Turkey: Recent Developments and Future Prospects

ISBANK
Economic Research Division
June 2019
Macroeconomic Outlook
Strong Economic Growth Cycle

- GDP of 784 bn USD (2018), 9.6k USD (2018) per capita
- Average GDP growth rate of 5.0% between 2006-2018
- 17th largest economy in the world & 6th largest economy amongst the EU countries (2017)
- More than 8.5 mn job creation since 2005
- Prudent fiscal policy since 2002
Turkey’s GDP came in at 784 billion USD in 2018.

Source: Datastream, Turkstat
Turkish economy contracted by 2.6% yoy in Q1

Real GDP Growth (%)

Contributions to Growth (2009=100 chain linked volume index % points)

Source: Datastream, Turkstat
Slowdown in economic activity…

Calendar Adjusted Industrial Production
(yoy, % change)

Confidence Indices

Real sector confidence index
Economic confidence index
Consumer confidence index

Source: Turkstat, Datastream
8.6 million new jobs were created since 2005.

Labor Market Indicators*

<table>
<thead>
<tr>
<th>Year</th>
<th>Unemployment (%)</th>
<th>Labor Participation Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>9.7</td>
<td>45</td>
</tr>
<tr>
<td>2007</td>
<td>8.9</td>
<td>45</td>
</tr>
<tr>
<td>2009</td>
<td>9.2</td>
<td>44</td>
</tr>
<tr>
<td>2011</td>
<td>8.5</td>
<td>45</td>
</tr>
<tr>
<td>2013</td>
<td>8.8</td>
<td>47</td>
</tr>
<tr>
<td>2015</td>
<td>9.1</td>
<td>47</td>
</tr>
<tr>
<td>2017</td>
<td>9.8</td>
<td>49</td>
</tr>
<tr>
<td>2019</td>
<td>12.7</td>
<td>53</td>
</tr>
</tbody>
</table>

Employment*

<table>
<thead>
<tr>
<th>Year</th>
<th>Employment (million persons)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>20</td>
</tr>
<tr>
<td>2007</td>
<td>20</td>
</tr>
<tr>
<td>2009</td>
<td>20</td>
</tr>
<tr>
<td>2011</td>
<td>21</td>
</tr>
<tr>
<td>2013</td>
<td>23</td>
</tr>
<tr>
<td>2015</td>
<td>24</td>
</tr>
<tr>
<td>2017</td>
<td>25</td>
</tr>
<tr>
<td>2019</td>
<td>28</td>
</tr>
</tbody>
</table>

(*) Seasonally adjusted figures. Latest figure as of February 2019.

Source: Turkstat, Datastream
Fiscal Discipline

- Budget deficit to GDP ratio was 2% in 2018.

**Budget Deficit** (% GDP)

- 2012: 1.9%
- 2013: 1.0%
- 2014: 1.1%
- 2015: 1.0%
- 2016: 1.1%
- 2017: 1.5%
- 2018: 2.0%

Maastricht criterion: 3%

**General Government Debt Stock** (% GDP)

- 2012: 32.7%
- 2013: 31.4%
- 2014: 28.8%
- 2015: 27.6%
- 2016: 28.3%
- 2017: 28.3%
- 2018: 30.4%

Maastricht criterion: 60%

Source: Turkstat, Ministry of Treasury and Finance
Export volume reached all-time highs.

Exports

Exports* (billion USD)


107 102 114 135 152 158 168 170

Export volumes

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Motor vehicles</td>
<td>152</td>
<td>158</td>
<td>157</td>
<td>157</td>
<td>168</td>
<td>170</td>
<td></td>
</tr>
<tr>
<td>Boilers and machineries</td>
<td>135</td>
<td>152</td>
<td>158</td>
<td>157</td>
<td>168</td>
<td>170</td>
<td></td>
</tr>
<tr>
<td>Iron and steel</td>
<td>114</td>
<td>135</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td>170</td>
<td></td>
</tr>
<tr>
<td>Knitted and crocheted goods</td>
<td>107</td>
<td>114</td>
<td>135</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td></td>
</tr>
<tr>
<td>Electrical machinery and equipment</td>
<td>102</td>
<td>132</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td>170</td>
<td></td>
</tr>
<tr>
<td>Precious stones</td>
<td>135</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td>170</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Articles of iron and steel</td>
<td>114</td>
<td>135</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td>170</td>
<td></td>
</tr>
<tr>
<td>Non knitted and crocheted goods</td>
<td>107</td>
<td>114</td>
<td>135</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td></td>
</tr>
<tr>
<td>Plastic and articles</td>
<td>102</td>
<td>132</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td>170</td>
<td></td>
</tr>
<tr>
<td>Mineral fuels and oils</td>
<td>135</td>
<td>152</td>
<td>158</td>
<td>168</td>
<td>170</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(*1) 12-month cumulative figures as of April 2019

Source: Turkstat, Datastream
Turkey has been successful in diversifying export markets.

### Top 10 Export Markets

<table>
<thead>
<tr>
<th>2007</th>
<th>% of total</th>
<th>2019*</th>
<th>% of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Germany</td>
<td>11.2</td>
<td>1. Germany</td>
<td>9.3</td>
</tr>
<tr>
<td>UK</td>
<td>8.0</td>
<td>2. UK</td>
<td>6.5</td>
</tr>
<tr>
<td>Italy</td>
<td>7.0</td>
<td>3. Italy</td>
<td>5.6</td>
</tr>
<tr>
<td>France</td>
<td>5.6</td>
<td>4. Iraq</td>
<td>5.0</td>
</tr>
<tr>
<td>Russia</td>
<td>4.4</td>
<td>5. USA</td>
<td>4.9</td>
</tr>
<tr>
<td>Spain</td>
<td>4.3</td>
<td>6. Spain</td>
<td>4.7</td>
</tr>
<tr>
<td>USA</td>
<td>3.9</td>
<td>7. France</td>
<td>4.3</td>
</tr>
<tr>
<td>Romania</td>
<td>3.4</td>
<td>8. Netherlands</td>
<td>2.8</td>
</tr>
<tr>
<td>UAE</td>
<td>3.0</td>
<td>9. Israel</td>
<td>2.4</td>
</tr>
<tr>
<td>Netherlands</td>
<td>2.8</td>
<td>10. Romania</td>
<td>2.3</td>
</tr>
</tbody>
</table>

The share of first 10: 53.6%  
The share of first 10: 47.7%

(*) 12-month cumulative figures as of April 2019

Source: Turkstat, Datastream
Import volume was 207 billion USD as of April.

Imports* (billion USD)

<table>
<thead>
<tr>
<th>Year</th>
<th>2007</th>
<th>2009</th>
<th>2011</th>
<th>2013</th>
<th>2015</th>
<th>2017</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Value</td>
<td>170</td>
<td>141</td>
<td>186</td>
<td>241</td>
<td>237</td>
<td>252</td>
<td>242</td>
</tr>
<tr>
<td>Value</td>
<td>207</td>
<td>241</td>
<td>237</td>
<td>252</td>
<td>242</td>
<td>237</td>
<td>252</td>
</tr>
<tr>
<td>Value</td>
<td>207</td>
<td>237</td>
<td>252</td>
<td>242</td>
<td>237</td>
<td>252</td>
<td>207</td>
</tr>
</tbody>
</table>

Imports* (% of total)

- Mineral fuels and oils: 21.3%
- Boilers and machineries: 11.2%
- Iron and steel: 8.0%
- Electrical machinery and equipment: 7.3%
- Plastic and articles: 5.8%
- Motor vehicles: 5.4%
- Precious Stones: 4.8%
- Organic chemicals: 2.7%
- Optical products: 2.1%
- Pharmaceutical products: 2.1%

(*) 12-month cumulative figures as of April 2019

Source: Turkstat, Datastream
28.2% of imports are from Russia, Germany and China.

### Top 10 Import Markets

<table>
<thead>
<tr>
<th>2007</th>
<th>% of total</th>
<th>2019*</th>
<th>% of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Russia</td>
<td>13.8</td>
<td>1. Russia</td>
<td>10.2</td>
</tr>
<tr>
<td>2. Germany</td>
<td>10.3</td>
<td>2. Germany</td>
<td>9.0</td>
</tr>
<tr>
<td>3. China</td>
<td>7.8</td>
<td>3. China</td>
<td>9.0</td>
</tr>
<tr>
<td>4. Italy</td>
<td>5.7</td>
<td>4. USA</td>
<td>5.6</td>
</tr>
<tr>
<td>5. USA</td>
<td>4.8</td>
<td>5. Italy</td>
<td>4.4</td>
</tr>
<tr>
<td>6. France</td>
<td>4.6</td>
<td>6. India</td>
<td>3.5</td>
</tr>
<tr>
<td>7. Iran</td>
<td>3.9</td>
<td>7. France</td>
<td>3.1</td>
</tr>
<tr>
<td>8. UK</td>
<td>3.2</td>
<td>8. Iran</td>
<td>3.1</td>
</tr>
<tr>
<td>9. Switzerland</td>
<td>3.1</td>
<td>9. UK</td>
<td>3.0</td>
</tr>
<tr>
<td>10. Ukraine</td>
<td>2.7</td>
<td>10. South Korea</td>
<td>2.9</td>
</tr>
</tbody>
</table>

The share of first 10: 59.9%

### Composition of Imports (%)

<table>
<thead>
<tr>
<th>Year</th>
<th>Capital Goods</th>
<th>Intermediate Goods</th>
<th>Consumption Goods</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>11.0</td>
<td>72.7</td>
<td>15.9</td>
</tr>
<tr>
<td>2019*</td>
<td>9.5</td>
<td>77.2</td>
<td>12.9</td>
</tr>
</tbody>
</table>

Source: Turkstat, Datastream

(*) 12-month cumulative figures as of April 2019
Tourism sector has recovered considerably.

**Tourism Revenues**
(USD bn)

2007: 19
2009: 23
2011: 23
2013: 28
2015: 30
2017: 27
2019: 25

The Number of Tourists
(million persons)

- Russia: 6.2
- Germany: 4.6
- Bulgaria: 2.5
- UK: 2.3
- Georgia: 1.9
- Iran: 1.7
- Ukraine: 1.4
- Iraq: 1.2
- Netherlands: 1.1
- Azerbaijan: 0.9

*12-month cumulative figures as of March 2019.
**12-month cumulative figures as of April 2019.

Source: CBRT, Ministry of Culture and Tourism
Saving-investment gap of Turkey...

Savings & Investments

Investments and Savings (% of GDP)

Source: Turkstat, New Economic Program (2019-2021)
Current account deficit declined to 8.6 billion USD.

Current Account Deficit (% of GDP)

<table>
<thead>
<tr>
<th>Year</th>
<th>2006</th>
<th>2008</th>
<th>2010</th>
<th>2012</th>
<th>2014</th>
<th>2016</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deficit</td>
<td>5.7</td>
<td>5.5</td>
<td>5.1</td>
<td>1.8</td>
<td>5.8</td>
<td>5.5</td>
<td>6.7</td>
</tr>
</tbody>
</table>

Financing of CAD (12-month cumulative, billion USD)

- Foreign Direct and Long Term Investments*
- Portfolio and Short Term Investments**
- Current Account Deficit

Source: Turkstat, CBRT

(*) Long term capital movements are sum of banking and real sectors’ long term net credit and bonds issued by banks and the Treasury
(**) Short-term capital movements are sum of banking and real sectors’ short term net credits and deposits in banks.
Volatile capital inflows....

**Portfolio Inflows**
(12-month cumulative, billion USD)

**Foreign Direct Investment Inflows**
(12-month cumulative, billion USD)

Source: CBRT
Central Bank has implemented tight monetary policy.

Annual CPI Inflation* (%)

Interest Rates (%)

Interest Rate Corridor
One Week Repo Rate
CBRT Weighted Average Cost of Funding
Late Liquidity Window

(*) Latest figure as of May 2019

Source: CBRT, Turkstat, Datastream
Mixed outlook in EMs...

USD vs Local Currencies
(Dec. 31, 2017 = 100)

- Turkey
- Brazil
- Russia
- Indonesia
- South Africa

Equity Indices
(Dec. 31, 2017 = 100)

- Turkey
- Brazil
- Russia
- Indonesia
- South Africa

Latest figure as of June 10, 2019

Source: Datastream
High risk premium for Turkish assets...

5Y Government Bond Yields

5Y CDS Spreads

Latest figure as of June 10, 2019

Source: Datastream
Banking Sector Dynamics
Banking Sector Dynamics

- Increased intermediation activity by financing the growth of Turkish economy
- Diversification of funding sources by increasing access to international markets
- Shifting focus from growth to asset quality and stable funding structure
- Strengthened asset quality confirmed by low NPL ratios
- High capital adequacy ratio
- Strong growth potential
Increase in foreign bank presence…

**Number of Banks***

- **Public**
- **Foreign**
- **Domestic Private**

<table>
<thead>
<tr>
<th>Year</th>
<th>Public</th>
<th>Foreign</th>
<th>Domestic Private</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>8</td>
<td>15</td>
<td>25</td>
</tr>
<tr>
<td>April 2019</td>
<td>10</td>
<td>28</td>
<td>13</td>
</tr>
</tbody>
</table>

**Share in Total Assets (%)**

- **Public**
- **Foreign**
- **Domestic Private**

<table>
<thead>
<tr>
<th>Year</th>
<th>Public</th>
<th>Foreign</th>
<th>Domestic Private</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>38</td>
<td>3</td>
<td>58</td>
</tr>
<tr>
<td>April 2019</td>
<td>40</td>
<td>27</td>
<td>33</td>
</tr>
</tbody>
</table>

(*) Excluding the banks under the administration of the SDIF

Source: BRSA
Basic Indicators

Branch network and banking sector employment...

Number of Domestic Branches

Number of Domestic Staff

Source: BRSA
Strong growth performance in the banking sector…

Basic Indicators

Source: BRSA, Turkstat
Increasing financial intermediation role of banks…
 Deposits have been the main funding source of the banking sector.

Latest figure as of May 31, 2019

Source: BRSA
Loan growth has lost momentum since the last quarter of 2017.

Loans

Source: BRSA

Latest figure as of May 31, 2019
Non-Performing Loans

NPL ratio was 4.1% as of April.

(As of 2018 H1.)

Source: BRSA, EBA
Manufacturing industry has the highest share among main industry groups.

<table>
<thead>
<tr>
<th>Industry Group</th>
<th>Share (%)</th>
<th>NPL (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing industry</td>
<td>20.2</td>
<td>4.0</td>
</tr>
<tr>
<td>Wholesale and Retail Trade</td>
<td>12.3</td>
<td>6.0</td>
</tr>
<tr>
<td>Construction</td>
<td>9.2</td>
<td>6.0</td>
</tr>
<tr>
<td>Electricity, Gas and Water Resources</td>
<td>7.9</td>
<td>3.3</td>
</tr>
<tr>
<td>Real Estate Bro., Renting and Business Act.</td>
<td>6.2</td>
<td>3.5</td>
</tr>
<tr>
<td>Transportation, Storage and Communication</td>
<td>5.8</td>
<td>2.2</td>
</tr>
<tr>
<td>Agriculture, Hunting and Forestry</td>
<td>4.0</td>
<td>4.0</td>
</tr>
<tr>
<td>Tourism</td>
<td>3.4</td>
<td>4.3</td>
</tr>
<tr>
<td>Financial Intermediation</td>
<td>2.3</td>
<td>0.5</td>
</tr>
<tr>
<td>Defense and Public Administration</td>
<td>2.1</td>
<td>0.1</td>
</tr>
</tbody>
</table>

(*) as of April 2019

Source: BRSA
Non-manufacturing sectors have the highest credit demand.

Loans by Sectors

- Wholesale trade: Share 6.7%, NPL 4.0%
- Agriculture: Share 4.0%, NPL 4.0%
- Research, consulting etc: Share 5.5%, NPL 3.8%
- Retail trade: Share 3.8%, NPL 2.6%
- Textile: Share 4.0%, NPL 3.4%
- Main metal: Share 4.0%, NPL 3.3%
- Food, beverage and tobacco: Share 4.0%, NPL 3.0%
- Hotels: Share 3.9%, NPL 2.7%
- Financial Institutions: Share 4.8%, NPL 1.8%
- Retail sell of motor vehicles and oil: Share 4.0%, NPL 0.3%

(*) as of April 2019

Source: BRSA
Short-term FX risks have been managed carefully by the non-financial sector.

Net FX Position of the Non-Financial Sector
(bn USD)

Source: CBRT
Majority of FX loans of non-financial companies were raised from domestic banks.

**FX Liabilities of NFCs** (bn USD)

- Import Payables
- External Loans
- Domestic Loans

**FX Assets of NFCs** (bn USD)

- Securities
- Direct Investment Abroad
- Export Receivables
- Deposits

Source: CBRT
Turkey’s external financing needs in the coming 12 months…

<table>
<thead>
<tr>
<th>April 2019 (*)</th>
<th>(bn USD)</th>
<th>Share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central Bank</td>
<td>5.4</td>
<td>3.1</td>
</tr>
<tr>
<td>General Government</td>
<td>3.0</td>
<td>1.7</td>
</tr>
<tr>
<td>Banks</td>
<td>88.4</td>
<td>50.4</td>
</tr>
<tr>
<td>Credits</td>
<td>40.5</td>
<td>23.1</td>
</tr>
<tr>
<td>FX Deposits</td>
<td>19.5</td>
<td>11.1</td>
</tr>
<tr>
<td>Bank Accounts</td>
<td>14.8</td>
<td>8.5</td>
</tr>
<tr>
<td></td>
<td>Branches and Affiliates Abroad</td>
<td>7.3</td>
</tr>
<tr>
<td>TRY Deposits</td>
<td>13.5</td>
<td>7.7</td>
</tr>
<tr>
<td></td>
<td>Branches and Affiliates Abroad</td>
<td>6.8</td>
</tr>
<tr>
<td>Other Sectors</td>
<td>78.5</td>
<td>44.8</td>
</tr>
<tr>
<td>Trade Credits</td>
<td>53.2</td>
<td>30.3</td>
</tr>
<tr>
<td>Other Credits</td>
<td>25.3</td>
<td>14.4</td>
</tr>
<tr>
<td>Public</td>
<td>0.1</td>
<td>0.0</td>
</tr>
<tr>
<td>Private</td>
<td>25.3</td>
<td>14.4</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>175.3</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

(*) External debt maturing within 1 year or less regardless of the original maturity.

Source: CBRT
In line with strict regulations, FX liabilities belong mostly to large-scale corporates that generate or have potential to generate FX revenues.

Not: Loans extended abroad and used via the intermediacy of domestic banks are included.

Source: CBRT
Banks have diversified their funding sources.

Net FX Position*
(billion USD)

External Borrowings of the Banks
(outstanding amount, billion USD)

(*) Latest figure as of May 31, 2019

Source: BRSA
- Turkish banks continued to be very well capitalized.

**Capital Adequacy Ratio**

![Graph showing Capital Adequacy Ratio from 2005 to April 2019 for various countries with Turkey's ratio highlighted.]

**Capital Adequacy Ratio (%, 2018)**

- Netherlands: 22.4%
- Ireland: 22.0%
- Croatia: 21.2%
- Latvia: 21.3%
- Bulgaria: 20.0%
- Malta: 19.9%
- Belgium: 19.7%
- Germany: 19.1%
- EU Average: 19.0%
- Czech Rep.: 18.6%
- Slovakia: 18.5%
- Austria: 18.2%
- France: 17.9%
- Poland: 17.6%
- Slovakia: 17.6%
- Turkey: 17.3%
- S. Cyprus: 16.5%
- Italy: 16.1%
- Greece: 15.9%
- Hungary: 15.5%
- Spain: 15.3%
- Portugal: 15.0%

Source: BRSA, EBA
Alternative Banking Channels

A promising innovative future for mobile banking in Turkey...

Internet Banking
(number of active customers, thousand persons)

- 2011 Q1: 7,227
- 2018 Q1: 12,527

Mobile Banking
(number of active customers, thousand persons)

- 2011 Q1: 230
- 2018: 32,047

Source: The Banks Association of Turkey
Net interest margin is 3.2%.

(*) Net interest income / average total assets
(**) 12-month cumulative as of March
(*** As of March

Source: BRSA
Profitability

Profitable banking sector...

ROAA


2.5% 1.7% 1.8% 1.6% 1.3% 1.2% 1.5% 1.5% 1.4% 1.3%*

ROAE


20% 15% 16% 14% 12% 11% 14% 14% 16% 13%*

(*) As of Q1

Source: BRSA
Turkish equity market has erased its gains for 2019.
Despite the fast growth in the sector, penetration ratios are still low.

Banking Sector’s Assets in Turkey (% GDP)

Banking Sector’s Comparison with Euro Area (2018)

<table>
<thead>
<tr>
<th></th>
<th>EA-19</th>
<th>Turkey</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets/GDP</td>
<td>267</td>
<td>104</td>
</tr>
<tr>
<td>Loans/GDP</td>
<td>162</td>
<td>65</td>
</tr>
<tr>
<td>Housing Loans/GDP</td>
<td>38</td>
<td>5</td>
</tr>
<tr>
<td>Deposits/GDP</td>
<td>156</td>
<td>57</td>
</tr>
</tbody>
</table>

Source: BRSA, Turkstat, ECB, Eurostat
### Forecasts

<table>
<thead>
<tr>
<th></th>
<th>2018 (R)</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP Growth (%)</td>
<td>2.6</td>
<td>1.0</td>
</tr>
<tr>
<td>Current Account Deficit (% of GDP)</td>
<td>3.5</td>
<td>2.1</td>
</tr>
<tr>
<td>CPI (%)</td>
<td>20.3</td>
<td>16.0</td>
</tr>
</tbody>
</table>

(R) Realization
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