



Monthly Economic Review

June 2013



Global Economy

- ◆ In its "Economic Outlook" report published on May 30th, Organization for Economic Cooperation and Development (OECD) lowered its global growth forecast for 2013 from 3.4% to 3.1% due to the weaker than expected economic activity.
- ◆ Although the consumption expenditures in the United States registered the highest increase since the end of 2010, the first quarter growth rate of the country was revised down to 2.4% from 2.5% due to the negative impacts of public spending cuts.
- ◆ The minutes of the Fed's monetary policy meeting held in April 30-May 1 revealed that there is not a consensus among the Committee members about the timing of the curtailing the asset purchase program. This increased the views that Fed might implement an earlier than expected exit strategy.
- ◆ Euro Area economy contracted by 0.2% in the first quarter of 2013 compared to the previous quarter. Thus, Euro Area economy contracted by six consecutive quarters, the longest recession recorded in the region since the establishment of the single currency in 1999.
- ◆ Japan's economy registered a rapid growth by 3.5% on an annual basis in the first quarter of 2013 thanks to the supportive policies implemented by the government and the central bank.
- ◆ The recent figures in China showed somewhat mixed signals regarding the course of economy. In April, industrial production and retail sales increased. However, the purchasing managers index in China declined below the 50 threshold and was realized as 49.6 in May, indicating a contraction in production activities.

Turkish Economy

- ◆ International credit rating agency Moody's upgraded Turkey's credit rating by one notch from "Ba1" to "Baa3". Moody's became the second rating agency following Fitch which rated Turkey as an investment grade country.
- ◆ The calendar adjusted industrial production index registered a limited increase by 1.4% in March compared to the same period of the previous year. On quarterly basis, industrial production index increased by 2.5% compared to the same quarter of the previous year, indicating that the expected recovery in economy has been lower than expected in the first three months of the year.
- ◆ Leading indicators were registered a gradual recovery in May.
- ◆ In February, the unemployment rate increased by 0.1 point to 10.5% compared to the same month of the previous year.
- ◆ According to data released by Turkstat, exports decreased in April while imports increased sharply. Thus, foreign trade deficit widened by 55.1% to 10.3 billion USD, well above the expectations.
- ◆ In March, current account deficit contracted by 13.9% compared to the same month of the previous year and was realized as 5.4 billion USD. 12-month cumulative current account deficit declined from 48 billion USD in February to 47.1 billion USD in March, falling below its 2012 year-end level.
- ◆ In April, central government budget posted 595 million TL surplus. Budget surplus decreased by 57.9% compared to April 2012.
- ◆ In May, the price developments in unprocessed food were influential on the lower than expected CPI.
- ◆ At its meeting on May 16th, CBRT Monetary Policy Committee decided to cut the policy rate together with the upper and lower bounds of the interest rate corridor.

Contents

| | |
|------------------------|-----------|
| Turkish Economy | 1 |
| Banking Sector | 10 |
| Graphs | 12 |
| Tables | 15 |

Türkiye İş Bankası A.Ş. - Economic Research Division

İzlem Erdem - Manager
izlem.erdem@isbank.com.tr

Alper Gürler - Unit Manager
alper.gurler@isbank.com.tr

Kıvılcım Eraydın - Economist
kivilcim.eraydin@isbank.com.tr

Erhan Gül - Economist
erhan.gul@isbank.com.tr

Bora Çevik - Economist
bora.cevik@isbank.com.tr

Besime Işıldak - Sub-Manager
besime.isildak@isbank.com.tr

Eren Demir - Asst. Economist
eren.demir@isbank.com.tr

M. Kemal Gündoğdu - Asst. Economist
kemal.gundogdu@isbank.com.tr

Gamze Can - Asst. Economist
gamze.can@isbank.com.tr

Moody's upgraded Turkey's credit rating to investment grade.

International credit rating agency Moody's upgraded Turkey's credit rating by one notch from "Ba1" to "Baa3". Moody's became the second rating agency following Fitch which rated Turkey as an investment grade country. Moody's announced that the decision for the upgrade was based on the improvement in economic and fiscal indicators. The rating agency also noted that the structural reforms will insulate the economy from capital inflows in the coming period.

Turkey's Credit Rating

| | Date of Last Change | Credit Rating | Outlook |
|---------|---------------------|---------------|---------|
| Moody's | May-13 | Baa3 | Stable |
| Fitch | Nov-12 | BBB- | Stable |
| S&P | Mar-13 | BB+ | Stable |

After Moody's decision, Turkey received investment grade rating from two rating agencies for the first time since 1992. Analyzing the macroeconomic indicators of the countries which have the same credit rating with Turkey shows that Turkey has a larger economy than the majority of these countries and has the highest per capita income after Uruguay. The only indicator which Turkey diverges negatively from other countries is the relatively high current account deficit to GDP ratio. Moody's expects that the said ratio will continue to decline in the medium to long-term thanks to the planned structural reforms.

The increase in the external financing opportunities and the decline in the cost of financing due to the investment grade is expected to support the resilience of the economy against external shocks. Thus, the improvement in Turkey's riskiness indicators will continue to improve in the coming period.

Countries with the Same Credit Rating of Turkey

| Moody's (Baa3) | Fitch (BBB-) |
|----------------|--------------|
| Turkey | Turkey |
| India | India |
| Uruguay | Uruguay |
| Romania | Romania |
| Indonesia | Indonesia |
| Azerbaijan | Azerbaijan |
| Colombia | Colombia |
| Namibia | Namibia |
| Costa Rica | Croatia |
| Iceland | Morocco |
| Spain | Bulgaria |
| | Philippines |

JCR and DBRS also upgraded Turkey's credit rating.

In addition to the leading credit agencies, JCR (Japanese Credit Rating Agency) also increased Turkey's credit rating by two notches to investment grade of "BBB-" with a stable outlook. In its statement following the decision, the agency cited Turkey's successful handling of the economic uncertainties stemming from the global crisis. JCR highlighted the increase in net exports and the decline in the unemployment rate during 2012 and noted that these developments point out the strong growth potential of Turkey. In addition, Canadian rating agency DBRS (Dominion Bond Rating Service) also started to rate Turkey as of May 24 and rated Turkey as an investment grade country with a "BBB-" rating.

Standard & Poor's' comments...

On the other hand, Standard & Poor's, which has been keeping Turkey's rating below the investment grade, announced that Turkey's economy has entered in a sustainable recovery path. However, the agency also said that CBRT is implementing a challenging policy against the impacts of loose monetary policies of advanced economies in order to find the balance between growth and financial stability in Turkey.

Macroeconomic indicators of countries which has the same credit rating with Turkey (December 2012)

| | Turkey | Colombia | India | Indonesia | Namibia | Romania | Azerbaijan | Uruguay |
|---|--------|----------|--------|-----------|---------|---------|------------|---------|
| Real Growth Rate (%) | 2.2 | 4.0 | 4.0 | 6.2 | 4.0 | 0.3 | 2.2 | 3.8 |
| GDP in Current Prices (billion USD) | 786.3 | 366.0 | 1824.8 | 878.2 | 12.3 | 169.4 | 68.8 | 49.4 |
| GDP Per Capita (USD) | 10,504 | 7,855 | 1,492 | 3,592 | 5,705 | 7,935 | 7,450 | 14,614 |
| Annual Inflation (% change) | 6.2 | 2.4 | 11.2 | 4.3 | 6.2 | 5.0 | -0.3 | 7.5 |
| Imports (annual % change) | -1.8 | 11.3 | 2.7 | 14.0 | 4.0 | -1.3 | 10.7 | 10.6 |
| Exports (annual % change) | 13.0 | 4.0 | 0.9 | -1.7 | 4.7 | -3.2 | -7.2 | 4.6 |
| Unemployment Rate (%) | 9.2 | 10.4 | - | 6.2 | - | 7.0 | 6.0 | 6.1 |
| Population | 74.9 | 46.6 | 1223.2 | 244.5 | 2.2 | 21.3 | 9.2 | 3.4 |
| General Gov. Budget Revenues (% of GDP) | 34.7 | 28.4 | 19.2 | 17.8 | 33.7 | 32.9 | 40.7 | 31.9 |
| General Gov. Budget Expenditures (% of GDP) | 36.1 | 28.2 | 27.5 | 19.1 | 37.8 | 35.4 | 37.5 | 34.6 |
| Public Net Debt Stock (% of GDP) | 17.0 | 24.6 | - | - | 24.4 | - | - | 36.3 |
| Public Gross Debt Stock (% of GDP) | 39.7 | 32.8 | 66.8 | 24.0 | 26.6 | 37.0 | 11.6 | 53.7 |
| Current Account Balance (billion USD) | -47.5 | -12.4 | -93.3 | -24.2 | -0.2 | -6.5 | 14.0 | -1.7 |
| Current Account Balance (% of GDP) | -6.0 | -3.4 | -5.1 | -2.8 | -1.6 | -3.8 | 20.3 | -3.4 |

Industrial production came in lower than expected in March...

The calendar adjusted industrial production index increased by 1.4% in March compared to the same month of the previous year. The manufacturing sector index increased by 2.5%. On the other hand, the declines in “electricity, gas, steam and air conditioning supply” and “mining and quarrying” sectors limited the increase in total industrial production. The seasonal and calendar adjusted index, on the other hand, declined by 0.9% compared to the previous month. Analyzing the quarterly figures, the calendar adjusted index increased by 2.5% compared to the same quarter of the previous year. This indicates that the expected recovery in economy has been lower than expected in the first three months of the year.

Capacity utilization rate was realized as 74.8%.

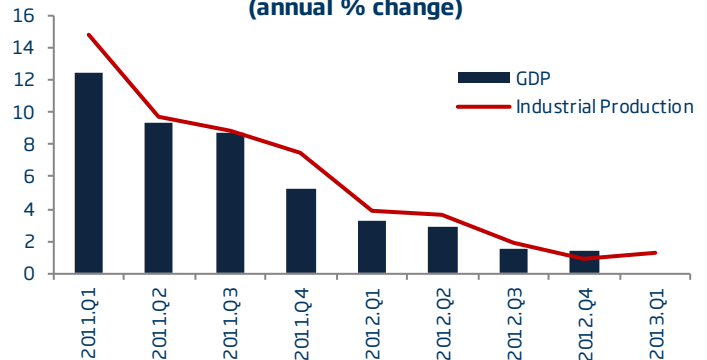
According to the data announced by CBRT, the Real Sector Confidence Index declined by 1.3 points to 112.5 in May compared to the same month of the previous year. The seasonally adjusted index, on the other hand, increased by 0.7 points compared to previous month and was realized as 105.7. In May, the capacity utilization rate in manufacturing industry increased by 0.1 point to 74.8% compared to the same month of the previous year. Moreover, the seasonally adjusted capacity utilization rate increased by 0.3 points compared to the previous month and was realized as 74.6%. The seasonally adjusted leading indicators point out that the economy entered a gradual recovery phase in the second quarter.

The consumer confidence index, which is calculated by Turkstat and CBRT, increased by 1.9 points to 77.5 in May. The increase originated from the improvement in the general economic situation expectation and financial situation expectation of the household for the next 12 months. The probability of saving expectation also increased. On the other hand, the 2.2% monthly decline in the expected number of unemployed persons was notable.

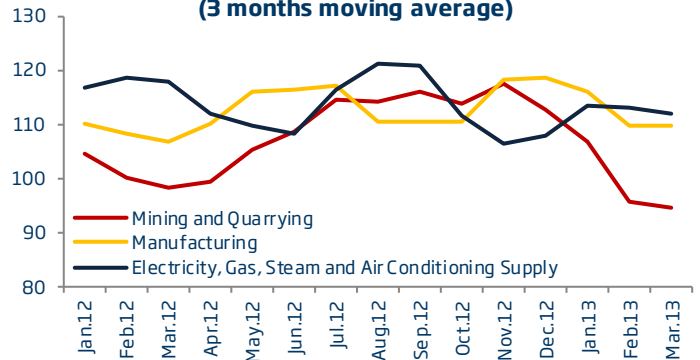
The unemployment rate was realized as 10.5% in February.

In February, the unemployment rate increased by 0.1 point to 10.5% compared to the same month of the previous year. During the same period, total employment increased by 1 million 208 thousand persons and reached 24 million 546 thousand persons. Despite this increase in employment, the higher rate of increase in labor force participation than that of employment led to a rise in the unemployment rate. The seasonally adjusted unemployment rate, on the other hand, declined by 0.2 point compared to the previous month. In the coming period, we expect that the decline in unemployment rate will continue thanks to the seasonal factors.

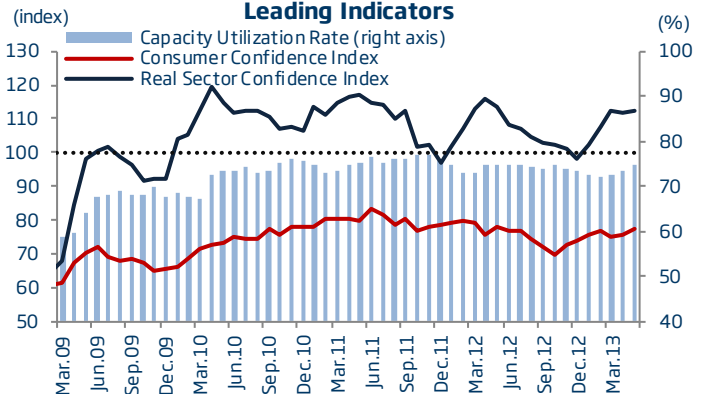
Industrial Production and GDP (annual % change)



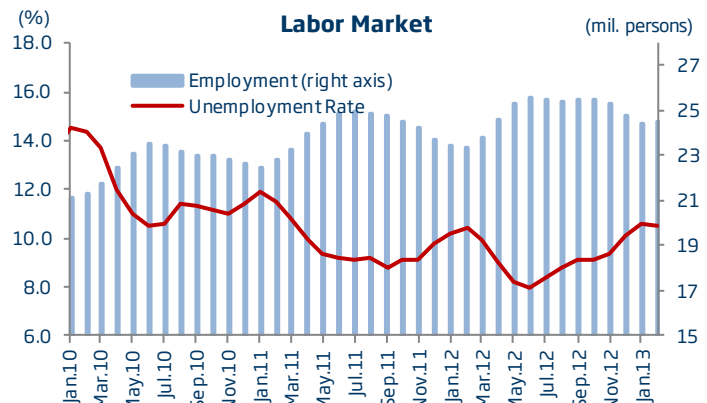
Sub-Indices of Industrial Production (3 months moving average)



Leading Indicators



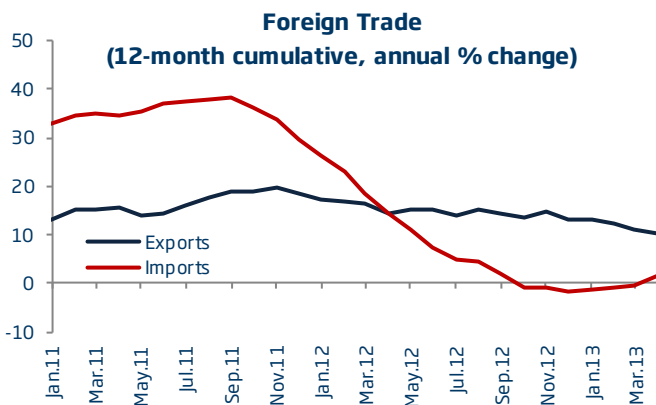
Labor Market



Source: Turkstat, CBRT

In April, foreign trade deficit was realized as 10.3 billion USD, well above the expectations.

According to data released by Turkstat, imports increased by 18.4% in April compared to the same month of the previous year and were realized as 22.8 billion USD while exports decreased by 0.9% to 12.5 billion USD. During the same period, foreign trade deficit widened by 55.1% to 10.3 billion USD, well above the expectations. The import coverage ratio fell sharply from 65.5% in April 2012 to 54.9% in April 2013 due to the decline in exports together with the rapid increase in imports.



Calendar adjusted data also indicated that imports increased by 14.3% annually in April while exports declined by 3.8% in the same period.

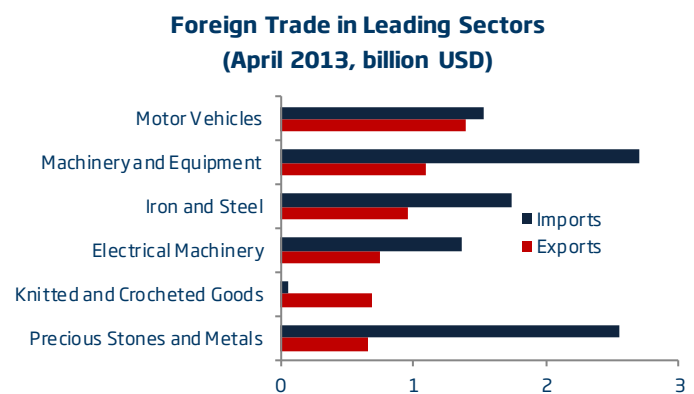
In the first four months of the year, foreign trade deficit widened by 17.5%.

During the first four months of 2013, exports and imports rose by 3.4% and 8.5%, respectively. During the same period, foreign trade deficit registered an increase of 17.5%. However, the rapid increase in gold imports had a significant impact on foreign trade deficit in 2013 and when gold trade was excluded, foreign trade deficit in the first four months was realized close to the last year's level in the same period. The deceleration in exports confirms the views that the contribution of domestic demand will be the main driver of growth in 2013 in contrast with the previous year when the net exports made the highest contribution to growth. In fact, the annual growth in exports was 11% in 2012 while imports contracted by 2.4%.

| Foreign Trade Balance | (USD billion) | | | | | |
|------------------------------|---------------|--------------|-------------|---------------|--------------|-------------|
| | April | | | January-April | | |
| | 2012 | 2013 | Change (%) | 2012 | 2013 | Change (%) |
| Exports | 12.6 | 12.5 | -0.9 | 47.9 | 49.6 | 3.4 |
| Imports | 19.3 | 22.8 | 18.4 | 75.2 | 81.6 | 8.5 |
| Foreign Trade Balance | -6.6 | -10.3 | 55.1 | -27.3 | -32.0 | 17.5 |
| Import Coverage Ratio (%) | 65.5 | 54.9 | - | 63.7 | 60.7 | - |

Motor vehicles ranked first in exports with 1.4 billion USD...

Analyzing the exports by sectors, it was seen that the motor vehicles exports ranked first in total exports by 1.4 billion USD in April rising by 2.1% compared to the same month of the previous year. Machinery and equipment sector followed this sector with an exports volume reaching 1.1 billion USD by rising 11.5% in the same period. On the other hand, precious stones and metals exports declined by 56.9% compared to the same month of the previous year, mainly due to the sharp fall in gold exports. This also further lowered the exports volume.



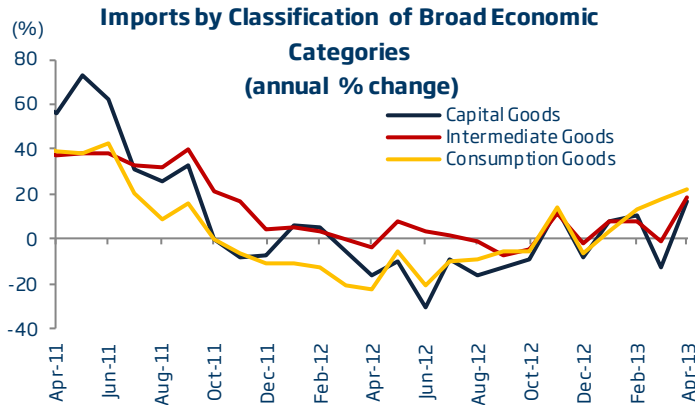
The share of European Union in total exports recorded a slight increase in April.

The share of European Union in total exports, having declined to 33.6% in August 2012, increased by 1.4 points compared to the same month of 2012 and reached 39.4% in April 2013. Exports directed to Germany, the biggest trading partner of Turkey, decreased by 4.2% in April. Another noteworthy development was the 14.4% increase in exports to Iraq.

Imports of consumption goods are accelerating.

After having increased in March by 17.8%, the consumption goods imports registered an annual increase of 22.2% in April. This rapid increase in the consumption goods imports stemmed from the rise in domestic demand as a result of the CBRT's policies implemented since the second half of 2012. In the same period, the intermediate goods imports rose by 18.2%, the highest increase observed since October 2011.

Source: Turkstat



In the first four months of 2013, on the other hand, the consumption goods imports rose by 14.7% compared to the same period of the previous year. In the same period, intermediate goods and capital goods imports increased by 8.3% and 4.6%, respectively.

In the first four months of the year, gold imports amounted to 5.3 billion USD.

Gold trade continued to be effective in foreign trade balance in April. Gold exports declined to their lowest level since January 2012 by 346 million USD. During the first four months, gold exports were realized as 1.8 billion USD, well below their level of 2.6 billion USD recorded during the same period of the previous year. On the other hand, gold imports were realized as 5.3 billion USD, almost three times of its level in previous year. Unlike last year, Turkey became a net importer of gold by 3.4 billion USD in the first four months of 2013. The strong pace of gold imports indicates that the course of the gold trade will continue to be watched by the

markets also in the coming periods, as there is a lagged relationship between imports and exports.

Expectations...

Foreign trade deficit in April came in well above the expectations mostly driven by the sharp increase in the volume of gold imports. Moreover, CBRT's supportive monetary policies implemented since the second half of 2012 are also thought to be influential on the widening in the foreign trade deficit. A higher than expected foreign trade deficit intensified the pressure on USD/TL which already began moving upwards by the concerns related with the recent rumors of Fed's early exit plan and the outflow of foreign capital just after Turkey received the second investment grade. When the pass-through between the exchange rate and inflation is taken into account, CBRT is expected to adopt a cautious approach and lower TL liquidity in the markets should the depreciation in TL continue.

Lower than expected current account deficit in March...

In March, current account deficit contracted by 13.9% compared to the same month of the previous year and was realized as 5.4 billion USD, lower than the market consensus of 5.9 billion USD. On a quarterly basis, current account deficit decreased by 2.3% to 15.9 billion USD compared to the first quarter of the previous year.

12-month cumulative current account deficit declined from 48 billion USD in February to 47.1 billion USD in March, falling below its 2012 year-end level. The narrowing of the deficit indicated a slower than expected recovery in domestic demand in the first quarter of the year.

Tourism revenues had a positive impact on the balance of payments.

Tourism revenues were realized as 1.6 billion USD in March. The increase in tourism revenues was higher than that of tourism expenditures in the first quarter of the year. Thus, net tourism revenues increased by 35.4% and reached 3 billion USD during this period. Regarding the 12-month cumulative figures, tourism revenues, which followed an upward trend in the last 6 months, have been one of the main factors limiting the expansion of the current account deficit.

Foreign direct investments continued to decline.

Analysis of the financing side of current account deficit revealed that the non-residents' foreign direct investments continued to decline. FDI inflows decreased to 597 million USD in March, the lowest level recorded since September 2012. As of the first quarter of the year, FDI inflows declined by 55.2% compared to the same period of the previous year and were realized as 2 billion USD. On the other hand, residents' direct investments abroad reached 688 million USD in the first quarter and led net foreign direct investments to contract by 40.4% compared to the same period of the previous year.

Portfolio investment inflows were strong.

Net portfolio investments kept their upward trend in March by increasing 29% compared to the same month of the previous year and were realized as 3.9 billion USD. This increase mainly stemmed from the Treasury's debt security issues held in March. Indeed, capital inflows registered via debt securities were 2.4 billion USD in March, 1.6 billion USD of this amount stemmed from Treasury's domestic debt security issues. On the other hand, banking sector's bond issues in international capital markets in this period amounted to USD 670 million. In addition, foreign capital inflows via equity securities were realized as 511 million USD in March.

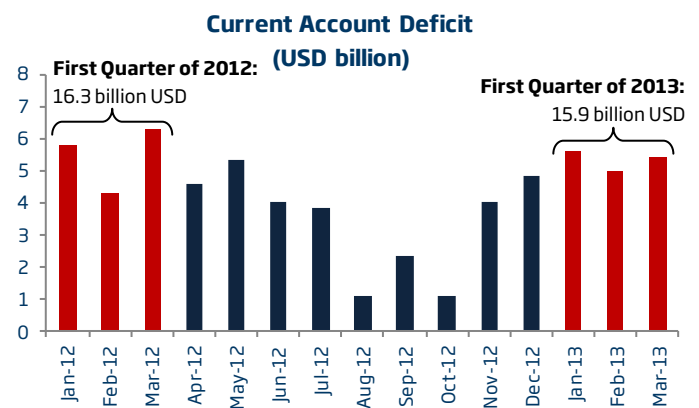
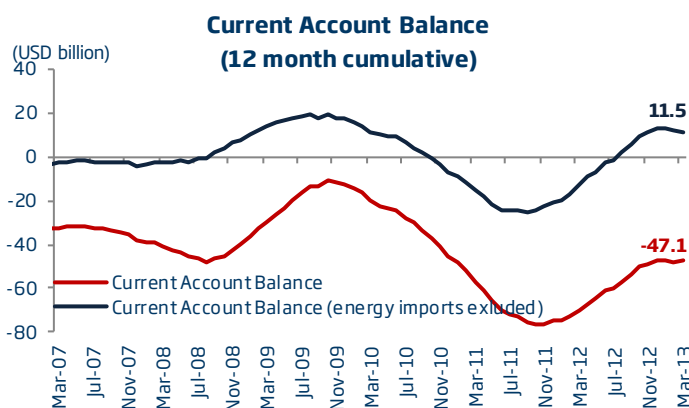
On a quarterly basis, net portfolio investments increased by 69.1% compared to the first quarter of the previous year and were realized as 8.8 billion USD. During this period, banking sector's bond issues in international capital markets increased more than five times of their level in the first quarter of 2012.

Banking sector's loans from abroad were effective in the increase in the other investments.

Analyzing the other investments, it was noteworthy that banking sector raised significant amount of short-term loans from abroad in March. During this period, short-term loans raised from abroad by the banking sector amounted to 3.7 billion USD, the highest level recorded since December 2010. In terms of long-term loans, banks were net credit borrowers in March while they were net credit payers in the first quarter of the year. On the other hand, non-banking sector, which was net credit user from abroad in the first two months, became net credit payer in March.

In the first quarter, banks raised net 6.8 billion USD loans from abroad while this amount was 169 million USD for the non-banking sector.

Analyzing 12-month cumulative figures, it was seen that long term debt roll-over ratio of the banking sector was



93% and that of non-banking sector was 113%.

Rapid increase in reserves In March...

Reserve assets increased by 2.4 billion USD partly due to the CBRT's increase in the reserve option coefficients in its March meeting. The increase in the reserve assets reached 7 billion USD in the first quarter and 27.1 billion USD in the last 12 months.

Expectations ...

The 12-month cumulative current account deficit, which increased in February, decreased again in March and pointed out that the recovery in domestic demand was slower than expected. However, the current account deficit is expected to widen in the coming period as an outcome of the CBRT's latest rate cut decisions and supportive monetary policy stance. However, the gradual economic recovery indicated that this increase would remain limited.

| | | | | | (USD million) |
|---------------------------------------|---------------|----------------------------|----------------|-------------|------------------------|
| | March 2013 | January-March 2012 2013 | | % Change | 12 Month Cumulative |
| Current Account Balance | -5,396 | -16,300 | -15,917 | -2.3 | -47,138 |
| Foreign Trade Balance | -5,737 | -16,783 | -17,047 | 1.6 | -65,986 |
| Services Balance | 1,263 | 2,050 | 2,873 | 40.1 | 24,332 |
| Tourism Revenues (net) | 1,188 | 2,216 | 3,001 | 35.4 | 22,344 |
| Income Balance | -946 | -1,929 | -1,975 | 2.4 | -6,721 |
| Current Transfers | 24 | 362 | 232 | -35.9 | 1,237 |
| Capital and Financial Accounts | 6,856 | 10,566 | 19,543 | 85.0 | 55,340 |
| Direct Investments (net) | 424 | 2,275 | 1,355 | -40.4 | 7,561 |
| Portfolio Investments (net) | 3,887 | 5,175 | 8,750 | 69.1 | 44,355 |
| Assets | 1,006 | 757 | 1,455 | 92.2 | 3,346 |
| Liabilities | 2,881 | 4,418 | 7,295 | 65.1 | 41,009 |
| Equity Securities | 511 | 920 | 393 | -57.3 | 5,747 |
| Debt Securities | 2,370 | 3,498 | 6,902 | 97.3 | 35,262 |
| Other Investments (net) | 4,992 | 3,823 | 16,473 | 330.9 | 30,610 |
| Assets | -1,903 | -901 | 1,444 | - | 1,896 |
| Currency and Deposits | -840 | -581 | 1,935 | - | 3,851 |
| Liabilities | 6,895 | 4,724 | 15,029 | 218.1 | 28,714 |
| Trade Credits | 1,158 | -127 | 3,539 | - | 4,674 |
| Loans | 3,296 | 1,118 | 6,567 | 487.4 | 14,582 |
| Banking Sector | 4,176 | -406 | 6,805 | - | 12,049 |
| Non-bank Sectors | -1,058 | 1,921 | 169 | -91.2 | 4,616 |
| Deposits | 2,433 | 3,738 | 4,916 | 31.5 | 8,961 |
| Foreign Banks | 1,804 | 2,740 | 3,952 | 44.2 | 8,325 |
| Foreign Exchange | -150 | 2,809 | 3,346 | 19.1 | 5,766 |
| Turkish Lira | 1,954 | -69 | 606 | - | 2,559 |
| Non-residents | 705 | 1,252 | 1,202 | -4.0 | 2,863 |
| Reserve Assets (net) | -2,447 | -690 | -7,024 | 918.0 | -27,148 |
| Net Errors and Omissions | -1,460 | 5,734 | -3,626 | - | -8,202 |

Source: CBRT

In April central government budget posted a surplus.

In April, budget expenditures increased by 7.8% compared to the same month of the previous year while revenues rose by 4.7%. Central government budget surplus decreased by 57.9% to 595 million TL compared to April 2012.

In the first four months of the year, the budget deficit declined significantly to 302 million TL compared to the same period of the previous year. During the same period, primary surplus increased by 5.7% to 17.9 billion TL and reached 94.1% of the year-end target.

Tax revenues increased by 20.9% yoy in April.

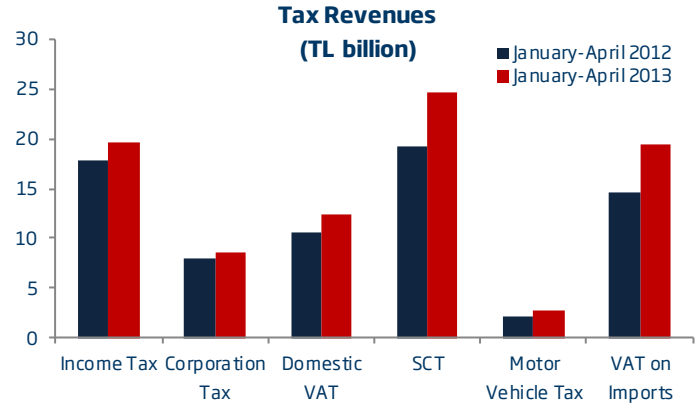
In April, tax revenues increased by 20.9% compared to the same month of the previous year. Rapid increase in tax revenues was mainly stemmed from the rises in Petroleum and Natural Gas Special Consumption Tax (SCT), Value Added Tax (VAT) on Imports, Income Tax and Domestic VAT revenues. Analyzing the sub items by increase rates, the rises in SCT, Domestic VAT and VAT on imports were realized as 23.7%, 19.1% and 21.3%, respectively.

In the first four months of the year, tax revenues followed a course parallel to year-end budget targets in general. However, SCT revenues seem to undershoot the budget target in case of a similar trend in the rest of the year. Weak performances in tobacco and alcoholic beverages SCT was effective in this trend.

Fall in other budget revenues...

Non-tax revenues decreased by 30.6% to 6.4 billion TL in April compared to the same month of previous year. Mentioned decrease was mainly due to strong basis created by CBRT's high dividend payments to central government budget observed in April 2012.

During January-April period, on the other hand, other revenues increased by 4.7% as the decline in portfolio revenues of Treasury in April was balanced by 4.2 billion TL rise in privatization revenues in January.



Interest expenditures decreased by 33.8%.

In April, non-interest expenditures increased by 16.2% to 26.8 billion TL compared to the same month of previous year. In this period, current transfers which is the most significant expenditure item of central government budget increased by 19.5%, while goods and services purchases decreased by 6.2%. On the other hand, significant decrease in interest expenditures was noteworthy. During this period, interest expenditures decreased by 33.8% to 3.1 billion TL.

In January-April period, non interest expenditures increased by 19.1% while interest expenditures declined by 17%. In general, sub items of budget expenditures perform parallel to year-end targets.

Expectations ...

Central government budget displays a positive performance in an environment that data regarding the first four months of the year pointed out a slower than expected recovery in economic activity. Assuming that the ongoing supportive stance of the CBRT will continue to promote the upward trend in tax revenues, we think there would not be any problem in reaching the year-end budget targets.

Central Government Budget

| | April | | | January-April | | | (TL billion) | |
|---------------------------|-------------|-------------|--------------|---------------|--------------|--------------|---------------|-------------------|
| | 2012 | 2013 | % Change | 2012 | 2013 | % Change | Budget Target | Real./ Target (%) |
| Expenditures | 27.7 | 29.9 | 7.8 | 111.6 | 124.9 | 12.0 | 404.0 | 30.9 |
| Interest Expenditures | 4.6 | 3.1 | -33.8 | 22.0 | 18.2 | -17.0 | 53.0 | 34.4 |
| Non-interest Expenditures | 23.1 | 26.8 | 16.2 | 89.6 | 106.7 | 19.1 | 351.0 | 30.4 |
| Revenues | 29.1 | 30.5 | 4.7 | 106.5 | 124.6 | 17.0 | 370.1 | 33.7 |
| Tax Revenues | 20.0 | 24.1 | 20.9 | 84.4 | 101.5 | 20.2 | 317.9 | 31.9 |
| Other Revenues | 9.2 | 6.4 | -30.6 | 22.1 | 23.2 | 4.7 | 52.1 | 44.4 |
| Budget Balance | 1.4 | 0.6 | -57.9 | -5.0 | -0.3 | -94.0 | -34.0 | 0.9 |
| Primary Balance | 6.1 | 3.7 | -39.4 | 16.9 | 17.9 | 5.7 | 19.0 | 94.1 |

Numbers may not add up to total due to rounding

Source: Ministry of Finance

The increase in CPI was below expectations in May.

In May, compared to the previous month, CPI and PPI increased by 0.15% and 1.00%, respectively. According to the Reuters' survey, markets' monthly CPI and PPI inflation expectations were 0.45% and 0.44%, respectively. According to the CBRT's survey of expectations, CPI was expected to rise by 0.46% in May.

In May, annual CPI inflation increased due to the base effect.

In May, although the monthly CPI inflation was lower than expected, the annual CPI rose to 6.51% due to the base effect. In the same period, annual PPI increased by 2.17% and kept its low level.

The price developments in food and non-alcoholic beverages group were influential on the course of CPI.

In May, it was seen that the price developments in unprocessed food were influential on the lower than expected CPI. Indeed, the prices in food and non-alcoholic beverages group, which has the highest share in CPI, declined by 2.18% compared to the previous month and led CPI to decrease by 44 basis points. On the other hand, while other consumption groups followed a stable path, prices in clothing and footwear group registered a sharp increase due to the seasonal factors in May. The prices in this group increased by 8.85% compared to the previous month and made an upward contribution to the monthly CPI inflation by 51 basis points.

Core inflation increased slightly...

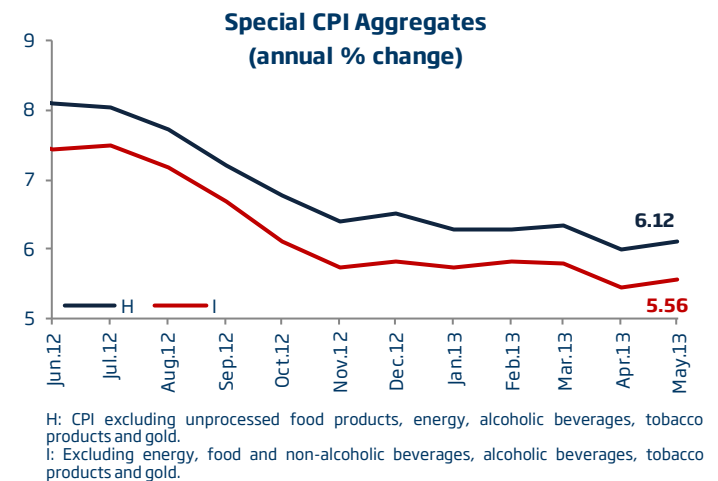
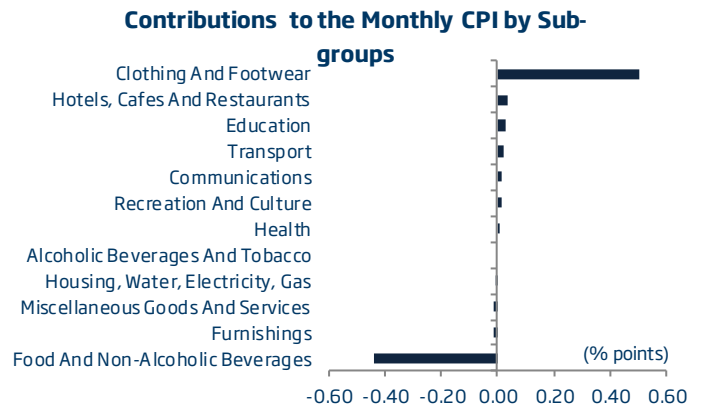
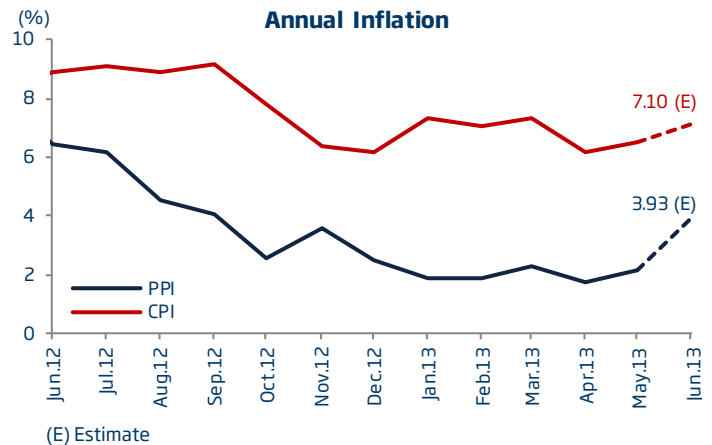
Analysis of the core inflation indicators revealed that the special CPI aggregates made an upward contribution to inflation in May. Following April, CBRT's favorite core inflation aggregates increased also in May. In this period, core aggregates denominated by H and I rose by 1.29% and 1.47%, respectively on monthly basis while the annual increases in these aggregates were realized as 6.12% and 5.56%, respectively.

Higher than expected PPI in May...

In May, increase in the agricultural sector prices were influential on PPI. The prices in the said group increased by 5.96% compared to the previous month and contributed PPI inflation by 90 basis points. In addition to that, electricity and gas production and the manufacture of textile products were also influential on the rise of the PPI.

Expectations...

In June, we anticipate that the monthly CPI would fall due to the seasonal factors in the food and beverages group while the annual inflation would rise due to the base effect. On



the other hand, we expect that the impact of recent increase in currency basket will be reflected in PPI initially. The magnitude of the secondary effects on CPI will depend on the possible measures to be taken by the policy makers. In this context, we expect CPI to decrease by 0.35% while PPI to increase by 0.20%.

Source: Turkstat

CBRT further cut the policy rate by 50 basis points.

Having cut the policy rate together with the upper and lower bound of the interest rate corridor in its April meeting, CBRT Monetary Policy Committee (MPC) decided to further cut the said interest rates by 50 basis points at its meeting on May 16th. Thus, one week repo rate (policy rate) has been cut to 4.5% and upper (overnight lending rate) and lower (overnight borrowing rate) bounds of interest rate corridor have been lowered to 6.5% and 3.5%, respectively.

CBRT stated that the weakening global demand and the decline in commodity prices reduced the risks on inflation outlook. In addition, CBRT indicated that capital inflows remained strong and keeping interest rates at low level would be proper in order to maintain financial stability.

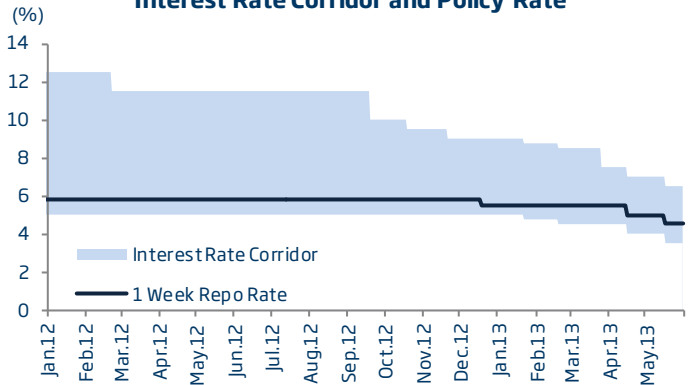
FX reserve requirement ratios and reserve option coefficients were increased.

CBRT pointed out that the course of annual credit growth rate stayed above the reference rate and adopted a moderate tightening in monetary policy via reserve requirement ratios and the reserve option coefficients (ROCs). In this framework, FX reserve requirement ratios were increased for different maturities. Besides, in the context of the facility that allows banks to hold TL required reserves in FX, one more tranche has been added to the existing tranches by keeping the upper limit unchanged, and the reserve option coefficients (ROCs) have been raised by 0.1 point for all tranches excluding the first tranche. Thus, the average ROC increased from 1.78 to 1.83. CBRT announced that the banks utilize this facility with a rate of 84.1% (50.5/60) and hold FX worth of 30.9 billion USD for Turkish Lira required reserves. Should the facility continue to be used at the same level after the revisions, CBRT expects FX reserves to increase by approximately 0.8 billion USD.

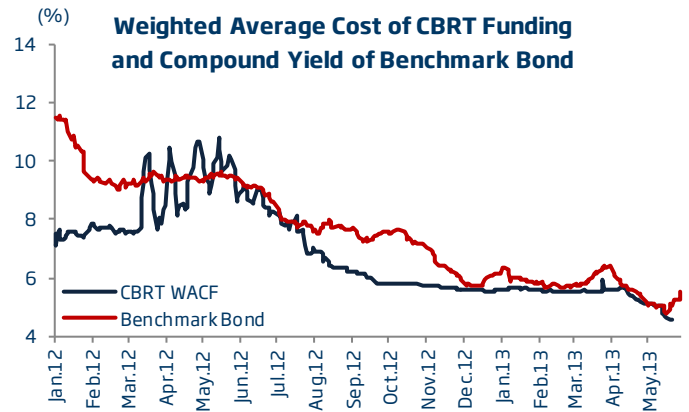
CBRT released the Financial Stability Report.

In the Financial Stability Report published on May 30th, CBRT mentioned that the continuation of the expansionary monetary policies in advanced economies nurtured the capital flows to developing economies and added that the global risk appetite continued to follow an unstable course due to the existing global vulnerabilities. According to CBRT, portfolio flows to developing economies exhibited a volatile course resulting from these developments. CBRT pointed out the necessity of the flexible monetary policies considering the macro-financial risks regarding the ongoing uncertainties in global economy. In this context, CBRT has been using structural and cyclical tools in order to preserve both the financial and price stability. In this framework,

Interest Rate Corridor and Policy Rate



Weighted Average Cost of CBRT Funding and Compound Yield of Benchmark Bond



CBRT expressed that efficient usage of reserve option mechanism as an automatic stabilizer reduced the necessity of a wide interest rate corridor. On the other hand, CBRT drew attention to the high interest rates charged to overdraft accounts which are of similar nature to credit cards and which have increased notably in the recent period. In order to address financial stability risks and strengthen the monetary transmission mechanism, CBRT put a cap on the interest rates charged for this type of accounts.

Deposits...

According to BRSA's Weekly Bulletin, as of May 24th, 2013, total deposit volume increased by 5.1% to 858.4 billion TL compared to the year-end. During this period, TL deposits and FX deposits in USD terms increased by 4.7% and 2.1% respectively. The annual increase in deposit volume was realized as 14.2%.

Loans...

As of May 24th, 2013, total loan volume increased by 9.7% compared to year-end and reached 883.7 billion TL. During the same period, TL loans and FX loans in USD terms increased by 9.9% and 5.1%, respectively. The annual increase in total loan volume was 20.6%.

Analyzing by types of loans, as of May 24th, 2013, consumer loans increased by 11.3% compared to the year-end. During the same period, installment commercial loans and other loans which are composed of large scale corporate loans expanded by 15.9% and 8.5%, respectively.

As of May 24th, 2013, NPL ratio was realized as 3.0%. The said ratio was 2.1% in consumer loans, 3.3% in installment commercial loans and 5.6% in individual credit cards. The NPL ratios in the first two credit types remained flat compared to year-end while NPL ratio in credit cards increased by 0.5 points.

Securities portfolio...

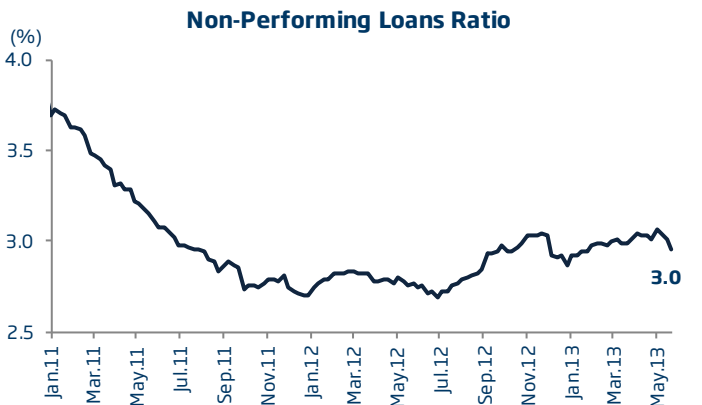
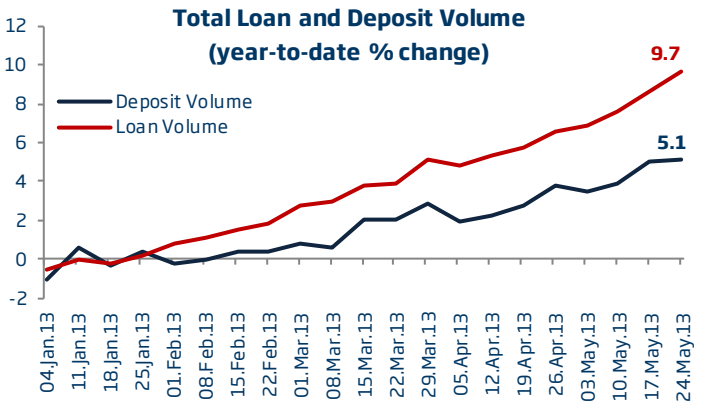
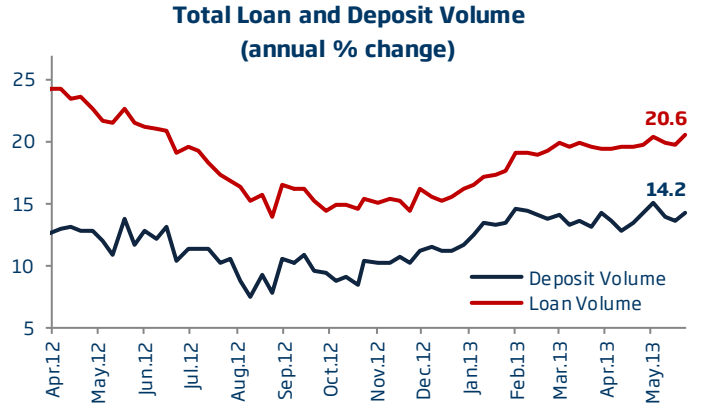
Securities portfolio decreased by 0.6% to 270.6 billion TL as of May 24th, 2013, compared to year-end.

Securities portfolio held in custody accounts...

As of May 24th, 2013, securities portfolio held in custody accounts grew by 13.6% compared to year-end and reached 246.1 billion TL. In this period, residents' and non-residents' portfolio expanded by 9.8% and 17.3%, respectively.

Net FX position...

As of May 24th, 2013, net FX position of the banking sector was (+) 2.1 billion USD. Banks' on-balance sheet FX position was (-) 18.2 billion USD while off-balance sheet FX position was (+) 20.3 billion USD.



Source: BRSA Weekly Bulletin

Despite the relative improvement in global financial conditions, economic activity displayed only a gradual recovery in the United States while it remained weak in the Euro Area. In this context, although the rumors that Fed might begin the exit strategy earlier than expected increased, the loose monetary policies in the Euro Area and Japan are expected to continue. This indicates the improvement in the financial conditions since the second half of 2012 will continue in the remaining part of 2013. However, the uncertainties regarding the public finance in the United States and implementation process of structural reforms in the Euro Area continued to be the major risk factors that might cause economic activity to remain under pressure. The steps that will be taken to solve the economic problems in these countries would lead the economic activity to display a more favorable outlook in the second half of the year.

On the other hand, although the measures taken in order to stimulate the economy in Japan reinforced the optimistic expectations for the global economic activity, the recent data announced in China, which gave mixed signals, increased the tensions again.

Industrial production and the current account deficit figures pointed out that the recovery in Turkish economy was slightly below expectations in the first quarter of 2013. However, credit rating upgrade by a second rating agency to investment grade and the upgrades by two other regional rating agencies would increase Turkey's external financing opportunities. In this context, the decline in borrowing costs and increasing maturities will enable Turkish economy to be more resilient to external shocks.

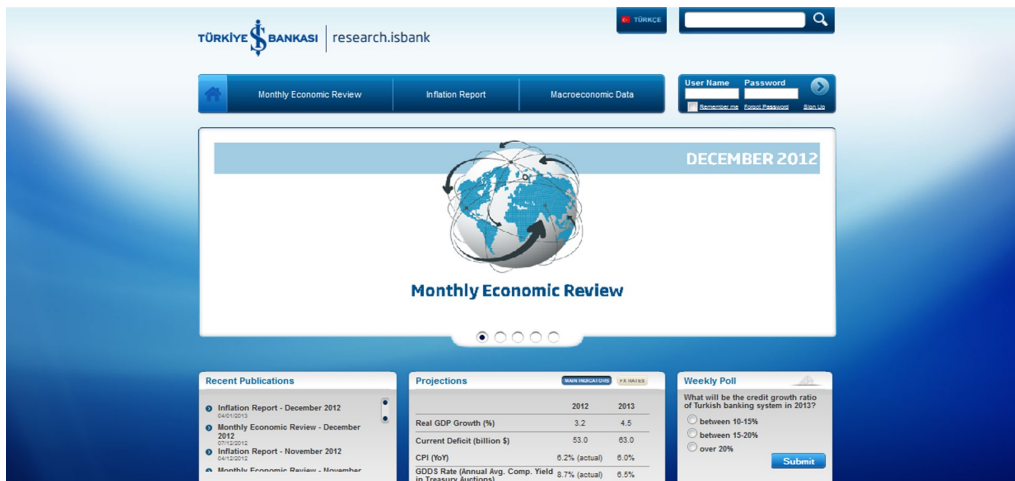
| Forecasts | 2012 (R) | 2013 |
|--------------------------|----------|--------|
| Growth (%) | 2.2 | 4.5 |
| CA Deficit (USD billion) | 47.5 | 60 |
| CA Deficit/GDP (%) | 6.0 | 6.7 |
| Inflation (%) | 6.2 | 6.0 |
| GDDI Interest* (%) | 8.7 | 6.4 |
| USD/TL | 1.7826 | 1.7750 |
| EUR/TL | 2.3517 | 2.2365 |

(*) Annual compound average interest rate in treasury auctions

(R) Realization

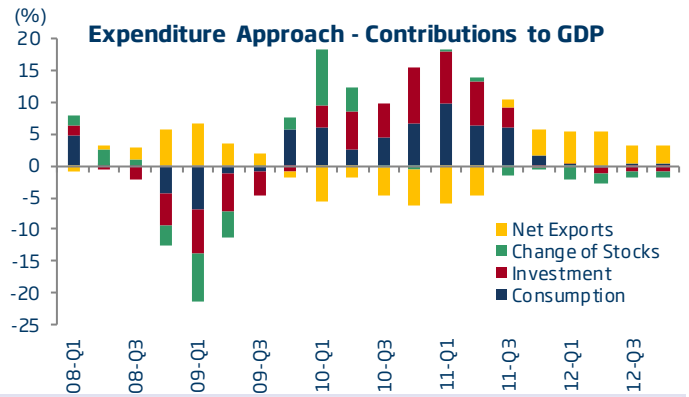
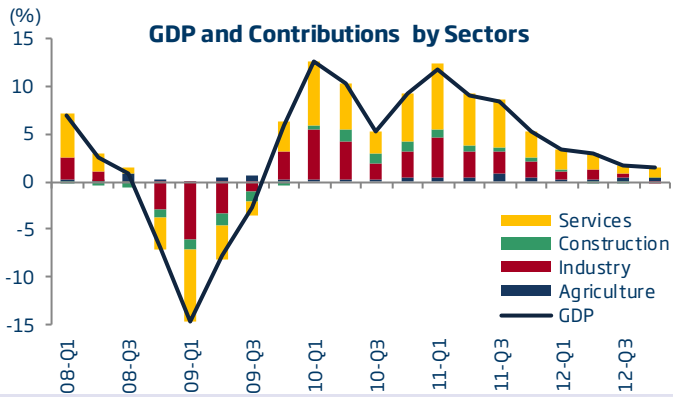
FX, interest and inflation are year-end forecasts

Our reports are available on our website <http://research.isbank.com.tr>

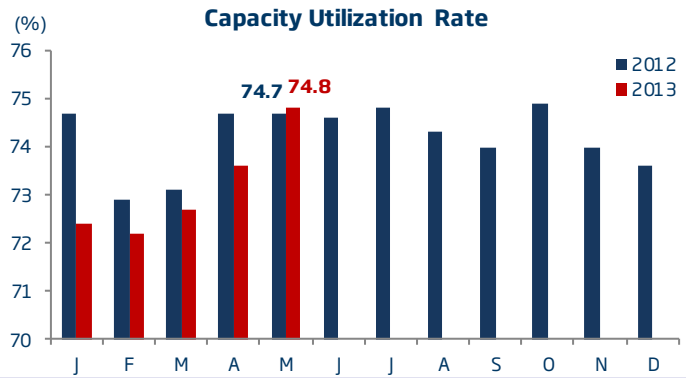
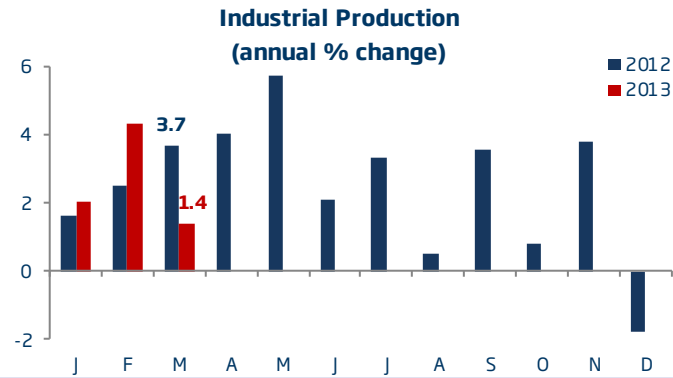


The screenshot shows the website interface for Türkiye Bankası's research department. The main navigation includes 'Monthly Economic Review', 'Inflation Report', and 'Macroeconomic Data'. A search bar and user login fields are present. The central focus is the 'Monthly Economic Review' for December 2012, which includes a globe graphic. Below the main content, there are three sections: 'Recent Publications' listing reports from December 2012 and November 2012; 'Projections' comparing 2012 and 2013 data for Real GDP Growth (3.2% vs 4.5%), Current Deficit (53.0 vs 63.0 billion \$), CPI (0.2% actual vs 0.0%), and GDDI Rate (8.7% actual vs 6.5%); and a 'Weekly Poll' asking for the credit growth ratio of the Turkish banking system in 2013, with options: between 10-15%, between 15-20%, and over 20%.

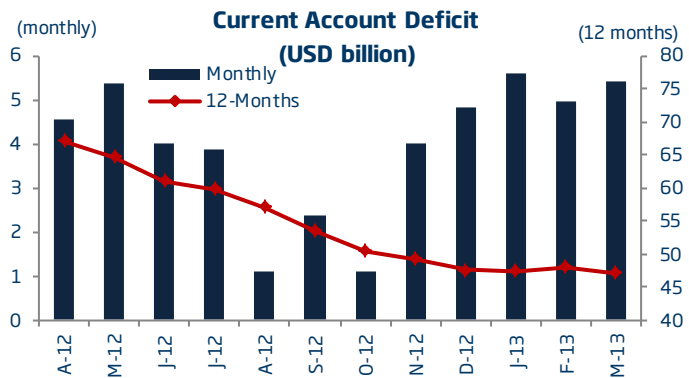
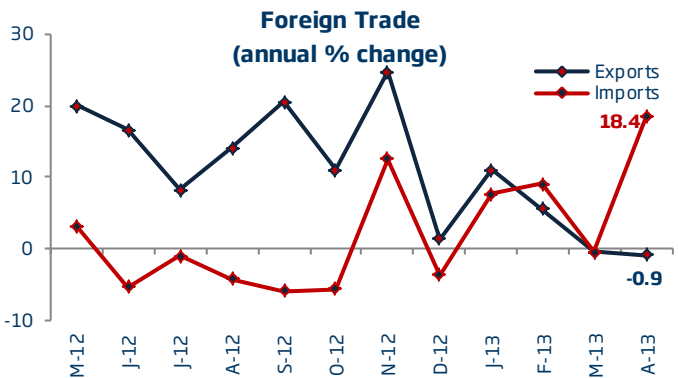
Growth



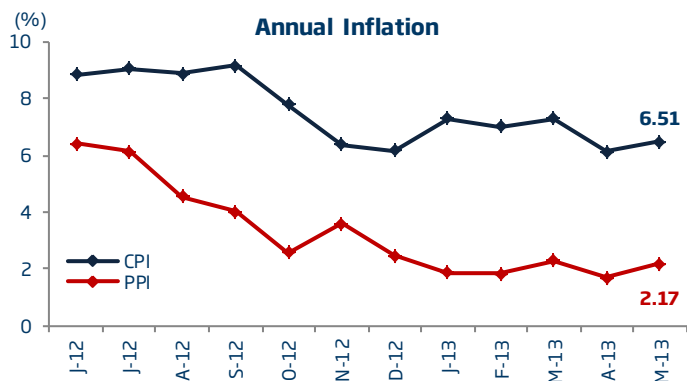
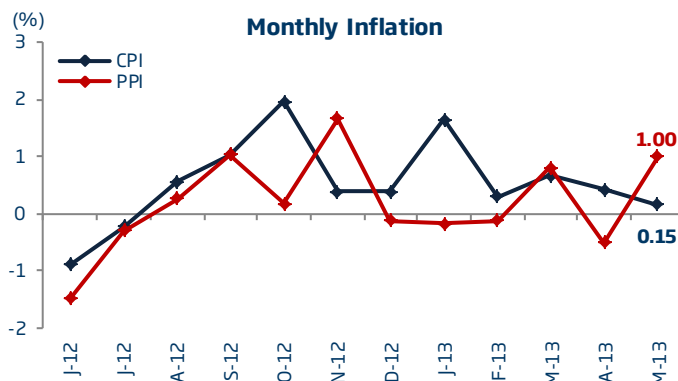
Industrial Production



Foreign Trade and Current Account Balance

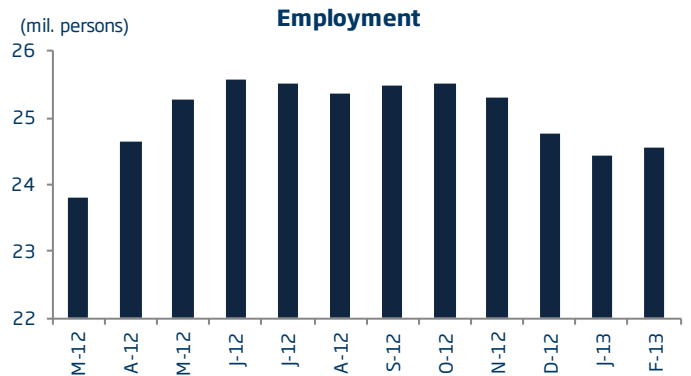
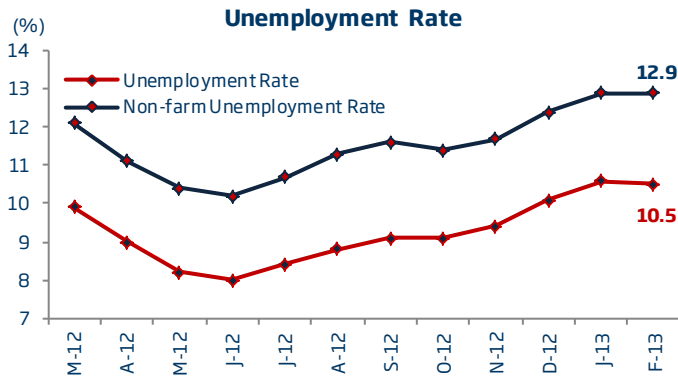


Inflation

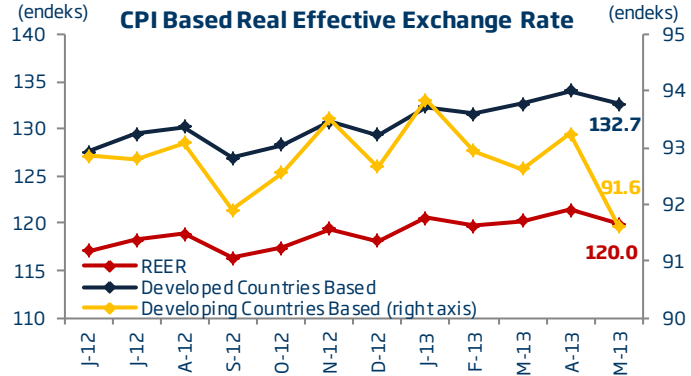
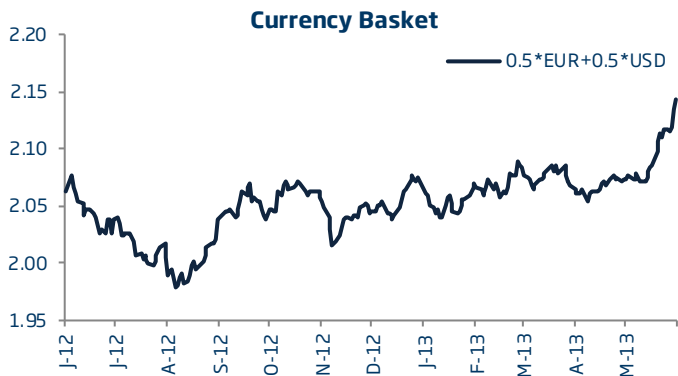


Source: Turkstat, CBRT

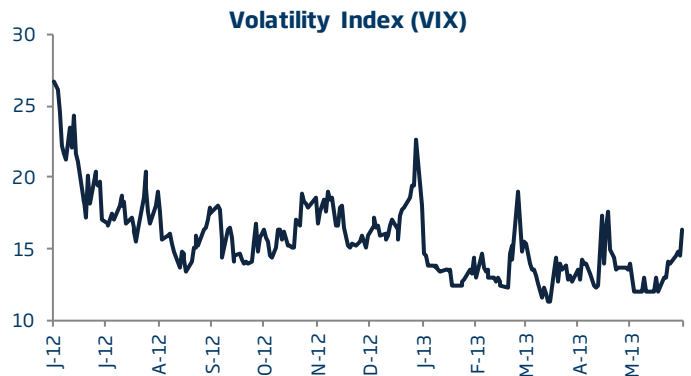
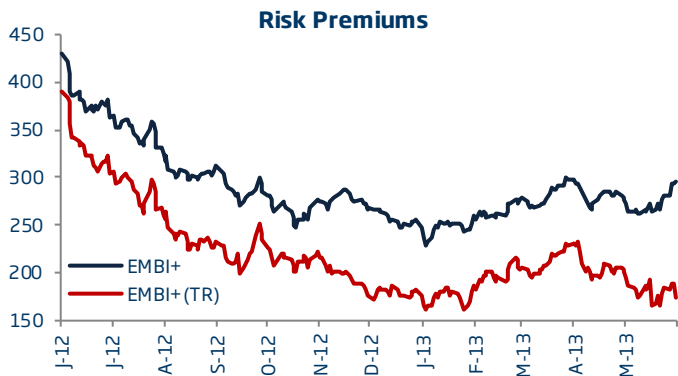
Labor Market



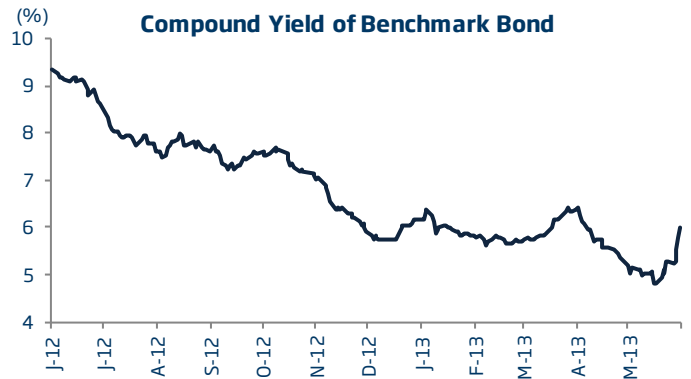
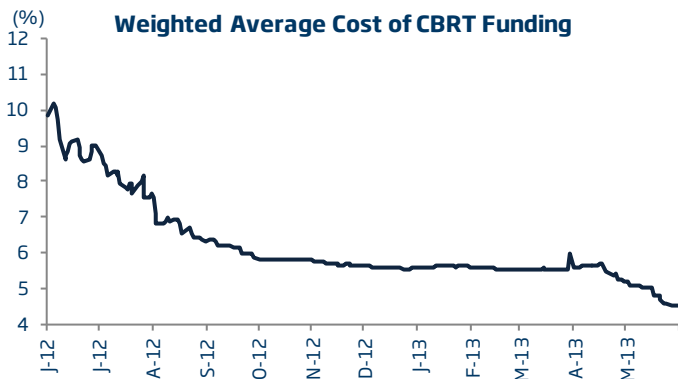
FX Market



Risk Indicators

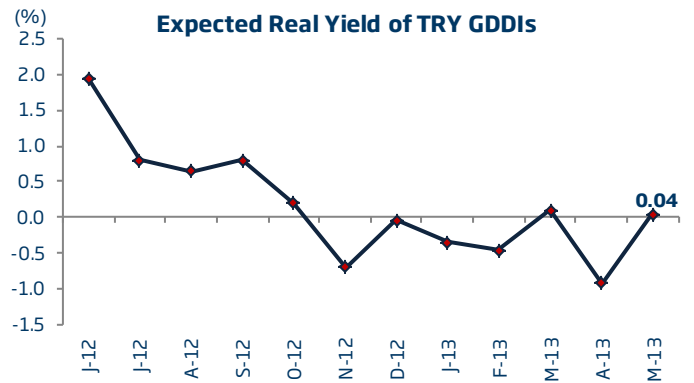
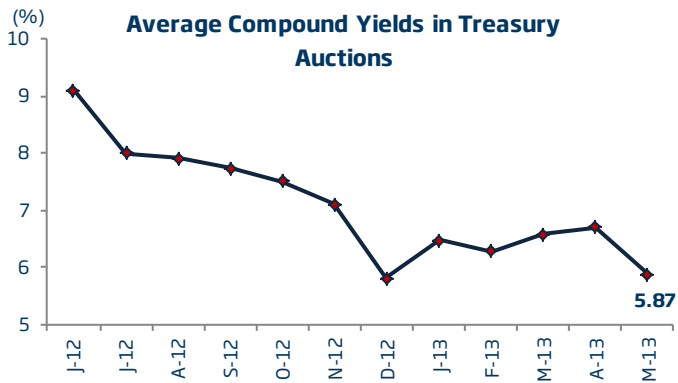


Interest Rates

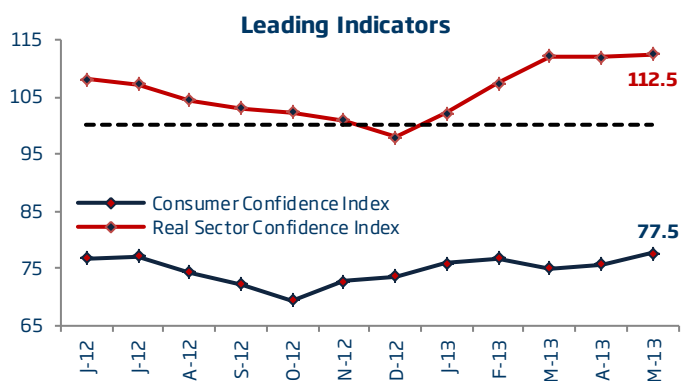
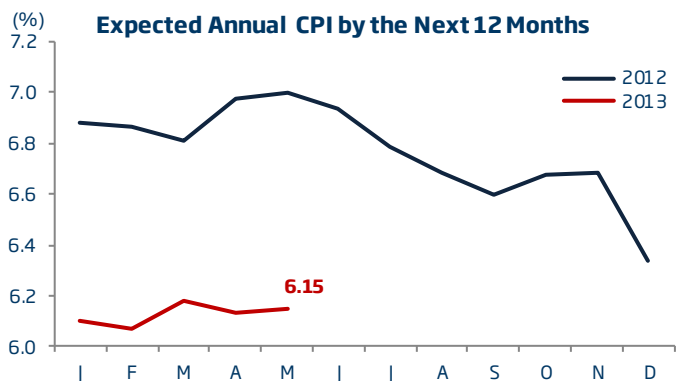
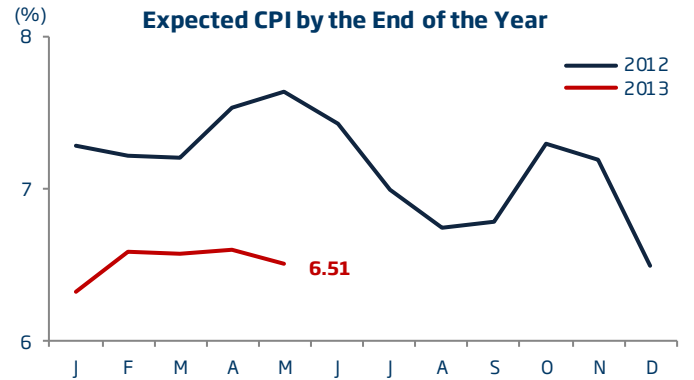
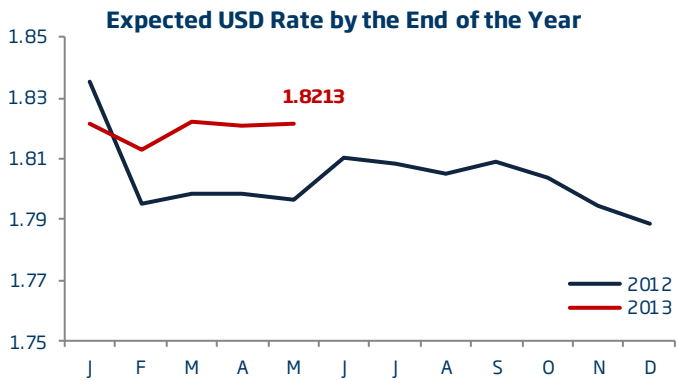
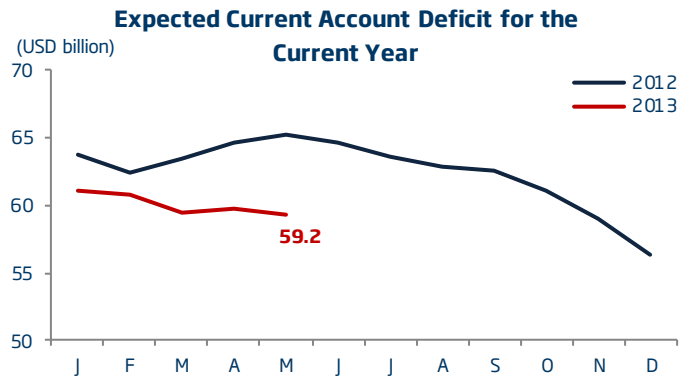
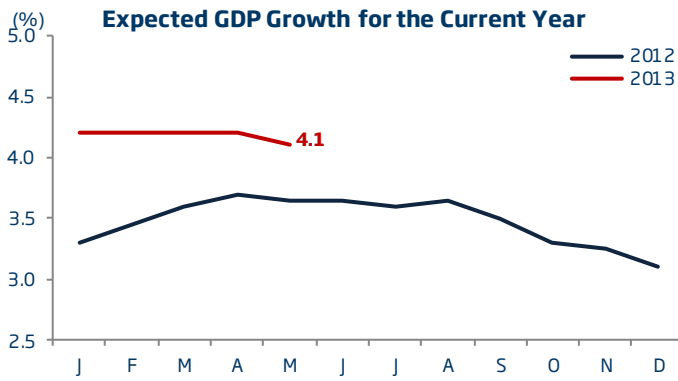


Source: Turkstat, CBRT, JP Morgan, Reuters, ISE

Bond-Bill Market



Survey of Expectations and Other Leading Indicators



Source: Treasury, ISE, CBRT, Economic Research Division

Turkish Economy at a Glance

| | 2008 | 2009 | 2010 | 2011 | 2012 | 13-Q1 | 13-Q2 | 13-Q3 |
|--|--------------|--------------|--------------|---------------|--------------|---------------|---------------|---------------|
| Growth | | | | | | | | |
| GDP (USD Billion) | 742.1 | 616.7 | 731.6 | 774.0 | 786.3 | | | |
| GDP Growth Rate (%) | 0.7 | -4.8 | 9.2 | 8.8 | 2.2 | - | - | - |
| Inflation (%) | | | | | | Mar-13 | Apr-13 | May-13 |
| CPI (annual) | 10.1 | 6.5 | 6.4 | 10.4 | 6.2 | 7.3 | 6.1 | 6.5 |
| PPI (annual) | 8.1 | 5.9 | 8.9 | 13.3 | 2.5 | 2.3 | 1.7 | 2.2 |
| Labor Market | | | | | | Dec-12 | Jan-13 | Feb-13 |
| Unemployment Rate (%) | 11.0 | 14.0 | 11.9 | 9.8 | 9.2 | 10.1 | 10.6 | 10.5 |
| Employment (thousand persons) | 21,194 | 21,277 | 22,594 | 24,110 | 24,821 | 24,766 | 24,433 | 24,546 |
| FX Rates | | | | | | Mar-13 | Apr-13 | May-13 |
| CPI Based Real Effective Exchange Rate | 114.9 | 116.8 | 125.7 | 109.5 | 118.2 | 120.3 | 121.4 | 120.0 |
| USD/TL | 1.5123 | 1.5057 | 1.5460 | 1.9065 | 1.7826 | 1.8137 | 1.7953 | 1.8661 |
| EUR/TL | 2.1408 | 2.1603 | 2.0491 | 2.4592 | 2.3517 | 2.3206 | 2.3501 | 2.4208 |
| Currency Basket (0.5*EUR+0.5*USD) | 1.8266 | 1.8330 | 1.7976 | 2.1829 | 2.0672 | 2.0672 | 2.0727 | 2.1435 |
| Foreign Trade Balance⁽¹⁾ (USD billion) | | | | | | Feb-13 | Mar-13 | Apr-13 |
| Exports | 132.0 | 102.1 | 113.9 | 134.9 | 152.5 | 154.3 | 154.2 | 154.1 |
| Imports | 202.0 | 140.9 | 185.5 | 240.8 | 236.5 | 239.5 | 239.4 | 242.9 |
| Foreign Trade Balance | -69.9 | -38.8 | -71.7 | -105.9 | -84.1 | -85.2 | -85.2 | -88.8 |
| Import Coverage Ratio (%) | 65.4 | 72.5 | 61.4 | 56.0 | 64.5 | 64.4 | 64.4 | 63.4 |
| Current Account Balance⁽¹⁾ (USD billion) | | | | | | Jan-13 | Feb-13 | Mar-13 |
| Current Account Balance | -40.4 | -12.2 | -45.4 | -75.1 | -47.5 | -47.3 | -48.0 | -47.1 |
| Capital and Financial Accounts | 37.4 | 9.3 | 44.0 | 65.7 | 46.4 | 48.6 | 52.6 | 55.3 |
| Direct Investments (net) | 17.2 | 7.1 | 7.6 | 13.7 | 8.5 | 8.2 | 8.0 | 7.6 |
| Portfolio Investments (net) | -5.0 | 0.2 | 16.1 | 22.0 | 40.8 | 41.2 | 43.5 | 44.4 |
| Other Investments (net) | 24.2 | 2.1 | 33.2 | 28.2 | 18.0 | 26.5 | 28.1 | 30.6 |
| Reserve Assets (net) | 1.1 | -0.1 | -12.8 | 1.8 | -20.8 | -27.2 | -26.9 | -27.1 |
| Net Errors and Omissions | 3.0 | 2.9 | 1.4 | 9.4 | 1.9 | -1.3 | -4.6 | -8.2 |
| Current Account Deficit/GDP | -5.4 | -2.0 | -6.2 | -9.7 | -6.0 | - | - | - |
| Budget⁽²⁾⁽³⁾ (TL billion) | | | | | | Feb-13 | Mar-13 | Apr-13 |
| Expenditures | 227.0 | 268.2 | 294.4 | 314.6 | 360.5 | 64.9 | 95.0 | 124.9 |
| Interest Expenditures | 50.7 | 53.2 | 48.3 | 42.2 | 48.4 | 10.2 | 15.1 | 18.2 |
| Non-interest Expenditures | 176.4 | 215.0 | 246.1 | 272.4 | 312.1 | 54.7 | 79.9 | 106.7 |
| Revenues | 209.6 | 215.5 | 254.3 | 296.8 | 331.7 | 69.4 | 94.1 | 124.6 |
| Tax Revenues | 168.1 | 172.4 | 210.6 | 253.8 | 278.8 | 56.0 | 77.4 | 101.5 |
| Budget Balance | -17.4 | -52.8 | -40.1 | -17.8 | -28.8 | 4.5 | -0.9 | -0.3 |
| Primary Balance | 33.2 | 0.4 | 8.2 | 24.4 | 19.6 | 14.7 | 14.3 | 17.9 |
| Budget Balance/GDP | -1.8 | -5.5 | -3.6 | -1.4 | -2.0 | - | - | - |
| Central Government Debt Stock (USD billion) | | | | | | Feb-13 | Mar-13 | Apr-13 |
| Domestic Debt Stock | 181.7 | 219.2 | 228.2 | 195.2 | 216.8 | 216.5 | 217.2 | 219.2 |
| External Debt Stock | 69.8 | 74.1 | 78.1 | 79.2 | 81.7 | 80.6 | 79.9 | 81.8 |
| Total | 251.5 | 293.2 | 306.3 | 274.4 | 298.6 | 297.2 | 297.0 | 301.0 |

(1) 12 month cumulative

(2) Year-to-date % change

(3) According to Central Government Budget

Source: Turkstat, CBRT, Treasury, Ministry of Finance, Reuters

BANKING SECTOR ACCORDING TO BRSA'S MONTHLY BULLETIN FIGURES

| (TL billion) | 2008 | 2009 | 2010 | 2011 | 2012 | Feb-13 | Mar-13 | Change ⁽¹⁾ |
|-------------------------------------|--------------|--------------|---------------|---------------|---------------|---------------|---------------|-----------------------|
| TOTAL ASSETS | 732.5 | 834.0 | 1006.7 | 1217.7 | 1370.7 | 1397.1 | 1427.7 | 4.2 |
| Loans | 367.4 | 392.6 | 525.9 | 682.9 | 794.8 | 815.3 | 833.6 | 4.9 |
| TL Loans | 262.1 | 288.2 | 383.8 | 484.8 | 588.4 | 604.1 | 619.9 | 5.4 |
| Share (%) | 71.3 | 73.4 | 73.0 | 71.0 | 74.0 | 74.1 | 74.4 | - |
| FX Loans | 105.3 | 104.4 | 142.1 | 198.1 | 206.4 | 211.1 | 213.7 | 3.5 |
| Share (%) | 28.7 | 26.6 | 27.0 | 29.0 | 26.0 | 25.9 | 25.6 | - |
| Non-performing Loans | 14.1 | 21.9 | 20.0 | 19.0 | 23.4 | 24.8 | 25.6 | 9.2 |
| Non-performing Loan Rate (%) | 3.7 | 5.3 | 3.7 | 2.7 | 2.9 | 3.0 | 3.0 | - |
| Securities | 194.0 | 262.9 | 287.9 | 285.0 | 270.0 | 272.2 | 270.7 | 0.3 |
| TOTAL LIABILITIES | 732.5 | 834.0 | 1006.7 | 1217.7 | 1370.7 | 1397.1 | 1427.7 | 4.2 |
| Deposits | 454.6 | 514.6 | 617.0 | 695.5 | 771.9 | 786.1 | 789.4 | 2.3 |
| TL Deposits | 294.1 | 341.4 | 433.5 | 460.0 | 520.3 | 529.1 | 530.7 | 2.0 |
| Share (%) | 64.7 | 66.3 | 70.3 | 66.1 | 67.4 | 67.3 | 67.2 | - |
| FX Deposits | 160.5 | 173.2 | 183.5 | 235.5 | 251.6 | 256.9 | 258.7 | 2.8 |
| Share (%) | 35.3 | 33.7 | 29.7 | 33.9 | 32.6 | 32.7 | 32.8 | - |
| Securities Issued | 0.0 | 0.1 | 3.1 | 18.4 | 37.9 | 42.9 | 44.0 | 16.3 |
| Payables to Banks | 92.7 | 86.1 | 122.4 | 167.4 | 173.4 | 183.0 | 195.7 | 12.9 |
| Funds from Repo Transactions | 40.8 | 60.7 | 57.5 | 97.0 | 79.9 | 73.9 | 92.0 | 15.1 |
| TOTAL SHAREHOLDERS' EQUITY | 86.4 | 110.9 | 134.5 | 144.6 | 181.9 | 186.5 | 186.2 | 2.4 |
| Profit (Loss) of the Period | 13.4 | 20.2 | 22.1 | 19.8 | 23.5 | 4.3 | 7.1 | - |
| RATIOS (%) | | | | | | | | |
| Loans/Assets | 50.2 | 47.1 | 52.2 | 56.1 | 58.0 | 58.4 | 58.4 | - |
| Securities/Assets | 26.5 | 31.5 | 28.6 | 23.4 | 19.7 | 19.5 | 19.0 | - |
| Deposits/Liabilities | 62.1 | 61.7 | 61.3 | 57.1 | 56.3 | 56.3 | 55.3 | - |
| Deposits/Loans | 123.7 | 131.1 | 117.3 | 101.8 | 97.1 | 96.4 | 94.7 | - |
| Capital Adequacy (%) | 18.0 | 20.6 | 19.0 | 16.6 | 17.9 | 17.6 | 17.4 | - |

(1) Year-to-date % change



LEGAL NOTICE

This report has been prepared by Türkiye İş Bankası A.Ş. economists and analysts by using the information from publicly available sources believed to be reliable, solely for information purposes; and they are not intended to be construed as an offer or solicitation for the purchase or sale of any financial instrument or the provision of an offer to provide investment services. The views, opinions and analyses expressed do not represent the official standing of Türkiye İş Bankası A.Ş. and are personal views and opinions of the analysts and economists who prepare the report. No representation or warranty, express or implied, is made as to the accuracy or completeness of the information contained in this report. All information contained in this report is subject to change without notice, Türkiye İş Bankası A.Ş. accepts no liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

This report is copyright-protected. Reproducing, publishing and/or distributing this report in whole or in part is therefore prohibited. All rights reserved.
