RESEARCH SECTOR

Global economic dynamics: review of 2018 & prospects in 2019

For targeted recipients only

January 2019

In 2018, world economy moderated and markets experienced a series of shocks caused by geopolitical tensions, uncertainty

In 2018 global financing conditions have tightened (Fed raised rate for 4 times), industrial production has moderated, trade tensions were elevated, international trade and investment have softened, and large emerging market and developing ***economies have experienced significant financial market stress****.*

US-China trade dispute*. In may 2018, US authorities declared the need for “effective measures to substantially reduce” the USD337bln annual trade deficit with China. As a result of retaliatory tariffs (US levied 10% tariffs on ~USD250bln in Chinese goods; China – on ~USD100bln in US goods) momentum of 2nd largest economy faded, while 1st largest economy reconsidered monetary policy from supportive to tightening.*

Brexit*. UK is scheduled to leave EU on 29 March 2019 regardless of whether there is a deal with EU or not. During 2018 UK and EU authorities have been actively deciding on terms of Brexit and did not reach agreement yet, which caused much uncertainties for EU and UK markets.*

Faced with these headwinds, the recovery in ***emerging market*** *and developing economies has lost momentum. Downside risks have become more acute and include the possibility of disorderly financial market movements and an escalation of trade disputes. Debt vulnerabilities in emerging market and developing economies, particularly low-income countries, have increased.*

Developed markets *were also volatile during 2018. The S&P 500 ended 2018 down 6.2%, while the FTSE All World Index shed 11.5% for the year.*

Source: Samruk-Kazyna

Key global events in 2018 (1/2)

January

US imposes sanctions on Russia's 21 individuals and 9 companies

Russia started to decrease dollar holdings for foreign exchange reserves purposes

February

US fiscal deficit concerns are addressed by US President

Pressure on the Fed's policy and trade policy of US

March

- *US tariffs on USD50bln import from China*
- *EU sanctions on Russia extended to Sep 18*
- *Fed raised rates to 1.5-1.75%*

Start of outflow of portfolio investments from emerging markets

April

New US sanctions on Russia (Rusal)

Metals (nickel, aluminium, palladium) prices surge. Highly volatile trading in metals.

May

- *Withdraw of US from the Iran nuclear deal*
- *US sanctions on Iran*

Oil price went up on supply worries

June

Fed raised interest rates to 1.75% - 2%. US economic projections for 2018-2021 were updated indicating faster growth

Wall Street ends lower, Treasuries sell off after Fed rate rise

Average price for the month						
Brent	69.1	65.7	66.7	71.8	77.0	75.9
USDKZT	327.1	321.9	320.7	324.7	328.1	336.1

Key global events in 2018 (2/2)

July

US tariffs on import from China reach USD250bln

Global growth outlook darkens, prices on commodities continue to fall

August

•US sanctions on Turkey;
•New US sanctions on Russia, effective 27 Aug
• Intensification of US-China trade tensions

US's trading partners slapped retaliatory tariffs on US exports

September

• Turkey raised interest rate by 625bps to 24%.
•Russia raised interest rate by 25bps to 7.5%

USDKZT weakened from 345 to 380 in Aug-Sept, spurred mainly by contagion effect from EM currency turmoil

October

Weakening of global economic growth. Confidence in trade has fallen

Sell off on stock markets. ~9% decline in S&P 500

November

90-day trade truce between US and China started

US and China started negotiations to settle trade dispute by March 2019

December

•OPEC+ decided to cut output by 1.2mln bpd
•Fed rate rise to 2.25-2.5%

Production cut supported oil prices, however prices are still volatile. Sell off on stock markets after the rate hike

	Average price for the month					
Brent	75.0	73.8	79.1	80.6	65.9	57.7
USDKZT	344.2	357.0	366.8	367.8	370.2	372.4

Global economy and international trade moderated in 2018. Global growth is expected to slow to 2.9% in 2019

Real GDP growth YoY, %

Region/Country	2017	2018e	2019f
World	**3.1**	**3.0**	**2.9**
Advanced economies	**2.3**	**2.2**	**2.0**
US	2.2	2.9	2.5
Euro-area	2.4	1.9	1.7
UK	1.8	1.3	1.7
Emerging markets	**4.3**	**4.2**	**4.2**
China	6.9	6.6	6.2
India	6.7	7.3	7.4
Russia	1.5	1.8	1.3
Turkey	7.4	3.2	0.3
Kazakhstan	4.0	4.1	3.8

CPI Inflation YoY change, %

Region/Country	2017	2018e	2019f
World	**3.3**	**4.2**	**3.6**
Advanced economies	**1.7**	**2.0**	**2.0**
US	2.1	2.4	2.1
Euro-area	1.5	1.8	1.6
UK	2.7	2.5	2.1
Emerging markets	**4.5**	**5.7**	**4.7**
China	1.6	1.9	2.3
India	3.6	4.7	4.9
Russia	3.7	3.9-4.2	5.0-5.5
Turkey	11.1	16.2	17.8
Kazakhstan	7.4	5.3	4-6

Government gross debt, % of GDP

Region/Country	2017	2018e	2019f
Advanced economies	**103.4**	**102.8**	**102.6**
US	105.2	106.1	107.8
Euro-area	86.6	84.4	82.0
UK	87.5	87.4	87.2
Emerging markets	**48.6**	**50.4**	**51.8**
China	47.0	50.1	53.9
India	71.2	69.6	68.1
Russia	15.5	15.3	15.4
Turkey	28.3	32.3	33.6
Kazakhstan	20.8	17.8	16.8

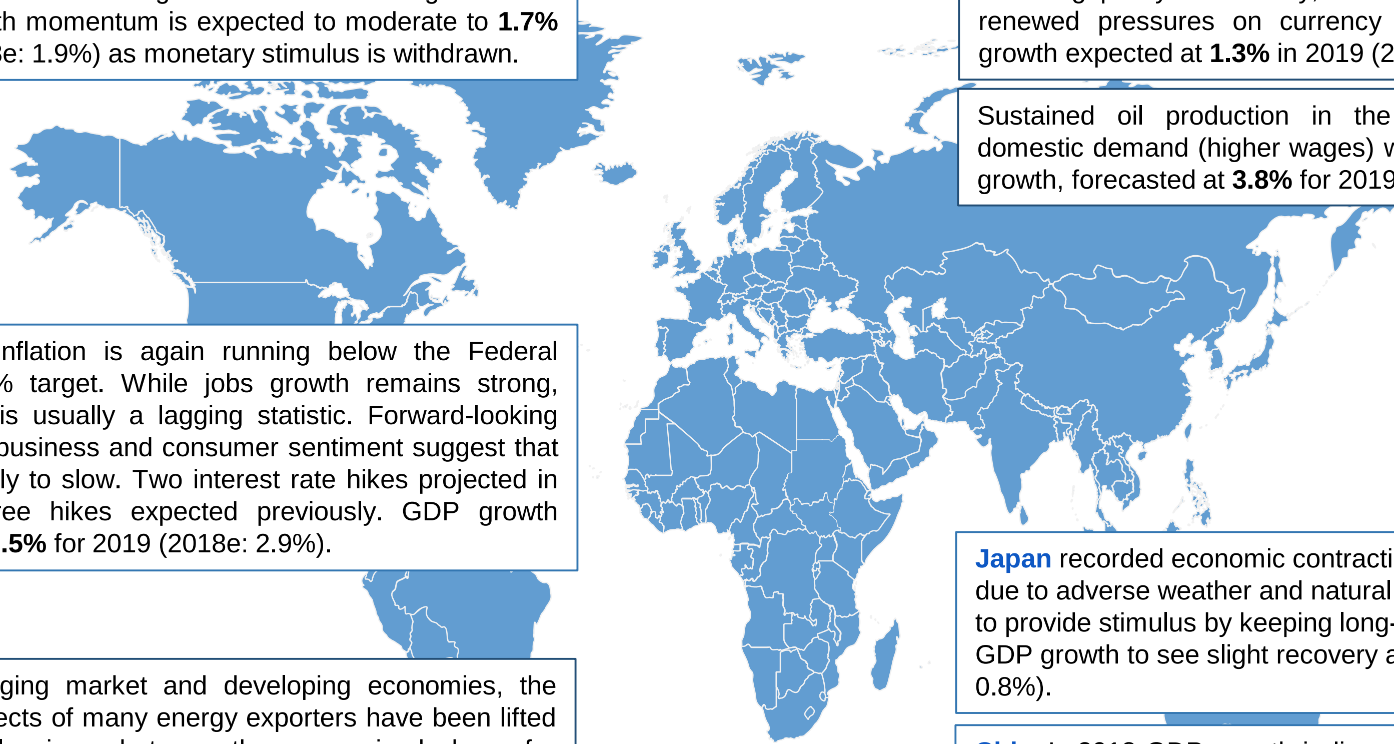
Current account balance, % of GDP

Region/Country	2017	2018e	2019f
Advanced economies	**0.9**	**0.7**	**0.5**
US	-2.3	-2.5	-3.0
Euro-area	3.2	3.0	2.7
UK	-3.8	-3.5	-3.2
Emerging markets	**0.0**	**0.0**	**0.0**
China	1.4	0.7	0.7
India	-1.9	-3.0	-2.5
Russia	2.2	6.2	5.2
Turkey	-5.6	-5.7	-1.4
Kazakhstan	-3.4	-0.2	0.2

Source: GDP and CPI - official Central Banks' projections, where CBs do not provide forecasts – Bloomberg forecast, government gross debt and current account balance – from International Monetary Fund

Snapshot on global economic developments

Downside risks to global growth in the context of rising trade barriers, reversal of capital flows to emerging markets, and tighter monetary conditions. The **International Monetary Fund** revised downward projections for global GDP growth to **3.5% for 2019** (earlier forecast 3.7%), while the **World Bank** maintains a more conservative growth outlook of **2.9% for 2019** (earlier projection 3.0%).



Europe lacks economic energy and the uncertainties associated with Brexit, French protests, German political transition and Italian budget issue are challenges to the region. Growth momentum is expected to moderate to **1.7%** in 2019 (2018e: 1.9%) as monetary stimulus is withdrawn.

In **Russia**, growth has been resilient, supported by private consumption and exports. However, momentum has slowed, reflecting policy uncertainty, recent oil price declines, and renewed pressures on currency and asset prices. GDP growth expected at **1.3%** in 2019 (2018e: 1.8%).

Sustained oil production in the Kashagan oilfield and domestic demand (higher wages) will support **Kazakhstan**'s growth, forecasted at **3.8%** for 2019 (2018e: 4.1%)

In the **US**, inflation is again running below the Federal Reserve's 2% target. While jobs growth remains strong, employment is usually a lagging statistic. Forward-looking indicators of business and consumer sentiment suggest that growth is likely to slow. Two interest rate hikes projected in 2019 vs. three hikes expected previously. GDP growth projected at **2.5%** for 2019 (2018e: 2.9%).

Japan recorded economic contractions in 1Q18 and 3Q18 due to adverse weather and natural disasters. BOJ continues to provide stimulus by keeping long-tern rates near zero. GDP growth to see slight recovery at **0.9%** in 2019 (2018e: 0.8%).

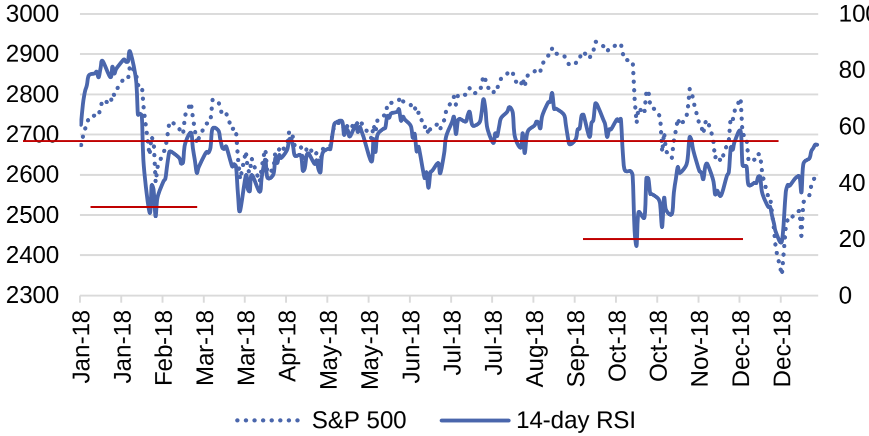
Among emerging market and developing economies, the growth prospects of many energy exporters have been lifted by higher oil prices, but growth was revised down for **Argentina, Brazil, Iran**, and **Turkey**, among others, reflecting country-specific factors, tighter financial conditions, geopolitical tensions, and higher oil import bills.

China's 2018 GDP growth in line with expectations at 6.6% in 2018. Forecast for 2019 is slightly lower **6.2%** due to China is underpinned by fiscal and monetary measures introduced by the government to boost growth.

Source: International Monetary Fund, World Bank, Financial Times

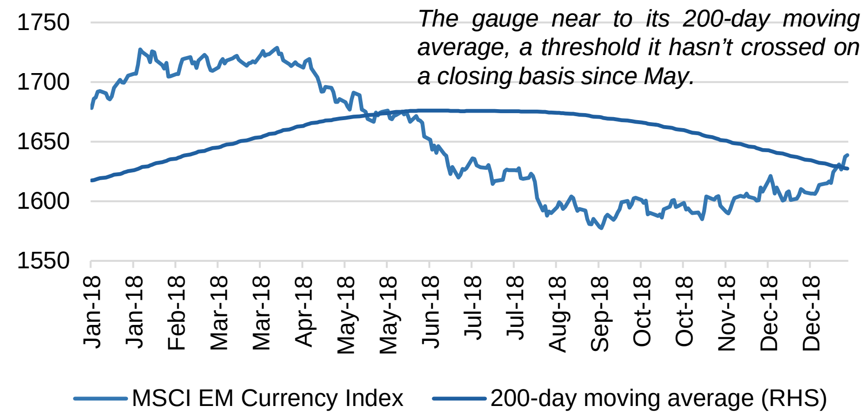
Investors closely watch equity markets that ended lower in 2018 and saw a rebound in early 2019

S&P 500



To confirm that US stocks have shrugged off their recent correction, momentum needs to recover with share prices. S&P Index's 14-day relative strength index showed momentum has rallied back to the critical level of 50 after diverging from prices with 24 December low.

MSCI Emerging Markets Currency Index



Emerging-market assets are getting a lift from renewed risk appetite. An MSCI Inc. index that tracks currencies, which has risen in eight of the past 10 weeks, extended its advance to reach the highest level since July.

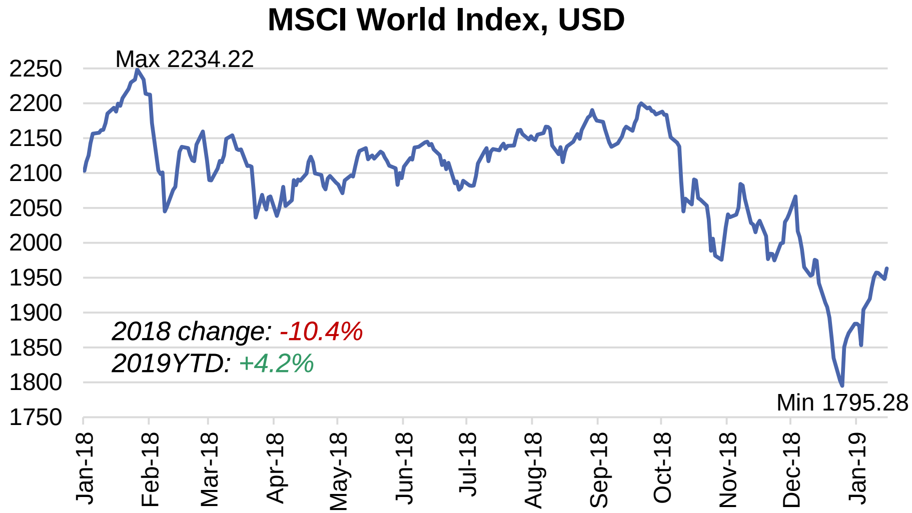
- In 2018, the S&P 500 was down 6.9%, Japan's Topix fell 18%, the Stoxx Europe 600 declined15%, the MSCI Emerging Markets Index dropped 18%. Ten-year Treasury yields rose 36 basis points, to 2.77%. Investment-grade US corporate bonds lost 2.8% and European ones 1.2%. The Bloomberg Dollar Spot Index rose 3.4%. The Bloomberg Commodity Index fell 11%.

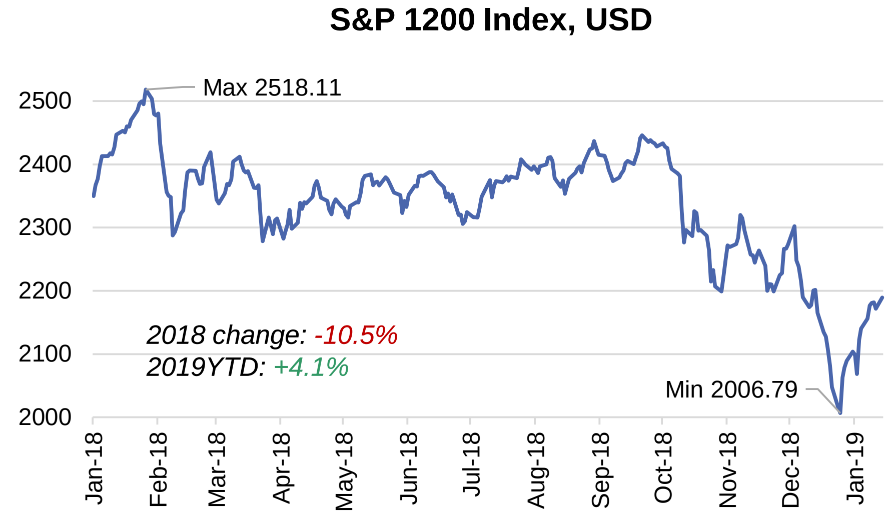
- Although stock markets rebounded in early January on rising optimism over trade talks between US and China, upcoming geopolitical events, lower global economic growth and weaker corporate revenues might spur worldwide volatility.

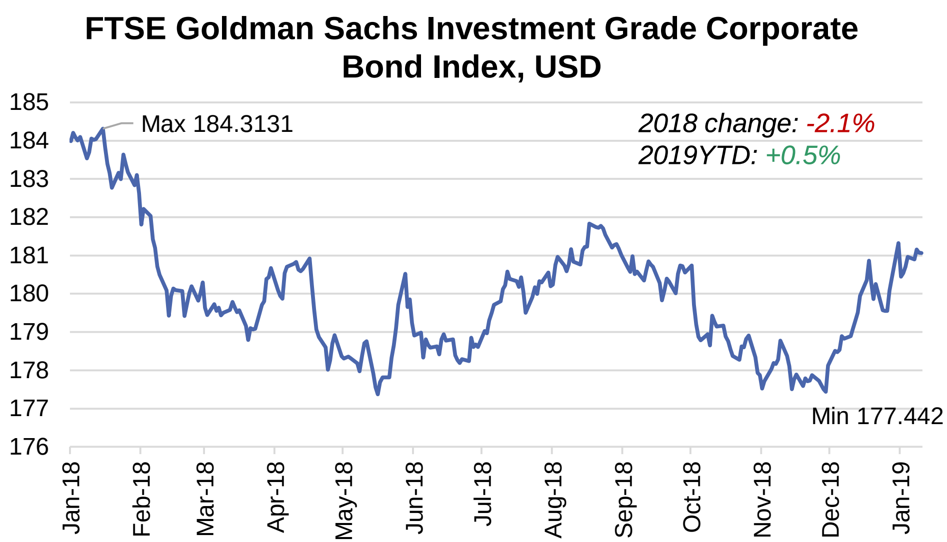
- On S&P 500, Wall Street firms tempering their optimism after US stocks suffered their worst year in a decade. Barclays expect S&P 500 at 2,750 points in 2019, as corporate profits will grow less than expected earlier. Citigroup and BMO Capital Markets forecast 2,850 points and 3,000 points respectively by end-2019.

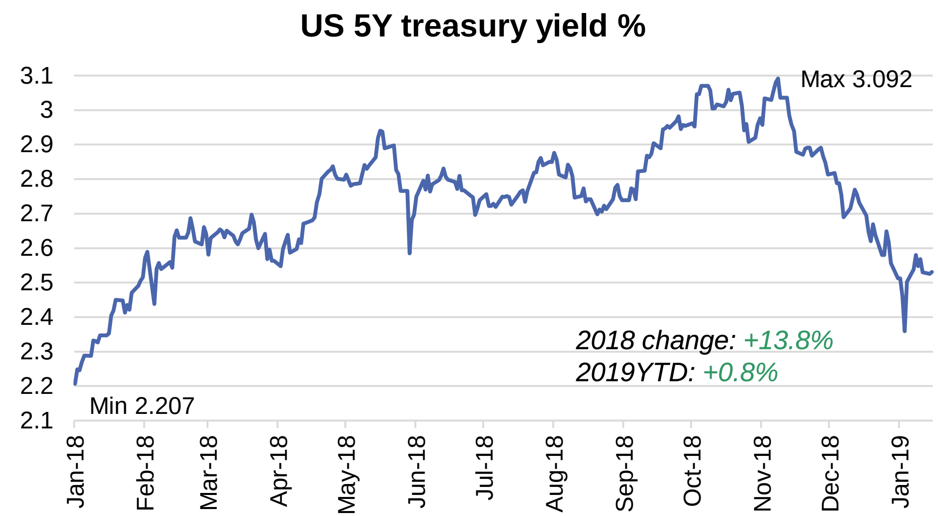
Source: Bloomberg

Global capital market indices





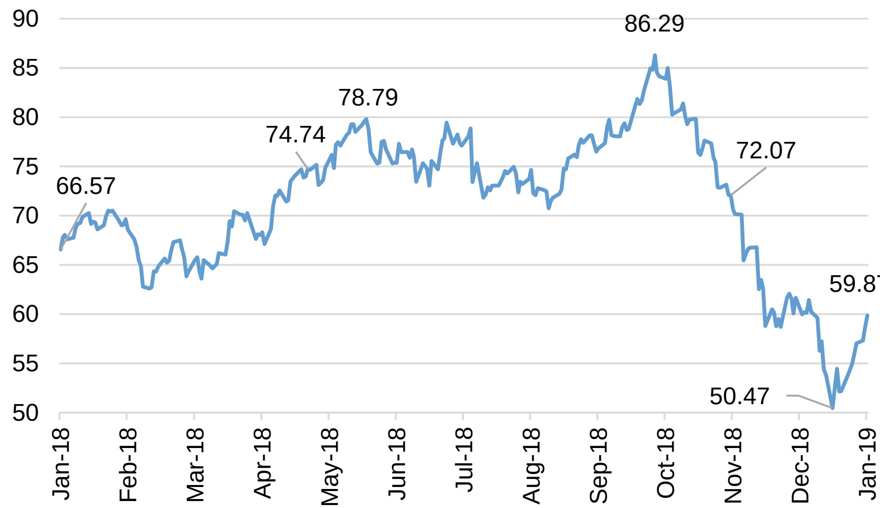




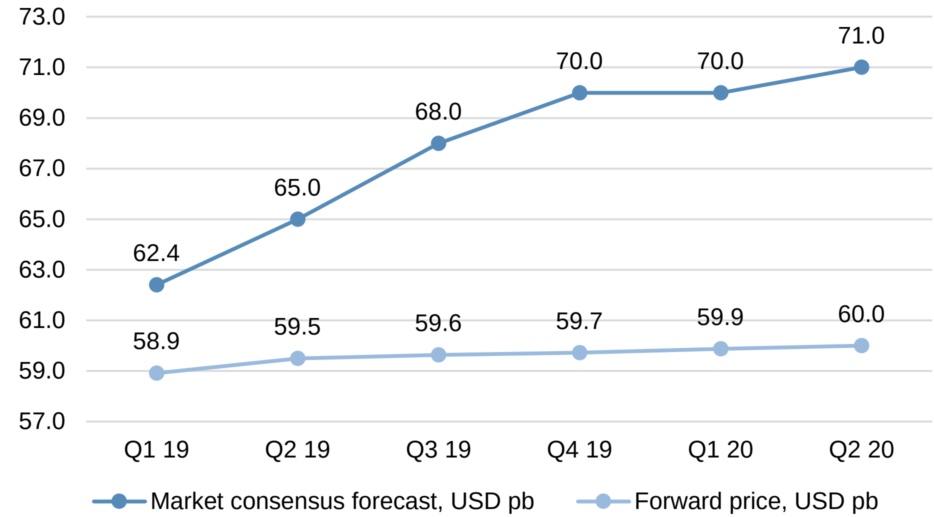
Source: Bloomberg

Lower oil demand is possible in 2019, median forward price for 2019 is USD59.44pb

Brent crude prices from beginning of 2018 to date, USD pb



Brent crude prices short-term forecast as of Jan19



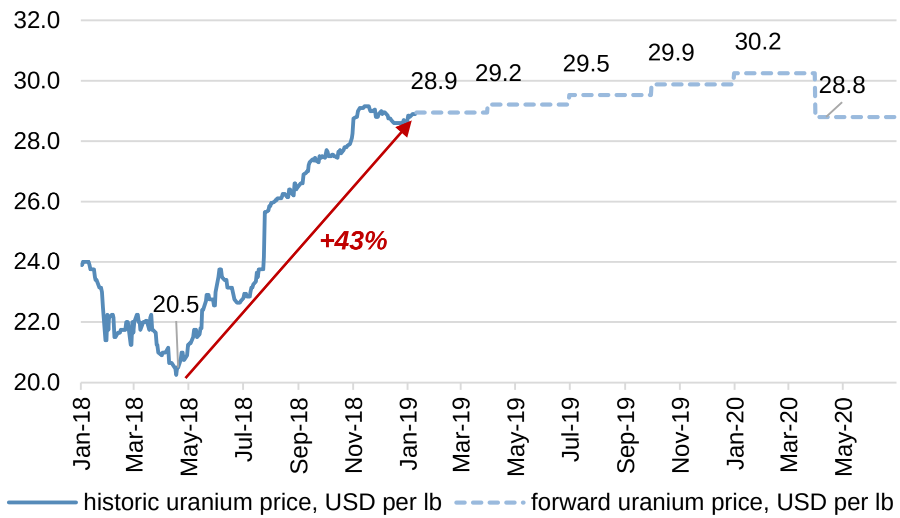
- For first **three quarters of 2018, oil price trend was upward** due to the following factors:
  - ✓ 8 May 18: President Trump signed an executive order to withdraw US from the Iran nuclear deal and will re-impose sanctions on Iran;
  - ✓ Market focused on upcoming US sanctions and speculations on supply shortage pushed crude prices up to their year maximum of USD86.74pb (October 3).
  - ✓ Supply cushion built by OPEC became a challenge after US provided waivers to 8 countries importing Iranian crude oil.
- For the whole **4Q18, oil prices were falling** as market adjusted prices based on fundamentals. Hedge funds and other money managers cut their net long positions in Brent to the lowest levels since Dec.2015.
- Saudi Arabia-led OPEC decided for 1.2mln bpd oil output cuts at its December 6 meeting to support oil prices.
- However, supply from US side is strong and constantly growing. New volumes from US's Permian field are expected to enter the market and to correct supply-demand balance in 1H2019.

- **Lower oil demand forecast possible for 2019.** Consensus has overplayed fears of a crude-oil supply shortfall while not recognizing potential demand erosion, and this is likely to persist in 2019.
- The IEA global oil **demand forecast for 2019** could be cut to **100.4mln bpd** from 100.5mln if trade talk progress stalls during 90-d truce, reflecting damage a trade war would inflict on economic growth.
- The IMF has already cut its real GDP growth forecast for 2019 to 3.7% from 3.9%, and an **extended conflict would effectively stifle nearly 10% of next year's incremental oil demand**. So the risk of lower demand shouldn't be overlooked.
- **Production** across key players Russia, Saudi Arabia and US **remains robust**, and analysts are still less convinced curbs will placate market fears about wider imbalances.
- **2019 median price forecast is USD66.4pb, 2019 median forward price is USD59.44pb**.

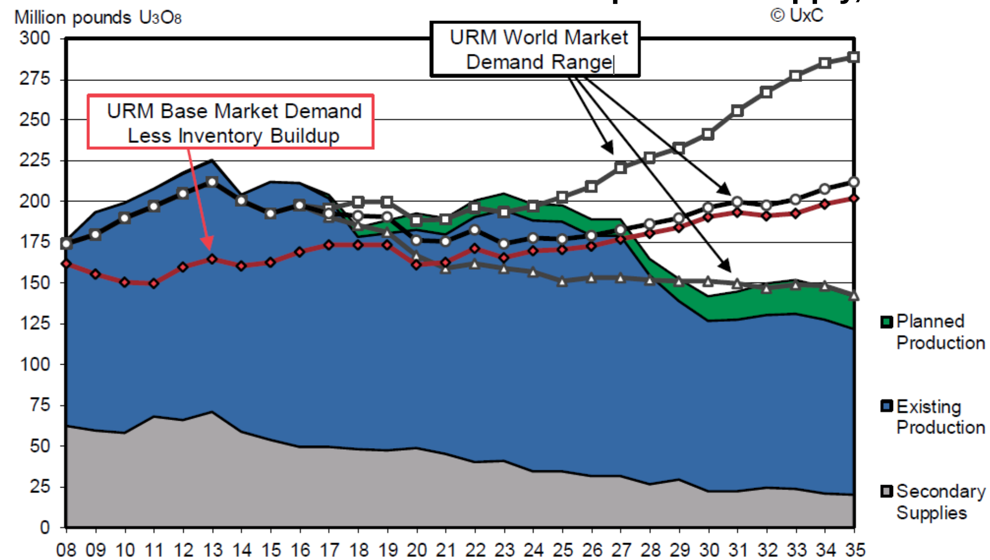
Source: Bloomberg, Samruk-Kazyna

Uranium production cuts by major miners helped to balance the market and supported 43% commodity price increase

Uranium prices surged 43% from 2018's low



Global uranium market demand vs. potential supply, mln lb



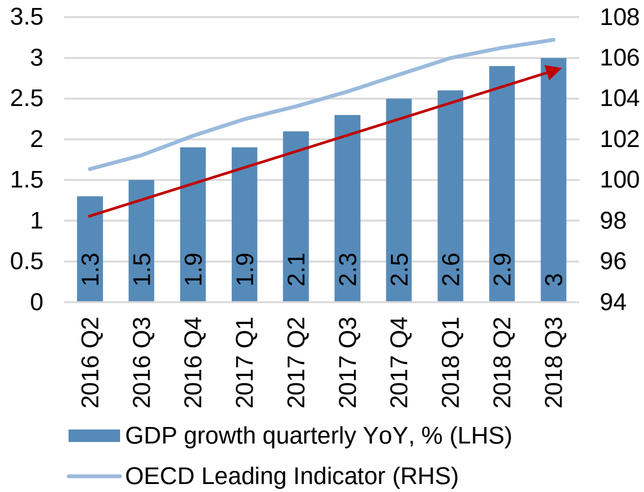
- **Uranium prices surged 43%** since touching last year's low of USD20.25lb in April, due to the combination of decrease in oversupply (as key producers cut output) and higher demand.
- Uranium spot price climbed for seven months through November, the longest run since 2014. Prices hit a **two-year high at USD29.15/lb on 14 November**.
- Uranium prices were last traded at USD28.9/lb on 10 January 2019.
- In the long-term, very few mines will be developed at today's price level, which can lead to the shortages of supply in the long-term.
- According to market research, approximately **50% of mines are still cashflow negative at current prices**. Producers would stop shutting output at USD45/lb and some new supply would come online at USD65-USD75. This, combined with a significant new nuclear power generation capacity being constructed in China and India, may support uranium prices in the longer-term.

- Recent primary production cuts served to realign supply with demand.
- For **2018**, market estimates world uranium production to decline by 19mln pounds to **136mln pounds**, **down 12%** from 155mln pounds in 2017.
- Combined with secondary supplies, **aggregate supply in 2018 is expected to total 184mln pounds**, which is **7mln pounds lower than base case demand estimate of 191mln pounds.**
- Although utility demand is not foreseen improving much in the 3-month forward period due to sizable inventory positions, some **US utilities could seek out US-origin material ahead of the Section 232** decision expected next year. Intermediaries are expected to remain active buyers, but this group is becoming less aggressive on the sell side.
- Base case demand for the **2019-2021** is nearly identical to 2018. For **2019**, utility uncovered requirements are **10.4mln pounds**. For **2020** – **22.8mln**, by 2021, uncovered requirements total 36.2mln pounds.

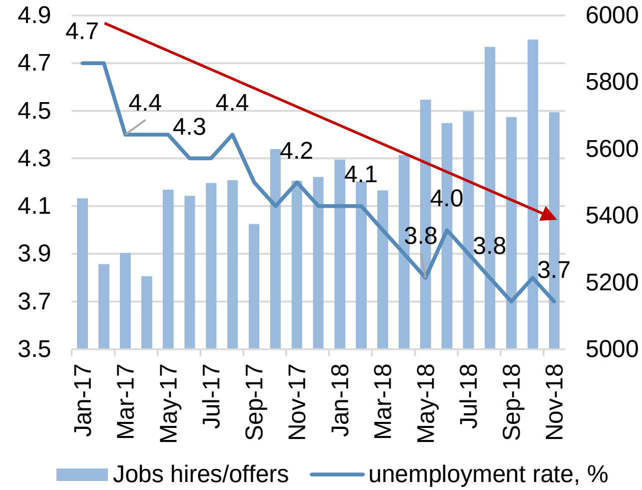
Source: UxC, Bloomberg, Samruk-Kazyna

US economy remains strong, bolstered by pro-cyclical fiscal stimulus and monetary policy

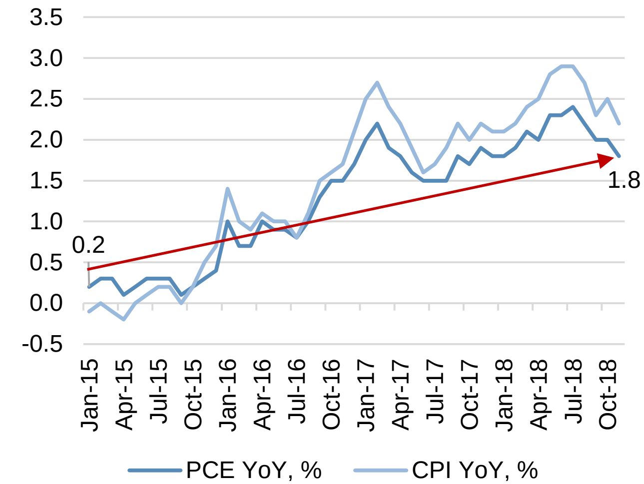
US economy was growing at a strong rate



Unemployment is at a 49-year record low



Inflation is below target level



- US economy was growing strongly estimated at **3.0% for 2018** (2017: 2.3%), and is expected to continue expanding moderately for at least 3 more years, amidst sustained low unemployment and stable inflation.
- GDP growth forecasts for **2019 is 2.3%**, 2% for 2020 and 1.8% in 2021. Long-run forecast is 1.9%.
- Corporate profits are rising strongly. And investment as a percentage of the economy is at about the level of the mid-2000s boom.
- **2018 GDP growth is estimated at 3.0%, forecast for 2019 is 2.3%.**

- Labor market continues to strengthen. During the last 12 months, unemployment rate in US stood at its **49-year record low level**. **Unemployment rate is estimated to fall to 3.7% in 2018** from previous year average of 4.35%, and to fall further to 3.5% in 2019 and 3.6% in 2020.
- Policymakers see 4.4% unemployment rate as the long-run sustainable level. Household spending and business fixes investment have grown strongly during the last 12 months.

- On a 12-month basis (as of Nov 2018), **inflation remains near 2% target**. PCE (personal consumption expenditures, Fed's basic measure of inflation) is estimated at 1.9% for 2018 (2017: 2.1%) and projected at 1.9% for 2019.
- **2018 YoY US' PCE is estimated at 1.9%, forecast for 2019 is 1.9%.**

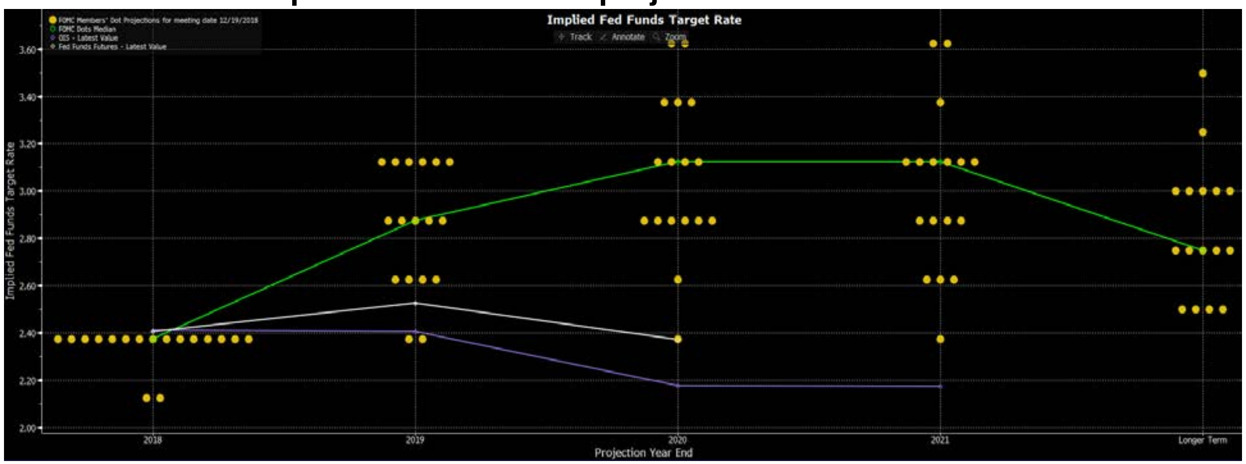
Source: US Federal Reserve, Bloomberg Economics, Samruk-Kazyna

US monetary policy review and outlook

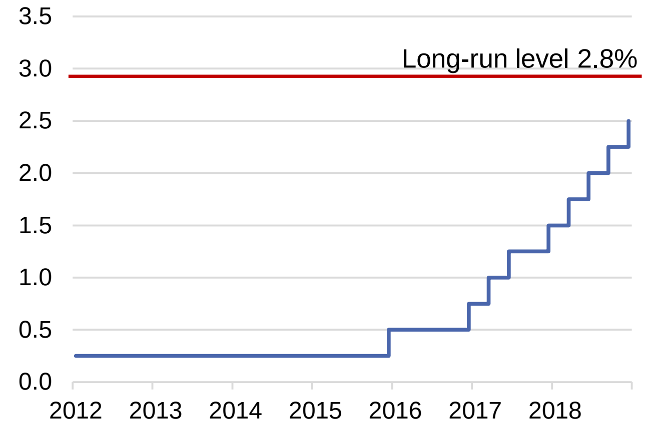
Official Fed's medium-term economic projections on US economy

Key indicators	2018e	2019f	2020f	2021f	Longer-run
Real GDP growth	3.0%	2.3%	2.0%	1.8%	1.9%
Unemployment rate	3.7%	3.5%	3.6%	3.8%	4.4%
PCE inflation	1.9%	1.9%	2.1%	2.1%	2.0%
Federal funds rate	**2.4%**	**2.9%**	**3.1%**	**3.1%**	**2.8%**

Fed's dotplot on interest rate projections as at December 2018



Fed's target interest rate – upper bound %

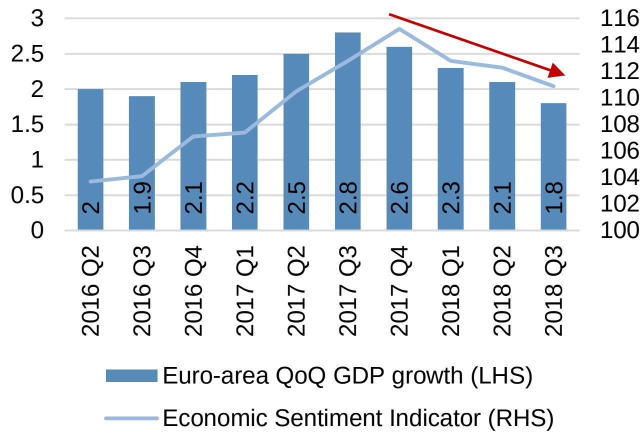


- In 2018, Federal Open Market Committee (FOMC) **raised the target range for the federal funds rate for 4 times** placing it to a range of 2.25-2.5% in line with market expectations and Fed's signals in 1H18. FOMC views the US economy as strong and follows now a **tightening policy**. Global economic risks implications to economic outlook are considered as roughly balanced.
- **Monetary policy outlook:** Fed's policymakers expect **2 rate increases in 2019**, and **1 increase in 2020**. Fed policymakers' median forecast puts interest rate at **3.1% by end-2020.**
- **Implications of anticipated rate hikes by Fed:** 1) spread between emerging and US market premiums will decrease which might lead to outflow of capital from EM, 2) cost of foreign capital for EM countries will go up, 3) pressure on EM currencies and possible increase of policy rates by Central Banks of developing countries.

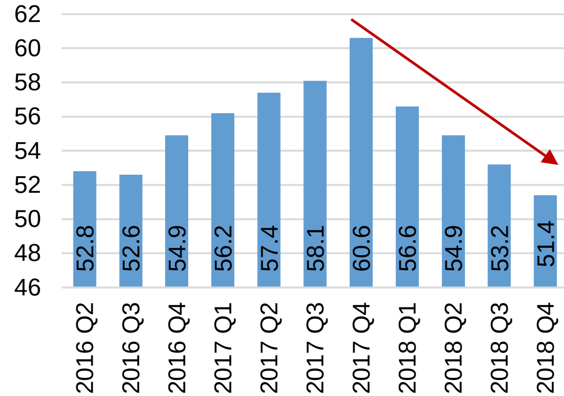
Source: US Federal Reserve, Samruk-Kazyna

Euro-area growth momentum has faded in 2018

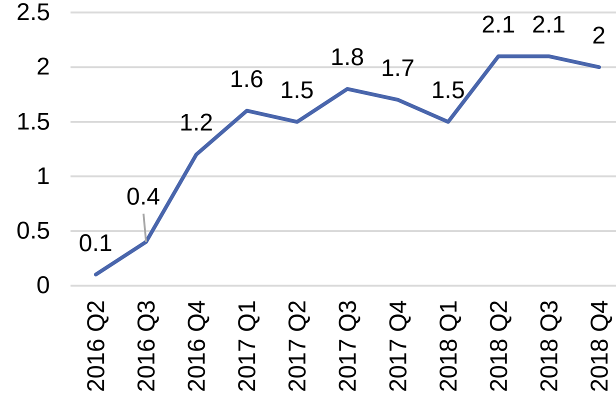
Euro-Area slowing beyond temporary factors



Euro-area PMI points to softer growth



EU-28 quarterly CPI YoY change, %



- The euro-area slowed in 3Q, with growth dipping to 1.8%. Part of the weakness was temporary, but underlying **momentum appears to have ebbed**. Persistent slowdown is a major source of concern to ECB and could **prompt a delay to higher interest rates**.
- Euro-area growth was disrupted by the auto industry in Germany and Italian economies' failure to expand.
- **2018 GDP growth is estimated at 1.9%, forecast for 2019 is 1.7%.**

- The euro-area composite **PMI** (purchasing managers index) **has been falling during 2018**. That confirmed **a loss of momentum in the region** relative to 2017 and suggests the slowdown in 3Q may be more than a blip.
- The survey figures are consistent with growth of around 1.8% in 3Q and poses a clear downside risk to forecast.
- Business surveys across the euro-area all point to a slowdown in growth as the year end approaches.

- EU inflation decreased to 2.0% YoY in 4Q18 from 2.1% in 3Q18. The core figure fell to 1.0% from 1.1% during the same period.
- That will allow the ECB (European Central Bank) to remain calm about the recent slowdown in GDP growth and focus on the **rising wage pressure**, as it ends its asset purchases in December.
- **2018 YoY Euro-area CPI** (consumer price index) **is estimated at 1.7%, forecast for 2019 is 1.5%.**

Source: Bloomberg, Samruk-Kazyna

EU's monetary policy is expected to tighten, economic forecasts are moderate

- **Monetary policy**. ECB interest rates on hold. The tool of monetary policy is now forward guidance over interest rates – by taking the yield curve up and down, the ECB can adjust monetary conditions in the economy. It is reasonable to expect a **small increase in a deposit rate in September 2019**. Lots could happen between now and then – a failure of wage pressure to translate into higher inflation, a blow to trade or a disorderly Brexit could all lead to a delay. A **later rate hike therefore seems more likely than an earlier withdrawal of stimulus**.

Official ECB's short-term forecasts for Euro-area

Key indicators	2017a	2018e	2019f	2020f
GDP YoY change, %	2.4	1.9	1.7	1.7
CPI YoY change, %	1.5	1.8	1.6	1.7
Compensation per employee YoY change, %	1.6	2.3	2.2	3.0
Unemployment rate, %	9.1	8.2	7.8	7.5
Current account, % of GDP	3.2	3.0	2.7	2.6
Budget, % of GDP	-1.0	-0.5	-0.8	-0.7
ECB policy rate (Q4), %	0.0	0.0	0.0*	0.5*
EURUSD (Q4)	1.20	1.15	1.18*	1.22*

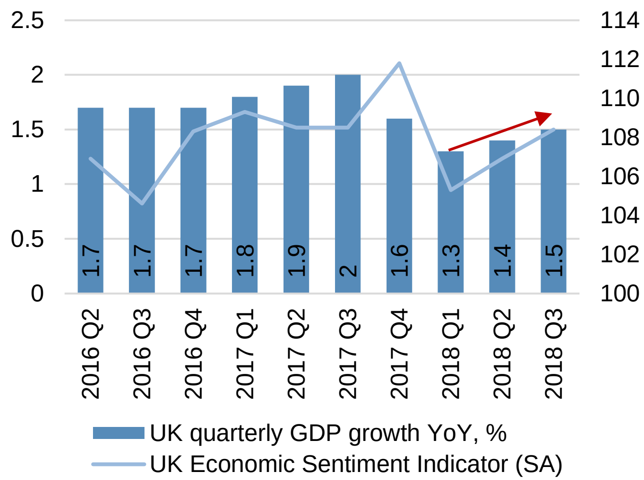
** Bloomberg forecasts (ECB does not provide policy rate and exchange rate forecasts)*

- Higher energy costs are pushing up on inflation (estimate for 2018 is 1.7%), but these will moderate to 1.5% in 2019.
- Robust wages growth is likely to continue in the coming quarters. With labor costs rising, it is only a matter of time before businesses pass these costs on to consumers. A sustained advance in CPI is expected to become more evident toward the end of 2019. In later years, growth will slow.
- The pace of expansion will depend largely on productivity growth, which has been weak, and the aging population is also likely to act as a drag. Once policy tightening begins, a **hike in interest rates is expected every six months**.
- **Next year will see the ECB withdraw monetary stimulus. The biggest risk to the outlook is Italy where there is a budget dispute between Rome and Brussels just as the economy flirts with a recession.**

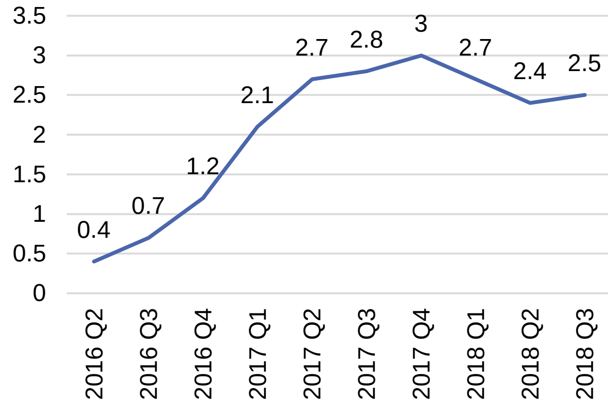
Source: ECB, Bloomberg Economics, Samruk-Kazyna

UK economy is operating at full capacity

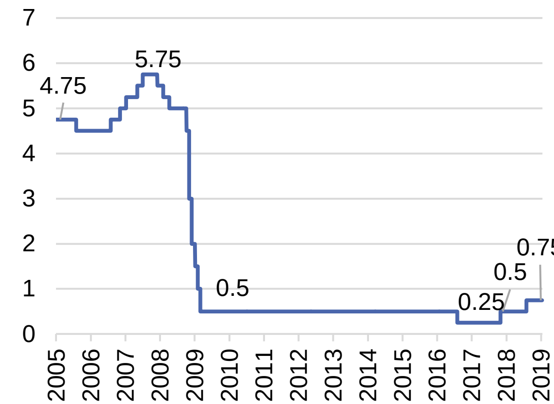
UK economy is operating at full capacity



UK quarterly CPI YoY change, %



Bank of England base rate, %



- Output growth was volatile in 2018. The most recent GDP data suggest the economy expanded above trend in **3Q18 with output advancing by 1.5% YoY**. **Market does not expect gains to persist at the same rate** in the near term as much of the boost came from temporary factors in 3Q18, while uncertainty about the outcome of **Brexit talks is likely to keep a lid on spending growth**.

- **2018 GDP growth is estimated at 1.3%, forecast for 2019 is 1.7%.**

- Having pushed inflation to 3.1% in November 2017 from 0.5% in June 2016, the impact of **sterling's depreciation in the aftermath of the Brexit vote is fading**.
- Inflation is only likely to slow slightly in the near term. Market forecasts inflation will move below target for a time as the hand-off from external to domestic cost pressures takes place. Inflation should return to target in early 2020.
- **2018 YoY UK core CPI is expected at 2.5%, forecast for 2019 is 2.1%.**

- The Bank of England (BoE) lifted interest rates for the first time in a decade in November 2017 and followed up with another increase in August.
- If Brexit is orderly, the BoE expects rates to advance further. Assuming no Brexit shock, another **two hikes are likely in 2019 - in May and November.**
- The BoE suggested that in the very **long term interest rates could rise to between 2% and 3%** in nominal terms.

Source: Bloomberg, Samruk-Kazyna

A Brexit deal could cause UK economy to overheat and likely to be met with two rate hikes in 2019

- **Growth is expected to slow in the near term** as Brexit uncertainty weighs on spending. Assuming the UK and EU agree on a deal this year, the economy should expand above trend given a number of cyclical tailwinds. The boost to the economy is likely to come from three sources - a less restrictive stance of fiscal policy, a real income lift as the rise in the pound associated with a deal helps slow inflation and more certainty about the future.

- The **biggest risk to the outlook is the possibility that UK leaves the EU without a deal**. However, risks exist even in the event of a deal. For example, the world economy may fail to provide as much support to growth as expected. There are also upside risks associated with household consumption potentially outpacing income gains.

- Market expects the economy to slow beyond 2019 as the cyclical tail winds fade and monetary policy is tightened in an effort to bring demand back in line with supply. The weakness of expansion relative to the pre-crisis average of 2.7% largely reflects the fact productivity growth has stagnated since 2008. Brexit is part of that story, too. Leaving the single market is likely to mean the trade intensity of the economy is lower, at least for a time, while weaker migration flows will also weigh on the economy.

Official Bank of England short-term forecasts for UK economy

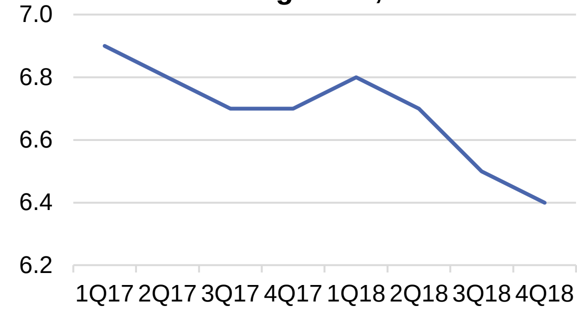
Key indicators	2017a	2018e	2019f	2020f
GDP YoY change, %	1.8	1.3	1.7	1.7
CPI YoY change, %	2.7	2.5	2.1	2.1
Unemployment rate, %	4.5	3.9	3.9	3.9
BOE policy rate (Q4), %	0.50	0.75	1.15*	1.50*
GBPUSD	1.35	1.28	1.36*	1.43*
EURGDP	0.89	0.90	0.87*	0.88*

** Bloomberg forecasts (BoE does not provide policy rate and exchange rate forecasts)*

Source: Bank of England, Bloomberg Economics, Samruk-Kazyna

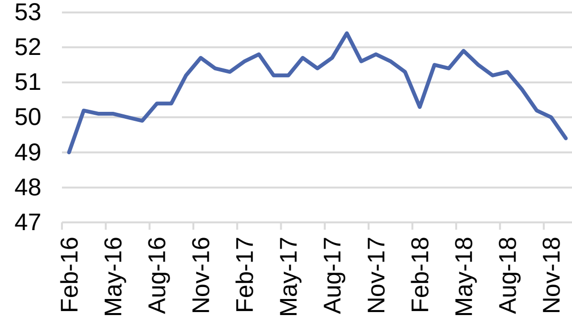
China's GDP growth in line with expectations at 6.6% in 2018, but the economy faces more external uncertainties in 2019

GDP growth, % YoY



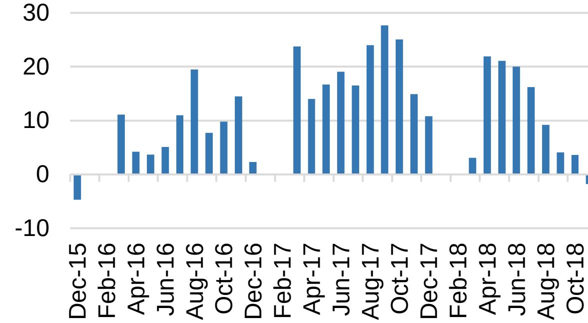
China' GDP growth was in line with expectations at 6.6% in 2018 (4Q18 growth came in at 6.4%), but the economy faces more external uncertainties in 2019.

China Manufacturing PMI SA



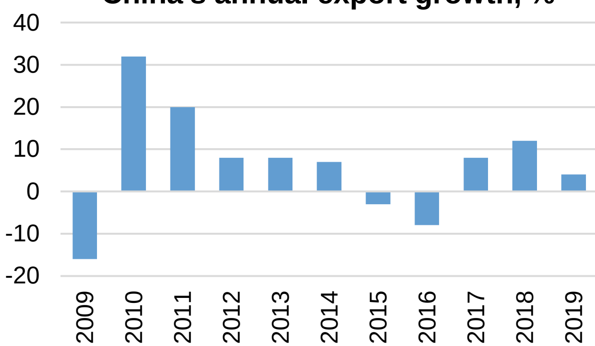
China's official manufacturing PMI, which primarily surveys state-owned groups, came in at 49.4 for December, the first reading below 50-point since July 2016.

China's industrial profits, % YoY



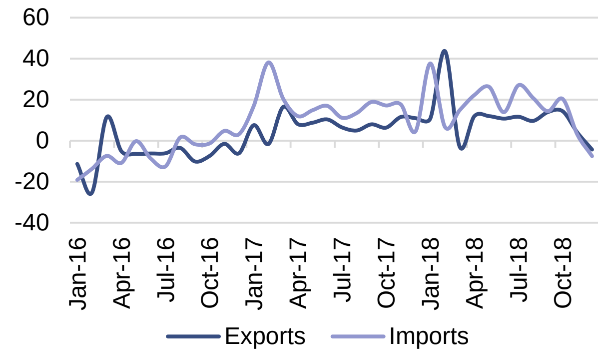
China's industrial profits declined for the first time in almost three years, as the effects of slowing economic growth, falling prices, and the trade war with the US start to surface.

China's annual export growth, %



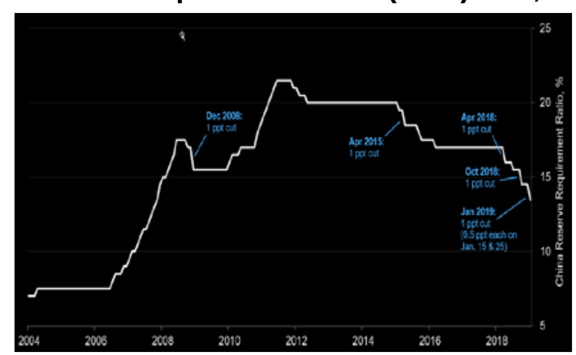
China's export growth will slow to a mere 4% next year amidst ongoing trade tensions with the US. Some 86% of companies affected by tariffs have already reported declines in orders (source: UBS Group AG survey).

China's exports/imports, % YoY



Chinese trade slumped in December, with the unexpected fall in both exports and imports underlining the impact of the trade war and economic slowdown. Exports in dollar terms fell 4.4% YoY, while imports in dollar terms dropped by 7.6% YoY/

Reserve requirement ratio (RRR) rate, %



China's central bank cut the amount of cash lenders are required to hold as reserves by 1 ppt in an effort to support a weakening economy. The RRR cut will be implemented in two steps -- 50bps each on 15 January and 25 January.

Source: Bloomberg, Samruk-Kazyna

Outlook for China's economy is gloomier in 2019

- The **outlook for China's economy is gloomier**. Market players expect GDP growth at 6.2% for 2019 as of 8 January 2019 vs. 6.6% in 2018. The latest PMIs signal real activity faces increasing pressure on the external and domestic fronts. A deteriorating environment abroad, reflected by weak US data and increasing financial market volatility, raises further concern on exports.
- The **impact of Sino-US trade talks will become clearer toward the end of February**. Meanwhile, positive developments on these fronts could mean a policy shift toward longer-term stabilization and reforms from the prevailing focus on stable growth. At present, the outcome of US-China trade talks also remains uncertain.
- China's top leadership highlighted a stance of "Counter cyclical Adjustment" in the Central Economic Work Conference held 19-21 December. This implies the **government is prepared to stimulate the economy by means of a demand-support policy package**, when necessary. The conference emphasized the role of a proactive fiscal policy, promising further tax cuts. Monetary policy was described as "prudent,“ but reference to "neutral" was removed -- suggesting there would be more easing. On 16 January, China has vowed to take action to support its slowing economy with a package of tax cuts for small businesses and higher public spending. Officials stated they would cut taxes “on a larger scale” in order to boost business activity, announced against a backdrop of disappointing industrial production figures and the first drop in car sales for almost three decades.
- The next few months will be crucial to determine the direction of the economy, as the market expects more efforts by the authorities to stabilize growth with the use of broad-based tools, such as further RRR cuts, is likely to be the method of choice. **There may be further general cuts in the reserve requirement of 100bps in 2019, as well as more targeted reductions in the RRR**, according to market expectations.
- **Market players view that monetary easing, combined with slowing growth and continued uncertainty about the trade talks will add downward pressure on the yuan**. On 7 January, USDCNY settled at 6.851, having weakened by 5.1% vs. 3 January 2018. For 1Q19, market players expect USDCNY at 6.94 (2Q19: 6.9, 3Q19: 6.85, 4Q19: 6.83), according to market consensus as of 8 January 2019.

Official National People Congress' short-term economic forecasts for China

Key indicators	2017a	2018a	2019f	2020f
GDP YoY change, %	6.9	6.6	6.2*	6.0*
CPI YoY change, %	1.6	1.9	2.3*	2.3*
Unemployment rate, %	3.9	4.5	4.0*	4.0*
1-year best lending rate, %	4.35	4.35	4.30*	4.25*
USDCNY	6.51	6.88	6.85*	6.70*

** Bloomberg consensus (NPC does not provide forecasts)*

Source: Bloomberg, Samruk-Kazyna

US sanctions sent the ruble tumbling in 2018, market players expect another round of geopolitical shock in coming months

USDRUB vs. USDKZT

- Due to the US sanctions in 2018, Central Bank of Russia suspended purchases of FX for the sovereign wealth fund to take some heat off the ruble and the Finance Ministry had to limit issues of new debt amidst rising yields. Russia's central bank resumed buying FX in January.
- **Fresh US sanctions are still on the way for Russia**. Pressure is rising in the US Congress for yet more restrictions, including a ban on purchases of new sovereign debt and strict limits on state-run lenders. The most draconian measures are on the back burner until at least the first few months of 2019. Market players expect only a mild impact, but a shock could rattle the ruble.
- However, **market players expect uncertainty around US sanctions to ebb by 2H19**. A boost from fiscal spending could arrive around that time. All of these should help growth rebound to an above-trend pace, absorbing most of the slack in the economy by end-2020.

Source: Bloomberg, Samruk-Kazyna

Russia's economy remains on course for expansion, but the pace is slower and risks are intensifying

- **Russia's economy remains on course for expansion, but the pace is slower and risks are intensifying**. GDP growth was at 1.8% YoY in November, compared with a 2.8% YoY in October and 1.5% in 3Q18. The Finance Ministry expects GDP growth at 1.3% for 2019.
- **Policy makers have taken steps to make the economy more resilient to shocks** - floating the ruble, targeting inflation and channeling energy revenue into reserves. President Putin has also promised to boost spending on infrastructure, healthcare and education. The market views that **deeper reforms are needed to avert stagnation**.
- **There is potential for an even sharper rebound in inflation than market players expect. If fresh sanctions materialize to rattle the ruble, that is almost assured**. Inflation breached CBR’s 4% target in December. Much of the pick-up to 4.2% has reflected ruble depreciation, a spike in fuel prices and unfavorable annual comparisons, particularly in food products. An increase in the value-added tax rate on 1 January should add another percentage point to headline price growth. CBR forecasts annual inflation to be 5-5.5% by end-2019 and its return to 4% in 2020. Meanwhile, market players expect the headline rate reaching 5.6% in January and peaking above 6% in March.
- **A certain tightening in monetary conditions is still ongoing**. On 14 December 2018, CBR decided to raise the key interest rate by 0.25% to 7.75%. Potential capital outflow from emerging markets coupled by geopolitical factors might enhance volatility in financial markets and affect exchange rate and inflation expectations. CBR Board of Directors will hold its next key rate review meeting on 8 February 2018.

Official Russian Central Bank’s short-term economic forecasts

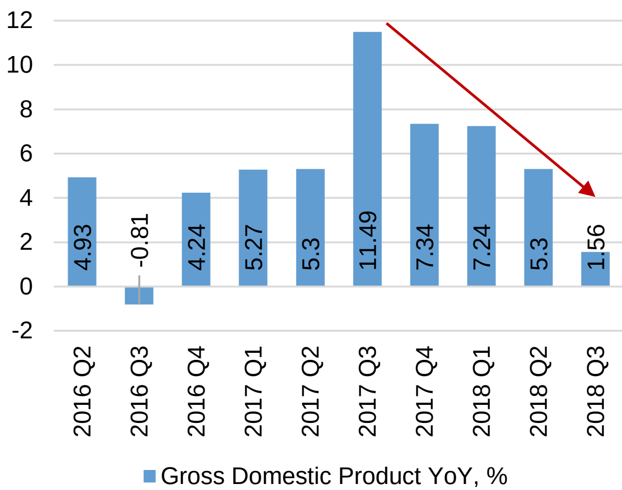
Key indicators	2017a	2018e	2019f	2020f
GDP YoY change, %	1.5	1.8	1.3	2.0
CPI YoY change, %	3.7	3.9-4.2	5.0-5.5	4.0
Unemployment rate, %	5.2	4.8*	4.8*	4.8*
Key rate, %	7.75	7.75	7.1*	7.05*
USDRUB	57.69	69.35	67.0*	66.5*

** Bloomberg consensus (RCB does not provide forecasts of key rate and exchange rate)*

Source: Central Bank of Russia, Bloomberg, Samruk-Kazyna

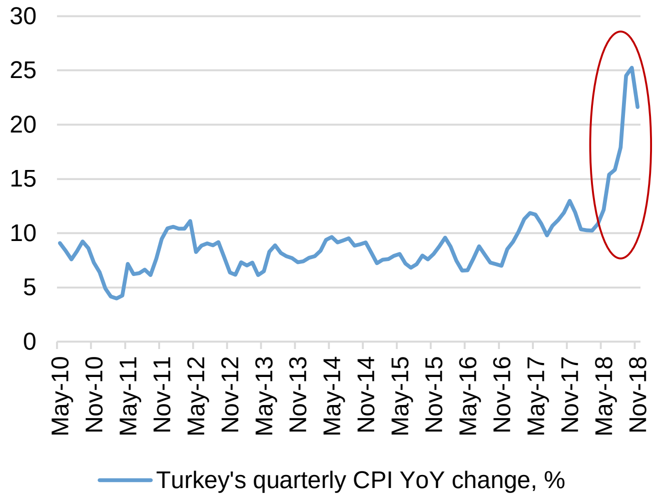
Turkey's economy is battling serious issues, consensus forecasts slower growth, higher Inflation

Turkey's economic growth slowed in 2018



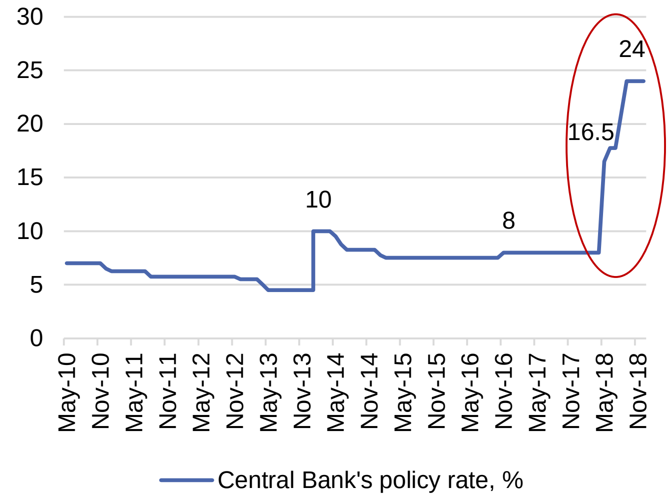
- Turkey's economy slowed sharply in 2Q, even before the worst of the currency crisis has been felt. Much of the depreciation came toward the end of the quarter and in 3Q.
- Turkey was among the fastest-growing economies in 2017, but this could not last. The **expansion was driven by excess government spending and rapid credit growth**, which led imports to swell and current account deficit to balloon.
- A combination of higher US interest rates and Turkey **President's meddling with monetary policy caused investor confidence to evaporate and the currency to plunge**.
- **2018 GDP growth is estimated at 3.2%, forecast for 2019 is 0.5%.**

Turkey's inflation screams crisis



- Turkey's **CPI rose by 25.24% in Oct.2018** – its highest reading since Sept.2003. The figure, driven by a run on the lira, forced the central bank to **hike policy rates 3 times in 2018**.
- The country's **currency lost a quarter of its value against the dollar** in August, driving up price of imports and, in turn, consumer costs.
- **2018 YoY Turkey core CPI is estimated at 16.3%, forecast for 2019 is 18.8%.**

Central Bank lifted rates to tame inflation



- The Central Bank of Turkey lifted the main repo rate to 24% on Sept. 13 from 17.75% (475 b. p. up). CB restored access to main repo window.
- Stemming the rout in the lira will prevent import costs from being driven up further and spare some businesses, who have borrowed in dollars, from collapse. Paradoxically, **higher rates now could mean lower rates later if the crisis fades.**

Official short-term economic forecasts for Turkey

Key indicators	2017a	2018e	2019f	2020f
GDP YoY change, %	7.4	3.2*	0.3*	2.9*
CPI YoY change, %	11.1	16.2	17.8*	12.8*
Unemployment rate, %	10.9	11.2*	12.3*	12.1*
1 week repo rate (eop), %	8.0	24.0	19.25*	15.25*
USDTRY	3.8	5.3	6.2*	6.3*

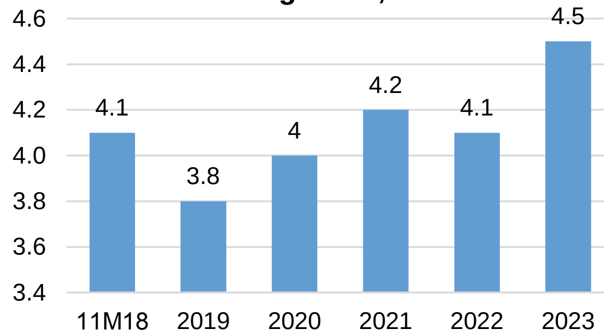
** Bloomberg consensus (Central bank does not provide forecasts)*

Source: Bloomberg, Samruk-Kazyna

Oil output growth stabilizes from 2018 onward, Kazakhstan's GDP growth will stabilize over the medium-term

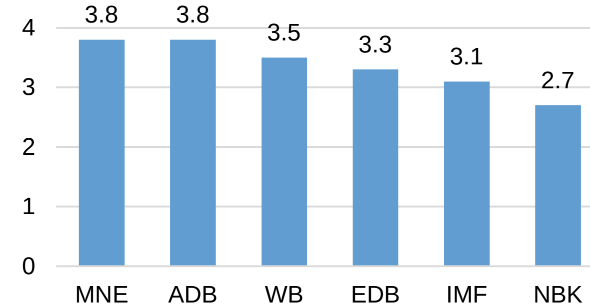
GDP growth for **2018** was at **4.1%**, according to pleminiraly estimates. In 2018, industrial production rose by 4.1% YoY with **mining sector showed a 4.6% increase**. Manufacturing industry experienced a 4% growth. Growth of utility sector was mixed with electricity, gas, steam and air conditioning increasing by 2.4%, and water supply, sewage sector declining by 1%. Key commodities, including crude oil, natural gas and metal ores, showed a positive growth dynamics, and production of food, tobacco, oil refining, chemical products, rubber and plastic products, the metallurgical industry and mechanical engineering also showed an increase.

GDP growth, %



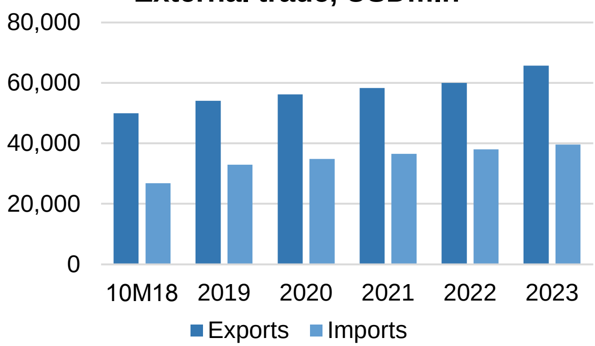
MNE and multilateral institutions expect lower GDP growth of 3.4% (median) for 2019, reflecting moderate oil price projections.

GDP growth 2019 estimates, %



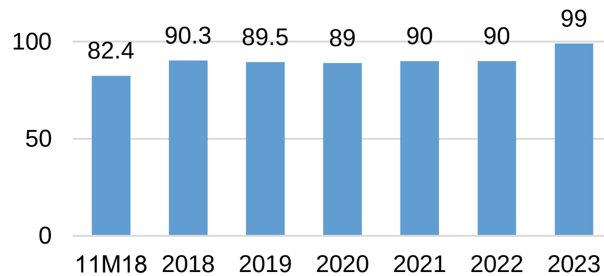
In 2019, consumer demand and overall economic growth are depended on the implementation of the state's social and economic policies aimed at increasing the population's income.

External trade, USDmln



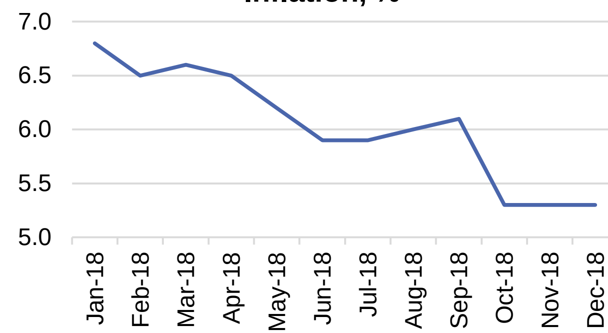
Exports are expected at USD54bln in 2019 (11M18: USD50bln). Growth of exports is expected to be mainly driven by oil and gas condensate production at the Kashagan oilfield.

Oil and condensate production, mln tons



Kazakhstan's oil and condensate output was estimated to have risen to 90.3 mln tons in 2018. The country's oil exports seen at 71.5 mln tons in 2018. Energy minister expects 2019 output at 89.5 mln tons.

Inflation, %



Inflation remains within the corridor of 5–7%. Inflation is forecasted to enter the new target corridor of 4-6%, close to its upper boundary in 2018. In 1H20 inflation will continue to ease gradually.

Source: Statistics Committee of Kazakhstan, various market sources

Snapshot on market sentiment for 2019

"The **next recession is somewhere over the horizon**, and we are less prepared to deal with that than we should be . . . and less prepared than in the last crisis in 2008 … Given this, countries should be paying attention to keeping their economy on a level trajectory, building buffers and not fighting with each other." - International Monetary Fund.

The World Bank warned that "a number of developments" could act as a "**further brake" on economic activity**. These range from a "sharper tightening of borrowing costs" to "past increases in private and public debt" to "intensifying trade tensions" which could "disrupt globally interconnected value chains" - World Bank.

The world economy seems to be heading **into just a mild cyclical slowdown**. Far more important is the adverse **longer-term structural and cyclical context** because it makes any short-term swing far more perilous.
Differential productivity trends, and the long-term debt cycle have made the world economy fragile.
The political and **policy instability**, combined with the exhaustion of safe options for credit expansion would make handling even a limited and natural short-term slowdown potentially so tricky - Financial Times.

Key uncertainties include the trajectory for Fed tightening and its impact on emerging markets, the intensity and economic fallout from US-China trade wars, and the economics - and politics - of tighter financial conditions in the euro zone. The **year ahead probably won't bring the end of the cycle, but risks are growing and new sources of fuel are needed** – Bloomberg.

"**Productivity**" should be viewed as a shorthand way of summarizing the shifts in global economic power, widening inequality, collapse in employment in manufacturing, rise of the digital economy and the "savings gluts" of past decades - Financial Times.

Lower economic growth is very different from a recession. The risks stem largely from **sentiment**, and from **politics**: (1) market jitters lead companies and consumers to cut back spending and investment earlier than they otherwise would, so accelerating the slowdown, (2) political risks (turbulence in the Eurozone, a disorderly UK exit from the EU, escalation of the US-China trade war) – Financial Times.

Source: Financial Times, International Monetary Fund, World Bank, Bloomberg

Summary of potential opportunities and challenges for 2019

- 1st largest world economy, **US**, is **performing strongly and 2019 outlook is positive**. 2nd largest economy, **China**, **takes extensive measures to support the economy and growth momentum**. This will support global economic growth and commodities demand.
- US and China hold 90-day trade negotiations until March, both sides provide signs of progress to **resolve trade dispute** and ease pressure on global economy and financial markets.
- Moderating exposure of Kazakhstan to fluctuations in biggest trade partner's economy: **Russia remains on course for expansion**, however at a slower pace; policymakers have taken steps to make the economy more resilient to shocks.
- **OPEC+ coordinated output cut** is expected to **stabilize oil prices in 2019**.

- **Global economy slowdown, which might lead to weaker demand for commodities, including for oil**.
- **Geopolitical tensions**: possible new sanctions on Russia, unresolved US-China trade dispute, Iranian sanctions.
- **Emerging markets exposure** to outflow of capital and volatile commodity prices.
- Due to strong performance of US economy Fed is likely to hold 2 rate hikes in 2019, and one increase in 2020, which might cause tighter financial conditions, **increase of cost of capital and pressure on tenge.**
- Uncertainties associated with Brexit, French protests, German political transition and Italian budget issue mean **EU and UK markets and currencies might be volatile.**

Source: Samruk-Kazyna

Possible implications on Kazakhstan of 2019 potential events

Commodities

- Anticipated decrease of global economy growth, consequent decline in demand for commodities, including oil and gas, coal, metals, increase Kazakhstan's exposure to volatile commodity prices.

US' protectionism trade policy

- "232 Investigation" is one of the US initiatives in the frames of protectionism trade policy. After results of investigation in April 2019, US President has the right to impose sanctions on any amount of KAP's uranium import to US without any additional alignment with other US authorities.

US Fed's policy

- 2 anticipated rate hikes by Fed in 2019 will increase cost of capital for Kazakhstan and pressure on tenge. National Bank of Kazakhstan might decide to increase base rate as a measure to counter foreign capital outflow.

Geopolitical tensions

- Sanctions on Russia and Iran will continue to affect Kazakhstan and the Fund's operations. The ruble remains highly sensitive to potential new legislation from the US. USDKZT dynamics closely mirrors USDRUB trends (close to 5.6), affecting Samruk-Kazyna's long-term financial sustainability. On corporate level, sanctions affected SE, KTZ, KMG to the most extent compared to other PCs.

Brexit

- According to EY, financial services companies confirmed transfer of ~GBP800bln of assets from the UK to Europe since 2016 referendum on EU membership, while operations and staff also continue to move across to Europe. In the longer-term, London may lose its position as a leading financial center to European markets, and also its function as a gateway to the EU single market. Currently, there are 3 Kazakhstan's companies listed in LSE (Kazatomprom, Kcell and Halyk Bank). Brexit outcome could have implication on future listing considerations for KZ companies.

Source: Samruk-Kazyna

Market moving evets of 2019

January – February 2019	March – April 2019	May – December 2019
US government shutdown	**March 1** – 90-day negotiation window ends	**May** – oil sanctions waivers expire
Late Jan. next round of US-China trade negotiations	**March 20** – FOMC meeting	**May 23-26** – EU parliamentary elections
January 24 – ECB meeting for policy rate decision	**March 21-22** – last EU council for UK	**June 6** – ECB meeting
January 22-25– World economic forum	**March 29** – Brexit day	**May 1, June 19** – FOMC meeting
January 30 – FOMC meeting	**March 31** – end of China tariff suspension on US autos and parts	**June 28-29** – G20 summit
February 17 – section 232 deadline	**March 31** – local elections in Turkey and Ukraine	
	April – OPEC+ meeting	

Source: Samruk-Kazyna

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