

Global Economy

- ◆ The US Federal Reserve raised the policy rate by 25 basis points at the last monetary policy meeting of the year held on December 13-14. The Fed members' interest rate projections signaled 3 rate hikes in 2017.
- ◆ The US economy grew more than expected in the third quarter, expanding by 3.5%. Recent macroeconomic data indicated that economic activity in the country has stabilized.
- ◆ Gentiloni was named as Italy's new prime minister following Renzi's resignation after losing the referendum on constitutional reform. Developments in the country's banking sector also came under focus in the recent period. As the Italian parliament has approved a 20 billion euro rescue package for the banking sector, the Government has announced that it will bail out Monte dei Paschi.
- ◆ Keeping the policy rate on hold, ECB made an adjustment to the asset purchase program at the monetary policy meeting held on December 8. ECB has reduced the amount of monthly asset purchases by 20 billion euro to 60 billion euro, effective from March 2017, while extending the asset purchase program until the end of 2017.
- ◆ The upward trend in producer prices in China continued in November.
- ◆ Gold prices, which had been on a declining trend since 2013, increased in 2016 on annual basis. However, the stronger outlook for the US dollar limited this increase.
- ◆ Oil prices, which have followed an upward trajectory after the oil producers' decision to cut production, reached their highest level of the year in December. In 2016, the price of Brent oil surged by 45.4% compared to the previous year.

Turkish Economy

- ◆ Turkstat has changed the calculation method of GDP. In this context, growth figures which had previously been expressed at constant prices now started to be calculated according to the chain-linked volume index (2009=100).
- ◆ Turkish economy, which shrank by 1.8% in the third quarter of the year, showed signs of recovery in the last quarter of 2016. Calendar adjusted industrial production posted an annual rise of 2% in October.
- ◆ Despite the significant recovery recorded in November, exports decreased by 1.7% yoy during the January-November period. The contraction in imports came in at 4.8% in this period thanks to the lower commodity prices. In this context, the foreign trade deficit narrowed by 11.8% compared to the first eleven months of 2015.
- ◆ In October, current account balance posted a deficit of 1.7 billion USD, in tandem with the market expectations. In the first ten months of the year, the current account deficit expanded by 6% yoy and became 26.5 billion USD. 12-month cumulative current account deficit stood at 33.8 billion USD, the highest since November 2015.
- ◆ Budget revenues rose by 38.6% yoy in October owing to tax regulations. Budget expenditures also expanded by 17.9% yoy in this period. Thus, budget, which gave a surplus of 0.8 billion TRY in November 2015, posted a surplus of 10 billion TRY in the same month of 2016.
- ◆ Annual CPI inflation, which fluctuated within a band of 6.6-9.6% in 2016, came in at 8.53% at the end of the year. Annual D-PPI inflation reached 9.94% at the end of 2016, the highest level of the last 26 months.
- ◆ After increasing policy rate in November for the first time since January 2014, CBRT kept the interest rates unchanged at its meeting in December.

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Turkstat adopted new standards for national accounts.

Turkstat has started to calculate GDP figures in accordance with the guidelines of the National Accounts System (SNA-2008) and the European Accounting System (ESA-2010). Therefore, growth figures which had previously been expressed at constant prices now started to be calculated according to the chain-linked volume index (2009=100). Turkstat also made methodological and statistical improvements. For example, "R&D" and "Military Weapon Systems", which had been classified as expenditures, are recognized as fixed capital formation. Labor input approach is used in calculating the informal sector. Loss premiums are incorporated into the insurance sector calculations. With the introduction of the new method, annual GDP and quarterly GDP figures will be released separately. Past GDP growth numbers were also revised according to the new standards.

Comparison of Annual GDP Figures

| | GDP (%) | | GDP Per Capita (USD) | |
|------|------------|-------------|----------------------|------------|
| | Old Method | New Method* | Old Method | New Method |
| 2009 | -4.8 | -4.7 | 8,561 | 8,980 |
| 2010 | 9.2 | 8.5 | 10,003 | 10,560 |
| 2011 | 8.8 | 11.1 | 10,428 | 11,205 |
| 2012 | 2.1 | 4.8 | 10,459 | 11,588 |
| 2013 | 4.2 | 8.5 | 10,822 | 12,480 |
| 2014 | 3.0 | 5.2 | 10,395 | 12,112 |
| 2015 | 4.0 | 6.1 | 9,257 | 11,014 |

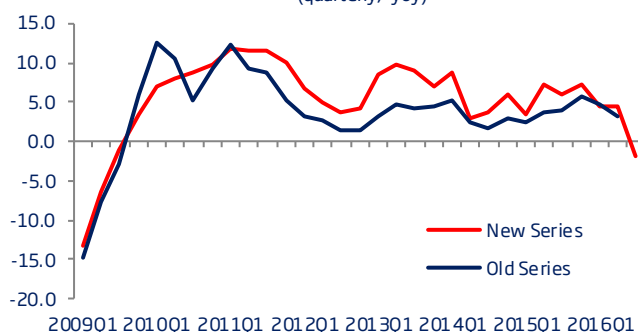
(*) Annual % change according to production approach.

Under the old method, the annual growth rate of Turkish economy, which was in a range of 2.1-4.2% during the last 4 years, has moved within a range of 4.8-8.5% based on new calculation. With this revision, GDP at current prices reached 2.3 trillion TRY in 2015. Also, GDP previously announced as 720 billion USD for 2015 has been revised up to 861 billion USD. Thus, GDP per capita has been 11,014 USD in 2015, higher than the previously released figure of 9,257 USD. As a result of the revisions made to quarterly data, GDP growth for the first quarter of 2016 decreased from 4.7% to 4.5%, while that for the second quarter surged from 3.1% to 4.5%.

In the third quarter of the year, Turkish economy contracted by 1.8%.

According to the chain-linked volume index, GDP in Turkey shrank by 1.8% in the third quarter of the year compared to the same period of the previous year. Hence, the Turkish economy has contracted for the first time after 27 quarters of uninterrupted positive growth. For the first nine months of the year, on the other hand, Turkish economy grew by 2.2% on an annual basis.

GDP Growth
(quarterly, yoy)



While household consumption expenditures decreased in the third quarter compared to the same period of the previous year, public sector has accelerated consumption expenditures. Investment spending, on the other hand, declined in this period.

Only construction sector expanded in the third quarter.

According to production approach, construction sector was the only main sector that recorded a real increase in the third quarter of 2016 compared to the same period of the previous year. The construction sector, which displayed a positive performance in the first two quarters of 2016, also grew by 1.4% in real terms in the third quarter.

Having contributed significantly to the growth in the third quarter of last year, agricultural sector fell by 7.7% due to the base effect. Leading indicators have already pointed to a weak outlook in this period. Accordingly, industrial and services sectors shrank by 1.4% and 8.4%, respectively. It was noteworthy that the share of the services sector in GDP at current prices declined to all-time record low level with 20.2%.

Saving rate became 24.8%.

Turkstat released official saving data based on the corporate sector accounts that have been published for the first time. Accordingly, Turkey's gross saving ratio is calculated as 24.8% of GDP in 2015. The rate was at 14.3% according to data released by Ministry of Development's based on previous methodology. Separately, according to Turkstat data household's saving ratio became 13.5% of total disposable income in 2015.

Expectations

Economic activity had been under considerable pressure during the third quarter of 2016 mainly stemmed from the failed coup attempt on July 15 as well as the weak performance of the tourism sector. In this period, the steps taken by public sector to support economic activity limited the contraction in GDP. In the last quarter of the year, on the other hand, leading indicators have indicated a partial recovery in economic activity. Public sector continued to support the economic activity in this period.

Source: Turkstat

The unemployment rate came in at 11.3%.

In September, the number of unemployed persons increased by 420 thousand compared to the same month of the previous year. The unemployment rate picked up by 1 percentage point to 11.3% in this period. Upsurge in unemployment rate mainly stemmed from the contraction in economy and the unfavorable outlook in the tourism sector during the third quarter. Besides these developments, the increase in labor force participation rate has played a role in rising unemployment rate. In fact, the participation rate in September reached a historic high of 52.8%.

Industrial production rose by 2% in October.

Turkish economy, which shrank by 1.8% in the third quarter of the year, showed signs of recovery in the last quarter. Calendar adjusted industrial production posted an annual rise of 2% in October. In this period, food products and motor vehicles made the highest contribution to the growth in industrial production.

to the same month of the previous year. Mortgaged house sales went up by 71.4% yoy, mainly due to easing of macroprudential measures on retail loans and fall in loan rates thanks to the interest rate cuts by the CBRT during March-September period.

According to the Automotive Manufacturers Association, automotive industry production expanded at an annual pace of 8% in the first 11 months of the year, particularly due to the increase in automobile exports. Thus, automotive production rose to a historic high of 1.3 million for the January-November period. In November, domestic automobile sales also climbed by 54% yoy as Special Consumption Tax hike pulled demand forward.

After contracting in October, domestic white goods sales also increased by 20% yoy in November.

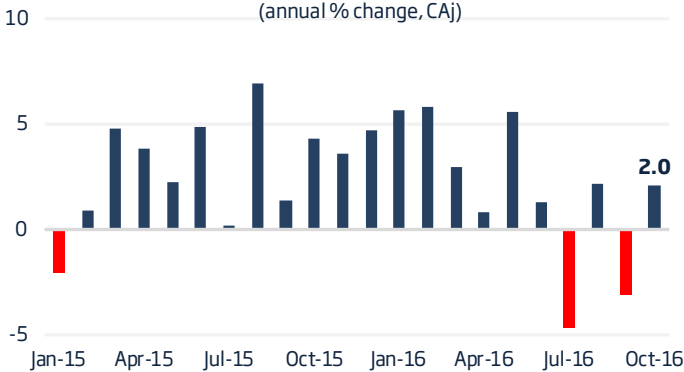
Manufacturing PMI remained below the threshold for 10 consecutive months...

The Purchasing Managers Index (PMI) indicated that manufacturing activity continued to be under pressure. Having recovered in October, manufacturing PMI dropped again in the following months. The index, which fell to 47.7 in December, was below the 50 threshold level for 10 months. On the other hand, assessments on employment in manufacturing sector increased for the fifth month in December, indicating a positive development.

Negative outlook on confidence indices...

In December, the real sector confidence index fell below the 100 level for the first time in 14 months. This reading indicated that economic activity in the sector displayed a weak performance. Consumer confidence also posted a monthly decline of 8% in the same period. Similarly, the economic confidence index fell by 18.5% to 70.5 in the same period.

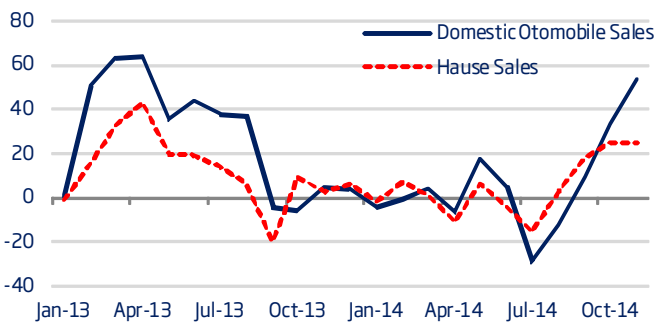
Industrial Production Index
(annual % change, CAj)



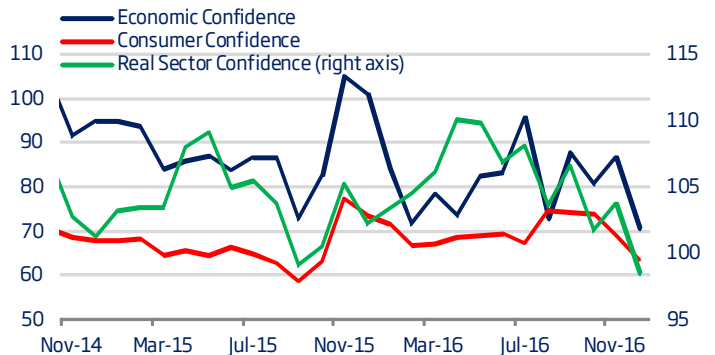
Recovery in domestic demand...

House sales, which started to accelerate in September, posted a strong performance in November as well. House sales in Turkey increased by 25.1% in November compared

Domestic Otomobile and House Sales
(annual % change)



Confidence Indicators



Source: Datastream, Turkstat, CBRT, Markit, TURKBESD

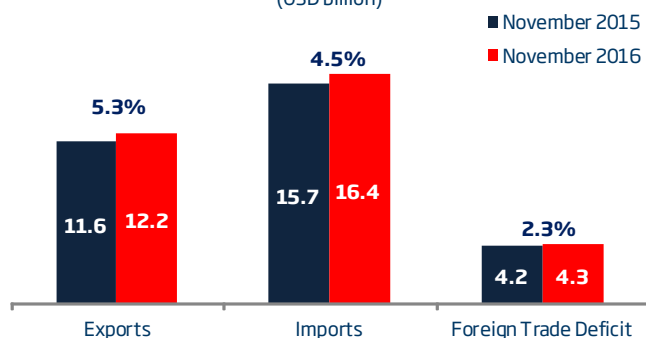
Strong growth in exports...

In November, exports recorded an annual increase of 9.7%, rising at the fastest pace of the year. Imports expanded by 6% from a year earlier. As a result, foreign trade deficit narrowed by 4.1% yoy and became 4.1 billion USD. The import coverage ratio, surging by 2.6 points compared to a year ago, reached 75.7%.

Despite the significant recovery recorded in November, exports decreased by 1.7% yoy in the January-November period. The contraction in imports came in at 4.8% in this period thanks to the lower commodity prices. In this context, the foreign trade deficit narrowed by 11.8% compared to the first eleven months of 2015.

Excluding Gold - Foreign Trade Figures

(USD billion)



The strong performance of exports was mainly led by gold exports.

Gold exports increased by 525 million USD to 627 million USD in November compared to the same period of the previous year. Thus, gold exports made a contribution of 4.5 percentage points to the annual increase in total exports. Excluding the gold trade, the foreign trade deficit widened by 2.3% yoy.

Exports of the motor vehicles, the biggest export item, picked up by 18.8% yoy in November. In addition to the gold exports, the rises in exports of iron-steel and ships were also noteworthy in this period.

In November, Germany and Britain were two of the biggest export markets of Turkey. As exports to the UAE more than tripled in November, the county ranked third. Gold exports to the UAE, which amounted to 478 million USD, played a

prominent role in this development.

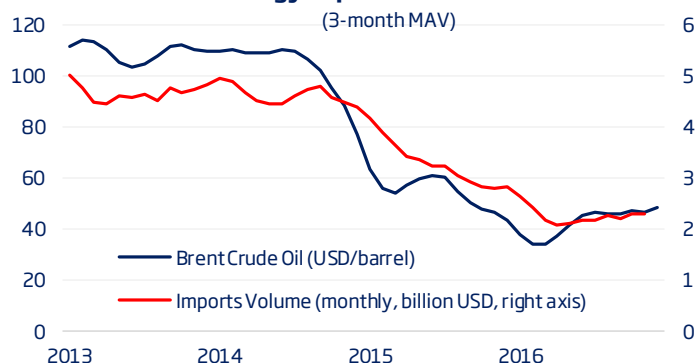
Exports to the EU countries, which have been the largest export market of Turkey, rose by 6.6% yoy in November. On the other hand, exports to the Near and Middle East countries expanded by 25.2% in this period on the back of the high gold trade. Accordingly, the share of the region in total exports surged to 23.6%.

The decline in energy bill has persisted.

Imports of mineral fuels and oils, which are the biggest import items in general due to the high energy import dependency, fell by 8.1% yoy in November. The fall in energy imports thanks to low energy prices and the drop in imports of iron-steel and aluminum had positive impact on foreign trade indicators in this period. On the other hand, gold imports, which doubled in November compared to the same month of last year, limited the favorable impact of the gold exports.

Energy Imports and Oil Prices

(3-month MAV)



Expectations

Having widened in September and October, foreign trade deficit narrowed in November due mostly to the rise in gold exports. We expect that there will be an upward pressure on imports in the upcoming period due to the fading positive impact of low energy prices and the steps taken to support domestic demand. However, we believe that the depreciation in TL will reduce this pressure somewhat. Exports, on the other hand, may exhibit a better performance should the ongoing problems regarding our main export markets diminish.

Foreign Trade Balance

(USD billion)

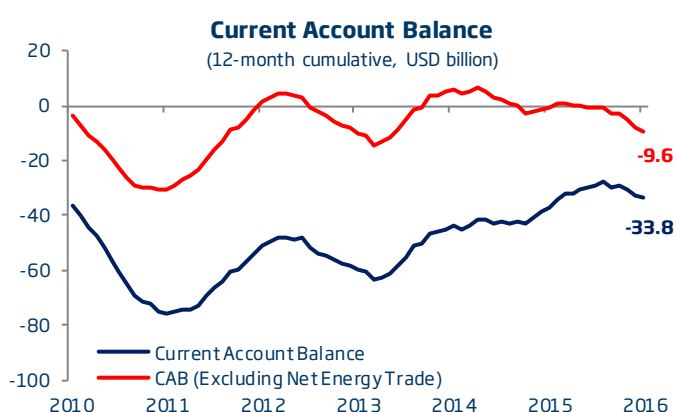
| | November | | Change (%) | Jan.-Nov. | | Change (%) |
|------------------------------|-------------|-------------|-------------|--------------|--------------|--------------|
| | 2015 | 2016 | | 2015 | 2016 | |
| Exports | 11.7 | 12.8 | 9.7 | 132.1 | 129.8 | -1.7 |
| Imports | 16.0 | 16.9 | 6.0 | 189.2 | 180.2 | -4.8 |
| Foreign Trade Balance | -4.3 | -4.1 | -4.1 | -57.2 | -50.4 | -11.8 |
| Import Coverage Ratio (%) | 73.1 | 75.7 | - | 69.8 | 72.0 | - |

Source: Datastream, Turkstat

Current account deficit came in line with the expectations in October.

In October, current account balance posted a deficit of 1.7 billion USD, in tandem with the market expectations. Current account had recorded a deficit of 343 million USD in the same month of the previous year.

In the first ten months of the year, the current account deficit expanded by 6% yoy and became 26.5 billion USD. 12-month cumulative current account deficit stood at 33.8 billion USD, the highest since November 2015. The current account deficit excluding net energy trade hit the highest level in the last 32 months with 9.6 billion USD, according to 12-month cumulative figures.



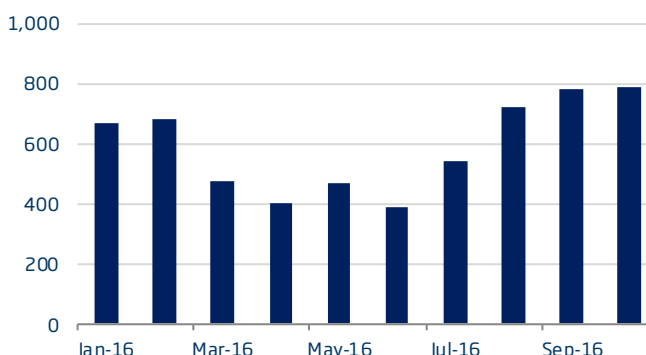
The fall in tourism revenues and the rise in foreign trade deficit weighed on the current account balance.

In October, the rise in the current account deficit mostly stemmed from the deterioration in services balance. The surplus in services balance fell by 916 million USD compared to a year ago. About 630 million USD of this amount was driven by the decline in tourism revenues. Nevertheless, it is seen that the fall in net tourism revenues has lost some momentum in the recent months.

The foreign trade performance also had a negative impact on the current account deficit in this period. Foreign trade deficit widened by 13.5% yoy due to the fall in exports.

Net Foreign Direct Investments

(3-month moving average, USD million)



Capital flows...

Net foreign direct investments to Turkey showed no significant change both on an annual and a monthly basis and became 665 million USD in October. This amount remained above the average of the January-October period.

In October, portfolio investments posted an inflow of 2 billion USD, the highest since April. Non-residents made purchases of around 0.5 billion USD in equity markets and sold 1.2 billion USD in government debt securities market. Government's and banks' total net borrowing of 3.1 billion USD through bond issues in international markets led the portfolio investment account to become positive in this period.

Other investments recorded a net inflow of 596 million USD in October. The inflows remained limited due to the rise in domestic banks' currency and deposits within their foreign correspondent banks and the decline in foreign banks' deposits held within domestic banks. Non-banking sector, on the other hand, raised a net 1.2 billion USD of credit from abroad and became the main contributor to the capital inflows under other investments account. Banking sector also borrowed a net 215 million USD and supported the capital inflows to the country.

Breakdown of Net Capital Inflows (12-month cumulative, USD million)

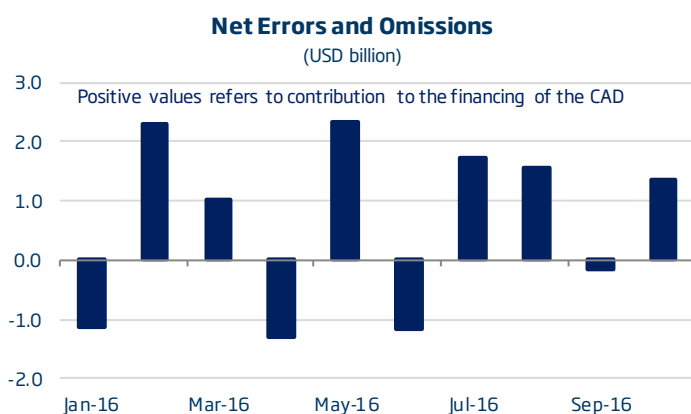
| | | | Breakdown of Net Capital Inflows (%) | |
|--|----------------|----------------|--------------------------------------|--------------|
| | Dec. 2015 | Oct. 2016 | Dec. 2015 | Oct. 2016 |
| Current Account Balance | -32,283 | -33,773 | - | - |
| Total Net Foreign Capital Inflows | 20,452 | 35,481 | 100.0 | 100.0 |
| -Direct Investments | 11,972 | 7,214 | 58.5 | 20.3 |
| -Portfolio Investments | -15,719 | 6,631 | - | - |
| -Other Investments | 14,924 | 17,105 | 73.0 | 48.2 |
| -Net Errors and Omissions | 9,296 | 4,523 | 45.5 | 12.7 |
| -Other | -21 | 8 | -0.1 | 0.0 |
| Reserves⁽¹⁾ | 11,831 | -1,708 | - | - |

Note: The numbers may not add up to total due to rounding.

(1) (-) sign indicates an increase in reserves while (+) sign indicates a decrease.

Source: Datastream, CBRT

Long-term debt rollover ratio for the banking sector continued to decline and became 119% while the ratio for the non-banking sectors stood at 164%, according to 12-month cumulative figures.



Reserves & net errors and omissions...

Having fallen fast in September, reserve assets posted an increase of 2.9 billion USD in October. Net errors and omissions, on the other hand, registered an inflow of 1.3 billion USD in this period, contributing to the financing of the current account deficit.

Expectations

While the decline in tourism revenues persisted despite losing some momentum, weak performance on the foreign trade front indicated that the upward risks on the current account deficit have increased. Even though the foreign trade deficit is expected to narrow in November as provisional data suggested, we foresee that the current account deficit might follow an upward trend if oil prices continue to rise in the period ahead.

| | (USD million) | | | | |
|-------------------------------------|-----------------|--------------------------|----------------|--------------|------------------------|
| | October 2016 | Jan. - Oct. 2015 2016 | | % Change | 12-Month Cumulative |
| Current Account Balance | -1,675 | -24,978 | -26,468 | 6.0 | -33,773 |
| Foreign Trade Balance | -2,804 | -39,980 | -33,772 | -15.5 | -41,906 |
| Services Balance | 1,793 | 22,253 | 13,702 | -38.4 | 15,596 |
| Travel (net) | 1,693 | 19,507 | 12,389 | -36.5 | 14,130 |
| Primary Income | -771 | -8,140 | -7,597 | -6.7 | -9,095 |
| Secondary Income | 107 | 889 | 1,199 | 34.9 | 1,632 |
| Capital Account | 0 | -6 | 23 | - | 8 |
| Financial Account | -328 | -13,693 | -19,927 | 45.5 | -29,242 |
| Direct Investments (net) | -665 | -10,364 | -5,606 | -45.9 | -7,214 |
| Portfolio Investments (net) | -1,990 | 11,665 | -10,685 | - | -6,631 |
| Net Acquisition of Financial Assets | 313 | 5,607 | -75 | - | 447 |
| Net Incurrence of Liabilities | 2,303 | -6,058 | 10,610 | - | 7,078 |
| Equity Securities | 471 | -921 | 1,209 | - | -265 |
| Debt Securities | 1,832 | -5,137 | 9,401 | - | 7,343 |
| Other Investments (net) | -596 | -10,022 | -12,203 | 21.8 | -17,105 |
| Currency and Deposits | 1,366 | 3,836 | -1,786 | - | -3,361 |
| Net Acquisition of Financial Assets | 827 | 16,209 | 1,757 | -89.2 | 696 |
| Net Incurrence of Liabilities | -539 | 12,373 | 3,543 | -71.4 | 4,057 |
| Central Bank | -50 | -826 | -442 | -46.5 | -532 |
| Banks | -489 | 13,199 | 3,985 | -69.8 | 4,589 |
| Foreign Banks | -115 | 9,431 | 3,580 | -62.0 | 4,091 |
| Foreign Exchange | 213 | 5,005 | -702 | - | -999 |
| Turkish Lira | -328 | 4,426 | 4,282 | -3.3 | 5,090 |
| Non-residents | -374 | 3,768 | 405 | -89.3 | 498 |
| Loans | -1,676 | -13,225 | -7,617 | -42.4 | -8,367 |
| Net Acquisition of Financial Assets | -362 | 466 | -13 | - | 313 |
| Net Incurrence of Liabilities | 1,314 | 13,691 | 7,604 | -44.5 | 8,680 |
| Banking Sector | 215 | 5,253 | -2,320 | - | -2,259 |
| Non-bank Sectors | 1,150 | 9,145 | 10,821 | 18.3 | 12,315 |
| Trade Credit and Advances | -283 | -371 | -2,812 | 658.0 | -5,389 |
| Other Assets and Liabilities | -3 | -262 | 12 | - | 12 |
| Reserve Assets (net) | 2,923 | -4,972 | 8,567 | - | 1,708 |
| Net Errors and Omissions | 1,347 | 11,291 | 6,518 | -42.3 | 4,523 |

The figures used in the table are according to the Sixth Edition of the Balance of Payments Manual. You can find the details [here](#).

Source: CBRT, Datastream

Budget posted 10 billion TRY surplus.

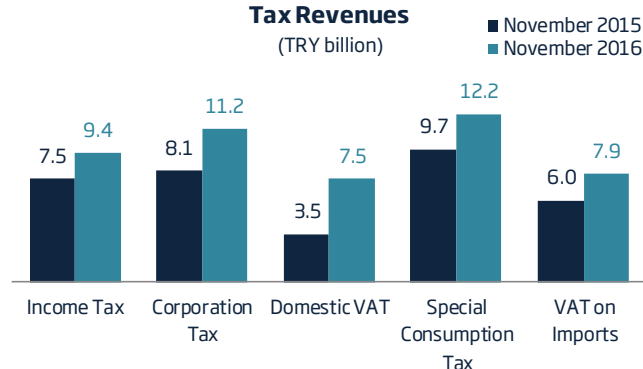
Budget revenues rose by 38.6% yoy in October owing to tax regulations. Similarly, budget expenditures expanded by 17.9% yoy in this period. Thus, budget, which gave a surplus of 0.8 billion TRY in November 2015, posted a surplus of 10 billion TRY in the same month of this year.

In the first 11 months of the year, budget revenues and expenditures surged by 15.1% yoy and 14.2% yoy, respectively. Budget deficit fell by 61% yoy to 2.1 billion TRY thanks to the strong performance of budget revenues. On the other hand, there was no significant change in the primary surplus due to the sharp increase in the non-interest expenditures.

Pick up in budget revenues...

In November, all sub-items of tax revenues exhibited a positive outlook. Having expanded by 37.2% yoy in November, tax revenues made 33 pp contribution to the increase in budget revenues. Domestic VAT revenues among tax revenues made the highest contribution to the growth in budget revenues by 9 pp. It was worth mentioning that revenues collected from special consumption tax and corporate tax climbed by 26% yoy and 38% yoy, respectively. An increase of 539 million TRY recorded under the tax amnesty also supported the increase in the budget revenues.

Tax Revenues
(TRY billion)

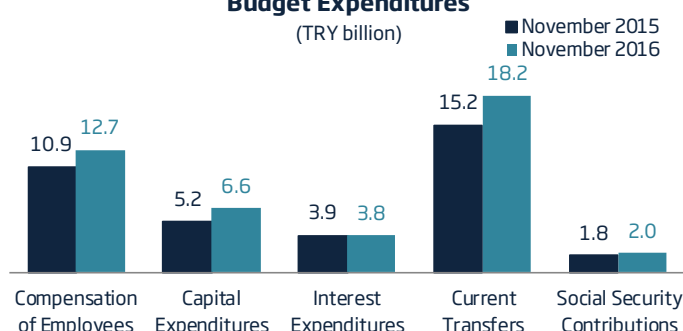


Budget expenditures...

The increase in budget spending in November mainly stemmed from the non-interest expenditures, rising by

around 20% yoy. Interest expenditures, on the other hand, remained broadly flat. In line with the government's increasing support to growth via investments; current transfers and capital expenditures surged in November. About two-thirds of the rise in budget expenditures was driven by these sub-items. Total current transfers increased by 19.6% yoy in this period. The total amount of 2.5 billion TRY transferred for the social security deficit finance had 5.8 pp upward impact on the total expenditure rise. It was noteworthy that the product purchase amounting to 1.2 billion TRY in November almost doubled compared to the previous year's figure. In this period, the amount of debt provided to public enterprises, increasing by 424 million TRY, made 1 pp contribution to the growth in budget expenditures.

Budget Expenditures
(TRY billion)



Expectations...

In November, budget revenues displayed a strong performance thanks to the upsurge in tax revenues and revenues collected under tax amnesty. Under the assumption that the average growth rate of 15% recorded in the budget revenues in the first 11 months will be sustained in December, budget revenues might exceed the MTP target by 10 billion TRY. On the spending front, taking MTP targets into consideration, it is seen that 70 billion TRY will be available to spend in December. Accordingly, government, having taken steps to support economic activity in the last quarter, has a room to spend about 80 billion TRY in December.

Central Government Budget

| | November | | | January-November | | | (TRY billion) | | |
|---------------------------|-------------|-------------|----------------|------------------|--------------|--------------|--------------------|--------------|---------------------|
| | 2015 | 2016 | % Change | 2015 | 2016 | % Change | 2016 Budget Target | MTP Target | Real/MTP Target (%) |
| Expenditures | 43.0 | 50.7 | 17.9 | 447.2 | 510.7 | 14.2 | 570.5 | 581.1 | 87.9 |
| Interest Expenditures | 3.9 | 3.8 | -1.0 | 51.3 | 48.4 | -5.6 | 56.0 | 51.5 | 94.0 |
| Non-Interest Expenditures | 39.1 | 46.9 | 19.8 | 396.0 | 462.3 | 16.8 | 514.5 | 529.6 | 87.3 |
| Revenues | 43.8 | 60.7 | 38.6 | 441.8 | 508.6 | 15.1 | 540.8 | 546.5 | 93.1 |
| Tax Revenues | 39.4 | 54.1 | 37.2 | 372.7 | 419.1 | 12.4 | 459.2 | 450.0 | 93.1 |
| Other Revenues | 4.4 | 6.7 | 51.7 | 69.0 | 89.5 | 29.6 | 81.7 | 96.5 | 92.7 |
| Budget Balance | 0.8 | 10.0 | 1,155.6 | -5.4 | -2.1 | -61.0 | -29.7 | -34.6 | 6.1 |
| Primary Balance | 4.7 | 13.9 | 196.8 | 45.8 | 46.3 | 1.0 | 26.3 | 16.9 | 273.9 |

Numbers may not add up to total value due to rounding.

Source: Datastream, Ministry of Finance

CPI inflation exceeded expectations in December.

CPI increased by 1.64% mom in the last month of the year, far above the market expectations. According to the Reuters survey, monthly CPI inflation had been anticipated to be 0.93%. Having recorded a monthly rise of 2% in November, Domestic PPI (D-PPI) kept its pace in December increasing by 2.98%.

| December | CPI | | D-PPI | |
|----------------|------|------|-------|------|
| Change (%) | 2015 | 2016 | 2015 | 2016 |
| Monthly | 0.21 | 1.64 | -0.33 | 2.98 |
| Annual | 8.81 | 8.53 | 5.71 | 9.94 |
| Annual Average | 7.67 | 7.78 | 5.28 | 4.30 |

Annual CPI inflation was 8.5% in 2016.

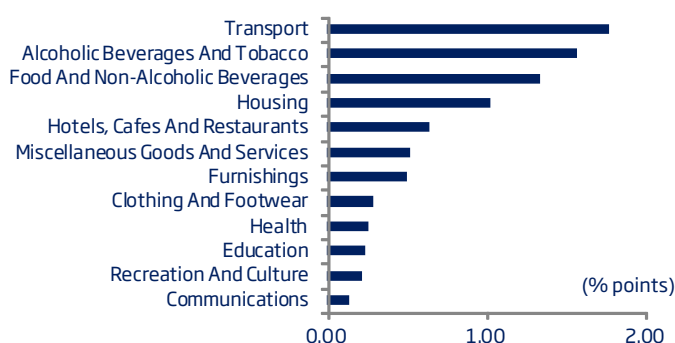
Annual CPI inflation, which fluctuated within a band of 6.6-9.6% in 2016, came in at 8.53% at the end of the year. Thus, annual CPI was realized above the CBRT's year-end forecast range 7-8%. Annual D-PPI inflation moved within a wide range throughout the year owing to the trajectory of commodity prices and FX rates. Annual D-PPI inflation reached 9.94% at the end of the year, the highest level of the last 26 months.

The rise in the CPI was widely spread across almost all sub-items.

Communications and clothing-footwear groups were the only two groups among the sub-items of CPI that recorded monthly decline in December. Owing to the upsurge in food and commodity prices as well as the price adjustments, the price hikes in alcoholic beverages, transport and housing groups played a significant role in CPI rise. Indeed, the price increases in these groups constituted 98% of the monthly increase in CPI.

Regarding the annual figures, prices in alcoholic beverages and tobacco group going up by 31.6% made a contribution of 1.57 percentage points to the annual CPI inflation. Prices in transportation group also rose by 12.4% in this period and pushed the annual CPI inflation up by 1.77 percentage points.

Contributions to the Annual CPI by Subgroups

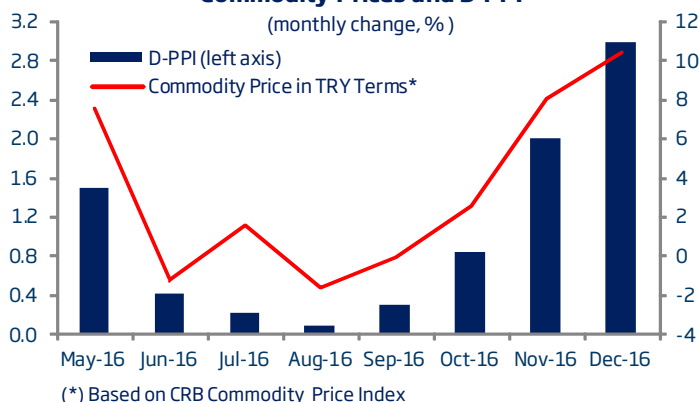


Seasonal products affected the CPI inflation favorably in December. In fact, annual inflation rose to 9.46% when seasonal products are excluded. CBRT's favorite core indices also deteriorated in this period.

Commodity prices in TRY terms were significant for the D-PPI.

The upsurge in oil prices as well as the depreciation of TL in the second half of 2016 pushed the D-PPI up. Moreover, the fall in D-PPI in the last months of 2015 was also responsible for the rise in producer prices in the same period of 2016. As basic metal prices posted an annual rise of 30.6% in December, this group contributed to the D-PPI by 2.77 percentage points. Also, it was worth mentioning that the prices of coke-refined petroleum products and metal ores climbed by 52.1% and 22.4% annually in 2016, respectively. On the other hand, prices in the electricity, gas production and distribution sector plunged by 11.8% from a year earlier and thus limited the D-PPI by 0.96 percentage point.

Commodity Prices and D-PPI



Expectations

We expect that the lagged impact of the depreciation in TL recorded in 2016 and the recent uptrend in commodity prices will continue to exert upward pressure on inflation in the upcoming period. With the start of the new year, the rise in bridge and highway toll prices and adjustments to administered prices will also be influential on the course of the inflation. Against this backdrop, we anticipate that all prices in all sub-items except clothing and footwear (thanks to seasonal discounts), will increase in January and the uptick in inflation will persist.

Source: Datastream, Turkstat

High volatility in global markets...

Particularly emerging markets have faced selling pressure following the US presidential elections. During this period, the US dollar gained strength against both developed and developing countries' currencies. As the Fed's meeting held in mid-December reinforced the view that interest rate hikes could accelerate in 2017, markets remained under pressure.

The intensified concerns over the financial system in the Euro Area arising from the developments in Italy in December also affected global markets negatively. The change in the ECB's asset-purchase program was another factor that led to an increase in the market volatility.

In domestic markets, geopolitical and political developments as well as weak economic data have caused financial indicators to fluctuate within a wide range.

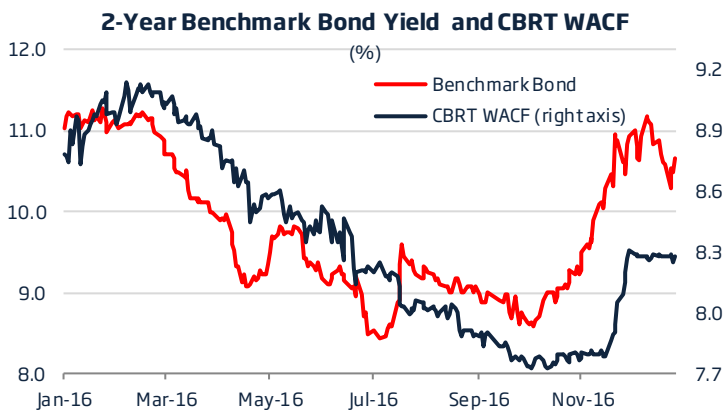
CBRT kept policy rate unchanged.

After increasing policy rate for the first time since January 2014 at its meeting held on November 24, CBRT kept the interest rates unchanged at its meeting on December 20. CBRT underlined that exchange rate movements due to recently heightened global uncertainty and the increase in oil prices posed upside risks on the inflation outlook. On the other hand, Central Bank indicated that the aggregate demand developments restrained these effects.

Interest rates...

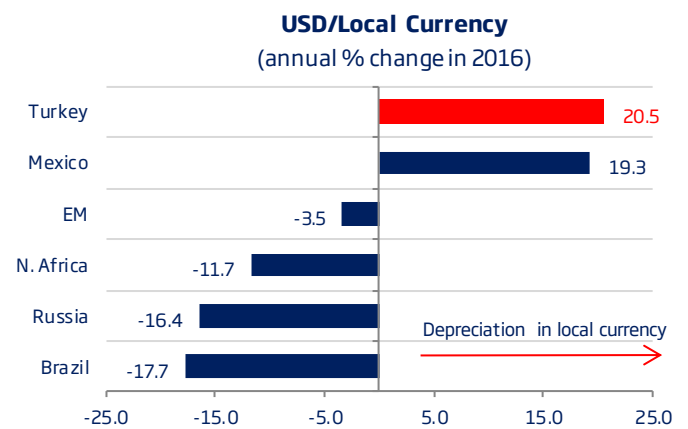
The weighted average funding cost of the CBRT rose from 7.8% at the beginning of November to 8.3% in December due to the interest rate hike.

The interest rate of the 2-year benchmark bond, which followed a volatile course at double-digit levels since mid-November, rose to 11.18% in December. As of December 30, the interest rate of the 2-year benchmark bond was realized as 10.63%, surging by 17 basis points compared to the end of November.



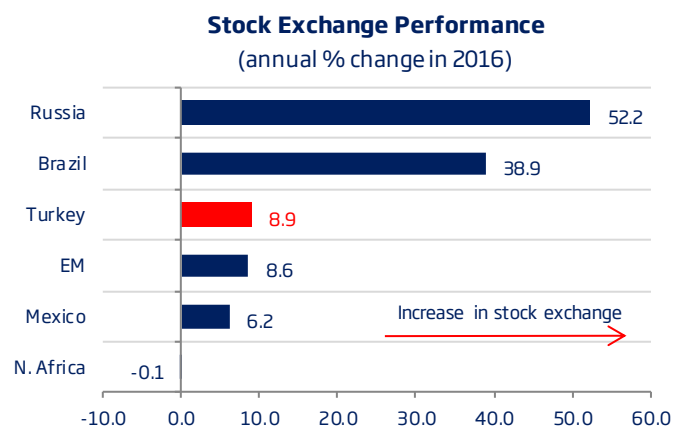
USD/TRY at record high of 3.5840...

Parallel to other emerging market currencies, Turkish lira also depreciated against the US dollar. Moreover, domestic uncertainties together with the geopolitical risks put additional pressure on TRY. For this reason, TRY displayed a weaker performance than other emerging market currencies. The USD/TRY tested the record high of 3.5840 on December 2. Although the USD/TRY declined below 3.40 due to profit taking in the following period, it again exceeded 3.50 because of the strengthening of the USD dollar. The USD/TRY went up by 20.5% in 2016 compared to the end of 2015.



BIST-100 index...

Domestic stock exchange market, in general, performed better than other emerging countries. In 2016, BIST-100 index increased by 8.9% compared to the end of 2015 to 78,139.

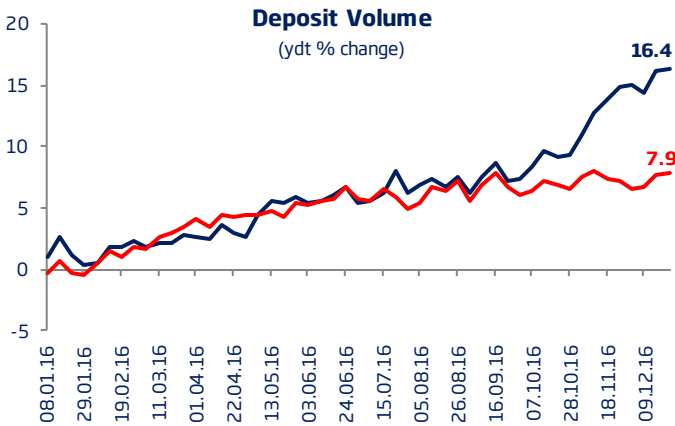


Source: CBRT, Reuters, Datastream

Deposit growth accelerated during the last weeks of the year.

Deposit volume increase gained momentum starting from mid-December. As of December 23, total deposits surged by 15.5% compared to the same period of the previous year and became 1,538 billion TRY. Compared to the end of 2015, expansion in deposit volume was 16.4%

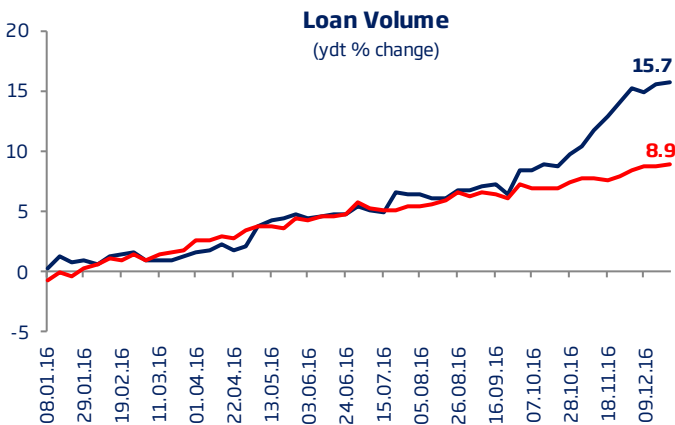
Deposit growth stemmed from the depreciation in TRY particularly since the second half of August. According to exchange rate adjusted figures, deposit volume rose by 7.9% in the year-to-date.



The volume of TRY deposits, which reached the highest level of 2016 with 880 billion TRY on November 11, decreased in the following weeks. However, the rise in TRY deposits has gained momentum again since mid-December. As of December 23, TRY deposits amounting to TL 871 billion accounted for 56.6% of the total deposits.

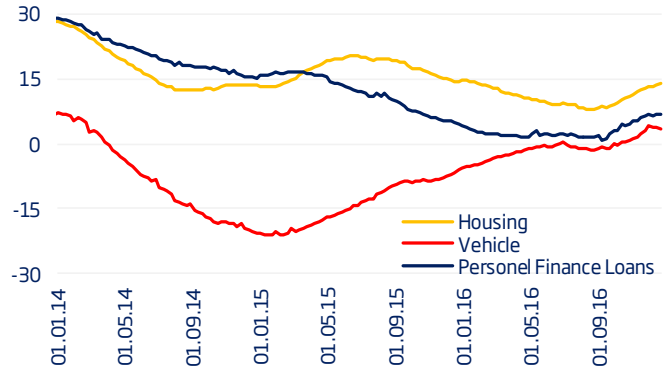
FX rates and recovery in consumer loans played a prominent role in loan growth.

As of December 23, loan volume picked up by 16.3% yoy to 1,750 billion TRY. According to year-to-date figures, loan growth was 15.7%. However, exchange rate adjusted loan growth rate was 8.9% in this period.



Consumer loans have accelerated considerably thanks to the recent steps taken to support credit growth. As of December 23, housing loans increased by 13.8% compared to the same month of the previous year. Vehicle credits, which contracted throughout the year, also went up by 3.5% yoy as the Special Consumption Tax hike pulled automobile demand forward. Personal finance loans, which remained broadly flat in 2016, have also recovered rapidly, expanding by 6.7% on annual basis.

Consumer Loans by Type (annual % change)



Securities held under custody...

There has been no significant change in the securities held under custody in the recent weeks. As of December 23, this item rose by 6.9% compared to the same month of the previous year to 238 billion TRY. It was seen that purchases of residents' have accelerated in the recent period while that of non-residents' decreased.

Net FX position...

As of December 23, banks' on-balance sheet FX position was (-)USD 20,253 million while off-balance sheet FX position realized as (+)USD 19,075 million. Hence, banking sector's net FX position became (-)USD 1,177 million.

Net FX Position (USD billion)



Having experienced big fluctuations in 2016 along with a series of unpredictable developments, global markets have started the year of 2017 with several uncertainties. Monetary policies of the major central banks, most notably the Fed, and the electoral calendar in Europe will be high on the global agenda this year. Other than these, Brexit process, economic policies of the new government in the US and geopolitical issues as well as the trajectory of oil prices will be monitored closely by the markets.

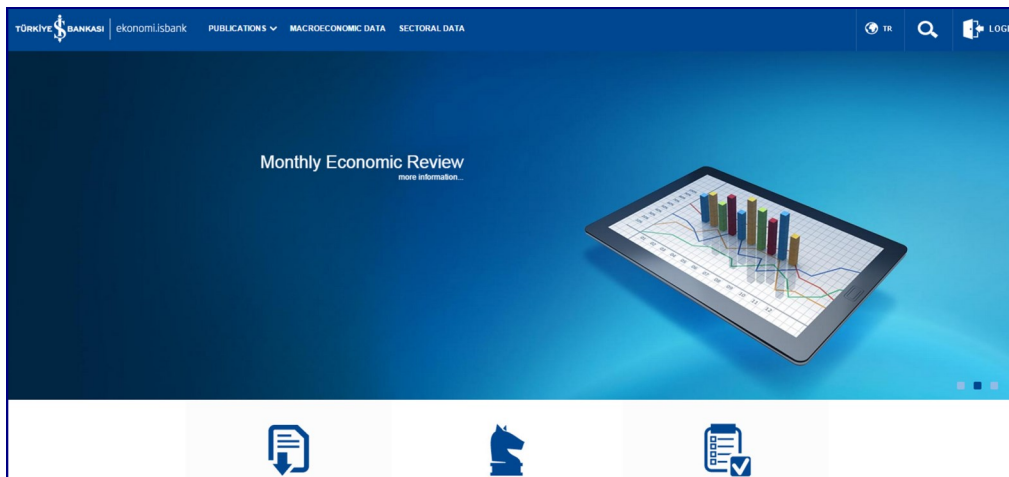
After the triumph of Trump, the expectations that economic growth will gain momentum and inflation will follow a rising trend in the US have been strengthened. Considering that the Fed members' latest interest rate projections signaled three rate hikes this year, the Fed might move faster in normalizing its monetary policy. On the other hand, given the fact that the details of the economic policy to be adopted by the Trump administration have not yet been clear enough, it is possible that protectionist policies in foreign trade may lead to an increase in risks to the global economy and therefore to a slower-than-expected pace of rate hikes by the Fed.

In addition to the protectionist policies that the new administration can follow in the US, anti-establishment tendencies in Europe that have been strengthened after Brexit and mounting geopolitical risks in the Middle East are among other factors that might weigh on the global economy in the period ahead. Turkish economy is also expected to follow a highly volatile pattern particularly in the first half of the year in the face of the global risks as well as country-specific vulnerabilities.

| Forecasts (%) | 2016 | 2017 |
|----------------|--------|------|
| Growth | 2.5 | 3.3 |
| CA Deficit/GDP | 3.9 | 4.2 |
| Inflation | 8.5(R) | 8.5 |

(R) Realization
Year-end forecast for inflation

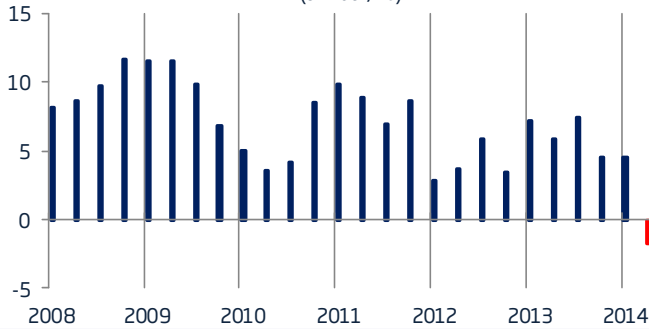
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Growth

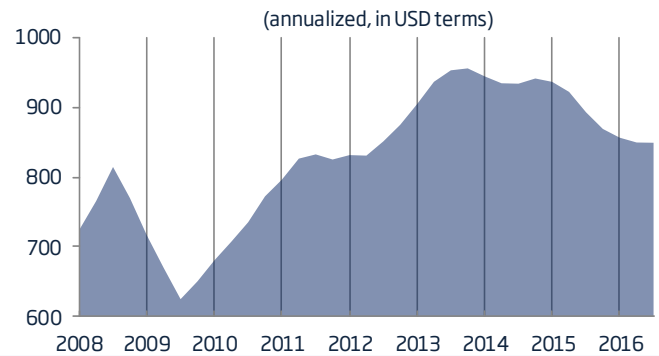
GDP Growth

(annual, %)



GDP

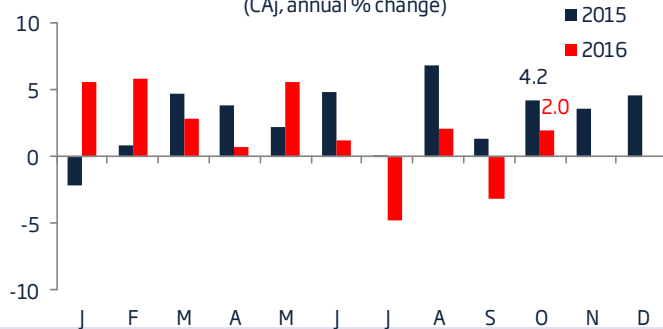
(annualized, in USD terms)



Industrial Production and Capacity Utilization Ratio

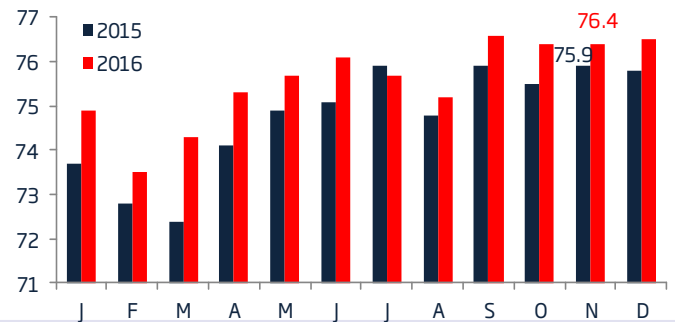
Industrial Production

(CAj, annual % change)



Capacity Utilization Ratio

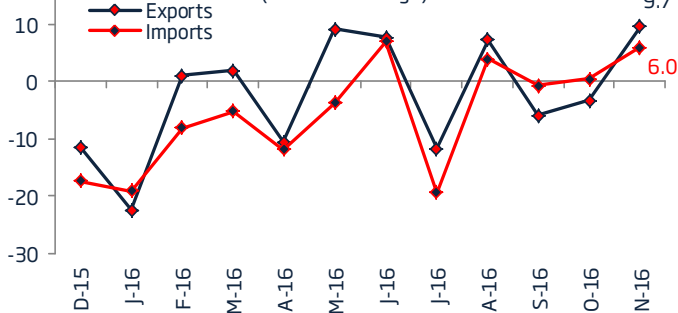
(%)



Foreign Trade and Current Account Balance

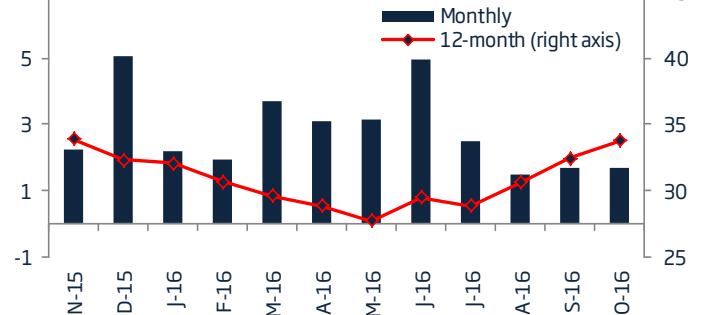
Foreign Trade

(annual % change)



Current Account Deficit

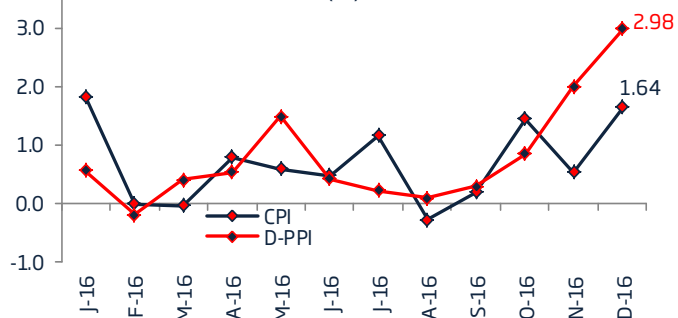
(billion USD)



Inflation

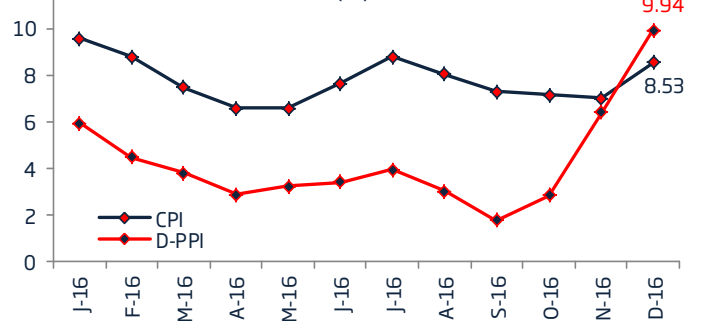
Monthly Inflation

(%)



Annual Inflation

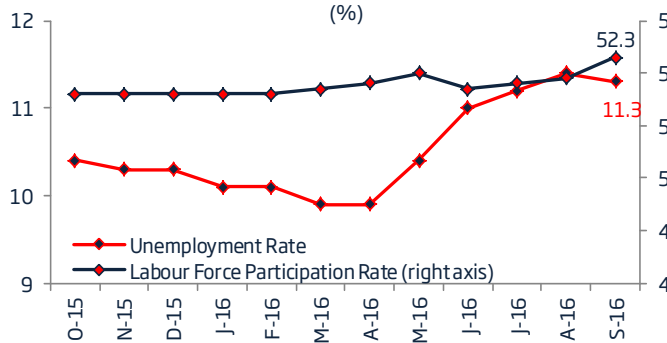
(%)



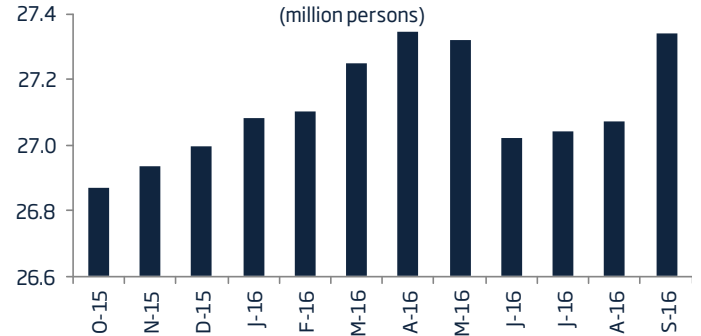
Source: CBRT, Datastream, Turkstat

Labor Market

Seasonally Adjusted Labour Force Indicators (%)

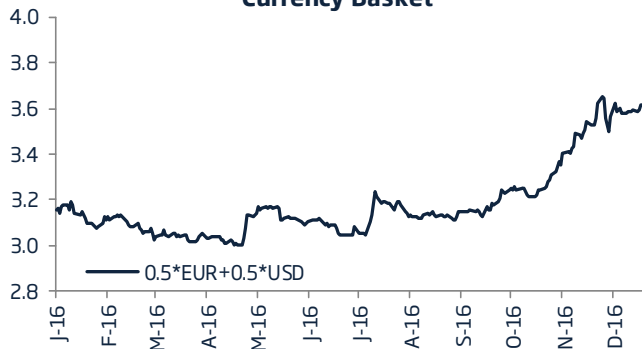


Seasonally Adjusted Employment (million persons)

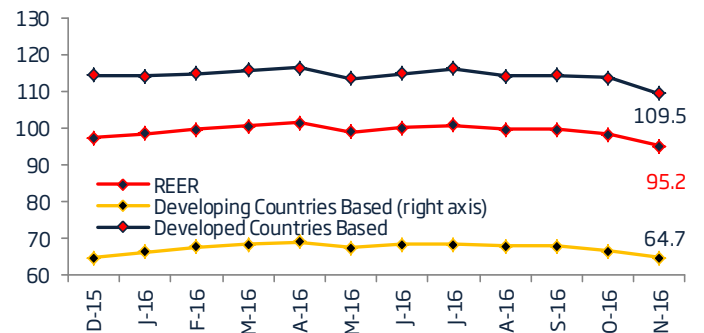


FX Market

Currency Basket

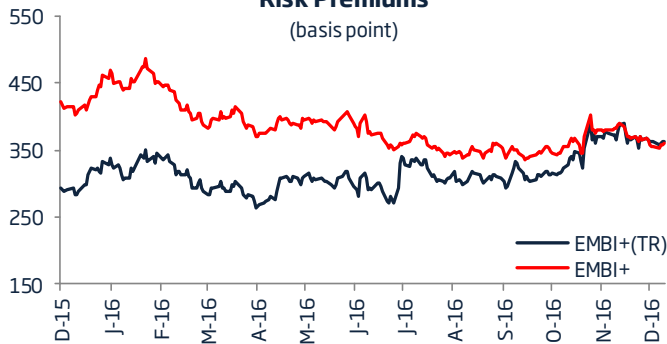


CPI Based Real Effective Exchange Rate

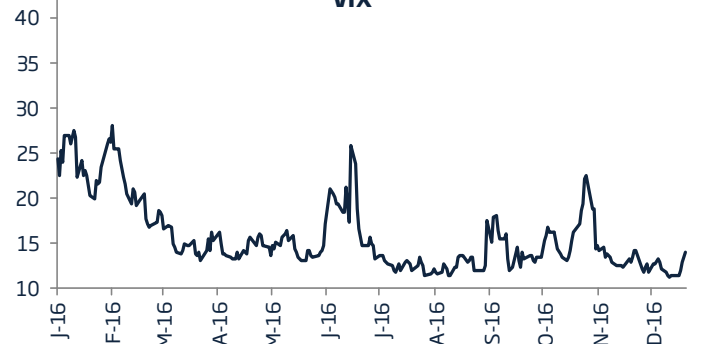


Risk Indicators

Risk Premiums (basis point)

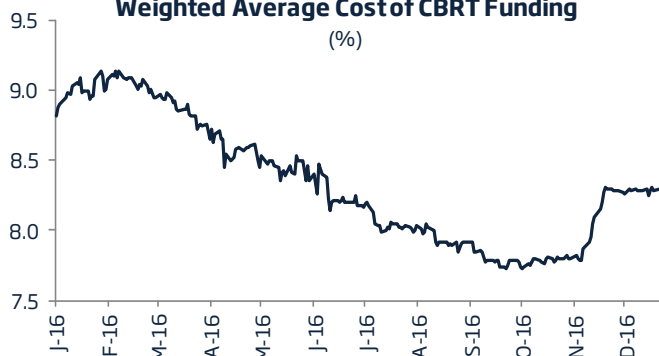


VIX

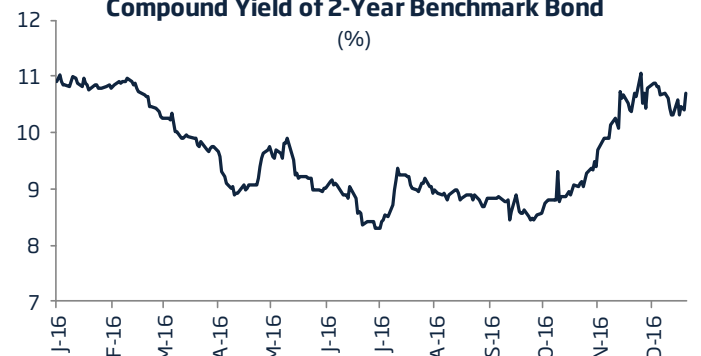


Interest Rates

Weighted Average Cost of CBRT Funding (%)

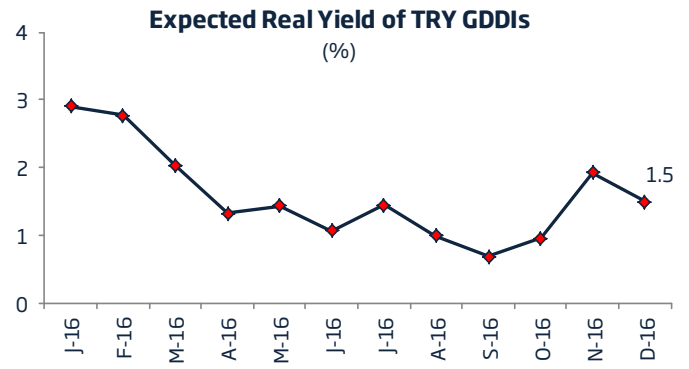
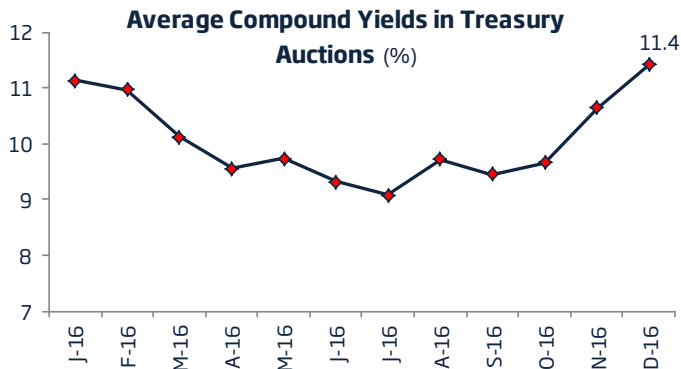


Compound Yield of 2-Year Benchmark Bond (%)

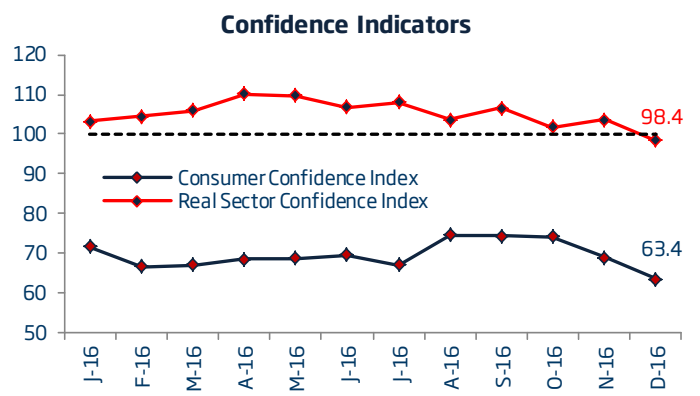
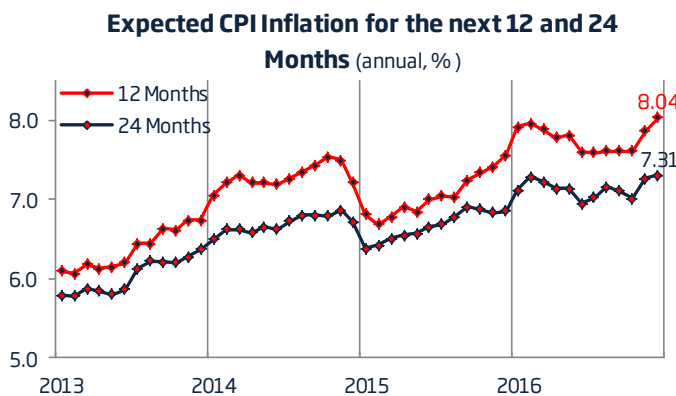
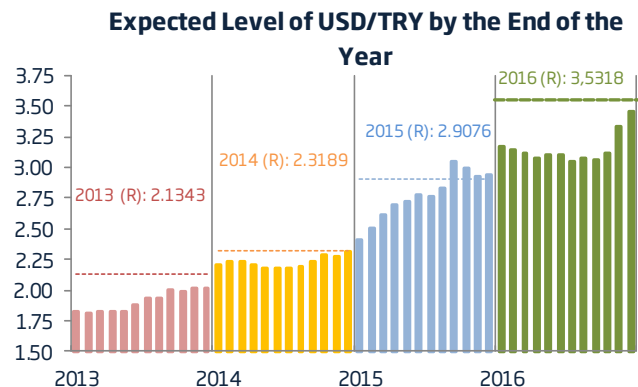
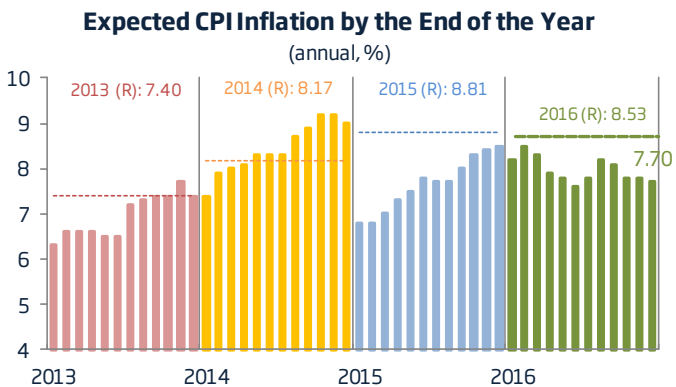
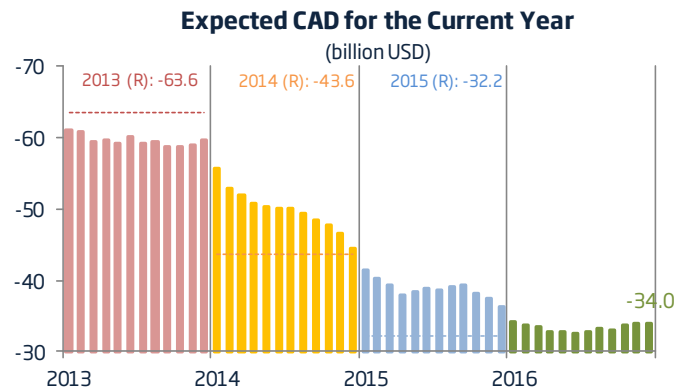
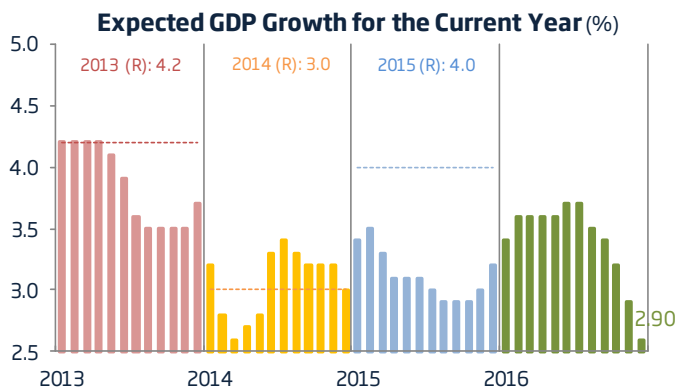


Source: BIST, CBRT, Datastream, JP Morgan, Reuters, Turkstat

Bond-Bill Market



CBRT's Survey of Expectations and Other Leading Indicators



(R) Realization

Source: BIST, CBRT, Datastream, Economic Research Division, Treasury

Turkish Economy at a Glance

| | 2011 | 2012 | 2013 | 2014 | 2015 | 16-Q1 | 16-Q2 | 16-Q3 |
|--|---------------|--------------|--------------|--------------|--------------|---------------|---------------|---------------|
| Growth | | | | | | | | |
| GDP (USD billion) | 832 | 871 | 950 | 935 | 861 | 189.8 | 216.3 | 221.6 |
| GDP (TRY billion) | 1,160 | 1,395 | 1,810 | 2,045 | 2,338 | 559.3 | 627.5 | 655.4 |
| GDP Growth Rate (%) | 8.5 | 11.1 | 8.5 | 5.2 | 6.1 | 4.5 | 4.5 | -1.8 |
| Inflation (%) | | | | | | Oct-16 | Nov-16 | Dec-16 |
| CPI (annual) | 10.45 | 6.16 | 7.40 | 8.17 | 8.81 | 7.16 | 7.00 | 8.53 |
| Domestic PPI (annual) | 13.33 | 2.45 | 6.97 | 6.36 | 5.71 | 2.84 | 6.41 | 9.94 |
| Seasonally Adjusted Labor Market Figures | | | | | | Jul-16 | Aug-16 | Sep-16 |
| Unemployment Rate (%) | 8.5 | 8.8 | 9.1 | 10.4 | 10.3 | 11.2 | 11.4 | 11.3 |
| Labor Force Participation Rate (%) | 47.2 | 48.5 | 48.5 | 50.9 | 51.6 | 51.8 | 51.9 | 52.3 |
| FX Rates | | | | | | Oct-16 | Nov-16 | Dec-16 |
| CPI Based Real Effective Exchange Rate | 102.8 | 110.3 | 100.3 | 105.0 | 97.5 | 98.4 | 95.2 | |
| USD/TRY | 1.8934 | 1.7819 | 2.1323 | 2.3290 | 2.9207 | 3.1052 | 3.4205 | 3.5223 |
| EUR/TRY | 2.4497 | 2.3508 | 2.9370 | 2.8297 | 3.1867 | 3.4024 | 3.6397 | 3.7132 |
| Currency Basket (0.5*EUR+0.5*USD) | 2.1716 | 2.0664 | 2.5347 | 2.5794 | 3.0537 | 3.2538 | 3.5301 | 3.6178 |
| Foreign Trade Balance⁽¹⁾ (USD billion) | | | | | | Sep-16 | Oct-16 | Nov-16 |
| Exports | 134.9 | 152.5 | 151.8 | 157.6 | 143.8 | 140.8 | 140.4 | 141.5 |
| Imports | 240.8 | 236.5 | 251.7 | 242.2 | 207.2 | 197.1 | 197.2 | 198.2 |
| Foreign Trade Balance | -105.9 | -84.1 | -99.9 | -84.6 | -63.4 | -56.3 | -56.8 | -56.7 |
| Import Coverage Ratio (%) | 56.0 | 64.5 | 60.3 | 65.1 | 69.4 | 71.4 | 71.2 | 71.4 |
| Balance of Payments⁽¹⁾ (USD billion) | | | | | | Aug-16 | Sep-16 | Oct-16 |
| Current Account Balance | -74.4 | -48.0 | -63.6 | -43.6 | -32.3 | -30.6 | -32.4 | -33.8 |
| Capital and Financial Accounts | -66.1 | -48.9 | -62.3 | -42.1 | -23.0 | -26.3 | -30.4 | -29.2 |
| Direct Investments (net) | -13.8 | -9.2 | -8.8 | -5.5 | -12.0 | -6.7 | -7.2 | -7.2 |
| Portfolio Investments (net) | -22.2 | -41.0 | -24.0 | -20.1 | 15.7 | -3.0 | -4.5 | -6.6 |
| Other Investments (net) | -28.3 | -19.6 | -39.5 | -16.0 | -14.9 | -18.2 | -16.4 | -17.1 |
| Reserve Assets (net) | -1.8 | 20.8 | 9.9 | -0.5 | -11.8 | 1.6 | -2.4 | 1.7 |
| Net Errors and Omissions | 8.3 | -0.9 | 1.4 | 1.6 | 9.3 | 4.3 | 2.0 | 4.5 |
| Current Account Balance/GDP (%) | -8.9 | -5.5 | -6.7 | -4.7 | -3.7 | - | - | - |
| Budget⁽²⁾⁽³⁾ (TRY billion) | | | | | | Sep-16 | Oct-16 | Nov-16 |
| Expenditures | 314.6 | 361.9 | 408.2 | 448.8 | 506.0 | 416.5 | 460.0 | 510.7 |
| Interest Expenditures | 42.2 | 48.4 | 50.0 | 49.9 | 53.0 | 41.7 | 44.6 | 48.4 |
| Non-interest Expenditures | 272.4 | 313.5 | 358.2 | 398.8 | 453.0 | 374.8 | 415.4 | 462.3 |
| Revenues | 296.8 | 332.5 | 389.7 | 425.4 | 483.4 | 404.5 | 447.9 | 490.1 |
| Tax Revenues | 253.8 | 278.8 | 326.2 | 352.5 | 407.5 | 329.0 | 365.0 | 419.1 |
| Budget Balance | -17.8 | -29.4 | -18.5 | -23.4 | -22.6 | -12.0 | -12.1 | -2.1 |
| Primary Balance | 24.4 | 19.0 | 31.4 | 26.5 | 30.4 | 29.6 | 32.4 | 46.3 |
| Budget Balance/GDP (%) | -1.5 | -2.1 | -1.0 | -1.1 | -1.0 | - | - | - |
| Central Government Debt Stock (TRY billion) | | | | | | Sep-16 | Oct-16 | Nov-16 |
| Domestic Debt Stock | 368.8 | 386.5 | 403.0 | 414.6 | 440.1 | 463.1 | 465.0 | 468.2 |
| External Debt Stock | 149.6 | 145.7 | 182.8 | 197.5 | 237.5 | 249.8 | 260.4 | 283.6 |
| Total Debt Stock | 518.4 | 532.2 | 585.8 | 612.1 | 677.6 | 712.9 | 725.4 | 751.8 |

(1) 12-month cumulative

(2) Year-to-date cumulative

(3) According to Central Government Budget

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

BANKING SECTOR ACCORDING TO BRSA'S MONTHLY BULLETIN FIGURES

| (TRY billion) | 2011 | 2012 | 2013 | 2014 | 2015 | Oct.16 | Nov.16 | Change ⁽¹⁾ |
|-------------------------------------|----------------|----------------|----------------|----------------|----------------|----------------|----------------|-----------------------|
| TOTAL ASSETS | 1,217.7 | 1,370.7 | 1,732.4 | 1,994.3 | 2,357.4 | 2,581.5 | 2,702.2 | 14.6 |
| Loans | 682.9 | 794.8 | 1,047.4 | 1,240.7 | 1,485.0 | 1,635.8 | 1,704.3 | 14.8 |
| TRY Loans | 484.8 | 588.4 | 752.7 | 881.0 | 1,013.4 | 1,095.7 | 1,114.5 | 10.0 |
| Share (%) | 71.0 | 74.0 | 71.9 | 71.0 | 68.2 | 67.0 | 65.4 | - |
| FX Loans | 198.1 | 206.4 | 294.7 | 359.7 | 471.5 | 540.1 | 589.8 | 25.1 |
| Share (%) | 29.0 | 26.0 | 28.1 | 29.0 | 31.8 | 33.0 | 34.6 | - |
| Non-performing Loans | 19.0 | 23.4 | 29.6 | 36.4 | 47.5 | 56.6 | 57.2 | 20.3 |
| Non-performing Loan Rate (%) | 2.7 | 2.9 | 2.8 | 2.9 | 3.1 | 3.3 | 3.2 | - |
| Securities | 285.0 | 270.0 | 286.7 | 302.3 | 329.7 | 334.5 | 347.9 | 5.5 |
| TOTAL LIABILITIES | 1,217.7 | 1,370.7 | 1,732.4 | 1,994.3 | 2,357.4 | 2,581.5 | 2,702.2 | 14.6 |
| Deposits | 695.5 | 772.2 | 945.8 | 1,052.7 | 1,245.4 | 1,363.0 | 1,430.8 | 14.9 |
| TRY Deposits | 460.0 | 520.4 | 594.1 | 661.3 | 715.4 | 831.9 | 843.6 | 17.9 |
| Share (%) | 66.1 | 67.4 | 62.8 | 62.8 | 57.4 | 61.0 | 59.0 | - |
| FX Deposits | 235.5 | 251.8 | 351.7 | 391.4 | 530.0 | 531.1 | 587.2 | 10.8 |
| Share (%) | 33.9 | 32.6 | 37.2 | 37.2 | 42.6 | 39.0 | 41.0 | - |
| Securities Issued | 18.4 | 37.9 | 60.6 | 89.3 | 97.8 | 108.9 | 114.8 | 17.3 |
| Payables to Banks | 167.4 | 173.4 | 254.2 | 293.2 | 361.3 | 375.8 | 413.0 | 14.3 |
| Funds from Repo Transactions | 97.0 | 79.9 | 119.1 | 137.4 | 156.7 | 143.3 | 138.2 | -11.8 |
| SHAREHOLDERS' EQUITY | 144.6 | 181.9 | 193.7 | 232.0 | 262.3 | 294.9 | 294.3 | 12.2 |
| Profit (Loss) of the Period | 19.8 | 23.5 | 24.7 | 24.6 | 26.1 | 32.1 | 35.0 | - |
| RATIOS (%) | | | | | | | | |
| Loans/GDP | 58.9 | 57.0 | 57.9 | 60.7 | 63.5 | - | - | - |
| Loans/Assets | 56.1 | 58.0 | 60.5 | 62.2 | 63.0 | 63.4 | 63.1 | - |
| Securities/Assets | 23.4 | 19.7 | 16.6 | 15.2 | 14.0 | 13.0 | 12.9 | - |
| Deposits/Liabilities | 57.1 | 56.3 | 54.6 | 52.8 | 52.8 | 52.8 | 53.0 | - |
| Loans/Deposits | 98.2 | 102.9 | 110.7 | 117.9 | 119.2 | 120.0 | 119.1 | - |
| Capital Adequacy (%) | 16.6 | 17.9 | 15.3 | 16.3 | 15.6 | 16.0 | 15.3 | - |

(1) Year-to-date % change



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