ◆ **European Bank for Reconstruction and Development (EBRD):** The EBRD provides loans for large projects, as well as technical assistance, in the areas of oil and gas development, mining, agriculture, and infrastructure development. The EBRD has developed a 100 million ECU program for small and medium enterprises (SMEs) with the former Kazakhstani Ministry of Economy and Finance and the NBK. The funds from this program will be channeled through selected participating banks in Kazakhstan to help local entrepreneurs draft a business plan to develop a bankable project, and issue loans to SMEs for up to US\$5 million.
- ◆ **International Finance Corporation (IFC):** The IFC, the private sector arm of the World Bank, provides loans for small-scale projects (not exceeding US\$10 million) in developing countries and emerging markets. The IFC is focusing its efforts in Kazakhstan on private sector development, and is actively analyzing small and medium-scale undertakings in the medical, agricultural (including food processing), and consumer goods sectors.

ANNEX-A
CONTACT INFORMATION FOR GOVERNMENT
AND NON-GOVERNMENT AGENCIES

A. Embassy in Japan and Investment Consulting Company (KAZINVEST)

Embassy of the Republic of Kazakhstan in Japan
Meguro-Ku, Himonya 5-9-8,
Tokyo 152 Japan
Tel: (03)3791-5275; Fax: (03)3791-5279

Investment Consulting Company (KAZINVEST)
9, Satpaeva Street, Almaty
The Republic of Kazakhstan
Tel: +7-3272-543553, 543554; Fax: +7-32772-507446

B. Government of Kazakhstan

Nursultan A. Nazarbayev
President of the Republic of Kazakhstan
Presidential Administration
11 Mira Street
Astana, Kazakhstan 473000
Tel: (3172)324-769, Fax: (3172)326-182

Nurlan Balgimbaev, Prime Minister
11 Mira Street
Astana, Kazakhstan 473000
Tel: (3172)323-104; Fax: (3172)324-023

State Committee on Investments
Uraz Dzhandosov, First Deputy Prime Minister/Chairman
11 Mira Street
Astana, Kazakhstan 473000
Tel: (3172)327-373; Fax: (3172)326-182
Homepage: <http://www.kazinvest.kz>

Agency for Strategic Planning and Reforms
Yerzhan Utembayev, Chairman
92 Abai Street
Astana, Kazakhstan 473000
Tel: (3172)336-358; Fax: (3172)326-228

Ministry of Agriculture
Sergey Kulagin, Minister
49 Abai Street
Astana, Kazakhstan 473000
Tel: (3172)323-784, 323-763; Fax: (3172) 324-541

Ministry of Energy, Industry and Trade
Mukhtar Ablyazov, Minister
37 Mira Street
Astana, Kazakhstan 473022
Tel: (3172)337-133, 337-134; Fax: 7 (3172) 337-164

National Academy of Sciences
Ministry of Science
Vladimir Shkolnik, Minister/President
28 Shevchenko St., corner of Valikhanov St.
Almaty, Kazakhstan 480021
Tel: (3272) 623-896; Fax: (3272) 696-116

Ministry of Finance
Sauat Mynbayav, Minister
60 Republic Avenue
Astana, Kazakhstan 473000
Tel: (3172) 280-065; Fax: (3172) 280-321

Ministry of Transport and Communication
Yerkin Kaliyev, Minister
49 Abai Prospect
Astana, Kazakhstan 437000
Tel: (3172)326-277; Fax: (3172)326-288

Committee on External Borrowing
Altai Zeinegabdin, Chairman
93/95 Ablay Khan St., corner of Kazibek Bi, Room 347
Almaty, Kazakhstan 480091
Tel: (3272)695-151; Fax: (3272)696-152

State Customs Committee
Gani Kasymov, Chairman
166 Pushkin Street
Astana, Kazakhstan 473000
Tel: (3172)750-447; Fax: (3172)753-016, 753-109

C. Financial Institutions

Citibank
41 Kazibek Bi St., 2nd floor
Almaty, Kazakhstan
Tel: (3272) 608-400; Fax: (3272) 608-399

ABN-AMRO Bank Kazakhstan
45 Khadzhi Mukana St.
Almaty, Kazakhstan 480099
Tel: (3272)507-301, 64-35-52; Fax: (3272)507-303, 507-298

Turan-Alem Bank
55 Aiteke Bi St, corner of Furmanov Street
Almaty, Kazakhstan 480091
Tel: (3272)500-100; Fax: (3272)500-224

Eximbank Kazakhstan
118 Pushkina St.
Almaty, Kazakhstan 480021
Tel: (3272) 622-815; 634-300; Fax: (3272) 507-549; 631-985

Kazkommertsbank
49 Bayseitova St.
Almaty, Kazakhstan 480013
Tel: (3272)505-107, 505-106; Fax: (3272)638-571
Homepage: <http://www.kazkombank.almaty.kz>

D. Multilateral Development Banks

International Bank for Reconstruction And Development (The World Bank)
41 Kazybek Bi, Building A, 4th floor
Almaty, Kazakhstan 480100
Tel: (3272)608-580; Fax: (3272)608-581

European Bank for Reconstruction and Development
10-A Abay St., corner of Furmanov 8th floor
Almaty, Kazakhstan 480013
Tel: (3272)632-247, 631-576; Fax: (327)-581-1424

Asian Development Bank
126\128 Panfilov St., corner of Zhambul St.
Almaty, Kazakhstan 480091
Tel: (3272)639-329; Fax: (3272)631-912
E-mail: karm@asdc.kz

E. Other Non-Government Organizations

ABT Associates, Inc.
60 Zhibek Zholy St., Apt.7
Almaty, Kazakhstan 480002
Tel: (3272)335-687; Fax: (3272)335-670

Booz-Allen & Hamilton/Trade and Investment
55 Tole bi, corner of Panfilov Street
Almaty, Kazakhstan 480091
Tel: (3272)695-095; Fax: (3272)692-812

Brif Social & Marketing Research Agency
Alexander Ruzanov, President
69a Kabanbay Batyr St., Room 313
Almaty, Kazakhstan 480100
Tel: (3272)618456; Fax: (3272)616-132

Business Information Service for the Newly Independent States (BISNIS)
International Trade Administration
14th & Constitution Ave., NW, Room 7413
Washington, DC 20230
Tel: (202)482-4655; Fax: (202)482-2293
E-mail: bisnis@usita.gov
Homepage: <http://www.mac.doc.gov/bisnis/bisnis.html>

Center of Marketing Research and Business (KIMEP)
Yelena Kireyeva, Director
4 Abay Ave., Room 417
Almaty, Kazakhstan 480100
Tel: (3272)64-44-10; Fax: (3272)643-720

Chamber of Commerce and Industry of the Republic of Kazakhstan
26 Masanchi St.
Almaty, Kazakhstan 480091
Tel: (3272)670-052, 677-832; Fax: (3272)507-029
E-mail: tpprkaz@online.ru

Delegation of the European Commission
20A Kazybek Bi St.
Almaty, Kazakhstan 480100
Tel: (3272)638-858, 639-939; Fax: (3272)637-752, 637-506

Information and Presentation Center
of the Raw Materials Complex of Kazakhstan
85 Dostyk Pr.
Almaty, Kazakhstan 480100
Tel: (3272)635-416; Fax: (3272)638-743

Institute for Development of Kazakhstan
Rustem Zholaman, President
60 Dzhandosov St., 4th floor
Almaty, Kazakhstan 480057
Tel: (3272)447-841; Fax: (3272)447-840

Kazakhstan Business Service Foundation (under Kazakhstan Center for Support
and Development of Entrepreneurship)
58-A Ablay Khan Pr.
Almaty, Kazakhstan 480004
Tel: (3272)336-566; Fax: (3272)501-998

Kazakhstan Center for Support and Development of Entrepreneurship
58-A Ablay Khan Pr.
Almaty, Kazakhstan 480004
Tel: (3272)334-955; Fax: (3272)339-482

ANNEX-B MAJOR ENTERPRISES IN THE MACHINERY INDUSTRY

A. Agricultural Machinery

- 1) Name of Enterprise: AZTM
Location: Almaty
Major Products: Fe, non Fe metal products
Sales Amount/month: 750 million Tenge
No. of Employee: 2005
Address: 480009, Almaty, Tole bi ave, 189
Tel: 327-2-459110

- 2) Name of Enterprise: Pavlodar Tractor
Location: Pavlodar
Major Products: Tractor, crawler
Sales Amount/month: 400 million tenge
No. of Employee: 8300
Address: 637027 Pavlodar, Kosmonavtov st, 1
Tel: 318-2-322438

- 3) Name of Enterprise: Die & Tool Division, Pavlodar Tractor
Location: Pavlodar
Major Products: Die & Tool
Sales Amount/month: n.a.
No. of Employee: 800
Address: Pavlodar city, Kosmonavtov st, 1
Tel: 318-2-322438

- 4) Name of Enterprise: Pavlodar Machine
Location: Pavlodar
Major Products: Gantry and overhead crane
Sales Amount/month: n.a.
No. of Employee: 420
Address: Pavlodar city, Lomov st, 180
Tel: 318-2-45366

- 5) Name of Enterprise: October Lathe
Location: Pavlodar
Major Products: Engineering with manufacturer
Sales Amount/month: 6.3 million Tenge
No. of Employee: 100
Address: Pavlodar, Lenin av, 160
Tel: 318-2-322934

- 6) Name of Enterprise: PZTM
Location: Petropavlovsk
Major Products: Spare parts, electric power and mine
Sales Amount/month: 30 million Tenge
No. of Employee: 2000
Address: 642023, Petropavlovsk, Gashek st, 1
Tel: 327-2-603601
- 7) Name of Enterprise: ZIKSTO
Location: Petropavlovsk
Major Products: 6t 2oxle trailer
Sales Amount/month: 300 million Tenge
No. of Employee: 2500
Address: 642004, Petropavlovsk, zavodskaya st, 1
Tel: 315-2-333265
- 8) Name of Enterprise: Kirov
Location: Petropavlovsk
Major Products: Electric parts, spare parts, farm machinery
Sales Amount/month: 14.2 million Tenge
No. of Employee: 700
Address: 642007, Petropavlovsk, Partizanskaya st, 48
Tel: 315-2-344067
- 9) Name of Enterprise: Akomolaselmash
Location: Akmola
Major Products: Farm implement
Sales Amount/month: 20.7 million Tenge
No. of Employee: 1000
Address: 473037 Akmola, Pushkina st, 166
Tel: 317-2-754232
- 10) Name of Enterprise: Gas Apparatus
Location: Akmola
Major Products: Gas stores and canisters
Sales Amount/month: 4 million Tenge
No. of Employee: 148
Address: Akmola city, 2 Nagornaya st, 1
Tel: 317-2-328030
- 11) Name of Enterprise: Tselinenergomont
Location: Akmola
Major Products: Electric power station equipment and maintenance
Sales Amount/month: 44 million Tenge.
No. of Employee: 800
Address: 473000, Akmola G.P.O.Box 27
Tel: 317-2-332812

- 12) Name of Enterprise: Eikos
Location: Almaty
Major Products: Water purifier
Sales Amount/month: n.a.
No. of Employee: 140
Address: 480016, Almaty Nusupbekov st, 32
Tel: 327-2-3049904
- 13) Name of Enterprise: Pisheremmash
Location: Almaty
Major Products: Food processing machine (meat, milk)
Sales Amount/month: 3 million Tenge
No. of Employee: 150
Address: 480057, Almaty Timingazev st, 42
Tel: 327-2-445434
- 14) Name of Enterprise: Diesel Engine Factory
Location: Kostanai
Major Products: Engine parts
Sales Amount/month: 1 million Tenge
No. of Employee: 600
Address: 458006, Kostanai, Rabochaya st, 147-a
Tel: 413-25-541326
- 15) Name of Enterprise: Agroremmash
Location: Almaty
Major Products: Flour mill
Sales Amount/month: 2 million Tenge
No. of Employee: 90
Address: 480019, Almaty Hahirllin st, 32
Tel: 327-2-301316

B. Mining Machinery

- 1) Name of Enterprise: Almaty Lathe Co.
Location: Almaty
Major Products: Lathe
Sales Amount/month: 14 million Tenge
No. of Employee: 100
Address: 480074, Almaty, Mailina st,85
Tel: 327-2-357335
- 2) Name of Enterprise: AZTM (Almaty Heavy Machine Building Co.)
Location: Almaty
Major Products: Pipes, wires producing equipment: specialized castings
Sales Amount/month: 975 million Tenge
No. of Employee: 2,500
Address: 480009, Almaty, Tole bi ave, 189
Tel: 327-2-459110

- 3) Name of Enterprise: Kargormash
Location: Karaganda
Major Products: Hydraulic facepost for coal mine
Sales Amount/month: 80 million
No. of Employee: 1,300
Address: Karaganda, Kosmonavtov st, 1a
Tel: 321-575311
- 4) Name of Enterprise: KCMZ (Karaganda Casting & Machinery Building Plant)
Location: Karaganda
Major Products: Mining equipment and repair
Sales Amount/month: 25 million Tenge
No. of Employee: 750
Address: Karaganda, Orew st, 103
Tel: 321-2449531
- 5) Name of Enterprise: Vostokmashzavod
Location: Ust-kamenogrsk
Major Products: Mining machines and tools
Sales Amount/month: 120 million Tenge
No. of Employee: 2,200
Address: 492018, Ust-Kamenogorsk, Lenin ave 86
Tel: 323-2-424414
- 6) Name of Enterprise: Karaganda Parkhomenko Plant
Location: Karaganda
Major Products: Mining machinery, construction machinery and metallurgical machine
Sales Amount/month: 10 million Tenge
No. of Employee: 310
Address: 47005, Karaganda, Amangelaly st, 25
Tel: 312-2-336560

C. Railway Rolling Stock

- 1) Name of Enterprise: Rysty-AECRW
Location: Almaty
Major Products: Passenger coach repair
Sales Amount/month: US\$ 1.3 million
No. of Employee: 2,000
Address: 480034, Almaty, Rayimbek AV, 206B
Tel: 327-2-431972
- 2) Name of Enterprise: Pavlodartractor
Location: Pavlodar
Major Products: Tractor
Sales Amount/month: 10.4 million Tenge
No. of Employee: 8,543
Address: 637027 Pavlodar, Kosmonavtor st, 1
Tel: 318-2-322438

- 3) Name of Enterprise: PZTM
Location: Petro-Pavlovsk
Major Products: Heavy machinery
Sales Amount/month: 1.3 million Tenge
No. of Employee: 2,876
Address: 642023, Petropavlovsk, Gashek st, 1
Tel: 327-2-603601
- 4) Name of Enterprise: Stepnogorsk Bearing plant (SBP)
Location: Steptonagorsk
Major Products: Roller bearing
Sales Amount/month: 18.3 million Tenge
No. of Employee: 3,700
Address: 474456, Stepnogorsk
Tel: 317-45-22306
- 5) Name of Enterprise: AWRZ
Location: Astana
Major Products: Freight wagon repair
Sales Amount/month: 0.7 million Tenge
No. of Employee: 820
Address: 473004, Astana, Kurskaya st,
Tel: 317-2-33-17-98
- 6) Name of Enterprise: DZMK (Dzhambul Metal Construction Workshop)
Location: Taraz
Major Products: Tank wagon repair, production
Sales Amount/month: 300 million (1996), 180 million (1997), 600 million (1998) Tenge
No. of Employee: Engineer(100), Worker(370)
Address: 484028, Taraz, Tole bui st, 178
Tel: 326-22-5-30-76

Note: US\$ 1=76 Tenge (As of June 1998)

