



Monthly Economic Review February 2016



Global Economy

- ◆ In the World Economic Outlook update published in January, IMF revised down the global growth forecasts for both 2016 and 2017 by 0.2 pp to 3.4% and 3.6%, respectively.
- ◆ The World Bank cut its global growth forecasts in January as well. This downward revision mostly stemmed from the anticipated deceleration in emerging economies.
- ◆ Fed acted in line with the expectations at its January meeting keeping the policy rate on hold. Fed stated that the inflation and employment indicators as well as the effects of global economic and financial developments would be monitored closely.
- ◆ The leading indicators released in recent period showed that the US economy continued to lose steam following the weak fourth quarter performance. In this context, the possibility for a March rate hike has dropped.
- ◆ Keeping interest rates unchanged in January, European Central Bank announced that monetary policy stance could be reviewed at its March meeting.
- ◆ Bank of Japan unexpectedly cut interest rates on current accounts that financial institutions hold at the Bank into negative territory at the end of January.
- ◆ The volatility observed in Chinese financial markets caused a significant deterioration in global risk appetite at the beginning of the year. Chinese economy grew by 6.9% yoy in 2015, the weakest annual performance since 1990.
- ◆ Expectations for capital inflows towards emerging markets painted a weak picture.
- ◆ Starting the year with a tumble, oil prices recovered somewhat in the second half of January.

Turkish Economy

- ◆ Calendar adjusted industrial production increased by 3.5% yoy in November. Among main industrial groups, 10.3% yoy rise in the manufacture of capital goods was noteworthy.
- ◆ The downward trend in foreign trade deficit continued in the last month of 2015. In 2015 as a whole, the fall registered in exports stemmed from the drop in exports to the Near and Middle Eastern countries and developments in EUR/USD parity. The decline in energy prices and moderate pace of domestic demand were the main drivers behind the contraction in imports. In 2015, foreign trade deficit decreased by 21.3 billion USD compared to 2014 and became 63.3 billion USD.
- ◆ In January-November period, the current account deficit recovered by 29.7% yoy and came in at 27.8 billion USD while 12-month deficit narrowed to 34.7 billion USD, the lowest level since September 2010.
- ◆ Central budget realizations indicated that Turkey maintained fiscal discipline in 2015. Budget deficit contracted by 3.3% yoy to 22.6 billion TRY in 2015. According to MTP estimates, the budget deficit to GDP ratio declined to 1.2% in this period.
- ◆ The upward pressure on inflation due to the developments in both food prices and exchange rates has persisted also in January. Thus, annual inflation approached double-digit levels in the first month of 2016. Having declined in the last 3 months of 2015, D-PPI posted a relatively modest annual increase despite the low base effect.

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Labor market indicators displayed a weaker outlook.

Having followed a flat trend (10.4%) in recent months, the seasonally adjusted unemployment rate increased to 10.6%, the highest reading in the last 11 months. Non-agricultural unemployment rate came in at 12.7% while youth unemployment rate maintained its high levels, standing at 19%. Employment fell by 39,000 persons on a monthly basis according to seasonally adjusted figures. Labor force participation rate declined by 0.1 pp and became 51.5% in this period.

Industrial production surged by 3.5% in November.

Calendar adjusted industrial production increased by 3.5% yoy in November. Among main industrial groups, the 10.3% yoy rise in the manufacture of capital goods was noteworthy. Analyses by the sub-sectors revealed that the mining and quarrying industry continued to perform weakly. The manufacture of mining of coal and lignite shrank around 20% yoy. The manufacture of mining of metal ores also contracted by 12.5% during this period.

Manufacturing PMI remained above the threshold level for 3 months in a row.

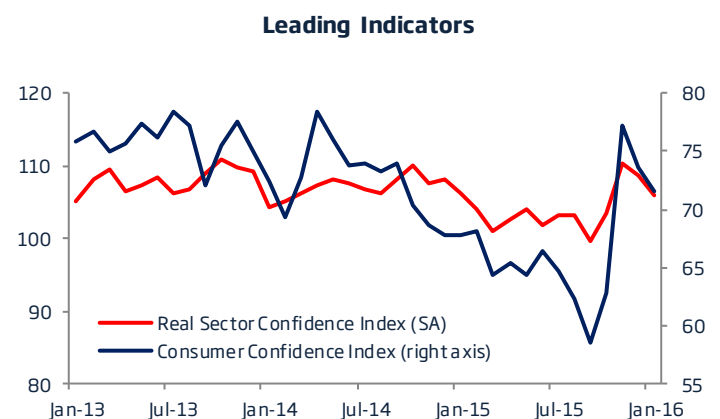
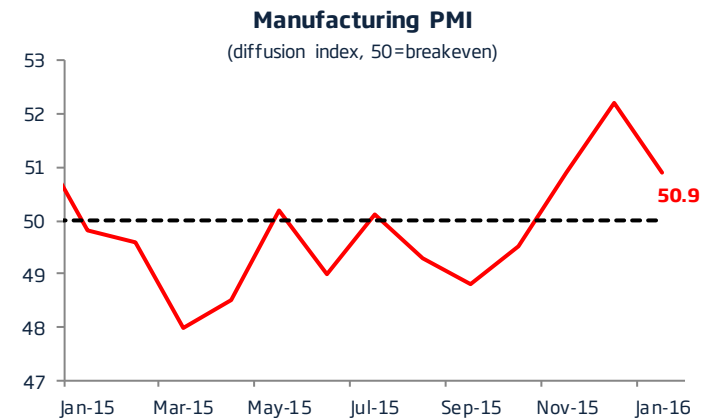
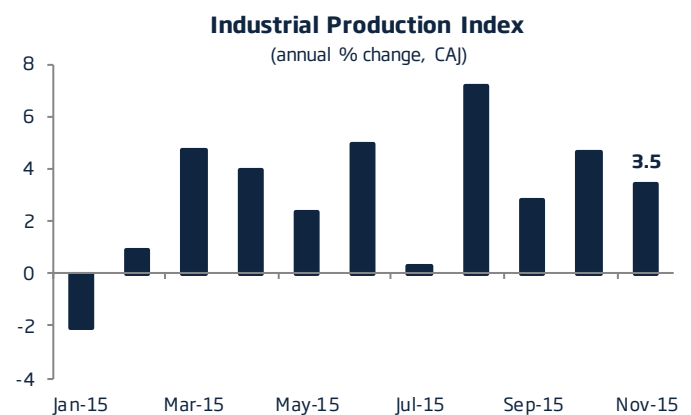
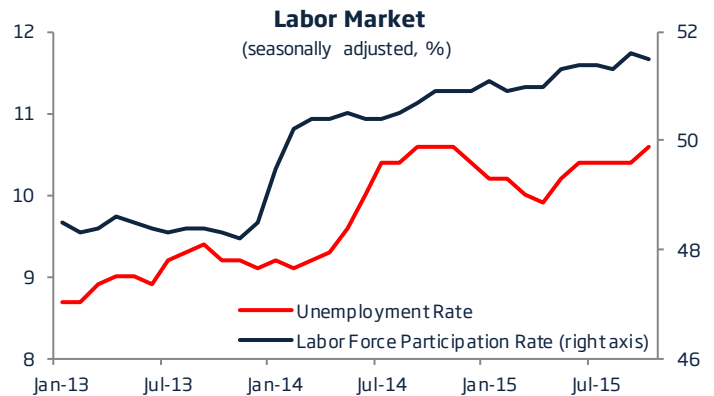
The manufacturing PMI declined by 1.3 points to 50.9 in January yet stood above the threshold level of 50 indicating that the growth trend in the sector has continued. Assessment on new orders and production boosted the overall index while the sharp decline in new export orders put downward pressure on it. Having been reported at 52.4 in December, new export orders plunged to 47.8 in January, falling below the threshold level for the first time in six months. Some survey participants stated that geopolitical risks and uncertainties had a negative impact on foreign demand. The surge in input prices arising from the depreciation in TRY was also worthy of attention in this period.

Capacity utilization ratio...

Registering an annual rise in 2015, capacity utilization ratio increased by 1.2 pps and became 74.9% in January. Capacity utilization ratios in manufacture of coke and refined petroleum products and motor vehicles kept growing at higher paces while the manufacture of tobacco products and the manufacture of computer, electronic and optical products recorded significant declines.

Confidence indicators...

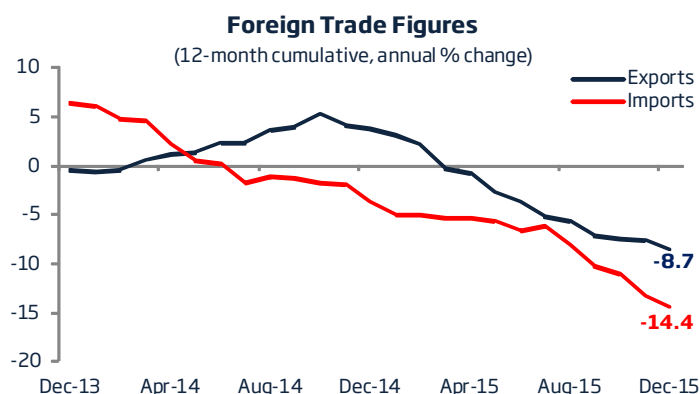
Having declined in December due to rising geopolitical concerns, confidence indices in general presented a weak picture also in January. The seasonally adjusted real sector confidence index dropped by 2.9 points mom and became 105.9. The consumer confidence index also receded by 2.7% to 71.6. Assessments on housing demand supported the overall index while the significant deterioration in the assessments on inflation pulled it down.



Source: Datastream, Turkstat, CBRT, Markit

In December, foreign trade deficit narrowed by 27.4%.

The downward trend in foreign trade deficit continued in the last month of 2015. Export volume decreased by 11.1% yoy in December while import volume diminished by 17.5%. As a result, trade deficit narrowed by 27.4% yoy in this period.



In 2015 as a whole, export volume declined by 8.7% yoy compared to the previous year and realized as 143.9 billion USD. Fall in the exports to the Near and Middle Eastern countries and weak performance of EUR/USD parity played a significant role in this development. Imports contracted by 14.4% yoy and came in at 207.2 billion USD in this period due to the decline in energy prices and moderate pace of domestic demand. In 2015, foreign trade deficit decreased by 21.3 billion USD compared to 2014 and stood at 63.3 billion USD.

Germany ranked first in total exports during 2015.

In 2015, Germany remained as the biggest export market of Turkey. UK, Iraq and Italy have become the other major markets. In 2015, export figures especially the ones toward the Euro Area countries were under pressure due to weakening EUR/USD parity. According to the foreign exchange adjusted figures for all types of currencies, it was observed that total export volume decreased by only 1.3% compared to the previous year.

Eurozone countries had a share of 29.8% in total export volume of Turkey in 2015 and this share remained flat. Last

Top Export Destinations (billion USD)

	2014		2015		Change (%)
	Value	Share %	Value	Share %	
Germany	15.1	9.6	13.4	9.3	-11.4
UK	9.9	6.3	10.6	7.3	6.7
Iraq	10.9	6.9	8.6	5.9	-21.4
Italy	7.1	4.5	6.9	4.8	-3.5
USA	6.3	4.0	6.4	4.4	0.9
France	6.5	4.1	5.8	4.1	-9.5
Spain	4.7	3.0	4.7	3.3	-0.1
UAE	4.7	3.0	4.7	3.3	0.6
Iran	3.9	2.5	3.7	2.5	-5.7
Russia	5.9	3.8	3.6	2.5	-39.5
S. Arabia	3.0	1.9	3.5	2.4	14.1
Other	79.4	50.4	72.1	50.1	-9.3
Total	158	100	144	100	-8.7

year as exports to Near and Middle Eastern countries decreased by 12.1% yoy, their share came in at 21.6%. It was noteworthy that share of Iraq and Russia in our total export volume shrank significantly.

In 2015, the biggest exporter industry was automotive, which was followed by machinery industry and precious stones and metals thanks to the increase in gold export. Reaching the record high levels on volume basis in 2015, automotive exports decreased by 3.6% in USD terms compared to 2014 due to the fall in EUR/USD parity as the major markets for this industry are European Union countries which generally trade with EUR.

The drop in energy import continued.

In December, all of the top 10 importing industries shrank annually. Mineral fuels and oils imports declined by 1.4 billion USD in this period and continued to have a favorable impact on foreign trade deficit.

In 2015, foreign trade volume posted the highest contraction rate since the crisis year of 2009 due to the moderate outlook in domestic demand and low energy prices.

Foreign Trade Balance

	(USD billion)					
	December		Change (%)	Jan.-Dec.		Change (%)
	2014	2015		2014	2015	
Exports	13.3	11.8	-11.1	157.6	143.9	-8.7
Imports	21.8	18.0	-17.5	242.2	207.2	-14.4
Foreign Trade Balance	-8.5	-6.2	-27.4	-84.6	-63.3	-25.2
Import Coverage Ratio (%)	60.9	65.6	-	65.1	69.5	-

Source:

Iranian Market

Iranian market came into prominence following the liftoff of the sanctions. The exports to neighboring Iran amounted to 3.7 billion USD in 2015. This figure made Iran the ninth largest export market of Turkey. Precious metals ranked first among exports directed to this country. Imports from Iran, on the other hand, stood at 6.1 billion USD in 2015. Mineral fuels and oil accounted for a significant share in this number as Iran being a country which has one of the largest reserves of oil and gas in the world.

advantageous for Turkey, yet only to some extent. Having refused to obey the sanctions, countries like Russia and China already achieved a better position in Iranian market. The trade relations and investment ties between Iran and the EU countries, which were the once important trading partners for Iran, are also expected to strengthen at a rapid pace.

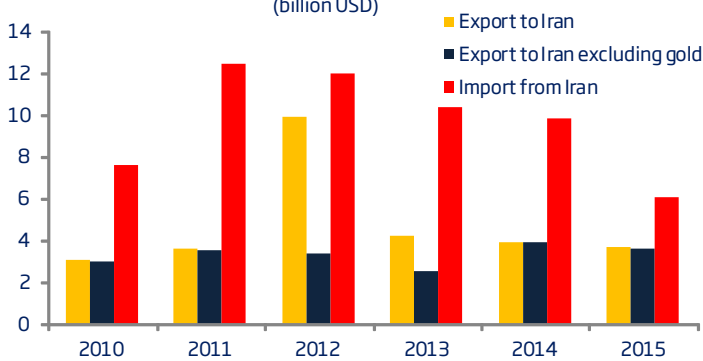
Expectations...

Rising geopolitical risks weighed on export performance in 2015 while the upturn in the EU countries moderated this unfavorable impact. Downward trend in energy prices yielded a significant drop in imports and, in turn, made a noteworthy contribution to the improvement in the foreign trade deficit. In 2016, on the other hand, the expected support to Turkey's exports by the anticipated recovery in the EU countries may balance the negative effect of the geopolitical risks on exports performance. Should the low energy prices persist and should domestic demand continue to present a moderate course, foreign trade balance will maintain its favorable outlook in the upcoming period.

According to the provisional data, in the first month of 2016 exports and imports fell by 21.2% and 19.6%, respectively. Largely thanks to the considerable contribution of the drop in energy imports, the contraction in foreign trade deficit became 15.2% in this period.

Trade Between Turkey and Iran

(billion USD)



As the sanctions on Iran are lifted, its trade volume is expected to grow at a substantial rate in the forthcoming period. In this context, being a neighbor to Iran can be

Current account posted a deficit of 2.1 billion USD in November.

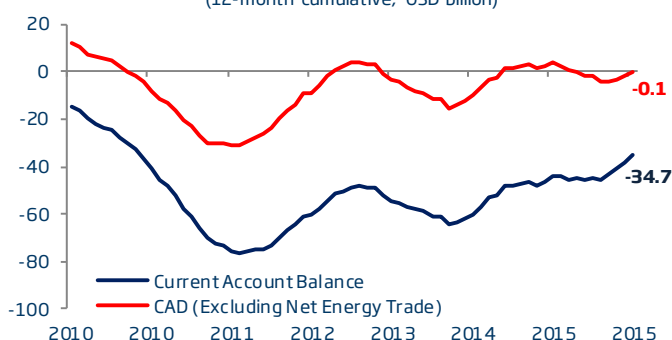
Current account balance presented a better outlook compared to the previous year in November as this was also the case throughout the year. Current account deficit, which was 5.8 billion USD in November 2014, became 2.1 billion USD in the same month of 2015. In January-November period, the deficit recovered by 29.7% yoy and came in at 27.8 billion USD while 12-month cumulative current account deficit narrowed to 34.7 billion USD, the lowest level since September 2010.

The annual contraction in trade balance during the January-November period amounted to 14 billion USD while net tourism revenues contracted by 2.7 billion USD.

An inflow of 9.2 billion USD in net foreign direct investments...

Making only a limited contribution to the financing of current account deficit (92 million USD) in November, net foreign direct investments have presented a stronger performance in the first eleven months of 2015. Net foreign direct investments, which were 4.8 billion USD in January-November 2014, reached 9.2 billion USD in the same period of 2015.

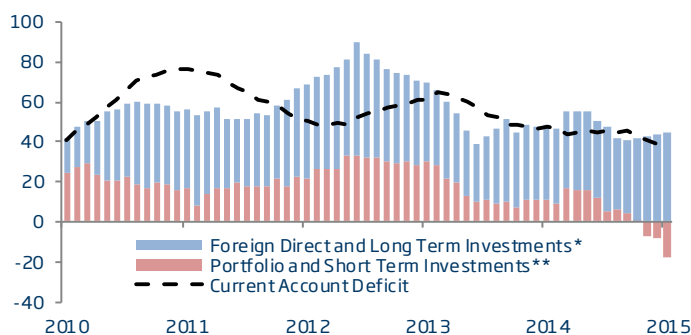
Current Account Balance
(12-month cumulative, USD billion)



Narrowing foreign trade deficit continued to support current account balance.

In the first eleven months of 2015, imports registered faster drops than exports mostly thanks to the persistent downward trend in energy prices. Parallel to the weak course of energy prices and the sharp decline in gold imports recorded in November, 55% plunge in foreign trade deficit has been instrumental in the improvement in current account balance. However, tourism revenues offered a lackluster outlook also in November due to the geopolitical risks and the ongoing economic crisis in Russia. Leaving the worst November performance since 2010 behind, net tourism revenues declined by 13% yoy exerting pressure on current account deficit.

Financing of Current Account Deficit
(12-month cumulative, USD billion)



(*) 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.

Capital outflow in portfolio investments in November...

Having posted a limited capital inflow in October, net portfolio investments recorded a huge outflow of 3.1 billion USD in November. It had registered an inflow of 3.3 billion USD in the same month of the previous year. 1.1 billion USD of this amount stemmed from the equity market while debt securities reported a net outflow of 623 million USD. Realizing at 1.4 billion USD, residents' portfolio investments abroad also weighed on the outlook in net portfolio

Breakdown of Net Capital Inflows

(12-month cumulative, USD million)

			Breakdown of Net Capital Inflows (%)	
	Dec. 2014	Nov. 2015	Dec. 2014	Nov. 2015
Current Account Balance	-46,526	-34,741	-	-
Total Net Foreign Capital Inflows	46,058	23,921	100.0	100.0
-Direct Investments	5,716	10,099	12.4	42.2
-Portfolio Investments	20,104	-13,637	43.6	-57.0
-Other Investments	16,942	16,693	36.8	69.8
-Net Errors and Omissions	3,366	10,773	7.3	45.0
-Other	-70	-7	-0.2	0.0
Reserves⁽¹⁾	468	10,820	-	-

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

investments.

Net capital outflows in portfolio investments reached 14.8 billion USD in the first eleven months of the year. The outflow registered in government debt securities' was responsible for more than 40% of this amount.

Private sector continued to obtain funds from abroad.

Despite the abrupt changes in global risk perception and unfavorable outlook of portfolio flows towards emerging markets, banks and other sectors did not face any difficulty in attaining funds from abroad in 2015. According to the 12-month cumulative figures, banks' and non-bank sectors' long-term debt roll-over ratios kept increasing in November and became 340% and 160%, respectively.

Details of credit accounts revealed that banking sector made a net repayment of 2 billion USD in short-term while it was a net credit borrower with 2.2 billion USD in long-term. Other sectors also made a net repayment 279 million USD in short term and raised credits amounting to a net 1.6 billion USD in long-term. Hence, loans raised from abroad contributed to the financing of current account deficit in November as this was also the case during the whole year.

Consequently, other investments exhibited a solid performance in November registering a net capital inflow of 4.7 billion USD also led by the 2.4 billion USD inflow recorded in cash and deposits account.

Reserve assets registered a fall in eight of the first eleven months in 2015. In November, the decline in this account was 212 million USD while net errors and omissions contributed to the financing of the deficit by 203 million USD. Net errors and emissions had a significant share in the sources of financing in January-November period with an inflow of 11.9 billion USD.

Expectations...

Should the economic upturn in European Union countries take place as strongly as expected reinforcing the export performance of Turkey and should low levels of energy prices prevail, current account deficit might keep drawing a favorable picture in the forthcoming period. Nevertheless, the rising geopolitical risks and the recent tension with Russia imply that current account deficit can come under pressure in 2016 via foreign trade and tourism channels.

Balance of Payments	(USD million)				
	November 2015	Jan. - Nov. 2014 2015		% Change	12-Month Cumulative
Current Account Balance	-2,105	-39,622	-27,837	-29.7	-34,741
Foreign Trade Balance	-2,953	-56,743	-42,693	-24.8	-49,534
Services Balance	1,484	24,461	23,554	-3.7	24,257
Travel (net)	1,179	23,568	20,835	-11.6	21,747
Primary Income	-719	-8,337	-9,560	14.7	-10,436
Secondary Income	83	997	862	-13.5	972
Capital Account	0	-69	-6	-91.3	-7
Financial Account	-1,902	-35,190	-15,935	-54.7	-23,975
Direct Investments (net)	-92	-4,805	-9,188	91.2	-10,099
Portfolio Investments (net)	3,076	-18,958	14,783	-	13,637
Net Acquisition of Financial Assets	1,396	1,603	6,937	332.8	6,080
Net Incurrence of Liabilities	-1,680	20,561	-7,846	-	-7,557
Equity Securities	-1,057	2,563	-1,978	-	-1,982
Debt Securities	-623	17,998	-5,868	-	-5,575
Other Investments (net)	-4,674	-16,595	-16,346	-1.5	-16,693
Currency and Deposits	-2,416	-1,545	-359	-76.8	577
Net Acquisition of Financial Asse	-1,995	-26	12,435	-	12,748
Net Incurrence of Liabilities	421	1,519	12,794	742.3	12,171
Central Bank	-51	-2,247	-877	-61.0	-963
Banks	472	3,766	13,671	263.0	13,134
Foreign Banks	354	667	9,785	1,367.0	9,214
Foreign Exchange	122	-1,704	5,127	-	3,977
Turkish Lira	232	2,371	4,658	96.5	5,237
Non-residents	118	3,099	3,886	25.4	3,920
Loans	-1,393	-13,632	-14,522	6.5	-15,945
Net Acquisition of Financial Asse	59	2,051	525	-74.4	337
Net Incurrence of Liabilities	1,452	15,683	15,047	-4.1	16,282
Banking Sector	188	10,732	5,039	-53.0	6,143
Non-bank Sectors	1,307	5,649	10,978	94.3	11,298
Trade Credit and Advances	-868	-949	-1,206	27.1	-1,064
Other Assets and Liabilities	3	-469	-259	-44.8	-261
Reserve Assets (net)	-212	5,168	-5,184	-	-10,820
Net Errors and Omissions	203	4,501	11,908	164.6	10,773

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: Datastream, CBRT

Budget posted a deficit of 22.6 billion TRY in 2015.

Central government budget followed the historical trend also in the last month of 2015, posting a relatively larger deficit. The budget posted a deficit of 17.2 billion TRY, increasing by 42.8% yoy.

Both budget revenues and expenditures rose by a relatively similar pace in 2015. Thus, budget deficit contracted by 3.3% yoy to 22.6 billion TRY in 2015, remaining below the year-end target of the Medium Term Program (MTP). On the other hand, primary surplus expanded by 14.5% yoy and reached 30.4 billion TRY.

Budget revenues displayed a weak performance in December.

Budget revenues surged by 8.1% yoy in December while they registered a decrease in real terms. This development stemmed from the fall in non-tax revenues. On the other hand, having risen by 12.6% yoy in this period, tax revenues displayed a relatively strong performance mostly thanks to the sharp increases in special consumption tax (SCT) and value-added tax (VAT) on imports revenues.

Regarding the whole year, budget revenues recorded an increase of 13.6% yoy, while tax revenues expanded by 15.6% yoy. SCT revenues, which constitute about 25% of total tax revenues, surged by 16.3% yoy in 2015. Income tax revenues also made a positive contribution to the budget indicators increasing by 16% yoy. On the other hand, corporate tax revenues remained below the year-end-target in 2015. Despite having dropped on annual basis,

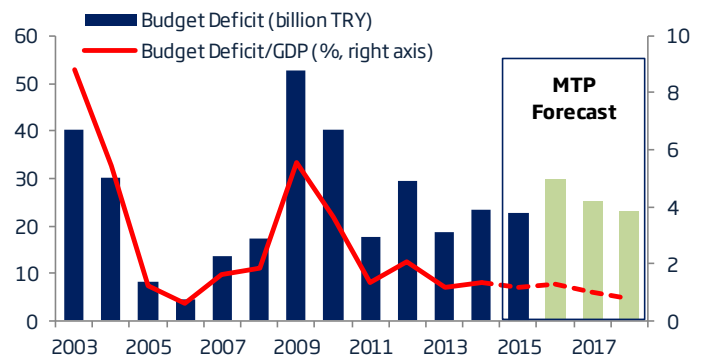
privatization revenues contributed to the budget revenues by 6.1 billion TRY.

Non-interest expenditures rose by 13.6% in 2015.

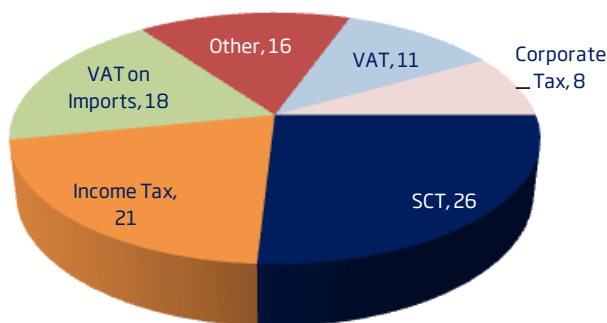
Budget expenditures increased by 16.3% in December due to the rises registered in personnel expenditures, capital expenditures and capital transfers. During this period, capital expenditures constituted one third of the total capital expenditures recorded in the whole year.

In 2015, budget expenditures rose by 12.8% yoy. Personnel expenditures and current transfers surged by 13.3% yoy and 12.6% yoy, respectively. The annual increase in interest expenditures, on the other hand, was lower with 6.2%. One fourth of the overall rise in budget expenditures in 2015 stemmed from governments premiums to social security agencies and shares of local governments from revenues.

Budget Deficit



Composition of Tax Revenues (% ,2015)



Expectations

Central budget realizations indicated that Turkey maintained fiscal discipline in 2015. Indeed, according to MTP estimates, the budget deficit to GDP ratio declined to 1.2% in this period. The MTP forecasts for the annual rises in revenues and expenditures for 2016 stand at 11.9% and 12.7%, respectively. Against this backdrop, budget deficit is expected to be 29.7 billion TRY and the deficit to GDP ratio is forecasted to be 1.3%.

Central Government Budget

(TRY billion)

	December			January-December			2015 Budget	MTP	Real/MTP
	2014	2015	% Change	2014	2015	% Change	Target	Target	Target (%)
Expenditures	50.5	58.8	16.3	448.8	506.0	12.8	472.9	503.0	100.6
Interest Expenditures	1.5	1.7	19.3	49.9	53.0	6.2	54.0	54.0	98.2
Non-Interest Expenditures	49.1	57.0	16.3	398.8	453.0	13.6	418.9	449.0	100.9
Revenues	38.5	41.6	8.1	425.4	483.4	13.6	452.0	478.5	101.0
Tax Revenues	30.9	34.7	12.6	352.5	407.5	15.6	389.5	405.8	100.4
Other Revenues	7.6	6.9	-10.0	72.9	75.9	4.2	62.5	72.8	104.3
Budget Balance	-12.0	-17.2	42.8	-23.4	-22.6	-3.3	-21.0	-24.5	92.3
Primary Balance	-10.6	-15.4	46.0	26.5	30.4	14.5	33.0	29.5	103.0

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

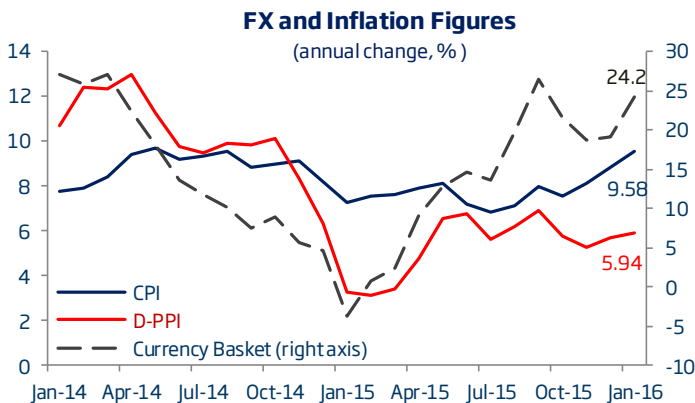
Inflation came in above expectations in January.

In January, CPI increased by 1.82% mom, surpassing the market expectations, while monthly Domestic PPI (D-PPI) inflation was realized as 0.55%. According to the Reuters poll and CBRT's Survey of Expectations, monthly CPI inflation expectations were 1.7% and 1.21%, respectively.

January	CPI		D-PPI	
Change (%)	2015	2016	2015	2016
Monthly	1.10	1.82	0.33	0.55
Year-to-Date	1.10	1.82	0.33	0.55
Annual	7.24	9.58	3.28	5.94
Annual Average	8.80	7.87	9.59	5.50

Annual inflation reached its highest level in 20 months.

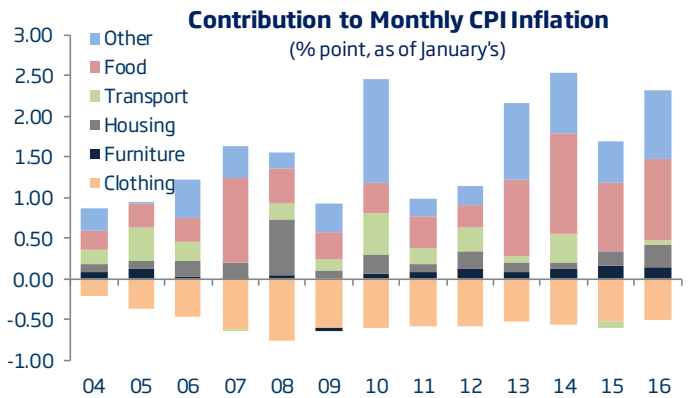
The upward pressure on inflation due to the developments in both food prices and exchange rates has persisted also in January. Thus, annual inflation approached double-digit levels in the first month of 2016. Having declined in the last 3 months of 2015, D-PPI posted a relatively modest annual increase despite the low base effect.



Turkstat revised the weight of the main expenditure groups in CPI basket for 2016. Accordingly, the weights of food-beverages and transportation subgroups have been decreased by 57 and 107 bps, respectively while the share of the hotels and restaurants has been increased by 49 bps.

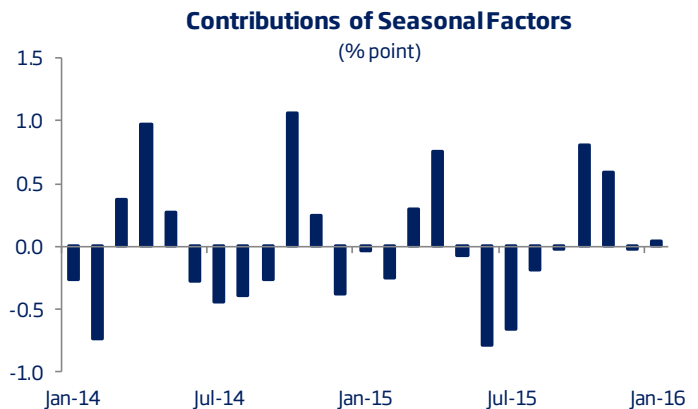
Ongoing increase in food prices...

Prices in food and non-alcoholic beverages group surged by 4.28% mom and made the highest contribution to CPI inflation by 102 bps. Prices in housing, alcoholic beverages and tobacco subgroups also rose in January mainly due to the price adjustments and tax hikes. Price increases in these groups made contribution to monthly inflation by a total of 75 bps. On the other hand, seasonal declines in the prices of clothing and footwear lowered the monthly CPI by 50 bps.



In January, the price increases in only education, housing, communication and transportation subgroups were lower than CBRT's year-end inflation forecast of 7.5%.

Seasonal factors displayed a balanced outlook in January as was the case in December. However, the upward trend in core inflation indicators observed since August 2015 has persisted in January.



Rise in D-PPI...

The crude petroleum and natural gas prices decreased by 26% mom in January. The prices in tobacco, petroleum products and wearing apparel also declined in this period. Nevertheless, the prices in other sub-sectors, especially in manufacturing of food products, led the increase in annual D-PPI inflation.

Expectations

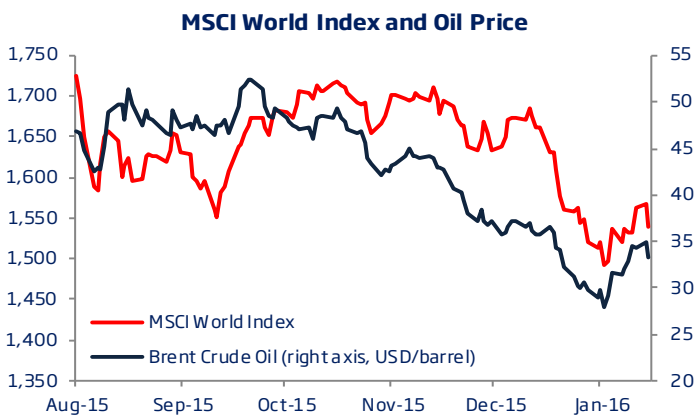
The price increases in administered prices and the minimum wage hike caused the inflation expectations to surge in January. We expect this deterioration in the inflation indicators to continue for some more time due to the lagged impact of the TRY depreciation and the elevated levels of food prices. Against this backdrop, the prices in the main expenditure groups excluding the clothing and footwear are more likely to post an increase also in February. The low base effect in D-PPI will last until April while oil price developments may limit this impact to some extent.

Source: Datastream, Turkstat

Global markets made a bad start to the year.

The increasing concerns over Chinese economy and the volatility in oil prices have weighed on global markets in the first half of January. The depreciation in yuan during the first days of the month and sharp slumps in stock exchanges resulted in a deterioration in risk perception on a global scale. The leading indicators in China released in this period showed that the economic activity has further lost steam. This, in turn, put additional downward pressure on oil prices.

During the second half of the month, on the other hand, global risk appetite recovered somewhat along with the accommodative announcements by major central banks and the upturn in oil prices. Expectations that the Fed might pause for a while in raising rates gained strength during this period. Moreover, ECB and The People's Bank of China emphasized their intentions to offer further stimulus to revive economy in 2016. Together with these, BoJ unexpectedly cut the interest rate into negative territory at its meeting held in the late January, a step which was welcomed by the global markets.



CBRT kept the policy rates intact.

CBRT held the policy rate at 7.5% at its meeting held in January 19. Making no reference to its simplification plans, CBRT suggested, in an indirect way, that the increasing volatility in the markets was the major reason behind this. Given that the term of the Governor Erdem Başçı ends in April, no significant change in CBRT's policies is expected until April.

Inflation is expected to gradually converge to the medium term target of 5% according to the first Inflation Report of the year published on January 26. After declining to 7.5% in 2016 and further to 6% in 2017, inflation is anticipated to achieve stability at 5% in 2018. The Central Bank Governor Erdem Başçı commented at the press conference that it was too early to move to a single policy rate framework. Pointing out that the current inflation outlook remained far from

achieving price stability, Başçı stated that the downward revisions in oil and import prices pulled down the inflation forecasts. Başçı also underlined that minimum wage hike and administered price adjustments have driven inflation projections up.

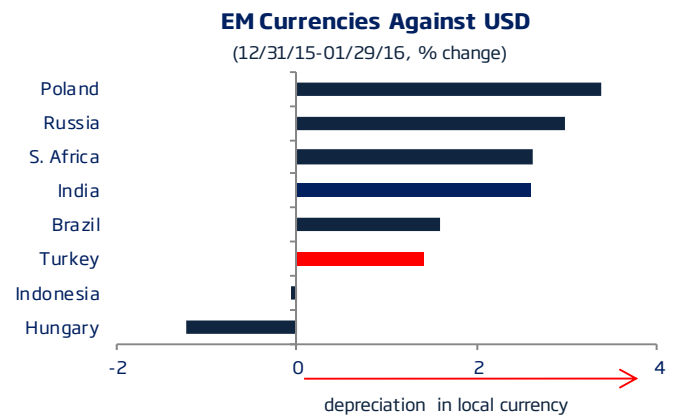
BIST-100 index rose by 2.4% ytd.

Closing 2015 at 71,727, BIST-100 index fell below 70,000 on January 20 due to the developments in global markets. The decline in Turkish stock exchange remained limited compared to its emerging market peers, thanks to the buying at lower levels and sliding oil prices that help reducing the fragility of the current account balance. The index rose in the following days parallel to the relatively positive environment reigned in the global markets. BIST-100 index rose by 2.4% ytd to 73,481 in January.

Reached as high as 11.28% in January, the 2-year benchmark yield declined slightly during the last days of the month with the help of the growing risk appetite. The benchmark yield became 10.99% as of January 29.

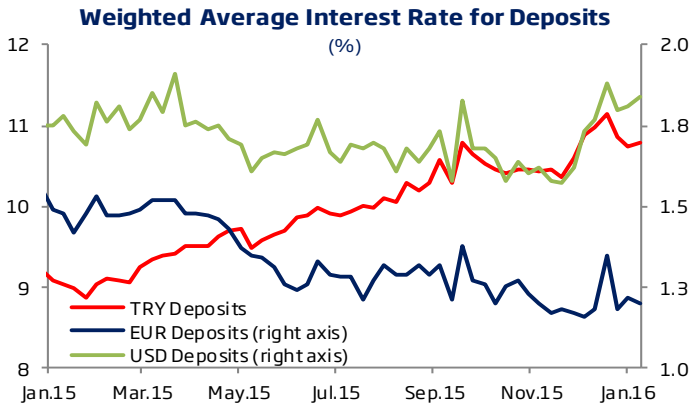
USD/TRY followed a volatile path in January.

TRY performed weakly in January due to the intensified pressure on emerging market currencies. USD/TRY surpassed the 3.06 level on January 20 along with the delay in CBRT's simplification steps. A relative improvement in global risk perception during the following days made it possible for USD/TRY to decline to as low as 2.95 on January 29.



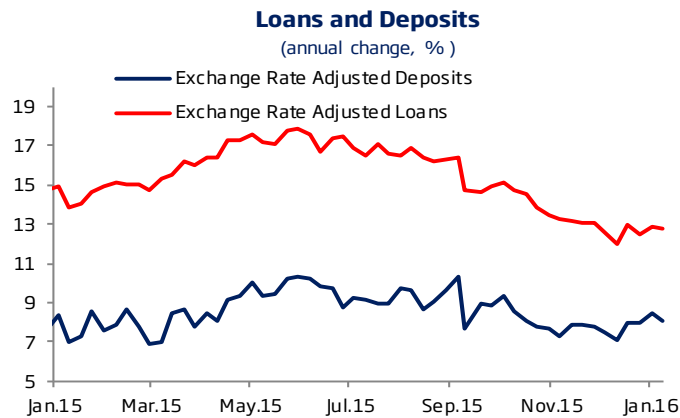
Upward movement in TRY deposits...

According to BRSA's Weekly Bulletin, deposit volume increased by 1.2% compared to end-2015 and was realized as 1,337 billion TRY as of January 22. FX deposits in USD terms fell by 2.9% ytd while TRY deposit volume grew by 1.7% in the same period. However, the surge in USD/TRY during the first 3 weeks of the year limited the impact of downturn in FX deposits in USD terms on total deposits.



Contraction in exchange rate adjusted loans...

Loan volume recorded a year-to-date increase of 0.7% and was realized as 1,523 billion TRY as of January 22. The upsurge in FX rates was the major driver behind this expansion. Indeed, according to exchange rate adjusted figures, loans dropped by 0.4% in this period.



TRY loans fell by 0.7% ytd while FX loans in USD terms recorded a limited increase of 0.1% as of January 22.

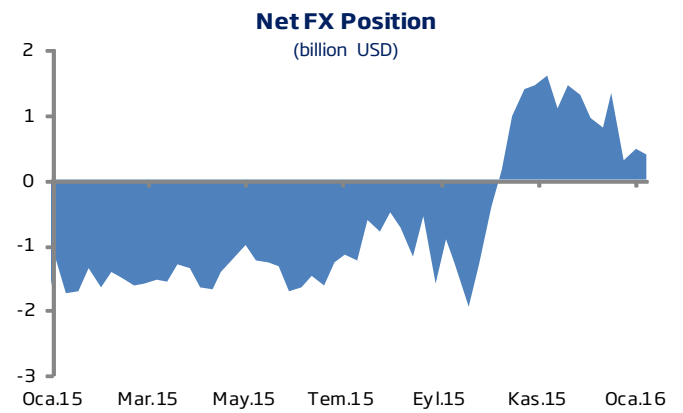
As of January 22, non-performing loans ratio was realized as 3.13%. The said ratio for consumer loans increased slightly compared to the end-2015 and reached 4.51% while that for commercial loans remained flat at 2.68%.

Securities portfolio...

Securities portfolio of banking sector rose by 1.3% ytd and was realized as 332 billion TRY as of January 22. Securities subject to repo transactions, which constitute about half of total securities, decreased by 3.4% in this period. Available for sale and held to maturity securities portfolios, on the other hand, expanded by 12% and 5.9% ytd, respectively.

Net FX position...

As of January 22, banks' on-balance sheet FX position was (-) 25,561 million USD while off-balance sheet FX position became (+) 25,948 million USD. Hence, banks' net FX position was realized as (+) 386 million USD.



Source: BRSA Weekly Bulletin

Concluding Remarks

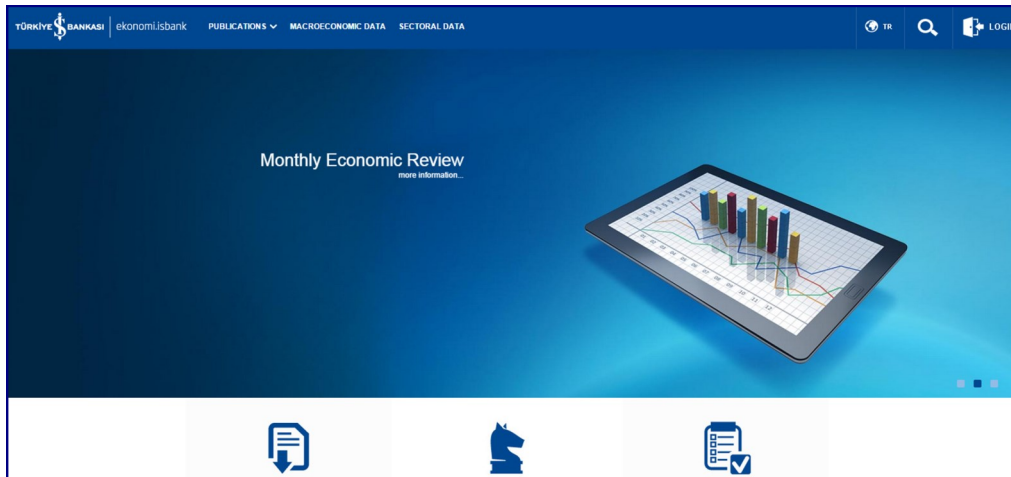
Global markets have tumbled during the first half of January in particular. Concerns over Chinese economy, geopolitical events being assessed as “significant risk factors” and sharp slump in oil prices played an important role in this development. This weak outlook has weighed largely on emerging markets including Turkey. The prominent financial institutions like IMF and World Bank, pointing to the downward risks facing emerging markets, have revised down their global growth forecasts recently.

Monetary policies conducted by major central banks have also been in focus of attention during the first month of the year. Even though a major source of uncertainty has been left behind with Fed raising rates in December, there remain questions over the pace and the size of the future rate hikes, of which expectations change abruptly. Contrary to the Fed’s normalization moves, European and Japanese Central Banks seemed to be inclined to introducing new measures combating low inflation and lackluster growth performances. Yet, the strength of their policy measures is still controversial. Considering all of these economic and financial developments together, global economy, as well as the Turkish economy, is expected to stay under pressure in the upcoming period.

Forecasts (%)	2015	2016
Growth	3.5	3.5
CA Deficit/GDP	4.9	5.5
Inflation	8.8 (R)	7.5

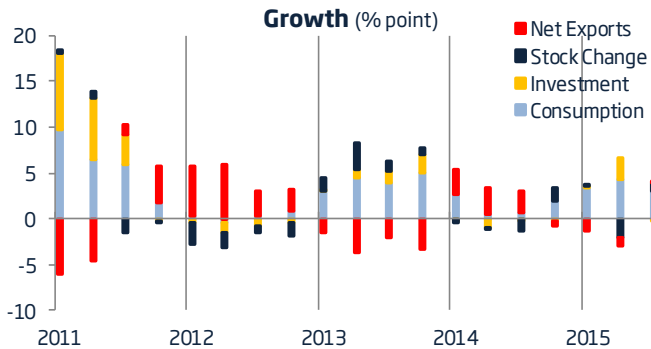
(R) Realization
Year-end forecast for inflation

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

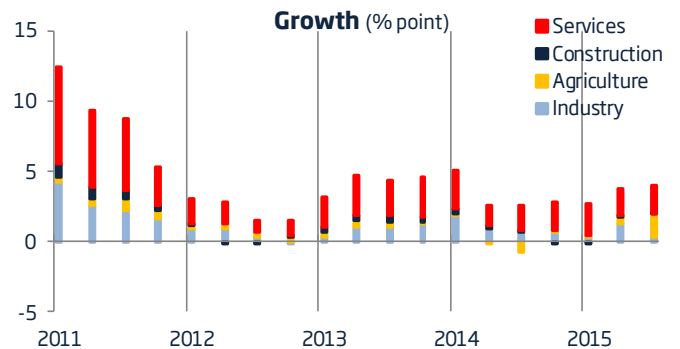


Growth

Expenditure Approach - Contributions to GDP

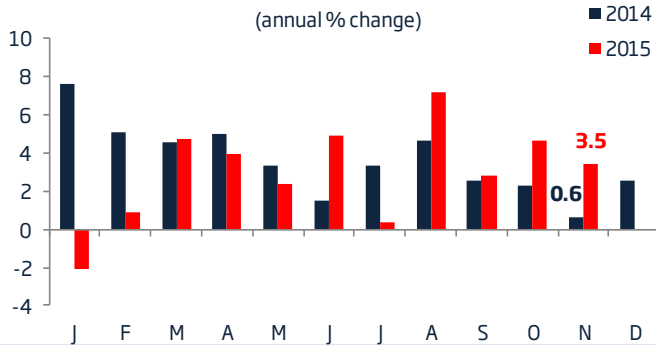


Production Approach - Contributions to GDP

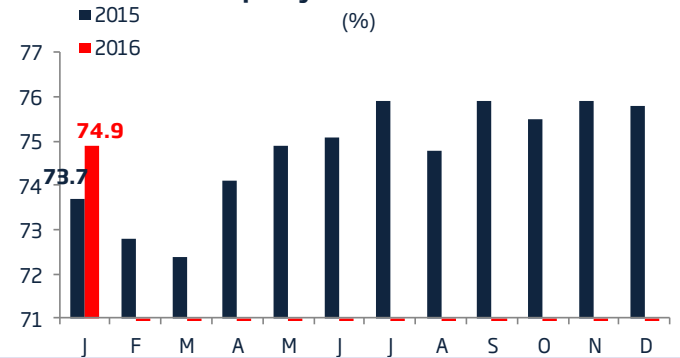


Industrial Production and Capacity Utilization Ratio

Industrial Production*

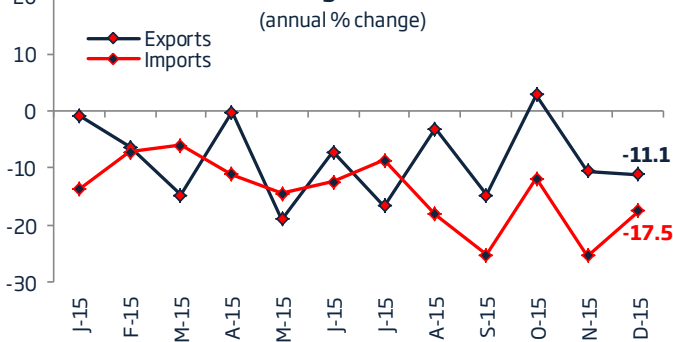


Capacity Utilization Ratio

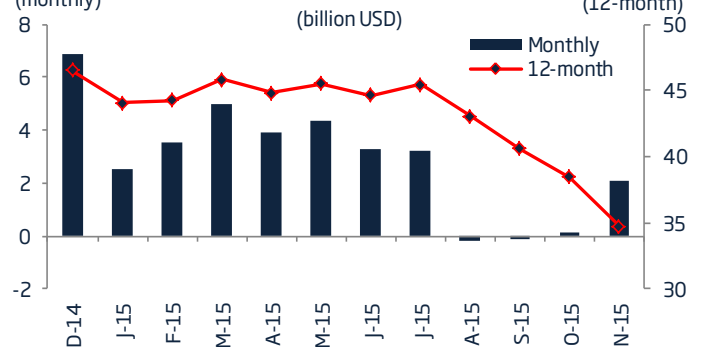


Foreign Trade and Current Account Balance

Foreign Trade

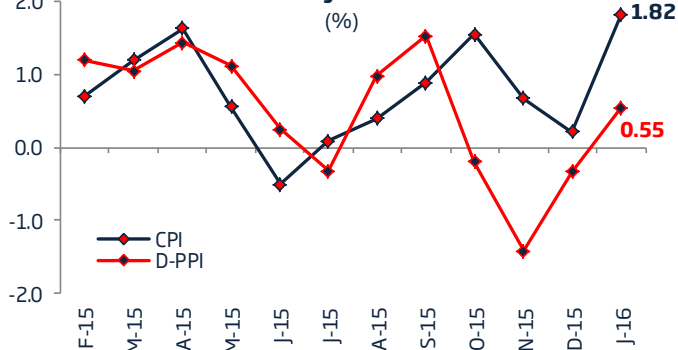


Current Account Deficit

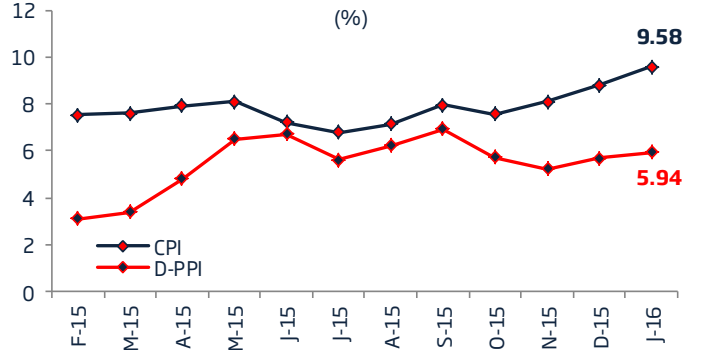


Inflation

Monthly Inflation



Annual Inflation

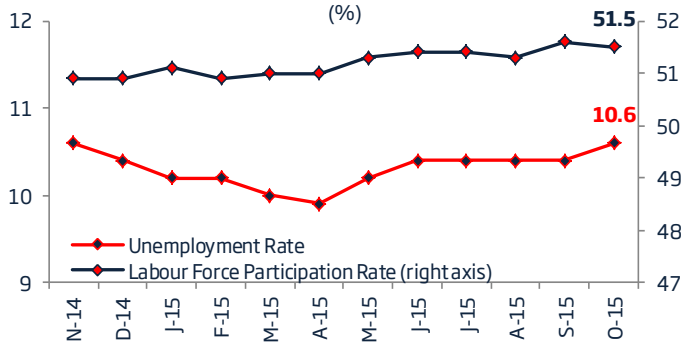


(*) Calendar adjusted figures

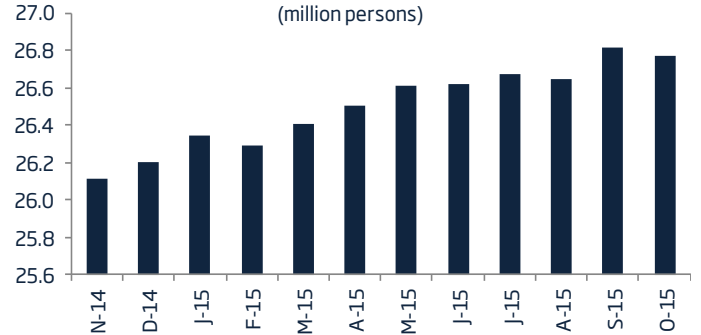
Source: CBRT, Datastream, Turkstat

Labor Market

Seasonally Adjusted Labour Force Indicators (%)

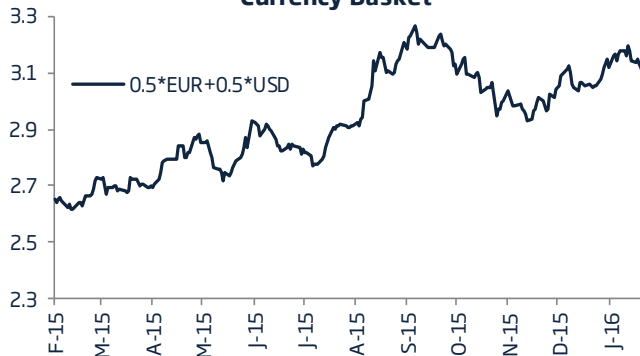


Seasonally Adjusted Employment (million persons)

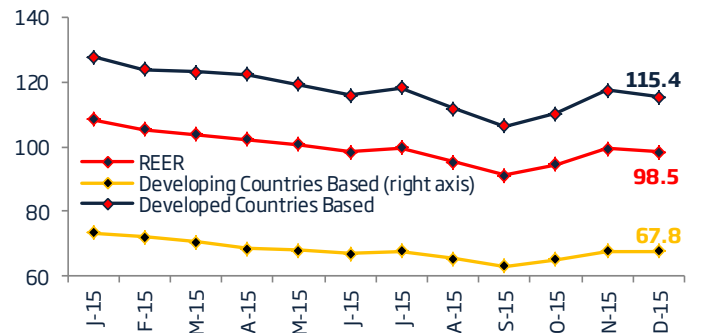


FX Market

Currency Basket

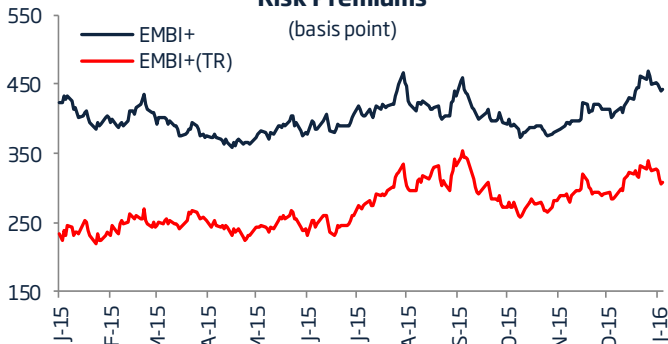


CPI Based Real Effective Exchange Rate

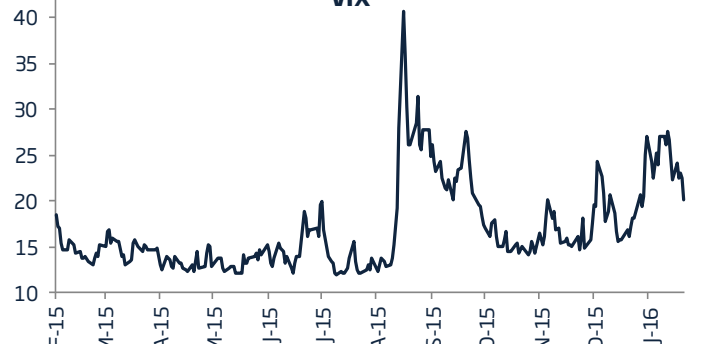


Risk Indicators

Risk Premiums (basis point)

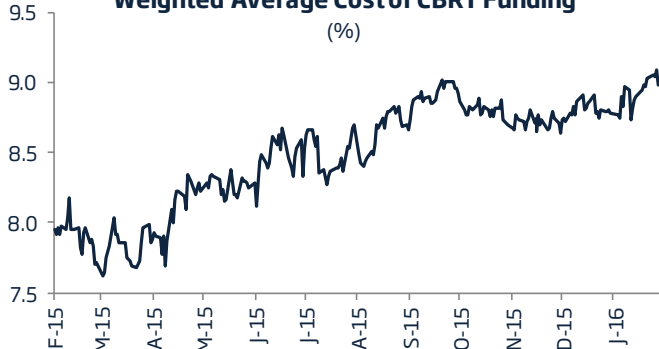


VIX

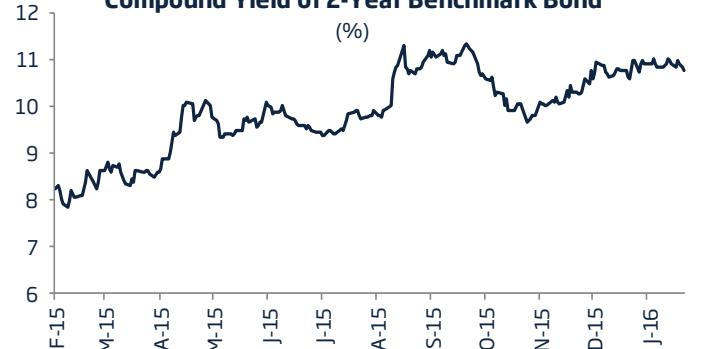


Interest Rates

Weighted Average Cost of CBRT Funding (%)

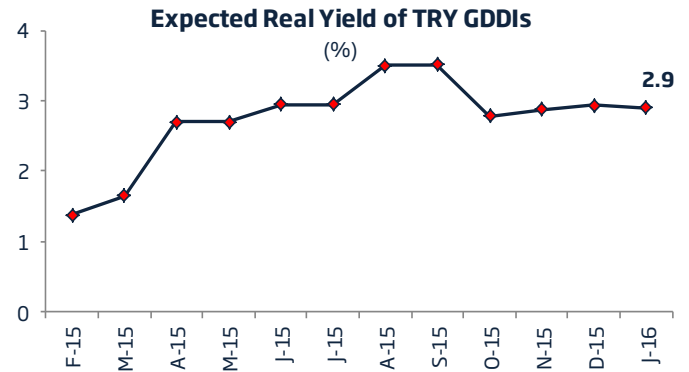
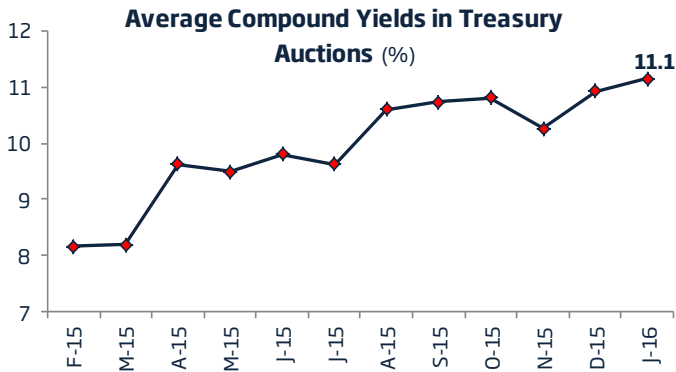


Compound Yield of 2-Year Benchmark Bond (%)

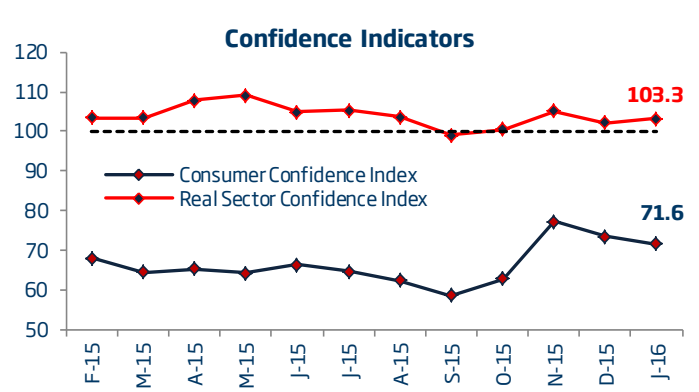
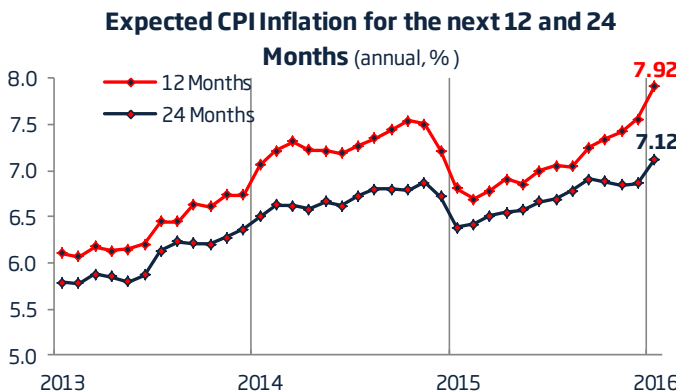
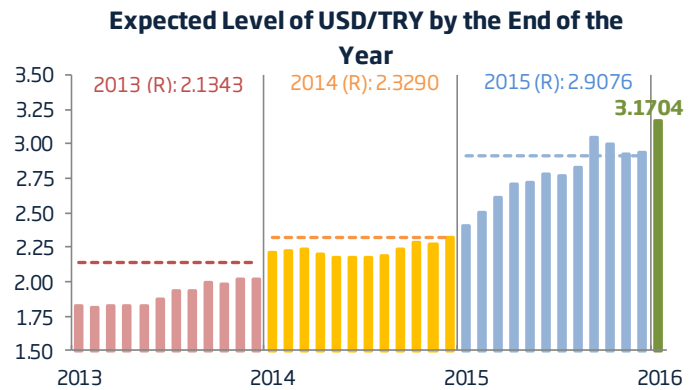
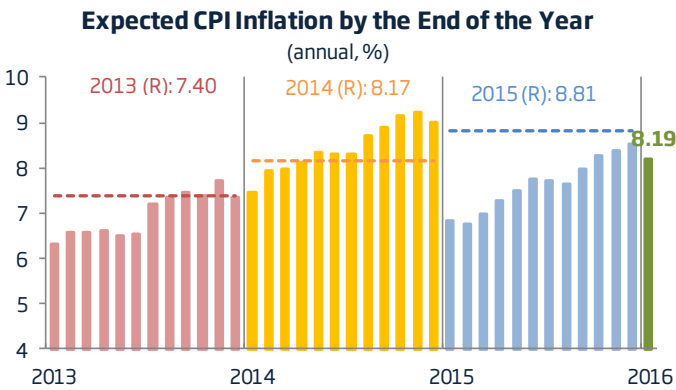
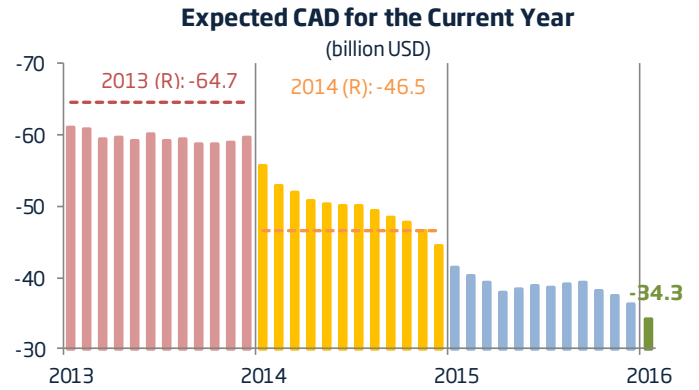
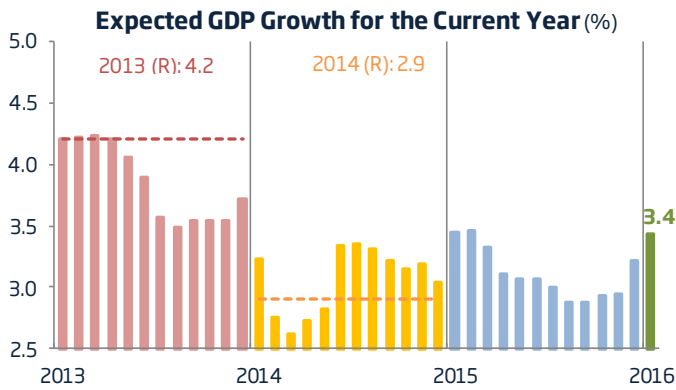


Source: BIST, CBRT, Datastream, JP Morgan, Reuters, Turkstat

Bond-Bill Market



Survey of Expectations and Other Leading Indicators



(R) Realization

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

Turkish Economy at a Glance

	2010	2011	2012	2013	2014	15-Q1	15-Q2	15-Q3
Growth								
GDP (USD billion)	731.6	774.0	786.3	823.0	799.0	181.1	180.7	184.2
GDP (TRY billion)	1,099	1,298	1,417	1,567	1,747	444.6	482.4	518.6
GDP Growth Rate (%)	9.2	8.8	2.1	4.2	2.9	2.5	3.8	4.0
Inflation (%)						Nov-15	Dec-15	Jan-16
CPI (annual)	6.40	10.45	6.16	7.40	8.17	7.58	8.10	9.58
Domestic PPI (annual)	8.87	13.33	2.45	6.97	6.36	5.74	5.25	5.94
Seasonally Adjusted Labor Market Figures						Aug-15	Sep-15	Oct-15
Unemployment Rate (%)	10.0	8.5	8.8	9.1	10.4	10.4	10.4	10.6
Labor Force Participation Rate (%)	47.1	47.2	48.5	48.5	50.9	51.4	51.3	51.5
FX Rates						Nov-15	Dec-15	Jan-16
CPI Based Real Effective Exchange Rate	119.2	102.8	110.3	101.0	105.5	99.5	98.5	
USD/TRY	1.5413	1.8934	1.7819	2.1323	2.3290	2.9135	2.9207	2.9635
EUR/TRY	2.0600	2.4497	2.3508	2.9370	2.8297	3.0822	3.1867	3.2321
Currency Basket (0.5*EUR+0.5*USD)	1.8007	2.1716	2.0664	2.5347	2.5794	2.9979	3.0537	3.0978
Foreign Trade Balance⁽¹⁾ (USD billion)						Oct-15	Nov-15	Dec-15
Exports	113.9	134.9	152.5	151.8	157.6	146.4	146.8	143.9
Imports	185.5	240.8	236.5	251.7	242.2	218.7	216.4	207.2
Foreign Trade Balance	-71.7	-105.9	-84.1	-99.9	-84.6	-72.3	-69.6	-63.3
Import Coverage Ratio (%)	61.4	56.0	64.5	60.3	65.1	66.9	67.8	69.5
Balance of Payments⁽¹⁾ (USD billion)						Sep-15	Oct-15	Nov-15
Current Account Balance	-45.3	-75.0	-48.5	-64.7	-46.5	-43.1	-40.6	-34.7
Capital and Financial Accounts	-45.1	-66.0	-48.2	-62.0	-43.2	-37.2	-32.3	-24.0
Direct Investments (net)	-7.6	-13.8	-9.2	-8.8	-5.7	-9.7	-9.3	-10.1
Portfolio Investments (net)	-16.1	-22.2	-41.0	-24.0	-20.1	1.1	5.5	13.6
Other Investments (net)	-34.2	-28.2	-18.9	-39.1	-16.9	-21.9	-21.3	-16.7
Reserve Assets (net)	12.8	-1.8	20.8	9.9	-0.5	-6.8	-7.1	-10.8
Net Errors and Omissions	0.2	9.0	0.3	2.8	3.4	5.9	8.3	10.8
Current Account Balance/GDP (%)	-6.2	-9.7	-6.2	-7.9	-5.8	-	-	-
Budget⁽²⁾⁽³⁾ (TRY billion)						Oct-15	Nov-15	Dec-15
Expenditures	294.4	314.6	361.9	408.2	448.8	367.7	404.2	506.0
Interest Expenditures	48.3	42.2	48.4	50.0	49.9	44.8	47.4	53.0
Non-interest Expenditures	246.1	272.4	313.5	358.2	398.8	322.9	356.8	453.0
Revenues	254.3	296.8	332.5	389.7	425.4	354.2	398.0	483.4
Tax Revenues	210.6	253.8	278.8	326.2	352.5	298.3	333.3	407.5
Budget Balance	-40.1	-17.8	-29.4	-18.5	-23.4	-13.5	-6.2	-22.6
Primary Balance	8.2	24.4	19.0	31.4	26.5	31.3	41.2	30.4
Budget Balance/GDP (%)	-3.6	-1.4	-2.1	-1.2	-1.3	-	-	-
Central Government Debt Stock (TRY billion)						Oct-15	Nov-15	Dec-15
Domestic Debt Stock	352.8	368.8	386.5	403.0	414.6	438.2	439.5	440.1
External Debt Stock	120.7	149.6	145.7	182.8	197.5	239.4	236.8	237.5
Total Debt Stock	473.6	518.4	532.2	585.8	612.1	677.6	676.2	677.6

(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)	2010	2011	2012	2013	2014	Nov.15	Dec.15	Change ⁽¹⁾
TOTAL ASSETS	1,006.7	1,217.7	1,370.7	1,732.4	1,994.3	2,346.6	2,357.5	18.2
Loans	525.9	682.9	794.8	1,047.4	1,240.7	1,468.9	1,484.9	19.7
TRY Loans	383.8	484.8	588.4	752.7	881.0	1,007.1	1,013.3	15.0
Share (%)	73.0	71.0	74.0	71.9	71.0	68.6	68.2	-
FX Loans	142.1	198.1	206.4	294.7	359.7	461.7	471.5	31.1
Share (%)	27.0	29.0	26.0	28.1	29.0	31.4	31.8	-
Non-performing Loans	20.0	19.0	23.4	29.6	36.4	46.4	47.5	30.5
Non-performing Loan Rate (%)	3.7	2.7	2.9	2.8	2.9	3.1	3.1	-
Securities	287.9	285.0	270.0	286.7	302.3	326.5	329.7	9.1
TOTAL LIABILITIES	1,006.7	1,217.7	1,370.7	1,732.4	1,994.3	2,346.6	2,357.5	18.2
Deposits	617.0	695.5	772.2	945.8	1,052.7	1,238.2	1,245.4	18.3
TRY Deposits	433.5	460.0	520.4	594.1	661.3	697.6	715.4	8.2
Share (%)	70.3	66.1	67.4	62.8	62.8	56.3	57.4	-
FX Deposits	183.5	235.5	251.8	351.7	391.4	540.7	530.0	35.4
Share (%)	29.7	33.9	32.6	37.2	37.2	43.7	42.6	-
Securities Issued	3.1	18.4	37.9	60.6	89.3	99.8	97.8	9.6
Payables to Banks	122.4	167.4	173.4	254.2	293.2	356.4	361.3	23.2
Funds from Repo Transactions	57.5	97.0	79.9	119.1	137.4	148.7	156.7	14.0
SHAREHOLDERS' EQUITY	134.5	144.6	181.9	193.7	232.0	259.1	262.2	13.0
Profit (Loss) of the Period	22.1	19.8	23.5	24.7	24.6	23.9	26.1	-
RATIOS (%)								
Loans/GDP	47.9	52.6	56.1	66.8	71.0	-	-	-
Loans/Assets	52.2	56.1	58.0	60.5	62.2	62.6	63.0	-
Securities/Assets	28.6	23.4	19.7	16.6	15.2	13.9	14.0	-
Deposits/Liabilities	61.3	57.1	56.3	54.6	52.8	52.8	52.8	-
Loans/Deposits	85.2	98.2	102.9	110.7	117.9	118.6	119.2	-
Capital Adequacy (%)	19.0	16.6	17.9	15.3	16.3	15.5	15.6	-

(1) Year-to-date % change



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