

# MACROECONOMIC REVIEW

## 01 – 06/2007

### 1. UZBEKISTANS ECONOMY - A BRIEF OUTLOOK

In the first half of 2007 Uzbekistan's GDP grew to a total of 10115,6 billion sum (approx. US\$7,99 billion, at an exchange rate of 1,265.49 sum for one dollar). According to government estimates in absolute terms this equals a growth by 9.7 percent in comparison with the appropriate period of previous year. Potential currency affects taken into account hint on a growth of approx. 6.2 percent, which is closer to more prudent forecasts of leading intelligence services (approx. 5.9%). The growth of industrial production was put at 11.6 percent (third highest in the CIS). The trade surplus amounted to US\$1.7 billion. When looking into Uzbekistan's economy it should be noted, that Tashkent region stands for approx. 22 percent of investments, 26 percent of industrial output and 37 percent of privatized enterprises, where on the contrary, 83 percent of all enterprises (out of a total of more than 460,000) are located in the regions. In particular the dominating part, approx. 90 percent, of the large number of private farms (more than 180,000 in total) is located in semi-urban or rural areas.

Economic and industry indicators, as reported by the Government of Uzbekistan, are summarized in the following table:

**Table 1: Main indicators**

Indicator	Volume, %, number(s)	Comments
Population	26,84 million	
GDP growth	9.7 %	6.2 %, US\$ affects considered
GDP sector distribution	-industry 25.9% -agriculture 11.8% -construction 6.7% -transport/communication 11.3 -trade 10.8%	Only very slight deviances from previous period (on the average 0.7%)
Number of privatized enterprises	281	281 presumed to include a variety of pure asset sales. Tashkent region absorbs > 37% of privatization projects.
Total number of enterprises	422,958	-farming 271,669 -manufacturing 21,425 -trade 49,496 -construction 14,944
Share of small and medium enterprises (SME) in the economy	38.1%	-44.9% individ. entrepreneurs, one third (34.9%) micro enterprises -SMEs supposed to stand for > 70% of employment
Industrial output	UZS8,566 billion (US\$6,7billion)	-machinery/equipment 14.7% -metal and steel 18.7% -food 8.4% -chemical products 5.0% -textile 15.6% -oil and energy 27.2% -construction materials 4.5%
Investments	-commitments: 2,361 billion sum (US\$1,865 billion) -investments carried out: 521 billion sum (US\$412 million)	-55% financed out of enterprises' own funds -13.9% government funds -19.8% foreign investments or foreign credit lines
Cotton output	656,074 tons	-Decrease of 8,6 thousand Tons (compared to 07/2007) -about 1,44 million hectares of land in use for cotton (approx. 41% of crop land)

<b>Foreign investment distribution</b>	-34.8% oil, fuel and energy -39.8 transport/communication -7.3% food/beverages	Transport/communication also dominated in 2006, oil/fuel up from 9.8%, light industries, second in previous period, down from a share of 14.6 to just about 6%. Food industries gained slightly.
<b>Foreign Trade (overall)</b>	Exports: US\$4,12 billion Imports: US\$2,47 billion Trade surplus: US\$1,65 billion	Main trading partners: -28.8% of trade with Russia -8.8% Kazakhstan -6.3% Ukraine -5.8% Turkey -5.5% China -5.4% Iran -4.5% Korea
<b>Export/import distribution</b>	Main export items: -metal/machinery 21.9% -energy, oil 19.8% -cotton 16.7%	Main import items: -machinery/equipment 44.4% -chemical products 14.8% -food/beverages 8.0%

Source: Statistical review 01-06/2007, State Committee of Statistics, own calculations

Published figures for inflation, 2.7 percent, should be seen against the background of recent hikes for minimum wages and public transport (both about 25 percent) or rising gasoline prices (17-22% depending on quality). These factors indicate inflation to be significantly above government's officially reported figures. Unnamed sources hint on two-digit inflation to still prevail (presumed around 15%). GDP growth figures should be assessed against the background of an existing shadow economy. An eventual channelling of shadow money flows into the "official" economy may suggest GDP growth affects. In addition, for industrial output statistics of state-owned enterprises, upside estimates might rather be the rule than the exception.

Also when taking into account presumed presidential elections at year's end, substantial changes in government policy are not expected. Security and economic ties with Russia and China may intensify. 2007/2008 will be characterized by further GDP growth. Whilst the IMF emphasizes the need to further reform, i.e. trade liberalization (Uzbekistan has currently WTO-observer status), flexible currency exchange or a strengthening of the banking sector, an overall stable Uzbek economy in the mid-term has been predicted. This outlook can be sustained by optimistic export expectations and a subsequent trade surplus for the country. A worldwide projected rise in raw materials of eight percent has been taken into account. The forecasts for cotton prices - Uzbekistan being one of the largest cotton exporters - are, however, sketchy at best. Some outlooks on the cotton industry presume rising prices (up to 14 percent), while more conservative estimates consider price volatility due to unsold inventories. Recent weather conditions in the USA have triggered upward prices. Crop prices on world markets are significantly influenced by China, which is both, the biggest consumer and producer. Higher outputs in China accordingly caused a slight fall in price (currently around US\$292 per bale, 15 percent above the 2006 price level). Estimates for gold, one of the main export items of the country presume the gold price to be steady, whilst Newmont, a leading gold mining corporation, puts very optimistic price expectations for the ounce even at US\$1,000. It should be noted, however, that international economic news agencies (such as Thomson Financial) hint on a potential trend change in commodity prices. This refers in particular to copper and nickel, but also gold is supposed to suffer from some volatility.

The risk for a dramatic depreciation of the sum is considered low. The depreciation of the sum against the dollar is likely to occur at slow pace (around 5% in the mid-term). 'The Economist' forecasts further rising investments in the country by energy corporations and an increasing demand-effective government spending. On the downside, analysts view a slow progress in reforms and the tendency to underestimate inflation risks (e.g. the IMF's own calculations for the previous period put the inflation rate at about 15 percent).

The following table highlights conclusively changes in selected economic indicators:

**Table 2: Selected indicators - changes occurred, figures in billion sum (if not marked otherwise)**

Indicator	Period 01-06/2006	Period 01-06/2007	Changes (absolute)	Comments*
Industrial output	7,675,7	8,566,7	11.6%	8.0%
Agricultural output	3,298,4	3,479,9	5.5%	2.1%
Construction works	900,24	1,084,8	20.5%	16.6%
Exports	2,970,7	4,129,4	39.0%	34.5%
Imports	2,258,3	2,472,9	9.5%	6.0%
Exports/imports to/from CIS countries	1,137,8 / 931,1	1,980,9 / 1,288,6	74.0% / 38.3%	-Significant growth of exports -slight imports increase
Export/imports to/from none-CIS	1,833,4 / 1,326,7	2,148,5 / 1,184,3	17.1% / (10.8)	-reduced imports from none-CIS states
Registered unemployed population (in thousands)	33,2 thousand	29,1 thousand	(12.4%)	Official data suggests a decrease in unemployment. Reliable data on the labor market does not exist, however → large „Informal sector“
Share of enterprises with foreign participation (in % of total enterprises)	0.9%	0.9%	+/-	Steady share of foreign partnerships (less than 1% only)
Cotton fibre (share in total exports)	22.8%	16.7%	(27%)	Reduced impact of cotton in overall exports. Represents about 30% of total trade with CIS countries and roughly 10% of exports to none-CIS
Light industry output	1,195,0	1,339,7	12.1%	8.5%
Chemical, petrochemical products	361,7	435,2	20.3%	16.4%
Metal industries	1,608,6	1,606,1	(0.16%)	(3.3%)
Vehicles (pieces)	63,750 pcs.	82,876 pcs.	30%	Further output increases due to new assembly agreements in upcoming period(s) expected
Grain (in thousand tons)	5,107,8 thsd. t	5,388,8 thsd. t	5.5%	
Cement (in thousand tons)	2,778,9 thsd. t	3,148,6 thsd. t	13.3%	3.3%
Exchange rate US\$ - Sum	1,225.01	1,265.49	(3.3%)	Sum depreciated by 3.3%

Source: Statistical review 01-06/2007, State Committee of Statistics, own calculations; \*US\$ adjusted growth rates

With few exceptions, growth could be sustained in all spheres. Remarkable appears the significant increase in exports. Whilst cotton as one of the most relevant export commodity items of the country reduced its share in overall exports, energy sources, gas and oil sustained their “reputation” as main export drivers (increase of their export share by almost half). Eyecatching is the fact, that trade with CIS countries excelled, in particular the strong boost (74%) in exports.

## 2. DEVELOPMENTS IN SELECTED INDUSTRIES

In the following Avesta Research explores on investment developments and latest events in selected industries. This list is not considered lavish, rather it provides a snapshot of what was going on in the country - in particular in the context of foreign investment - in recent months.

### BANKING

2007 has seen several changes in the legal environment for the banking sector, such as a change of bank taxation, moving away from income taxation to profit taxation (now set at 17 percent). Since the beginning of 2007 new capital requirements are in place, defining for commercial banks US\$5,0 million and for private banks US\$2,5 million as required capital minimum. Various banks, such as Kapitalbank, Ipak Yuly Bank, Promstroybank and others increased their share capital. Subsequently, the volume of share issuances increased significantly and exceeds UZ\$50 billion (US\$39,5 million). Further stock sales are expected, preliminary estimates put the whole volume for 2007 at more than UZ\$160 billion (US\$126 million).

A new resolution of the President of the Republic of Uzbekistan on 'further capitalization of banks and banks' stimulation for participation in investment projects in the process of modernizing the economy' has been approved, recommending, among others, to commercial banks to retain (at least) 30 percent of their net earnings. Whilst an increasing capitalization will strengthen the banks' operational basis, promote a more diversified shareholder structure and provide for a potential enhancement of interest-earning assets, it may affect shareholders' dividend expectations. Besides, experience shows that a higher capital basis leads, at least in the short run, to lower profitability. Tax benefits for commercial banks are foreseen with regard to interest income out of loans, the maturities of which exceed three years and with an investment purpose (e.g. technological upgrading and production in industry sectors of priority). In case of initial issuance of bank stocks, with the exception of private banks, no less than 25 percent of circulating shares will be distributed via the stock exchange. Bank shares should be listed at the stock exchange and undergo regulated public quotation. A further decree limits the access of non-resident and foreign investors to bank shares. Accordingly, for acquiring shares of residential banks in the Republic, non-residents or legal entities with more than 50 percent share capital owned by non-residents must receive an obligatory permission by the Central Bank of Uzbekistan before carrying out any transaction.

## **CAR INDUSTRY**

Japanese car maker Isuzu Motors Ltd. acquired eight percent of the Samarkand Automobile Factory ("SamAvto"). Sam Avto set up a new production line for smaller trucks, based on and in cooperation with Isuzu Motors. This cooperation will also provide for upgrading of production technologies, processes' redesign as well as staff training programs, thus, gradually allowing for production enhancement at full capacity. In the final stage an annual output of up to 4 thousand units has been foreseen.

A new agreement with General Motors Daewoo will allow for upgrading the Nexia cars, produced in the city of Asaka, from 2008 on. An increase of the "Lacetti"- car type output up to 30 thousand units per year and the assembly of the new model on the basis of the popular "Matiz" are foreseen. A limited number of about 2,5 thousand new vehicles of types Chevrolet "Takuma", Captiva" and "Epika" is supposed to be assembled under this cooperation.

## **CHEMICAL PRODUCTS**

The "Kungradskiy Soda Factory", 100percent state-owned, which construction works could be completed in last year, started its operations. Project engineering and factory construction were carried out by Chinese CITIC. It will deliver to the local market as well as target export markets, such as Kazakhstan and Russia. A subsequent selling of parts of the State's equity has been envisaged. With government support direct investments and international credit funds (in particular from China) a new project for production of fertilizers shall become operational and contribute to the reduction of imports from Russia. The three-year project's costs are estimated at US\$70 million. Besides covering local demand, fertilizer exports to the Central Asia region as well as China are envisaged. The Spanish "MAXAM S.A.U." acquired in a public tender 49 percent of "Electrochimprom" for US\$22 million with investment commitments of US\$53 million in addition.

## **CONSTRUCTION AND CONSTRUCTION MATERIALS**

A new high-rise business complex construction project will start in the Tashkent's city centre. This new real estate development project will be undertaken by Jisong Korea Industrial JV at an estimated investment volume of US\$470 million.

Concrete is the main locally produced type of construction material. It has also good export potential to neighboring countries Kazakhstan, Kyrgyzstan and Tajikistan, with Afghanistan as a future potential market. "Kyzylkumcement", the largest concrete factory of the country, with a planned production capacity exceeding three million tons of cement, has been incorporated in the government's modernization program for technological upgrading and reconditioning from 2007 onwards. After completion of all works an increase in limestone extraction by 500 thousand tonnes has been predicted. The annual output in cement shall grow by roughly one quarter to more than four million tons. Overall, the forecasted investment volume exceeds US\$150 million.

For an expected total of US\$486 million „TKB-Invest“, a Russian company, has started to set-up new concrete processing facilities in the Djizakh oblast. Expected project duration until full completion of facilities: three years.

## **GAS AND OIL**

Russian "Gazprom", the world's largest single gas exploitation and distribution industrial complex, concluded an agreement on export of Uzbek natural gas with a total volume of 13 billion cubic meters. "SoyuzNefteGaz East LTD" (a 100% subsidiary of the Russian "SoyuzNefteGaz") and the national holding company (NHC) "Uzbekneftegaz" have signed a memorandum on investigation and development of oil-and-gas deposits in the Central Ustyurt and Southwest Gissar regions. The envisaged investment volume has been put at more than US\$360 million. In late April, the state energy company, UzbekNefteGaz reached a deal with the China National Petroleum Corporation to construct a 530-kilometer pipeline with a projected capacity of 30 billion cubic meters of gas per year.

## **INSURANCE**

The insurance industry grows dynamically. Whereas 2006 shows a total of UZ\$48,5 billion in insurance premiums, this level could almost be reached in the first six months of 2007. Overall the 26 insurance providers collected UZ\$38,9 billion (US\$30,7 million), pay-outs amounted to about UZ\$2,8 billion (approx. US\$2,2 million). Subsequently, pay-outs in correlation to collected premiums further diminished and stand now at seven percent. The cumulative nominal capital of the insurance sector during the first six months of 2007 grew by roughly five percent (in comparison with the respective period of previous year). This should be seen in context with the government's efforts to tighten the capital requirements for insurance companies. For general insurance providers these stand now at US\$500 thousand, for life insurance at US\$750 thousand, for damage and collateral obligations at US\$1 million and at US\$3 million for re-insurers.

## **INTERNATIONAL CREDIT LINES**

Chinese Eximbank is supposed to provide about US\$12 million for modernization of postal services. This should be seen in context with the acquisition of 25.4 percent of shares of "Uzbekistan pochty", the national operator of postal services, by the Chinese Company Finex Ltd.. Alokabank has been granted a credit line offered by the Chinese Development Bank of up to US\$18 million, in particular for leasing financing related to equipment procurement investments of JSC "Uzbektelecom" and associated companies. The main equipment contractor is Huawei Technologies from China. (It should be noted that Uzbektelecom is a shareholder of Alokabank). NBU Bank and Eximbank of China signed loan agreements amounting to US\$15,9 million. Loans shall be used to purchase and install equipment for two hydroelectric power plants.

The European Bank for Reconstruction and Development (EBRD) concluded a loan agreement with Hamkorbank with the purpose to establish a trade finance facility, whereas the Islamic Development Bank approved three credit lines to Asakabank, Uzpromstroybank and Ipotekabank with a total volume of USD15 million. They are designed exclusively for investment projects in manufacturing and agriculture.

## **MACHINERY AND EQUIPMENT**

Russian "Peresvet-Invest" acquired 75 percent of shares of "Samarqand liftostroitelny Zavod" at US\$1,3 million in the framework of a tender organized by the State Property Committee (SPC) of Uzbekistan. Subsequently, Peresvet-Invest is expected to invest during a period of five years US\$7,5 million to modernize and increase capacities for cargo and passenger lifts. In addition, a US\$50 million investment in real estate development to be made by Peresvet-Invest has been envisaged. "Samarqand liftostroitelny zavod's" current production capacity is about 7,000 units, pre-sumed to be significantly underutilized (20 percent capacity utilization only). First orders have in the meantime been placed by the Russian Navy.

## **PRIVATIZATION**

Larger or strategic assets are frequently sold only with minority stakes being allocated to investors or remaining (substantial) government equity participation, yet with significant investors' investment commitments required. The State Property Committee reports a total of (up to) 281 privatization transactions for the first six months of 2007 with an estimated sales value of UZ\$50.8 billion (US\$40,1 million). The reported number of 281 is considered misleading as simple asset sales are supposed to be included in this figure. The effective number of privatized enterprises is supposed to be significantly lower. Main deals included "Electrochimprom" (49% acquired by "MAXAM S.A.U.", Spain, "Uzbekistan pochta", 25.4% acquired by "Finex", China, "Samarqand liftostroitelny Zavod", 75% acquired by "Peresvet-Invest", Russia, "Uzbekistantrans", 79% acquired by American investors).

The newly approved program on privatization for 2007-2010 includes about 200 objects expected to be (at least partly) sold in the mid term. Among others stocks in "Uzbekistan Airways", "UZDaewoo Cars", "Kurganski Soda Factory", "Asaka Bank" and "Ipoteka Bank" as well as from major insurance providers, such as "Uzbekinvest", "Uzagrosugurta" or "Kafolat" are on the agenda. For the latter three sales of equity participation between 20 to 49 percent can be expected, taking into account a part or full deinvestment of the state, while maintaining already existing private investors' share in equity.

## **REPUBLICAN STOCK EXCHANGE**

Trade turnover at the stock exchange shows a decrease by factor 1.5 in comparison with the previous period. The main reason should be seen in the absence of sizable share packages as this has been the case in 2006 with companies, such as "Fargona Electric Tarmoklari", Markazi osie trans kurilish" or Bukhara Electric Tarmoklari". These shares had been placed in the market subsequently to privatization and were considered likewise attractive for foreign direct investment. In 2007, on the contrary, remarkable stock tradings referred rather to additional issuances of bank stocks (in the context of capital increases), whereas larger IPOs as a result of enterprises' privatization did not occur. As far as larger privatization transactions took place, these occurred outside the securities markets. The total transaction volume amounts to approx. UZ\$34,8 billion (US\$27,5 million) and included shares from 284 issuers. Banks represented more than 38 percent of traded shares, followed by financial service providers (such as investment funds, leasing or insurance companies) with almost 12 percent and food/beverages respectively chemical products following with 11.13 and 9.93 percent. The three largest companies in terms of stock trading were "Pakhta Bank", "Surkhonosikovatsanoati" (food/beverages industry) and "Hamkorbank", which count for nearly one fifth of all tradings. By

presidential decree the issuing of bonds has been limited to legal entities with "open joint stock company"-status only.

### TELECOMMUNICATIONS

The Swedish-Finnish company TeliaSonera acquired 100 percent of shares of American MCT Corp., which manages telecommunications operators in Central Asia and Afghanistan -its subsidiary JV "Coscom" being the third biggest GSM operator in Uzbekistan- for US\$300 million, out of which an estimated 50 percent refer to Coscom shares. Taking into account the existing subscriber basis TeliaSonera paid on the average US\$385 per subscriber, while MTC's initial investment costs per subscriber amounted to US\$520. During the last seven years the number of subscribers to mobile phone services in the country increased by more than 20 times. In the context of its regional business development strategy, TeliaSonera may consider a re-branding, under which all services will be offered.

By mid 2007, the Russian Joint Stock Company "MTS" purchased the remaining 26 percent of shares of LLC "Uzdunrobita" (trade mark "MTS-Uzbekistan") for US\$250 million, thus acquiring 100 percent of Uzdunrobita's capital. MTC acquired a license for 3G net services.

With an estimated level of penetration of 13 percent lavish space for further market growth appears to exist. The leading company in Uzbekistan's telecommunications market is "Uzdunrobita" (subsidiary of OJSC "MTS"), with an estimated market 52.6 percent, followed by «Unitel" (subsidiary of "Vimpelcom") with approx. 32.4 percent, whereas "Coscom" comes in third with a market share of 11 percent or about 410 thousand subscribers.

### 3. CONCLUSION

Uzbekistan's economy has in the first half of 2007 been doing well. GDP-growth tendencies from previous years could be sustained. A boost in exports supported a trade surplus. Government reported growth figures (9.7%) appear to be on the upper side, while at the same time inflation figures seem with 2.7 percent overoptimistically calculated. The growth curve can be expected to lose somewhat its dynamic in the near future. Worldwide inflation concerns exist, no less with respect to Uzbekistan; recent price hikes will undoubtedly lead to unwelcome inflation affects, the more as significant further upward adjustments on pensions, social allowance and minimum wages (by an estimated 250%) in the upcoming three years have already been made public. Uzbekistan benefits from investors' search for higher yields and (partly) underlying geostrategically decision-making (e.g. Russia, China). In 2007 so far, as the various examples of successful direct investments (see paragraph 2) show, investor's interest could be observed almost in all relevant industries. A positive economic outlook for the world economy and the Central Asian region prevails. Latest turbulence in financial markets in the USA and Europe might delay investors' decision making process and boost a more risk-averse investment behaviour. Whether this will have any direct impacts on (planned) investments in Uzbekistan is debatable; a more conservative allocation of foreign investment sources might follow. The economic well-being of Russia (which appears so far not to be seriously affected by financial turmoil) is considered of particular concern for the country. New regulations for the banking sector will promote further capitalization, whilst, however, not necessarily secure market consolidation and may partly be perceived as limitation of foreign investors' access to bank equity.

A latest update on the country's economic outlook in September, provided by the Asian Development Bank (ADB), adjusted expected economic outcomes by year's end 2007 to 7.4 percent (or slightly above) in growth. As a result of continuous inflation concerns, the inflation rate estimates arrive at 10 percent. A positive export outlook will further strengthen the country's current account balance.

#### 4. WORLD ECONOMY - ECONOMIC FRAMEWORK IN THE FIRST HALF OF 2007

The overall outlook for the world economy is still rather positive, besides recent turbulence in international financial markets. The International Monetary Fund (IMF) observed a further economic upswing. Whilst, in upcoming years a more moderate growth is expected, still in 2007 and 2008 a more dynamic development takes place. Worldwide economic growth shall arrive at 5.2 percent by year's end 2007, worldwide inflation is estimated at 3.5 to 3.8 percent. In the Eurozone between 2.5 and 2.7 percent of GDP growth can be presumed, with some countries, such as Germany, already on the way to further upgrade previous estimates at beginning of the year from 2.8 to 3.2. Inflation target for the Eurozone is 2 percent. The first months of the year indicate a real inflation of 1.9, just slightly under the target figure. Subsequently, the European Central Bank has adjusted its main interest rate, currently at 4 percent and expected to go even higher in the course of the year.

The US economy suffers from large budget deficits (estimated at 6 percent of GDP), a decrease in real estate property prices in combination with a huge backlog in real estate property remaining unsold (several million entities) as well as rising inflation concerns. The Federal Reserve Bank of America published a 2.4 percent inflation rate for May 2007 with upward tendency. Overall, the US economy still grows, however, is supposed to arrive at a modest 0.7 percent GDP growth only.

The Asian markets expect overall a slight decrease in growth (in 2006: 7.6 percent), yet on the average no less than 7 percent, with China growing even in double digit rates. Economic analysts share concerns with respect to inflation. The largest markets in Asia show inflation rates between 2.2 and 6.5 percent, while on the average they arrive at 3.7 percent.

Bonds interest rates, such as for (state) treasury bonds, have seen a rebound from lows of previous years. Germany, for instance, notes now annual interest rates of above 4 percent and new highs of above 5.3 percent are not ruled out among experts. Concerns exist with respect to securities linked to real estate finance, where a drop in property prices or subsequent necessary adjustments of ratings are the downside risks. Overall, securities are doing well, however. The Dow Jones Index exceeded in the first half of 2007 for the first time 14,000 points, the German DAX reached in July with 8,151 points an all time high. The Euro noted by mid 2007 on its highest level against the dollar, 1.38, a presumed result of money inflows.

Besides a positive assessment of economic developments, the IMF sees risks, which may affect a gradual, while moderately declining of growth rates:

- An extreme slowdown of the US economy
- Rising inflationary tendencies, e.g. interest hikes in combination with rising commodity prices, rising salaries due to increasing order books and subsequent bottlenecks on the job market (in some European countries and selected industries salary increases nearby 9% have been observed, more recently wheat/bread prices increased by 5-7 percent due to Canadian harvest defaults) or unwelcome currency exchange effects (such as a rising Yuan, making China's exports more expensive)
- An upward fluctuation of oil prices (with pessimistic scenarios arriving at US\$95 per barrel).

Most recently negative impacts for financial markets as a result of high risk finance engagements, already earlier identified by the IMF as potential threats for further economic growth, became more evident when turbulence at the American mortgage market surfaced, resulting eventually in liquidity shortages (short-term refinancing of securitized mortgage loans).

A necessary bail-out of a German wholesale bank by banking sector's solidarity funds indicated the arrival of turbulence in Europe, where a perception of liquidity shortages at the European inter-bank markets and a subsequent rise of inter-bank interest rates prompted the European Central Bank to provide additional liquidity in excess of Euro160 billion to the banking sector. Also in the US and in Asian countries, such as Japan, the central banks started to supply the markets with additional liquidity. Most analysts worldwide expect that a longer general economic turmoil will be avoided. Current turbulences are supposed to be short-term and apply to financial markets only. Yet, opinions are split. More conservative voices warn of spreading loan defaults, reduced housing and construction investments and an increasing risk-adverse banking sector. Securities markets, at present, appear to be not too distressed. While main indices, such as the Dow Jones and the Frankfurt DAX suffered from some initial decline, they came back and note in the meantime well above 13,700 and 7,700 points respectively (compare year's end 2006 of 12,510 and 6,691).

## **5. CENTRAL ASIA - ECONOMIC REVIEW IN BRIEF**

The Central Asian Countries benefited, among others, from oil exports, as far as oil exporting countries concerned, high remittance inflows (e.g. Tajikistan) as well as demand for commodities. While oil prices in the first half of 2007 came down from their 2006 peaks (highest in 08/2006 US\$78.65 per barrel) the price for crude oil peaked in early July 2007 again with US\$77.32 favouring oil exporters, such as Kazakhstan, but necessarily leaving concerns on overall worldwide economic impacts.

The trend of commodity prices has also favoured economic development of some Central Asian countries. Since its low in 2002 the price for aluminium, for example, has constantly been on the rise, amounting in Summer 2007 to approx. US\$2,734 per ton, more than 70 percent above the 2002 price level. The gold price as well rose constantly over past years. With about US\$730 per ounce its price arrived at a level more than double its price of 2002. Countries like Tajikistan with its aluminium smelter at Turzunzade or Uzbekistan with an estimated 85 tons of annual gold extraction benefit from this trend.

After Central Asia produced already in previous years significant growth rates (the average in 2006 was about 11.2 percent, the highest among all transition economies). Further GDP growth, the fifth year in a row, is expected. The latest estimates of the IMF calculate (up to) 11.6 percent for 2007, partly triggered by exceptional growth of the oil-rich Azerbaijan (excluding Azerbaijan IMF experts arrive at 8.1 percent, still significantly high). Government household surpluses in 2006 (on the average 2.6 percent) were mainly the result of a strong oil export position, partly - as the case of Tajikistan - inflows from foreign aid. For 2007 a change is presumed. On average balance deficits of about one percent are in sight; mainly because of increased government spending for poverty alleviation, partly also because of more conservative assumptions for oil revenues must be taken into account. The latest inflation figures, as provided by the IMF, put the region's inflation at 11 percent on average, emphasizing the need to tight fiscal and monetary discipline by both, governments and central banks.

The outlook for 2008 for the region is positive with further growth expected practically in all Central Asian economies, while, however, favoring commodities exporters in particular; further inflation constraints very likely.

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