

### Global Economy

- ◆ Markets witnessed severe bouts of volatility due to the widely unexpected “leave” result of the Brexit referendum held on June 23. Sterling depreciated considerably and safe haven assets attracted strong demand.
- ◆ In the aftermath of the referendum, emerging expectations that leading central banks would loosen their monetary policies in order to struggle with rising risks stemming from the outcome of Brexit have given the markets the opportunity to take a sigh of relief. Indeed, the head of BoE, Mark Carney, hinted that policy rate, which currently stands at 0.5%, could be cut in summer months.
- ◆ The new picture arisen with Brexit and the Brexit-related issues caused the Fed’s rate hike expectations of the markets for 2016 weaken to a large extent while only 1 rate hike is anticipated in 2017. Fed officials also revised down their interest rate expectations for the coming years in June meeting.
- ◆ Euro Area consumer prices increased in June for the first time in 5 months. The final reading suggested that economic growth in the region came in at 0.6% qoq. It was a positive development that the highest contributions to growth came from household expenditures and private sector investments.
- ◆ Oil prices fluctuated during the recent weeks in response to the trajectory of the US dollar, the US crude inventories and the changing expectations for global growth.

### Turkish Economy

- ◆ Economic activity remained solid in the first quarter of 2016. Turkish economy expanded by 4.8% yoy in this period, slightly above the market expectations of 4.5%. Domestic demand was the main engine of growth during this period.
- ◆ Industrial production made a weak start to the second quarter of the year. Rising by 0.7% yoy in April, industrial production posted its poorest performance since July 2015. The slowdown in manufacturing industry was noteworthy during this period.
- ◆ Exports posted an annual rise of 9.6% in May, the fastest since March 2014. Imports, on the other hand, fell by 3.8% yoy, at the slowest pace in 18 months. Thus, foreign trade deficit continued to narrow in this period.
- ◆ Current account deficit decreased by 900 million USD yoy to 2,956 million USD in April. According to the 12-month cumulative figures, current account deficit declined to 28.6 billion USD.
- ◆ Central government budget sustained its strong performance in May. The budget surplus came in at 3.7 billion TRY rising by 2 billion TRY compared to a year ago.
- ◆ Downward trend in CPI halted in June due to the higher than expected increase in prices. During this period, annual consumer inflation reached its highest reading since February 2016 with 7.64%. Annual D-PPI inflation was 3.41% in June, increasing by 16 basis points compared to May.
- ◆ CBRT cut the upper band of the interest rate corridor (overnight lending rate) by 50 basis points to 9% in line with the expectations at its meeting held on June 21.

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**Turkish economy grew by 4.8% yoy in the first quarter.**

Economic activity remained solid in the first quarter of 2016. Turkish economy expanded by 4.8% yoy in this period, slightly above the market expectations of 4.5%. Yet, the downward trend in GDP in USD terms prevailed due to the TRY depreciation. Seasonal and calendar adjusted GDP grew by 0.8% qoq posting a relatively milder increase.

**Contributions by Expenditure Approach (1998 prices)**

% point	2015					2016
	Q1	Q2	Q3	Q4	Annual	Q1
<b>Consumption</b>	<b>3.3</b>	<b>4.3</b>	<b>3.1</b>	<b>4.3</b>	<b>3.7</b>	<b>5.9</b>
Private	3.0	3.5	2.3	3.2	3.0	4.8
Public	0.3	0.8	0.8	1.1	0.7	1.2
<b>Investment</b>	<b>0.1</b>	<b>2.4</b>	<b>0.0</b>	<b>0.9</b>	<b>0.9</b>	<b>0.0</b>
Private	0.2	2.0	-0.4	0.3	0.5	-0.1
Public	0.0	0.4	0.4	0.5	0.3	0.0
<b>Change in Stock</b>	<b>0.5</b>	<b>-1.8</b>	<b>0.9</b>	<b>-0.7</b>	<b>-0.3</b>	<b>0.4</b>
<b>Net Export</b>	<b>-1.4</b>	<b>-1.2</b>	<b>-0.1</b>	<b>1.3</b>	<b>-0.3</b>	<b>-1.5</b>
Exports	-0.4	-0.7	-0.4	0.6	-0.2	0.6
Imports	-1.1	-0.4	0.3	0.8	-0.1	-2.2
<b>GDP</b>	<b>2.5</b>	<b>3.7</b>	<b>3.9</b>	<b>5.7</b>	<b>4.0</b>	<b>4.8</b>

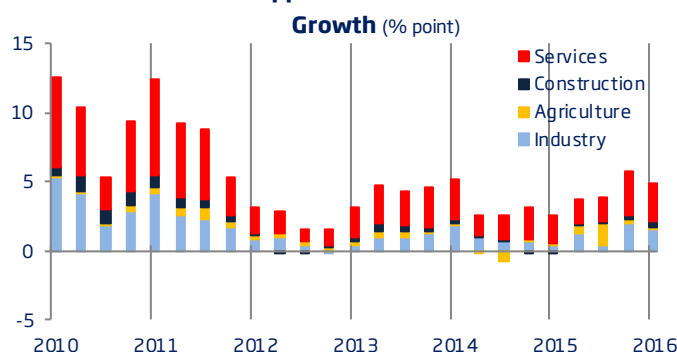
**Domestic demand strengthened further.**

Having a share of more than 80% in GDP, consumption expenditures increased at the fastest pace recorded in the last 18 months and made a 5.9 points contribution to the growth in the first quarter. This mainly stemmed from the surge in private consumption expenditures which have received support from the minimum wage hike. It was also worthy of attention that public consumption expenditures rose by 10.9% yoy, the strongest expansion in almost 5 years. This was mostly due to the pickup in purchases of goods and services which registered a rise of 17%, the highest annual increase since the last quarter of 2009. Therefore, public consumption expenditures added 1.2 points to the growth, a relatively strong contribution.

**Investment expenditures stayed away from recovery.**

Total investment expenditures had almost no impact on the first quarter growth figures. While private investment expenditures dragged down the growth by 0.1 point, public investment expenditures contributed only a negligible amount in the same period. The weak outlook in investment expenditures dims the medium term future prospects for growth.

**Production Approach - Contributions to GDP**



**Net exports dragged down the growth.**

Net exports could not sustain the improvement they had achieved in the last quarter of the previous year. They lowered the growth by 1.5 points in the first quarter of this year as imports recorded the sharpest increase in constant prices since the last quarter of 2013. Exports, on the other hand, expanded by 2.4% yoy in the same period against a background of problematic export markets and sluggish global demand. Alas, this was not enough to pull the contribution of net exports into positive territory.

**The construction sector grew fast in the first quarter.**

According to the production approach, services sector, which has the highest share in GDP with 62% in the first quarter of 2016, contributed 2.7 points to the growth albeit losing some momentum. However, negative developments in tourism sector would weigh on services sector and, in turn, its contribution to GDP might lessen in the forthcoming period. Industrial sector also pushed growth up by 1.6 points in the first quarter of the year. Despite its low share in GDP, construction sector marked the fastest annual increase of more than 2 years and added 0.4 point to GDP, while agriculture sector made the lowest contribution among the sub-groups placed under the production approach.

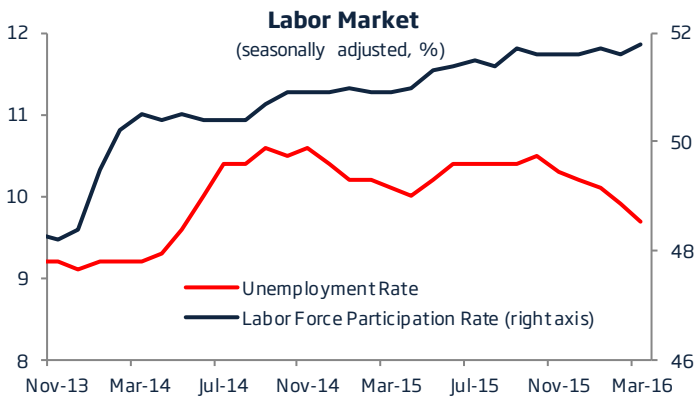
**Expectations...**

Having displayed a domestic demand driven growth performance in 2015 with also the aid of migrant influx, Turkish economy preserved the same tendency in the first quarter of 2016. Consumption expenditures are expected to be the fundamental dynamic of the growth in the second quarter of the year as well. Nevertheless, it is not within reach the opportunity to paint a favorable picture for net exports due to the ongoing problems in our major export destinations, the current trajectory of commodity prices and rising import demand. Against this backdrop, we think that the moderate trend in economic activity will prevail and the Turkish economy will grow by 3.5% in 2016.

Source: Datastream, Turkstat

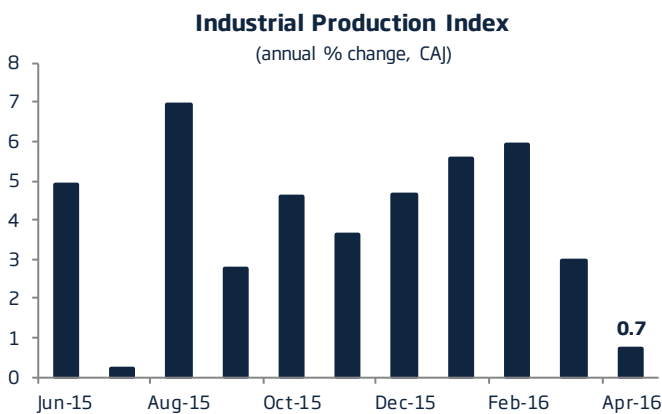
**Unemployment rate continued to decline.**

Unemployment rate dropped by 0.5 point compared to a year ago and became 10.1% in March. The fall in unemployment rate being accompanied by a rise of almost 1 point in labor force participation rate was regarded as a positive development. Seasonally adjusted unemployment rate also shrank for the fifth month in a row.



**Industrial production lost steam in April.**

Industrial production made a weak start to the 2<sup>nd</sup> quarter of the year. Rising by 0.7% yoy in April, calendar adjusted industrial production posted its poorest performance since July 2015. The slowdown in manufacturing industry during this period was noteworthy. Having made a considerable contribution to the industrial production last year, manufacture of motor vehicles slid 8.7% yoy.



**Automotive production recorded a rapid increase.**

Having posted a mild increase of 3% yoy in the first four months of the year, total automotive production surged by 42% yoy in May, according to the data released by Automotive Manufacturers Association (AMA). This development indicated that the unfavorable impact of the contraction in motor vehicles on industrial production might disappear in May. Despite the signs of an ongoing slowdown

**Automotive Production**

(12-month cumulative, annual % change)



in production activities suggested by the May PMI figures, there might be an upturn in industrial production with the support of automotive sector in this period.

**Recovery in CUR...**

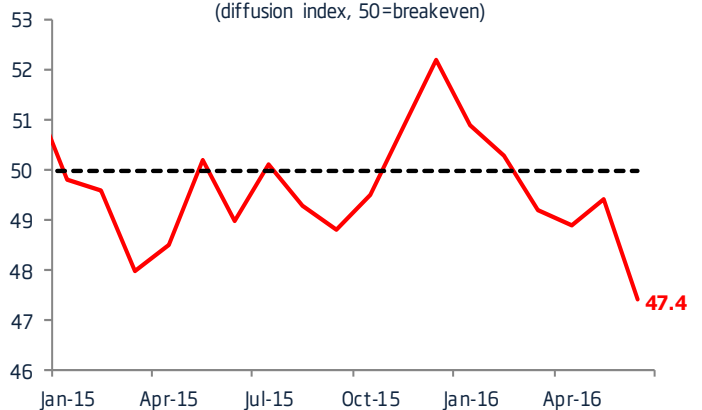
Capacity Utilization Ratio (CUR) in manufacturing industry rose by 1 point in June compared to a year ago and reached 76.1%, the highest level recorded since October 2013. After two consecutive months of deceleration, CUR in manufacture of motor vehicles picked up in this period. The decline in CUR in manufacture of coke and refined petroleum products also lost momentum.

**Manufacturing PMI dropped to 47.4.**

Manufacturing PMI remained under 50 threshold for the fourth consecutive month signaling that economic activity in the sector weakened further. The index fell to 47.4 in June, the lowest level since April 2009. Output and new orders posted sharp declines during this period.

**Manufacturing PMI**

(diffusion index, 50=breakeven)



**Confidence indices...**

Real sector confidence weakened in June as seasonally adjusted figures suggested. This performance stemmed mostly from the sharp deterioration in the assessments of both the output orders in the last 3 months and the general business situation. Consumer confidence, on the other hand, showed a marginal improvement in this period.

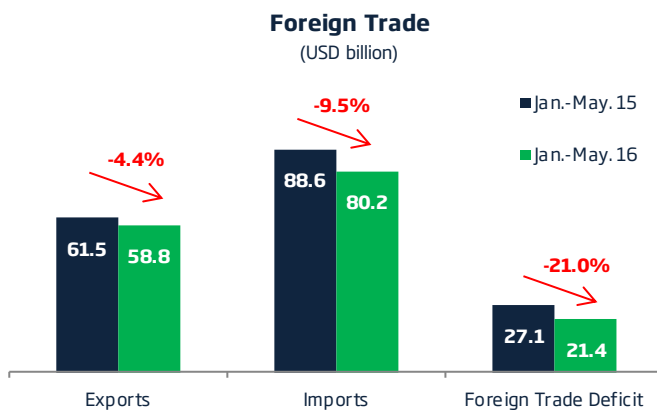
Source: Datastream, Turkstat, AMA, CBRT, Markit

(USD billion)	May		Change (%)
	2015	2016	
Exports	11.1	12.1	9.6
Imports	17.9	17.2	-3.8
<b>Foreign Trade Balance</b>	<b>-6.8</b>	<b>-5.1</b>	<b>-25.5</b>
Import Coverage Ratio (%)	62.0	70.6	-

### The foreign trade deficit continued to narrow.

Exports posted an annual rise of 9.6% in May, the fastest since March 2014. Imports, on the other hand, fell by 3.8% yoy, at the slowest pace in 18 months. Thus, foreign trade deficit continued to narrow and was realized as 5.1 billion USD in line with the market expectations.

Regarding the first five months of the year, exports and imports declined by 4.4% yoy and 9.5% yoy respectively. As a result, foreign trade deficit contracted by 21% yoy to 21.4 billion USD.



### Export growth was led by automotive, machinery and textile sectors.

It was noteworthy that motor vehicle exports, which have the biggest share in total exports, went up by 41% yoy in May while machinery and textile sectors provided a considerable support to the export performance. Gold exports, amounting to 1.1 billion USD, also had a significant favorable impact on trade figures. On the other hand, having a share of over 7% and %2 in our total exports respectively, the falls in both iron/steel and fruit exports put pressure on total exports.

### UK replaced Germany as the top export market of Turkey in May.

The rise in exports to the EU countries accelerated in May mainly thanks to the strong growth in motor vehicle and gold exports. Thus, share of the EU countries in our total exports increased to 48.5% in May from 42.5% in the same month of the previous year. UK, which has voted to leave the EU recently, became the top export market of Turkey replacing Germany thanks to the 600 billion USD gold exports to this country recorded in May. On the other hand,

trade relations with Russia have continued to weaken. However, latest steps taken by Turkey and Russia aiming at resolving the conflicts have provided better prospects for the coming period.

### Machinery imports surpassed energy imports also in May.

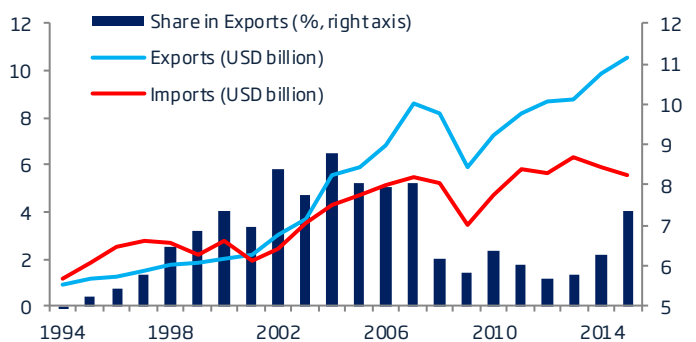
Imports of mineral oils and fuels declined rapidly by 37.1% yoy. Having climbed above the energy item in the previous month, imports of boilers and machineries have ranked first also in May.

After recording an annual contraction in April, consumption goods imports increased on an annual basis in May, sending positive signals on domestic demand. However, the falls in intermediate and capital goods imports continued albeit at a slower pace.

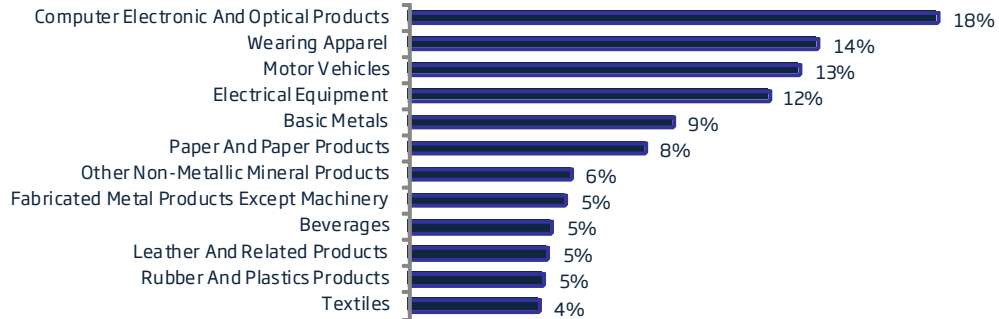
### Brexit's possible implications for the foreign trade performance of Turkey...

Brexit decision raised questions over the future of trade relations between Turkey and the UK. It is worth noting that the share of exports to the UK in total exports has been on an upward trend since 2013 in line with the upturn in the UK economy and the problems in our other export partners. Indeed, the UK had a share of 7.9% (11.2 USD billion) in our total exports in May and was the second most important export market after Germany as 12-month cumulative data suggested. The country held a quite low weight of 2.7% (5.5 USD billion) within total imports.

### Trade Relations with UK



As a net exporter in the trade relations of the two, Turkey experiences a high concentration in both its exports to and imports from the UK. Motor vehicles, wearing apparels and non-monetary gold exports constituted more than half of the total exports to the UK. Together with this, the sectors of computers, electronic and optical products and wearing apparel as well as automotive exhibit a high dependence on the UK market. The most imported items, on the other hand, were power-generating machinery, motor vehicles and metal ores.

**Exports to UK by Sectors As A Share of Sector's Total Exports to World  
(2015)**

Considering the supposedly two-year long transition period, no major risk is anticipated for the relations between Turkey and the UK in the short-run. Nonetheless, there can be a downward pressure especially on our exports if Brexit weakens the UK and/or the EU economies in the medium and longer term. Potential political developments in our major trade partner EU that might be fueled by Brexit can also weigh on the Turkish economy in an indirect way.

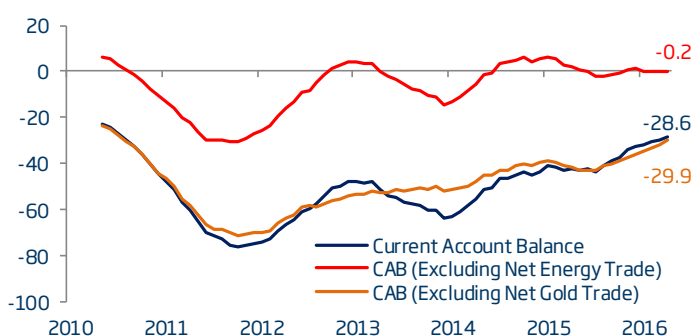
In the near future, on the other hand, the improvement in Turkey-Russia relations might provide a boost to our trade performance. Against this backdrop, we expect exports to display a favorable outlook and imports to retain its downward trend despite losing some steam as the aid of the moderate course in oil and other commodity prices persist while domestic demand strengthens.

### Current account deficit came in below expectations.

In April, current account deficit decreased by 900 million USD yoy to 2,956 million USD. In the first four months of the year, having contracted by 25.1% yoy, the deficit came in at 10.8 billion USD. Despite the recent loss of momentum, narrowing foreign trade deficit continued to have positive impact on current account balance.

According to the 12-month cumulative figures, current account deficit declined to 28.6 billion USD. In this period current account balance excluding net energy trade and excluding gold trade posted a deficit of 0.2 billion USD and 29.9 billion USD, respectively.

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



### Fall in foreign trade deficit slowed down.

According to the balance of payments figures, exports, which recorded only marginal annual growth in both February and March, declined by 10.0% in April. Import volume also decreased by 11.6% yoy in the same period. Thus, 71.4% of fall registered in current account deficit stemmed from the recovery in foreign trade balance. On the other hand, gold trade, which made a big contribution to the current account balance by 1.2 billion USD in April 2015, affected the balance negatively in the same month of this year. Furthermore, annual drop in net tourism revenues remained above 30%.

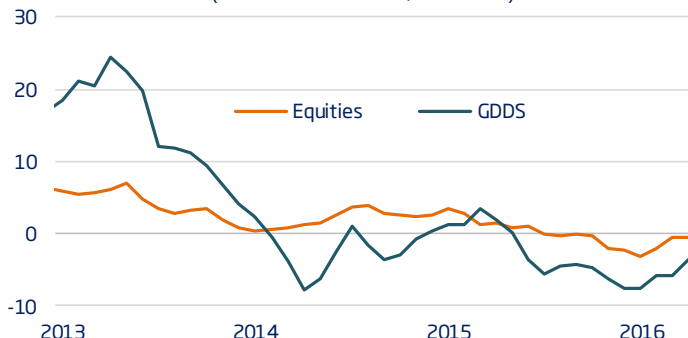
Regarding the first four months of the year, the contraction

in foreign trade deficit supported the current account balance while gold trade and tourism revenues limited this improvement.

### Portfolio investments accelerated.

Portfolio flows gained strength in April thanks to the positive mood in global markets. In this period, capital inflows towards Turkey surged. After registering a total of 3.7 billion USD inflows in February and March, portfolio inflows recorded an inflow of 3.6 billion USD in April. The non-resident investors' appetite for the equity markets continued, albeit diminishing, and their appetite for the debt securities remained strong. According to the 12-month cumulative figures, on the other hand, capital outflows were recorded under both items.

**Non-resident Investors' Portfolio Investment**  
(12-month cumulative, billion USD)



### Ongoing weakness in foreign direct investments...

Foreign direct investments kept their sluggish performance starting from the beginning of 2016. During January-April period, net foreign direct investments halved compared to the same period of the previous year.

### Non-bank sectors became a net borrower.

Other investments posted an inflow of 0.8 billion USD in April. Banking sector realized a net disbursement of 372 million USD in this month, most of this amount stemmed from repayment of long-term credits. Non-bank sectors, on

### Breakdown of Net Capital Inflows

(12-month cumulative, USD million)

			Breakdown of Net Capital Inflows (%)	
	Dec. 2015	Apr. 2016	Dec. 2015	Apr. 2016
<b>Current Account Balance</b>	<b>-32,199</b>	<b>-28,580</b>	-	-
<b>Total Net Foreign Capital Inflows</b>	<b>20,368</b>	<b>20,999</b>	<b>100.0</b>	<b>100.0</b>
-Direct Investments	11,731	9,715	57.6	46.3
-Portfolio Investments	-15,498	-8,647	-	-
-Other Investments	14,755	17,678	72.4	84.2
-Net Errors and Omissions	9,401	2,258	46.2	10.8
-Other	-21	-5	-0.1	0.0
<b>Reserves<sup>(1)</sup></b>	<b>11,831</b>	<b>7,581</b>	-	-

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

the other hand, were net borrowers both in short-term and long-term. According to 12-month cumulative figures, banking sectors' long-term debt rollover ratio came in at 229%, despite displaying a declining trend. The ratio for non-bank sectors kept its moderate upward trend and became 174%.

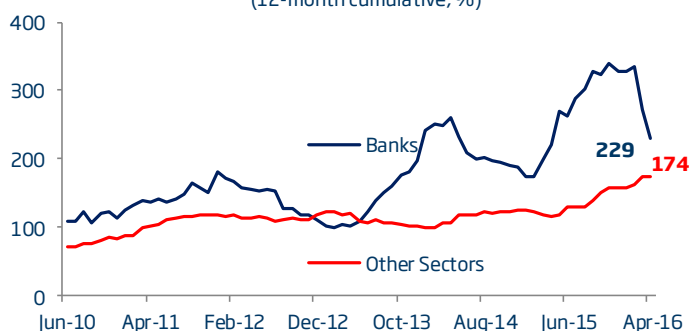
The upsurge in reserves has prevailed in April. Net errors and omissions item posted an outflow of 1.4 billion USD in the same period. The rise in reserves exceeded 2.5 billion USD in the first four months of the year while net errors and omissions item recorded an inflow of 0.9 billion USD in the same period.

#### Expectations...

Foreign trade developments have been the main driving force behind the favorable performance of the current account balance. On the other hand, as the summer season approaches, the contraction in tourism revenues is anticipated to exert additional pressure on the current account balance.

#### Long-term Debt Rollover Ratios

(12-month cumulative, %)



#### Balance of Payments

(USD million)

	April 2016	Jan. - Apr. 2015	Jan. - Apr. 2016	% Change	12-Month Cumulative
<b>Current Account Balance</b>	<b>-2,956</b>	<b>-14,397</b>	<b>-10,778</b>	<b>-25.1</b>	<b>-28,580</b>
Foreign Trade Balance	-2,929	-15,032	-11,168	-25.7	-44,261
Services Balance	847	4,225	2,633	-37.7	22,527
Travel (net)	748	3,976	2,665	-33.0	19,937
Primary Income	-1,185	-4,005	-3,078	-23.1	-8,588
Secondary Income	311	415	835	101.2	1,742
<b>Capital Account</b>	<b>0</b>	<b>-1</b>	<b>15</b>	<b>-</b>	<b>-5</b>
<b>Financial Account</b>	<b>-4,317</b>	<b>-6,334</b>	<b>-9,842</b>	<b>55.4</b>	<b>-26,327</b>
Direct Investments (net)	-299	-3,724	-1,708	-54.1	-9,715
Portfolio Investments (net)	-3,628	657	-6,194	-	8,647
Net Acquisition of Financial Assets	-278	1,113	463	-58.4	5,479
Net Incurrence of Liabilities	3,350	456	6,657	1,359.9	-3,168
Equity Securities	495	-142	1,677	-	-576
Debt Securities	2,855	598	4,980	732.8	-2,592
Other Investments (net)	-807	-1,541	-4,464	189.7	-17,678
Currency and Deposits	426	-1,482	-2,033	37.2	1,526
Net Acquisition of Financial Assets	259	6,884	3,211	-53.4	11,291
Net Incurrence of Liabilities	-167	8,366	5,244	-37.3	9,765
Central Bank	-37	-162	-103	-36.4	-857
Banks	-130	8,528	5,347	-37.3	10,622
Foreign Banks	-211	7,930	4,782	-39.7	6,794
Foreign Exchange	-156	6,813	947	-86.1	-1,158
Turkish Lira	-55	1,117	3,835	243.3	7,952
Non-residents	81	598	565	-5.5	3,828
Loans	-199	-1,940	-1,840	-5.2	-13,525
Net Acquisition of Financial Assets	120	264	675	155.7	1,203
Net Incurrence of Liabilities	319	2,204	2,515	14.1	14,728
Banking Sector	-372	1,767	-1,521	-	1,653
Non-bank Sectors	853	893	4,794	436.8	14,593
Trade Credit and Advances	-1,029	1,962	-682	-	-5,589
Other Assets and Liabilities	-5	-81	91	-	-90
Reserve Assets (net)	417	-1,726	2,524	-	-7,581
<b>Net Errors and Omissions</b>	<b>-1,361</b>	<b>8,064</b>	<b>921</b>	<b>-88.6</b>	<b>2,258</b>

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

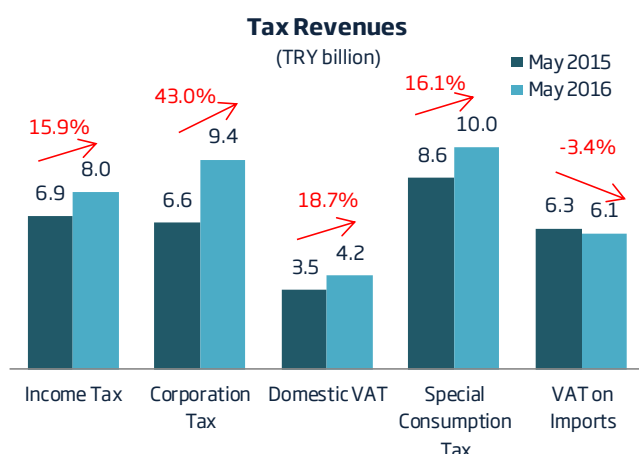
### Budget ran a surplus of 3.7 billion TRY.

Central government budget sustained its strong performance also in May. The budget surplus came in at 3.7 billion TRY rising by 2 billion TRY compared to a year ago. Primary budget figures suggested a solid outlook as well. Primary surplus increased by 58.6% yoy to 8.7 billion TRY.

Having given a deficit of 2.4 billion TRY in January-May 2015, the budget posted a surplus of 9.1 billion TRY during the same period of this year. The benign fiscal outcome so far this year reflected the 16.7% annual surge registered in revenues.

### Fast increase in tax revenues...

Budget revenues went up by 18.6% yoy in May. This was largely due to the 17% yoy rise in tax revenues which have a considerable share in total revenues. In particular, rapid growth in provisional corporation tax revenues was noteworthy in May. Domestic taxes on goods and services also supported this revenue expansion. Following the tax revenues, revenues obtained from "interest, shares and fines" boosted the budget by printing strong rises. However, portfolio revenue of Treasury put downward pressure on budget revenues in May as opposed to its prominent contribution in April.

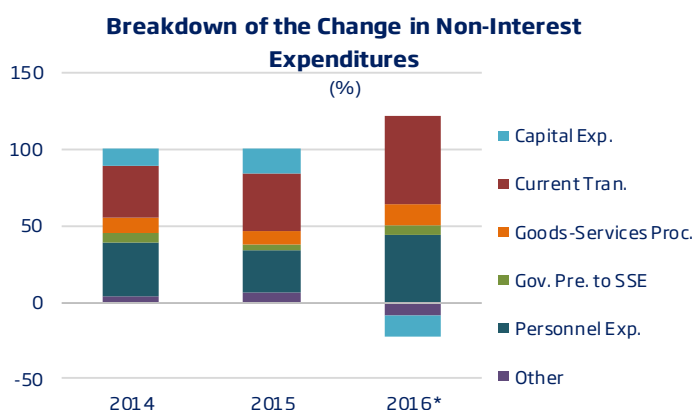


In the first 5 months, while the bulk of the rise in total revenues was mostly attributable to the increase in tax revenues, property income and capital revenues also had a favorable impact on total revenues. It was worthy of attention that non-

tax revenues reached 58.3% of the year-end targets by the end of May. The same ratio for tax revenues became 40%.

### Rise in personnel expenses and current transfers...

Budget expenditures rose by 14.3% in May compared to the same month of the previous year. Expansion in personnel expenses and current transfers accounted for 71% of the increase. However, interest expenditures, which exhibited a positive outlook in the first 4 months of the year, surged by 30.9% yoy in May and, in turn, limited the favorable budget performance.



Regarding the first 5 months of the year, especially surge in personnel expenses and current transfers pushed the budget expenditures up. Increase in personnel expenditures stemmed from the payments to the civil servants. Social security deficit finance, classified under the current transfers item, also picked up by 5 billion TRY yoy in this period and restrained the positive performance of the budget. Capital expenditures, on the other hand, reversed the trend this year contrary to the previous years.

### Expectations...

Despite the increases recorded in foremost expenditure items after the elections, strong budget revenues have been the main driver of the solid budget performance. Budget realizations for January-May period indicated that Turkey has come a long way in achieving the end-year targets. Nevertheless, questions remain over the sustainability of the high level of non-tax revenues that was attained in the first 5 months of the year.

### Central Government Budget

	May			January-May			2016 Budget	
	2015	2016	% Change	2015	2016	% Change	Target	Real./Target (%)
<b>Expenditures</b>	<b>40.1</b>	<b>45.9</b>	<b>14.3</b>	<b>200.3</b>	<b>221.9</b>	<b>10.8</b>	<b>570.5</b>	<b>38.9</b>
Interest Expenditures	3.8	5.0	30.9	28.0	24.2	-13.7	56.0	43.2
Non-Interest Expenditures	36.3	40.8	12.5	172.3	197.7	14.7	514.5	38.4
<b>Revenues</b>	<b>41.8</b>	<b>49.5</b>	<b>18.6</b>	<b>197.9</b>	<b>230.9</b>	<b>16.7</b>	<b>540.8</b>	<b>42.7</b>
Tax Revenues	36.2	42.4	17.0	164.4	183.4	11.5	459.2	39.9
Other Revenues	5.5	7.1	29.2	33.5	47.6	42.1	81.7	58.3
<b>Budget Balance</b>	<b>1.6</b>	<b>3.7</b>	<b>123.4</b>	<b>-2.4</b>	<b>9.1</b>	<b>-</b>	<b>-29.7</b>	<b>-</b>
<b>Primary Balance</b>	<b>5.5</b>	<b>8.7</b>	<b>58.6</b>	<b>25.6</b>	<b>33.3</b>	<b>29.9</b>	<b>26.3</b>	<b>126.4</b>

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

Source: Datastream, Ministry of Finance (\*) January-May period



June	CPI		D-PPI	
Change (%)	2015	2016	2015	2016
Monthly	-0.51	0.47	0.25	0.41
Year-to-Date	4.76	3.63	5.49	3.19
Annual	7.20	7.64	6.73	3.41
Annual Average	8.28	7.74	6.74	4.91

### Monthly CPI came in above the expectations.

CPI increased by 0.47% mom in June, well above the market expectations of 0.1%. Domestic PPI (D-PPI) also rose by 0.41% mom in this period.

### Annual inflation was realized as 7.64%.

Downward trend in CPI halted in June due to the higher than expected increase in prices. During this period, annual consumer inflation reached its highest reading since February 2016 with 7.64%. On the other hand, surge in energy and commodity prices continued to push D-PPI higher. Annual D-PPI inflation was 3.41% in June, increasing by 16 basis points compared to May.

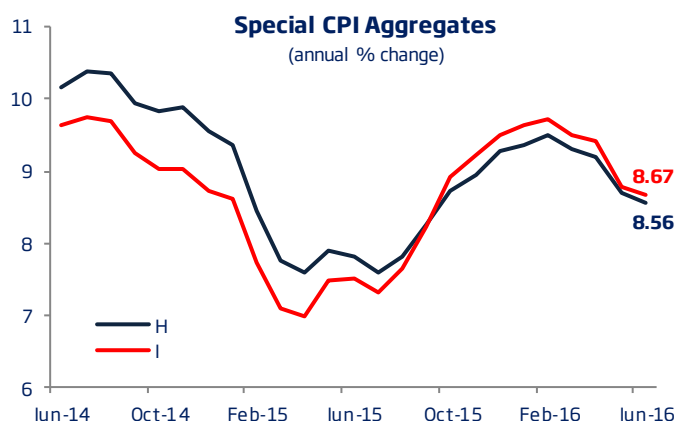
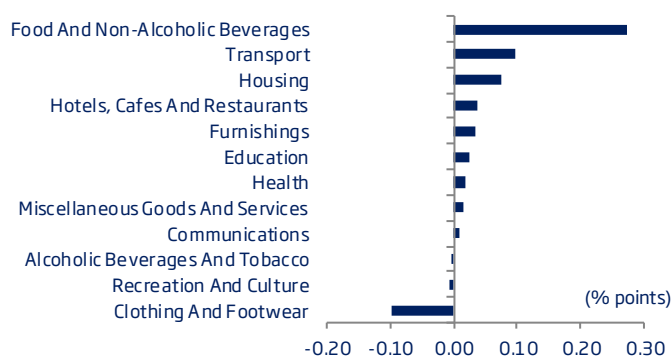
### Sharp pickup in food prices...

After having lowered the CPI in recent months, food prices have an upward impact on inflation in June mostly due to the Ramadan effect. Especially unprocessed food prices have lifted CPI by 22 basis points. Overall food prices, which have increased by 1.16% mom, made the highest contribution to CPI by 27 basis points. This group was followed by transportation and housing groups. On the other hand, clothing and footwear prices lowered CPI by 10 basis points thanks to the seasonal factors.

### Core inflation indicators continued to improve.

Core inflation indicators retained their gradual recovery trend in June. H and I core indices, which are closely monitored by the CBRT, increased by 8.56% yoy and 8.67% yoy, respectively. These rates correspond to the lowest levels since September 2015. The ongoing mild rebound in TRY depicts a favorable picture particularly for core inflation indicators.

### Contributions to the Monthly CPI by Subgroups



H: CPI excluding unprocessed food products, energy, alcoholic beverages, tobacco products and gold.  
I: Excluding energy, food and non-alcoholic beverages, alcoholic beverages, tobacco products and gold.

### Energy continued to play a significant part in D-PPI.

The recent rise in D-PPI was mostly attributable to the upturn observed in oil and commodity prices. Energy posted the way highest increase among the main industrial groupings. While annual D-PPI inflation still records moderate increases, monthly D-PPI rise mostly stemmed from the prices of coke and refined petroleum products by a contribution of 14 basis points. This item has been followed by crude oil and natural gas prices by a contribution of 10 basis points. It was noteworthy that the surge in food prices has been influential in producer prices as well as in consumer prices. Food prices drove the monthly D-PPI inflation up by 7 basis points.

### Expectations...

We expect that the fall in clothing and footwear prices will gather pace in July due to the seasonal factors. The disinflationary impact of food prices, which has been the main factor behind the recent downward trend in inflation, is likely to fade. The tobacco group along with the hikes in cigarette prices as well as transportation and communications groups is anticipated to put upward pressure on consumer price inflation in July. In addition to these, the TRY performance and energy prices seem to continue to be significant for the inflation outlook in the forthcoming period.

Source: Datastream, Turkstat

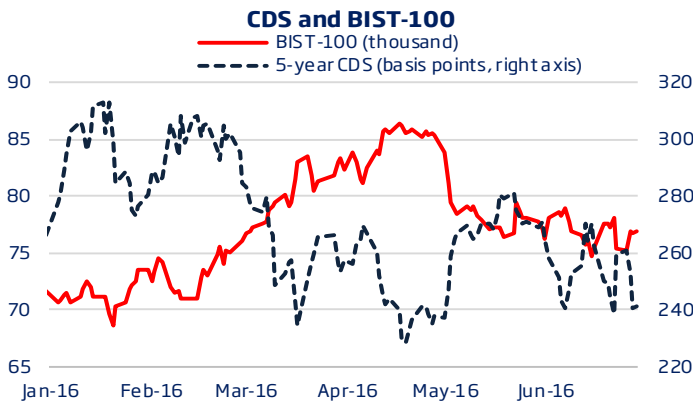
**Brexit heightened volatility in the markets.**

Expectations for the Fed’s rate hike and Brexit were at the top of the agenda in global markets during June. The disappointing US non-farm payrolls, which were released at the beginning of June, together with the uncertainty arising from the possibility of Brexit led expectations of Fed rate hike to delay. Until the referendum held on 23rd June, possibility of Brexit weighed on the markets. As UK voted to leave the EU in referendum, global risk appetite deteriorated in a significant manner and especially exchange rates suffered sharp moves. As the concerns eased in the following days, recovery helped offset market losses to a large extent.



**Volatile domestic markets...**

Investors’ demand towards TRY assets increased in line with the recovery in global risk appetite at the beginning of June. In the following days, on the other hand, markets became volatile in the face of Brexit concerns. The outcome of the referendum held on 23rd June accelerated the falls in domestic markets. In the last week of the month, domestic markets offset losses with the help of the upturn in global markets. In this period, latest steps taken by government aiming at restoring relations with Russia and Israel also supported domestic markets.

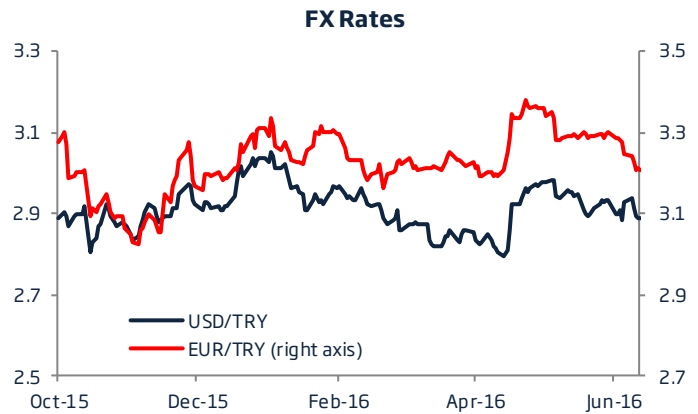


**BIST-100 index fell to the lowest level of the last 4 months.**

BIST-100 index, which had closed May at 78,000, reached 79,420 on the 7th June and starting from that day it followed a downward trend. Experiencing a sharp decrease after the Brexit referendum, index came in at the lowest level of the last 4 months. In the following days, however, BIST-100 index recovered its losses slightly closing June at the level of 76,817.

**USD/TRY exchange rate was below 2.90.**

USD/TRY, which was 2.95 at the end of May, dropped to 2.8775 due to the lower-than-expected US non-farm payrolls in May. Aftermath of the Brexit referendum, USD/TRY tested 3-level, but in the following period it moved downwards. USD/TRY was realized as 2.8757 as of 30th June.



**CBRT lowered the upper band by 50 bps in June.**

CBRT cut the upper band of the interest rate corridor (overnight lending rate) by 50 basis points to 9% in line with the expectations at its meeting held on June 21. The 1-week repo rate (policy rate) and the overnight borrowing rate remained unchanged at 7.5% and 7.25%, respectively. With this rate cut decision, CBRT has lowered the upper band by a total of 175 basis points since March.

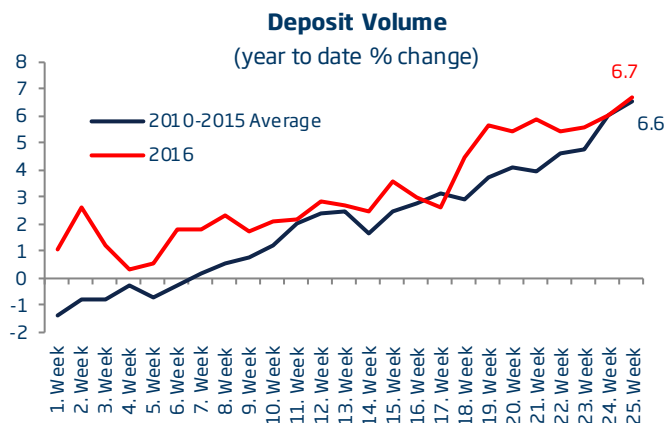
In its policy statement published after the meeting, CBRT pointed out that volatility in global markets surged in the recent period. Moreover, the Central Bank stated that tight monetary policy stance, cautious macro-prudential policy framework and effective use of policy tools as offered in the roadmap published in August 2015 increased the resilience of the overall economy against shocks. The Committee suggested that the inflation has had a clear downward trend in the recent period mainly due to the recovery in unprocessed food prices and core inflation indicators. CBRT reaffirmed that tight stance in liquidity policy would be preserved due to the developments in service inflation and unit labor costs.

Source: CBRT, Reuters, Datastream

**Deposit volume growth rate has been close to its 5-year average.**

Deposit volume expanded at the slowest annual pace of 10.7% in one and a half years as of June 10. However, deposit growth has recovered, reaching 12.2% yoy as of June 24. Recently, the composition of deposit volume altered in favor of TRY deposits. Indeed, TRY deposits expanded by 14% yoy while FX deposits in terms of TRY increased by 9% yoy. The share of TRY deposits in total deposit volume rose to 56.3% as of June 24, the highest level for more than 1 year.

In 2016 deposit growth followed a similar trajectory to those of historical averages according to year-to-date figures. Deposit volume surged by 6.7% ytd in the 25th week of 2016. The average growth rate of deposit volume for the same week of the 2010-2015 period was 6.6% ytd.

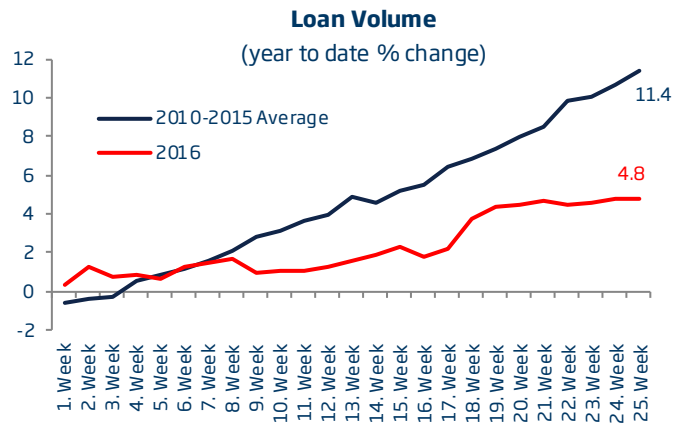


**Despite the decline in interest rates for TRY loans, loan growth remained weak.**

As CBRT lowered the upper band of the interest rate corridor by 175 basis points since March, the weighted average interest rates on consumer loans dropped by nearly 70 basis points and on commercial loans by nearly 100 basis points. Despite this development, the rise in TRY loan volume continued to lose momentum. The annual growth rate of TRY loan volume was recorded as 9.5% on 24th of

June.

In 2016, loan volume growth has remained well below the historical average when compared to the year-end figures. Loan volume registered a year-to-date rise of 4.8% in the 25th week of 2016. However, the average growth rate in loan volume for the same week of the 2010-2015 period was higher at 11.4%.



**NPL ratio was at 3.4%.**

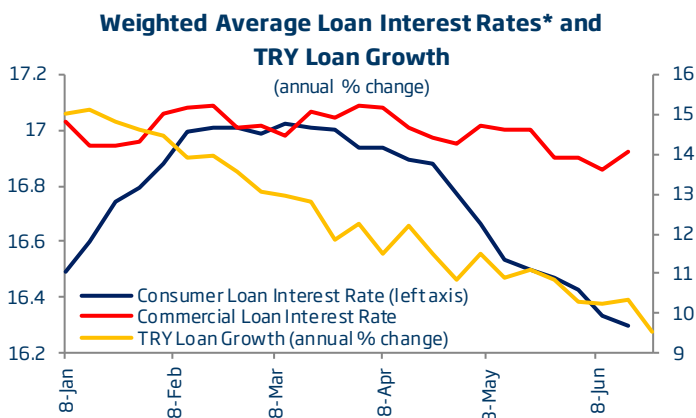
Exhibiting an upward trend throughout 2016, nonperforming loan ratio in banking sector was realized as 3.39% as of June 24. The NPL ratio for consumer loans and commercial loans became 4.6% and 3%, respectively.

**Demand for government debt securities increased.**

Banks' portfolio of securities held under custody, which had contracted annually in 2015, rose by 4.8% yoy as of June 24. Purchases of residents' have lost some momentum in June while that of nonresidents' gained pace in this period.

**Net FX position...**

As of June 24, banks' on-balance sheet FX position was (-)23,121 million USD while off-balance sheet FX position became (+)23,042 million USD. Hence, banks' net FX position stood at (-)79 million USD.



(\*) 3 weak moving average

Source: BRSA Weekly Bulletin

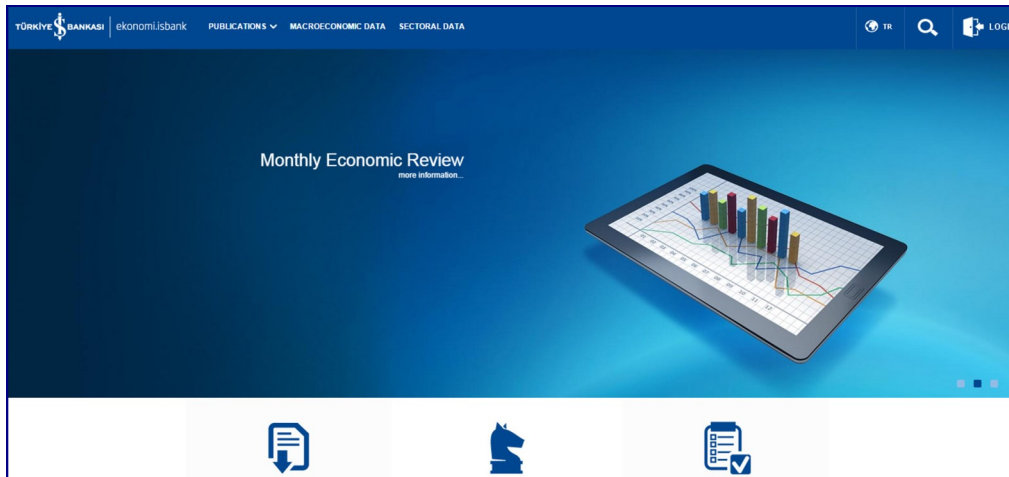
Markets witnessed severe bouts of volatility in June due to the “leave” result of the Brexit referendum. However, the negative impact of Brexit turned out to be temporary and the financial markets swiftly pared its losses in the following days. Considering that this transition process for the UK to leave the union will take some time, we do not expect the Brexit to pose considerable threat to world economy in the short-run. In the medium and long-term, however, reconstructing trade relations could cause significant uncertainty. Brexit has the potential to weigh on the global economy should the UK and/or EU economies weaken out of this decision. Another noteworthy outcome of Brexit is fading expectations of a Fed rate hike. Furthermore, rising prospects of monetary stimulus from leading central banks also supported the markets.

The developments in our major export market EU are of great significance for our economy. It is anticipated that Brexit would have only a marginal impact on Turkish economy in the short-run while, in the long run, Turkey could face several risks. On the other hand, the recent steps taken by Turkey and Russia to resolve conflicts lead to an improvement in the expectations regarding particularly tourism sector.

Forecasts (%)	2015(R)	2016
Growth	4.0	3.5
CA Deficit/GDP	4.5	5.0
Inflation	8.8	7.5

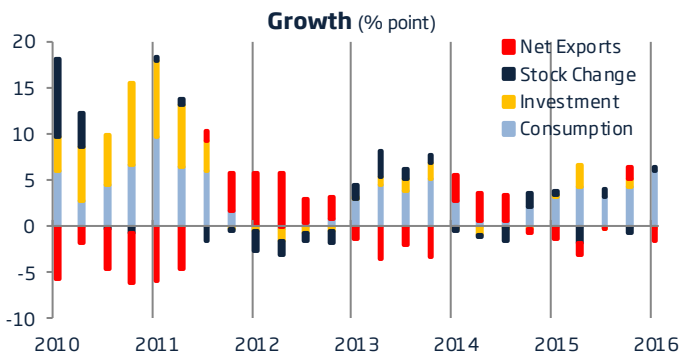
(R) Realization  
Year-end forecast for inflation

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

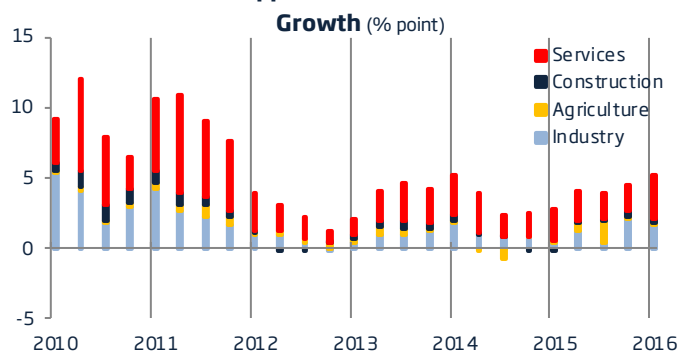


## Growth

### Expenditure Approach - Contributions to GDP

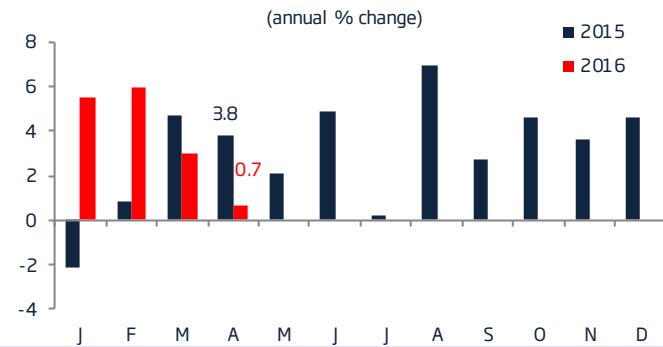


### Production Approach - Contributions to GDP

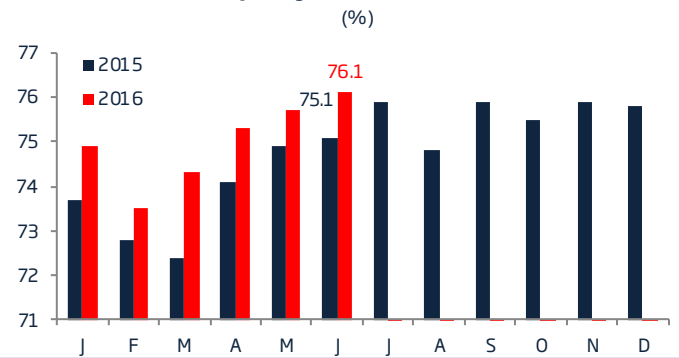


## Industrial Production and Capacity Utilization Ratio

### Industrial Production\*

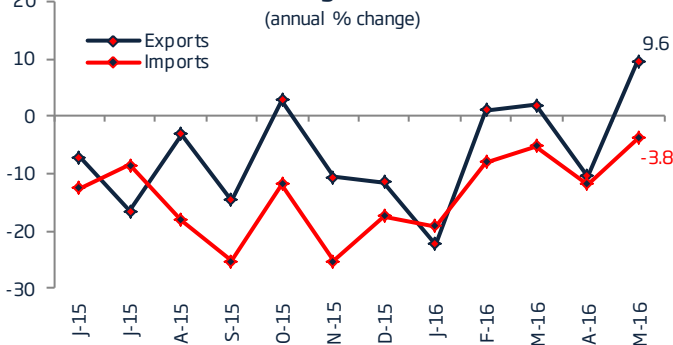


### Capacity Utilization Ratio

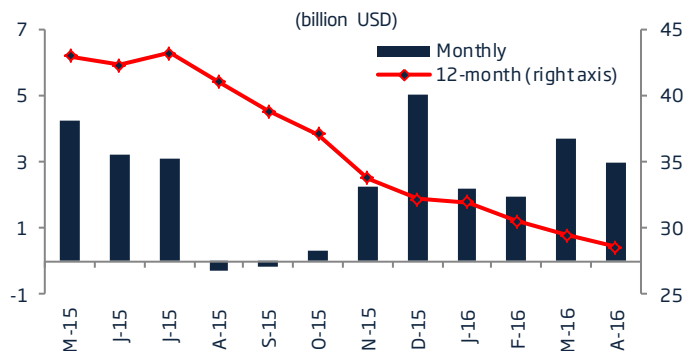


## Foreign Trade and Current Account Balance

### Foreign Trade

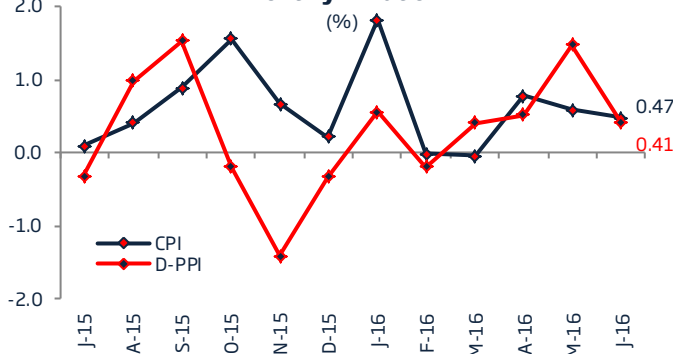


### Current Account Deficit

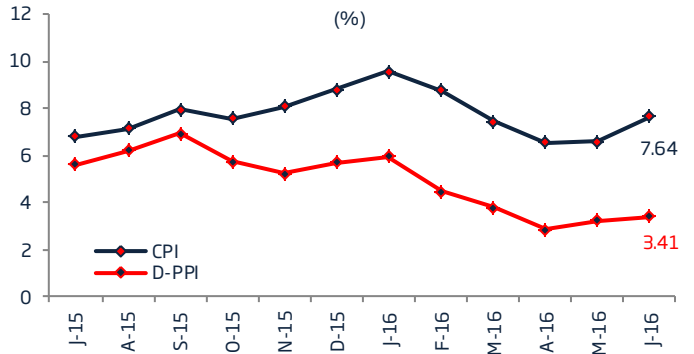


## Inflation

### Monthly Inflation



### Annual Inflation

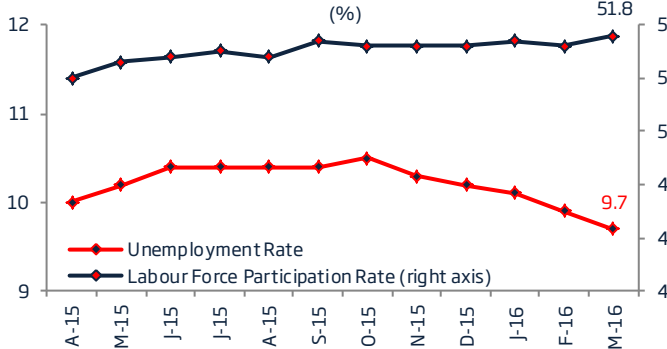


(\*) Calendar adjusted figures

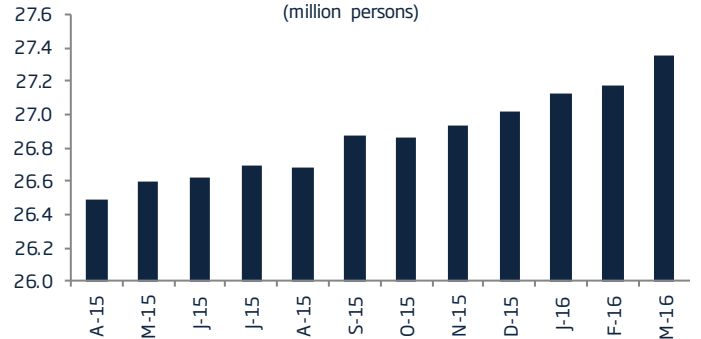
Source: CBRT, Datastream, Turkstat

## Labor Market

### Seasonally Adjusted Labour Force Indicators (%)



### Seasonally Adjusted Employment (million persons)

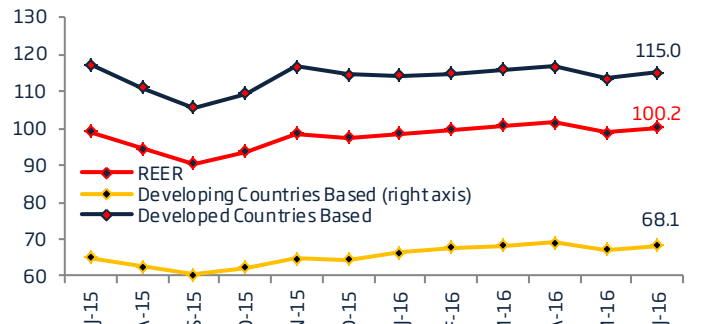


## FX Market

### Currency Basket

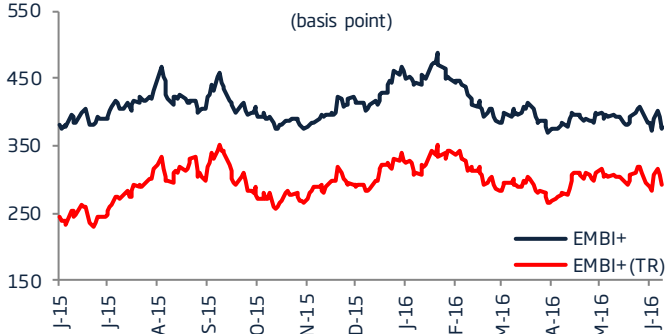


### CPI Based Real Effective Exchange Rate

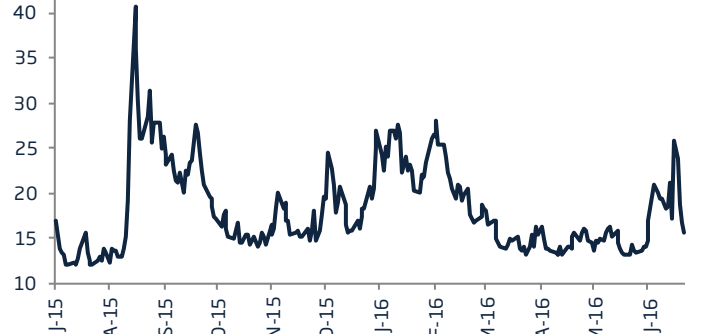


## Risk Indicators

### Risk Premiums (basis point)

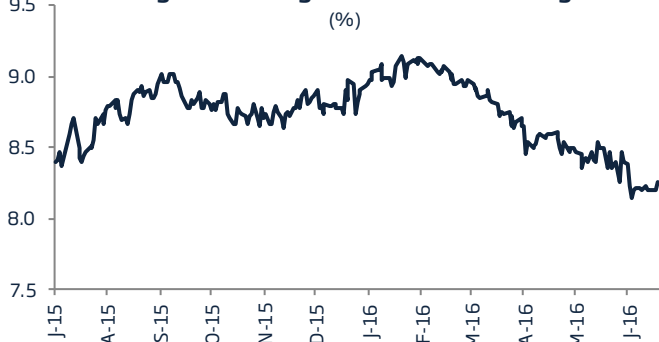


### VIX

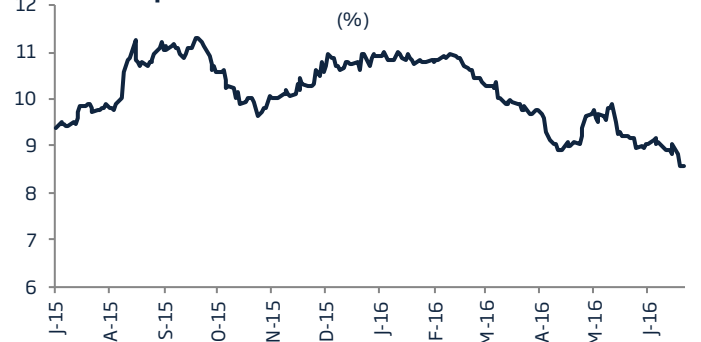


## Interest Rates

### Weighted Average Cost of CBRT Funding (%)

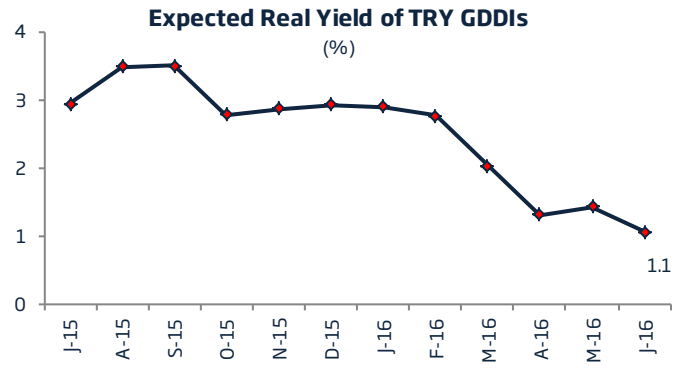
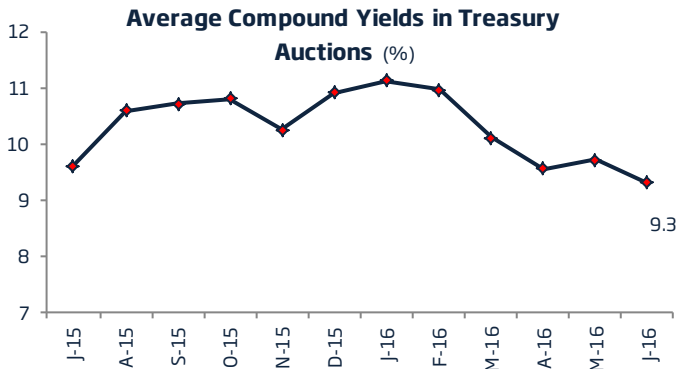


### Compound Yield of 2-Year Benchmark Bond (%)

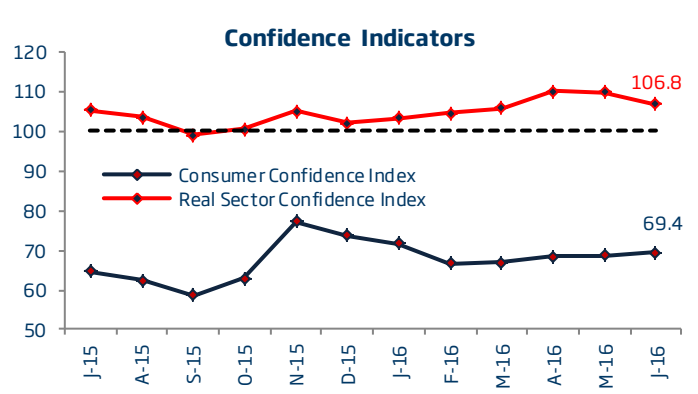
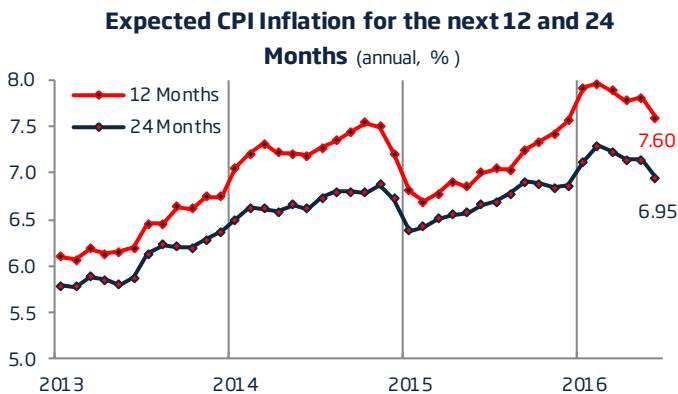
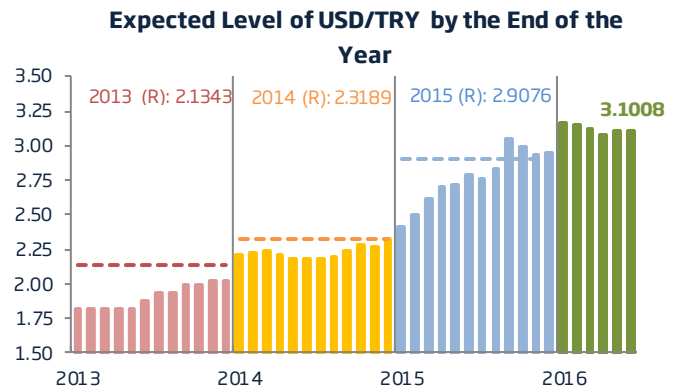
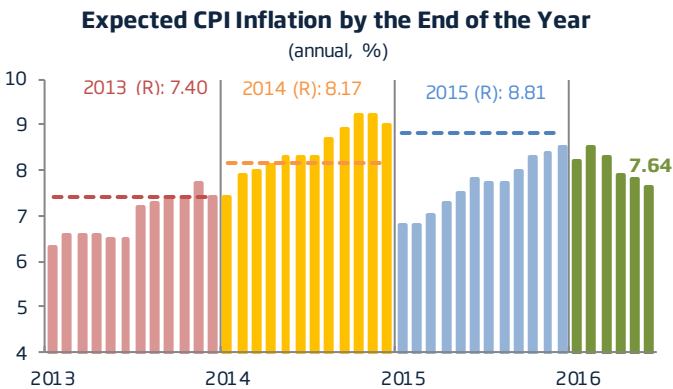
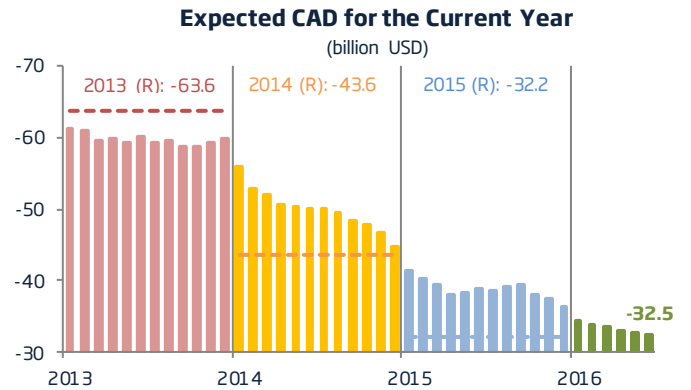
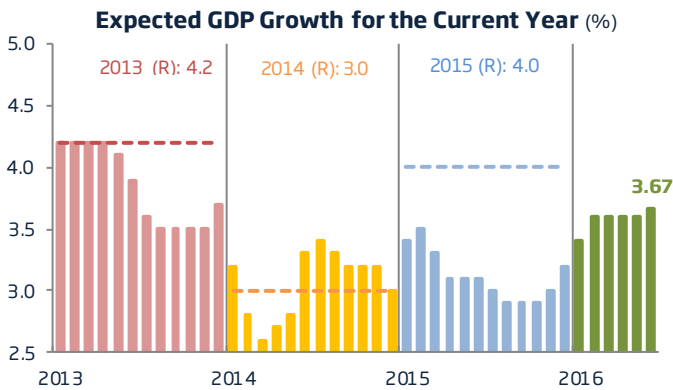


Source: BIST, CBRT, Datastream, JP Morgan, Reuters, Turkstat

## Bond-Bill Market



## CBRT's Survey of Expectations and Other Leading Indicators



(R) Realization

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

# Turkish Economy at a Glance

<b>Growth</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>16-Q1</b>	<b>16-Q2</b>	<b>16-Q3</b>
GDP (USD billion)	774	786	823	799	720	169.5	-	-
GDP (TRY billion)	1,298	1,417	1,567	1,748	1,954	499.3	-	-
GDP Growth Rate (%)	8.8	2.1	4.2	3.0	4.0	4.8	-	-
<b>Inflation (%)</b>						<b>Apr-16</b>	<b>May-16</b>	<b>Jun-16</b>
CPI (annual)	10.45	6.16	7.40	8.17	8.81	6.57	6.58	7.64
Domestic PPI (annual)	13.33	2.45	6.97	6.36	5.71	2.87	3.25	3.41
<b>Seasonally Adjusted Labor Market Figures</b>						<b>Jan-16</b>	<b>Feb-16</b>	<b>Mar-16</b>
Unemployment Rate (%)	8.5	8.8	9.1	10.4	10.2	10.1	9.9	9.7
Labor Force Participation Rate (%)	47.2	48.5	48.4	50.9	51.6	51.7	51.6	51.8
<b>FX Rates</b>						<b>Apr-16</b>	<b>May-16</b>	<b>Jun-16</b>
CPI Based Real Effective Exchange Rate	102.8	110.3	100.3	105.0	97.5	101.5	98.8	100.2
USD/TRY	1.8934	1.7819	2.1323	2.3290	2.9207	2.8039	2.9541	2.8874
EUR/TRY	2.4497	2.3508	2.9370	2.8297	3.1867	3.1937	3.2910	3.2106
Currency Basket (0.5*EUR+0.5*USD)	2.1716	2.0664	2.5347	2.5794	3.0537	2.9988	3.1226	3.0490
<b>Foreign Trade Balance<sup>(1)</sup> (USD billion)</b>						<b>Mar-16</b>	<b>Apr-16</b>	<b>May-16</b>
Exports	134.9	152.5	151.8	157.6	143.8	141.5	140.1	141.1
Imports	240.8	236.5	251.7	242.2	207.2	201.7	199.5	198.9
<b>Foreign Trade Balance</b>	<b>-105.9</b>	<b>-84.1</b>	<b>-99.9</b>	<b>-84.6</b>	<b>-63.4</b>	<b>-60.2</b>	<b>-59.4</b>	<b>-57.7</b>
Import Coverage Ratio (%)	56.0	64.5	60.3	65.1	69.4	70.1	70.2	71.0
<b>Balance of Payments<sup>(1)</sup> (USD billion)</b>						<b>Feb-16</b>	<b>Mar-16</b>	<b>Apr-16</b>
<b>Current Account Balance</b>	<b>-74.4</b>	<b>-48.0</b>	<b>-63.6</b>	<b>-43.6</b>	<b>-32.2</b>	<b>-30.6</b>	<b>-29.5</b>	<b>-28.6</b>
<b>Capital and Financial Accounts</b>	<b>-66.1</b>	<b>-48.9</b>	<b>-62.3</b>	<b>-42.1</b>	<b>-22.8</b>	<b>-23.7</b>	<b>-21.8</b>	<b>-26.3</b>
Direct Investments (net)	-13.8	-9.2	-8.8	-5.5	-11.7	-10.0	-10.0	-9.7
Portfolio Investments (net)	-22.2	-41.0	-24.0	-20.1	15.5	17.0	11.2	8.6
Other Investments (net)	-28.3	-19.6	-39.5	-16.0	-14.8	-16.5	-16.9	-17.7
Reserve Assets (net)	-1.8	20.8	9.9	-0.5	-11.8	-14.1	-6.1	-7.6
<b>Net Errors and Omissions</b>	<b>8.3</b>	<b>-0.9</b>	<b>1.4</b>	<b>1.6</b>	<b>9.4</b>	<b>6.9</b>	<b>7.7</b>	<b>2.3</b>
<b>Current Account Balance/GDP (%)</b>	<b>-9.6</b>	<b>-6.1</b>	<b>-7.7</b>	<b>-5.5</b>	<b>-4.5</b>	-	-	-
<b>Budget<sup>(2)(3)</sup> (TRY billion)</b>						<b>Mar-16</b>	<b>Apr-16</b>	<b>May-16</b>
<b>Expenditures</b>	<b>314.6</b>	<b>361.9</b>	<b>408.2</b>	<b>448.8</b>	<b>506.0</b>	<b>131.7</b>	<b>176.0</b>	<b>221.9</b>
Interest Expenditures	42.2	48.4	50.0	49.9	53.0	16.5	19.1	24.2
Non-interest Expenditures	272.4	313.5	358.2	398.8	453.0	115.2	156.9	197.7
<b>Revenues</b>	<b>296.8</b>	<b>332.5</b>	<b>389.7</b>	<b>425.4</b>	<b>483.4</b>	<b>131.7</b>	<b>181.4</b>	<b>230.9</b>
Tax Revenues	253.8	278.8	326.2	352.5	407.5	108.5	141.0	183.4
<b>Budget Balance</b>	<b>-17.8</b>	<b>-29.4</b>	<b>-18.5</b>	<b>-23.4</b>	<b>-22.6</b>	<b>0.0</b>	<b>5.4</b>	<b>9.1</b>
<b>Primary Balance</b>	<b>24.4</b>	<b>19.0</b>	<b>31.4</b>	<b>26.5</b>	<b>30.4</b>	<b>16.5</b>	<b>24.6</b>	<b>33.3</b>
<b>Budget Balance/GDP (%)</b>	<b>-1.4</b>	<b>-2.1</b>	<b>-1.2</b>	<b>-1.3</b>	<b>-1.2</b>	-	-	-
<b>Central Government Debt Stock (TRY billion)</b>						<b>Mar-16</b>	<b>Apr-16</b>	<b>May-16</b>
Domestic Debt Stock	368.8	386.5	403.0	414.6	440.1	448.2	449.4	452.3
External Debt Stock	149.6	145.7	182.8	197.5	237.5	235.2	233.3	248.2
<b>Total Debt Stock</b>	<b>518.4</b>	<b>532.2</b>	<b>585.8</b>	<b>612.1</b>	<b>677.6</b>	<b>683.5</b>	<b>682.8</b>	<b>700.5</b>

(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	Apr.16	May.16	Change <sup>(1)</sup>
<b>TOTAL ASSETS</b>	<b>1,217.7</b>	<b>1,370.7</b>	<b>1,732.4</b>	<b>1,994.3</b>	<b>2,357.4</b>	<b>2,396.1</b>	<b>2,469.0</b>	<b>4.7</b>
<b>Loans</b>	<b>682.9</b>	<b>794.8</b>	<b>1,047.4</b>	<b>1,240.7</b>	<b>1,485.0</b>	<b>1,515.1</b>	<b>1,555.4</b>	<b>4.7</b>
TRY Loans	484.8	588.4	752.7	881.0	1,013.4	1,041.8	1,054.8	4.1
Share (%)	71.0	74.0	71.9	71.0	68.2	68.8	67.8	-
FX Loans	198.1	206.4	294.7	359.7	471.5	473.3	500.6	6.2
Share (%)	29.0	26.0	28.1	29.0	31.8	31.2	32.2	-
Non-performing Loans	19.0	23.4	29.6	36.4	47.5	52.7	54.1	13.8
Non-performing Loan Rate (%)	2.7	2.9	2.8	2.9	3.1	3.4	3.4	-
<b>Securities</b>	<b>285.0</b>	<b>270.0</b>	<b>286.7</b>	<b>302.3</b>	<b>329.7</b>	<b>326.9</b>	<b>331.9</b>	<b>0.7</b>
<b>TOTAL LIABILITIES</b>	<b>1,217.7</b>	<b>1,370.7</b>	<b>1,732.4</b>	<b>1,994.3</b>	<b>2,357.4</b>	<b>2,396.1</b>	<b>2,469.0</b>	<b>4.7</b>
<b>Deposits</b>	<b>695.5</b>	<b>772.2</b>	<b>945.8</b>	<b>1,052.7</b>	<b>1,245.4</b>	<b>1,277.5</b>	<b>1,309.9</b>	<b>5.2</b>
TRY Deposits	460.0	520.4	594.1	661.3	715.4	731.0	756.0	5.7
Share (%)	66.1	67.4	62.8	62.8	57.4	57.2	57.7	-
FX Deposits	235.5	251.8	351.7	391.4	530.0	546.6	553.9	4.5
Share (%)	33.9	32.6	37.2	37.2	42.6	42.8	42.3	-
<b>Securities Issued</b>	<b>18.4</b>	<b>37.9</b>	<b>60.6</b>	<b>89.3</b>	<b>97.8</b>	<b>96.6</b>	<b>100.9</b>	<b>3.1</b>
<b>Payables to Banks</b>	<b>167.4</b>	<b>173.4</b>	<b>254.2</b>	<b>293.2</b>	<b>361.3</b>	<b>352.4</b>	<b>368.7</b>	<b>2.0</b>
<b>Funds from Repo Transactions</b>	<b>97.0</b>	<b>79.9</b>	<b>119.1</b>	<b>137.4</b>	<b>156.7</b>	<b>152.2</b>	<b>164.1</b>	<b>4.8</b>
<b>SHAREHOLDERS' EQUITY</b>	<b>144.6</b>	<b>181.9</b>	<b>193.7</b>	<b>232.0</b>	<b>262.3</b>	<b>277.5</b>	<b>278.2</b>	<b>6.1</b>
Profit (Loss) of the Period	19.8	23.5	24.7	24.6	26.1	11.0	14.1	-
<b>RATIOS (%)</b>								
Loans/GDP	52.6	56.1	66.8	63.5	76.0	-	-	-
Loans/Assets	56.1	58.0	60.5	62.2	63.0	63.2	63.0	-
Securities/Assets	23.4	19.7	16.6	15.2	14.0	13.6	13.4	-
Deposits/Liabilities	57.1	56.3	54.6	52.8	52.8	53.3	53.1	-
Loans/Deposits	98.2	102.9	110.7	117.9	119.2	118.6	118.7	-
Capital Adequacy (%)	16.6	17.9	15.3	16.3	15.6	15.8	15.5	-

(1) Year-to-date % change



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