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Kazakhstan: Corporate M&A 2020

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1. Trends

1.1 M&A Market

M&A market in Kazakhstan remained strong in 2019, as it was in 2018. Activity was largely driven by ongoing consolidation of Kazakh banks because of the increased capitalisation requirements of the financial regulator, consolidation in the telecommunications sector and acquisitions in the IT sector.

Banking Sector

In Kazakhstan, there is currently a trend for consolidation of banks which has resulted in increasing numbers of M&As in the banking sector. This trend is explained by various factors, including inability of Kazakh banks and their controlling shareholders to meet prudential requirements and expected competition from the foreign banks due to the acceding of Kazakhstan to the WTO.

Consolidation of banks

In 2018, JSC Halyk Bank, the largest Kazakh bank, acquired JSC Kazkommertsbank, the second largest Kazakh bank. JSC HalykBank also sold 60% of its subsidiary, JSC Altyn Bank, to Chinese investors China CITIC Bank Corporation Limited and China Shuangwei Investment Co Ltd.

In 2019, JSC First Heartland Securities acquired 99.8% in JSC Tsesnabank that was close to default situation. After recapitalisation by the new controlling shareholder, JSC Tsesnabank has merged with JSC First Heartland Bank, another Kazakh bank. The surviving bank is called JSC First Heartland Jýsan Bank. In May 2019, JSC Forte Bank, a bank from top five in Kazakhstan, acquired 100% in another Kazakh bank, JSC Bank Kassa Nova. Following the purchase in June 2019 of JSC Asia Credit Bank by Mr Orifdzhan Shodiyev, it was planned that JSC Asia Credit Bank will be merged with JSC Capital Bank Kazakhstan, also owned by Mr Shodiyev, and JSC TengriBank. However, in February 2020, the major shareholder of JSC Tengri Bank announced that the deal will not be closed.

Reorganisation of the financial regulator

In 2019, the decision was made by the Kazakh government to reorganise the financial regulator, the National Bank of Kazakhstan (NBK). The Agency for Regulation and Development of the Financial Market (AFM) was separated from the NBK and now is the main regulator of corporate issues, securities and the financial market, including various aspects of M&A transactions. Last year, the NBK initiated an asset quality review (AQR) program in order to identify key risks applicable to the customers of Kazakh banks and the ways to address them. One of the recommendations, following the completion of the AQR in January 2020, was additional capitalisation of Kazakh banks by their shareholders with their own funds, this time without the involvement of budget funds, as has regularly occurred throughout the last ten years following the world financial crisis.

It is expected that not all shareholders of Kazakh banks will be able or willing to meet additional capitalisation requirements. As a result, consolidation in the banking sector will continue, and there will be a number of mergers and/or acquisitions of middle and small-size banks. Investments are expected not only from local but also from international investors. According to public sources, the European Bank for Reconstruction and Development is monitoring the Kazakh market for equity investments in the banking sector.

Looking forward

In addition to further consolidation of Kazakh banks, more M&A transactions are expected in the microfinance sector. Microfinance organisations are real competitors to the banks, and even left some of them behind in terms of expansion growth. Accordingly, microfinance organisations are considered interesting targets for foreign and local investors. In 2019, Bopa pte (Singapore) acquired controlling stake in Asian Credit Fund Mircofinance Organization LLP, one of largest Kazakh microfinance organisations. Before the transaction, Bopa pte was already one of the existing participants of the target. Following the closing, Bope pte accumulated 98.1% of participatory interests.

Telecommunication Sector

In December 2018, JSC Kazakhtelecom, the national telecommunications operator in Kazakhstan, acquired 75% in the largest Kazakh mobile operator, JSC KCell, from Telia Company and Fintur Holdings. The transaction was considered a key M&A transaction, influencing the whole telecommunication market in Kazakhstan, and won an international TMT M&A Award for "Telecom M&A Deal of the Year – Asia". Interestingly, following the transaction, a number of minority shareholders of JSC Kazakhtelecom claimed buy out of their shares by JSC Kazakhtelecom as they disagreed with JSC KCell acquisition. The dispute had public resonance and was then closed by amicable settlement.

In 2019, JSC Kazakhtelecom acquired the remaining 49% in another large Kazakh operator, Tele2, and became a 100% shareholder (prior to the transaction, JSC Kazakhtelecom owned 51% in Tele2). As a result of these acquisitions, JSC Kazakhtelecom became a telecommunications conglomerate in Kazakhstan with two thirds of the mobile market share. These deals are controversial since they clearly affect competition in Kazakh telecommunication sector, which may lead to a deterioration of the quality of telecommunication services.

IT Sector

In 2019, Chocofamily, the largest internet holding in Kazakhstan, acquired 47% in the merged travel company Aviata.kz and Chocotravel.kz from two individual shareholders. As a result, Chocofamily became 100% shareholder of the mentioned travel services. Later in 2019, Kazakh businessman Mr Aidyn Rakhimbayev acquired 10% in Chocofamily.

1.2 Key Trends

Privatisation

In 2015, the Kazakh Government announced a privatisation programme for state and quasi state assets for 2016-20 that continues to boost the M&A market in Kazakhstan. The aim of the privatisation programme is to decrease the state's stake in the economy. Privatisation can be conducted in various ways, including private M&As and IPOs.

According to the public sources, 739 out of 1197 objects have been sold to private hands, with the remaining deals yet to come. In January 2020, the Ministry of National Economy announced that the list of objects that are subject to privatisation, will be increased.

The list of the companies subject to privatisation with the current status is available at: https://privatization.gosreestr.kz/en?Filter=top65.

Privatisation programme M&As

One example of M&A through privatisation programme in 2019 was Petro-Retail LLP's purchase of KMG Retail LLP, the owner of republic networks of petrol stations, from JSC NC KazMunaiGas, the national oil and gas company in Kazakhstan. It was also recently announced that Ramada Plaza Hotel located in Nur-Sultan city, the capital of Kazakhstan, will be sold within the privatisation programme.

Privatisation programme IPOs

The pipeline IPOs to be conducted in the course of privatisation programme included major blue chip companies such as JSC Kazakhtelecom, JSC Kazakhstan Temir Zholy (Kazakh railways), JSC NC Kaz Munai Gaz (oil and gas), JSC Samruk-Energy, JSC Tau-Ken Samruk (a mining company), JSC Kazpost, JSC Air Astana and others.

Belt and Road Initiative

Another trend that may boost the M&A market in Kazakhstan is the Belt and Road initiative which aims to improve trade relations between China and other countries, including Kazakhstan. In 2015, the governments of Kazakhstan and China signed investment agreements worth USD14 billion. In 2017, COSCO Shipping (PRC) and Lianyungang Port Holdings Group Co Ltd jointly acquired, from national railways operator JSC Kazakhstan Temir Zholy, a 49% stake in the dry port KTZE-Khorgos Gateway. The facility is located on the border between China and Kazakhstan and is an important transportation hub connecting China and Europe by rail.

This acquisition is one of the most significant acquisitions concluded within the Belt and Road initiative. In 2018, China CITIC Bank Corporation Limited and China Shuangwei Investment Co Ltd acquired 60% stake in JSC AltynBank from JSC HalykBank. One of the drivers for the transaction, according to the seller's management, was the desire of Kazakh customers to develop their business in China within the Belt and Road initiative. In 2019, JAC Motors and China National Machinery IMP and EXP Corporation jointly acquired 51% of Allur Group, the large automobile producer in Kazakhstan. We expect more acquisitions by Chinese investors in Kazakhstan as a part of the Belt and Road implementation.

AIFC

Modelled on the Dubai International Financial Centre, the Astana International Financial Centre (AIFC) was officially launched in 2018, established with the aim of bridging the gap between the world's major financial centres and a regional gateway for capital and investments. The AIFC aims to become a financial hub not only for Kazakhstan, but for the whole of Central Asia, the Eurasian Economic Union, the Caucasus, West China and Mongolia.

To date, more than 400 companies have registered as participants in the AIFC and, in the last year, IPOs of JSC NC Kazatomprom (uranium company) and JSC Halyk Bank, the largest Kazakh bank, were successfully closed on LSE and AIFC stock exchange (AIX). IPOs of other Kazakh blue-chip companies planned within the framework of privatisation programme, are also expected to take place on AIX due to the mandatory 20% local placement requirement of Kazakh law.

The AIFC has its own laws and regulations and even its own court and facility for arbitration (in effect, a "one country, two systems" arrangement has been introduced despite the fact that Kazakhstan is a unitary state). The key feature and siren call of the AIFC is, therefore, a new jurisdiction based on English law principles, as English law is familiar and convenient for investors. The AIFC is, however, a civil law jurisdiction because the AIFC's court lacks authority to act if there is no statute (ie, a court precedent is not a source of law in the AIFC). Moreover, unlike DIFC law, the AIFC's fall-back legislation is Kazakh law, rather than English law, which will apply to any cases governed by AIFC law where the AIFC is otherwise silent on a given issue.

The establishment of the AIFC may encourage foreign and local investors to use AIFC law instead of Kazakh law or foreign laws (including English law) and foreign jurisdictions (ie, offshore jurisdictions) for structuring M&A transactions in Kazakhstan, for the following reasons:

- AIFC law contains certain concepts that are common for English law jurisdictions but are not expressly recognised and regulated by Kazakh law (such as option, fiduciary duties, netting, misrepresentation, injunction, specific performance etc); and
- sale and purchase of the legal entities established within AIFC or securities listed on AIX, are exempt from capital gain tax until 2066.

Though the interplay between AIFC law and Kazakh law is yet to be seen and tested, and as there are no court precedents, a gradual increase in the popularity of the AIFC law as applicable law and the AIFC court as proper forum for structuring M&A transactions in Kazakhstan and, maybe, even throughout the whole of Central Asia, is expected.

1.3 Key Industries

As mentioned, the banking, telecommunication and IT sectors experienced significant M&A activity in the past 12 months.

In the upcoming years, further M&A transactions in these and other sectors of Kazakhstan's economy, including microfinance, transport, renewable energy and agriculture, are expected.

The renewable energy sector in Kazakhstan grows annually; it has grown from six renewable energy facilities in 2017 to 23 facilities in 2019 with a forecast of 108 facilities by the end of 2020. Kazakhstan law is favourable to investors focused on renewable energy, offering the guaranteed energy purchase at a price determined by way of public auction. A recent auction showed an interest of local investors, as well as those from Russia, China and Europe.

The agricultural sector in Kazakhstan has a huge potential. Kazakhstan is one of the top five countries in the world by pasture; 45% of population lives in the countryside. In 2019, American agribusiness titans, Tyson Foods, Kusto Group and Valmont Industries, signed agreements with the Kazakh Government for investments in a new meat processing plant and a new plant to produce irrigation systems in Kazakhstan.

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Originally published in https://practiceguides.chambers.com/practice-guides/corporate-ma-2020/kazakhstan

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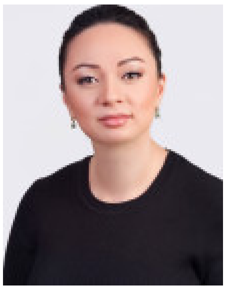

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