TÜRKİYE İŞ BANKASI | research.isbank

Monthly Economic Review

November 2017

Global Economy

- IMF raised its global growth forecasts. While the institution has more positive expectations for developed and emerging economies compared to the previous report, inflation forecasts have been revised down.
- US President Trump announced that his Fed chair nominee is Jerome Powell. It is interpreted that the Fed will maintain its current policy stance.
- At its meeting ended on November 1st, the Fed did not make any changes to its monetary policy, in line with expectations.
- The US economy, which grew above expectations at 3% in the third quarter, maintains a strong outlook despite the destruction caused by hurricanes.
- The political agenda prevailing in Euro Area has continued to be monitored closely. Besides, the bottlenecks in the Brexit talks, the declaration of independence by Catalan Parliament and the coalition talks in Germany have weighed on euro in October.
- Economic activity gained momentum in Euro Area. However, inflation indicators remained weak.
- The ECB announced at its October meeting that the asset purchase program will be reduced to 30 billion EUR starting from January 2018. On the other hand, the Central Bank extended the period of the program until September 2018.
- Chinese economy grew by 6.8% in the third quarter of the year.
- Oil prices have followed an upward trend along with the developments in northern Iraq as well as the expectations that OPEC will extend production cut.

Turkish Economy

- Recovery in employment indicators stumbled in July. Unemployment rate remained unchanged at 10.7% in this period compared to the same period of the previous year. Seasonally adjusted unemployment rate became 11.2% in July, rising by 0.1 point on a monthly basis.
- In August, industrial production grew by 5.2% yoy. Thus, in July-August period, industrial production expanded by 9.8% compared to the same period of the last year.
- In September, export volume increased by 8.7% yoy to 11.8 billion USD. Import volume rose by 30.6% yoy to 20 billion USD. As a result, foreign trade deficit expanded by 85% yoy, the fastest increase in more than six years.
- The current account deficit widened in August compared to the same period of the previous year and came in at 1.2 billion USD. While the expansion in foreign trade deficit pushed the deficit up, the recovery in tourism revenues played an important role in positive performance of the current account balance in this period. 12-month cumulative deficit stood at 37 billion USD.
- In September, budget expenditures recorded a limited increase by 2.6% compared to the same month of the previous year while budget revenues climbed by 32.9% yoy. Hence, the central government budget deficit, which was TRY 16.9 billion in September 2016, dropped to TRY 6.4 billion in the same month of this year. During January-September period, the budget deficit which came in at TRY 12 billion in 2016, reached TRY 31.6 billion in the same period of this year.
- Monthly CPI inflation was 2.08% in October, above market expectations. Annual CPI inflation reached 11.9% in this period.

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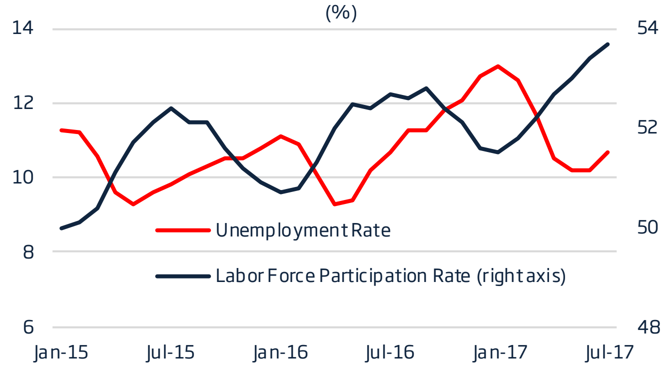
Employment indicators...

Unemployment rate remained unchanged at 10.7% in July compared to the same period of the previous year. Despite a rise of 1.1 million people in employment recorded during this period, the 1.2 million people increase in labor force offset the decline in unemployment rate. Seasonally adjusted data indicated that the recovery in the labor market since the beginning of the year has faded. Indeed, the seasonally adjusted unemployment rate, which declined gradually from 11.7% in January to 11.1% in June, rose by 0.1 point on a monthly basis and became 11.2% in July.

Labor Market
(%)



Strong performance in industrial production...

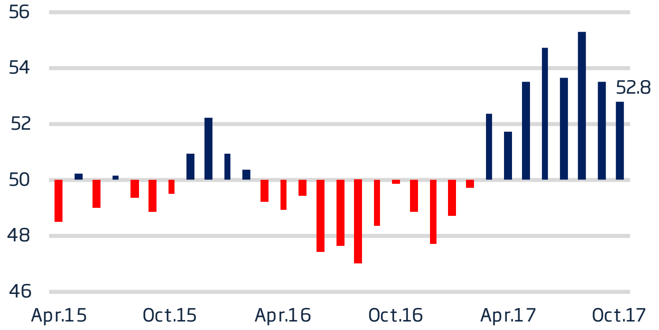
Calendar adjusted industrial production, which expanded by 14.5% yoy with the help of low base effect in July, continued to increase in August albeit losing some momentum. In August, industrial production grew by 5.2% compared to the same period of the previous year. Thus, in July-August period, industrial production expanded by 9.8% compared to the same period of the last year.

The manufacturing industry made the biggest contribution to the increase in industrial production in August with 4.4 points. Looking at the sub-sectors of the manufacturing industry, it is seen that the growth was widespread throughout the sectors. While manufacturing of machinery and equipment was the sector that provided the highest contribution to the manufacturing industry, manufacturing of fabricated metal products was another sector that stood out with its performance.

Manufacturing industry continues to grow.

The manufacturing PMI, which was 53.5 in September, declined to 52.8 in October. The slowdown in the rise of export orders and production was behind the loss of momentum seen in the last two months. On the other hand, as the index remained above threshold level of 50, positive prospects for the economic activity have strengthened.

Manufacturing PMI
(benchmark=50)

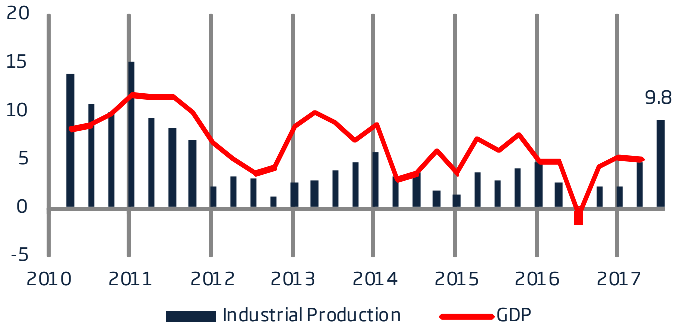


Ongoing improvement in real sector confidence...

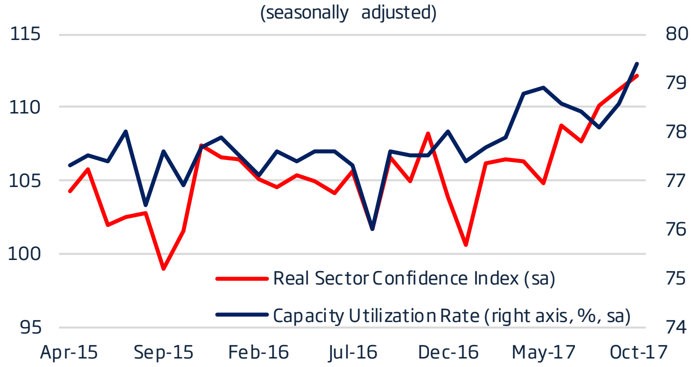
In October, the real sector confidence index reached 112.2 in seasonally adjusted terms, continuing its trajectory at the highest levels of the last six years. Looking at the sub-items of the index, it is seen that the recovery in the expectations for the volume of output for the next 3 months prevailed while assessments on general business situation have deteriorated.

Seasonally adjusted manufacturing industry capacity utilization rate became 79.4%, rising by 0.8 point on a monthly basis . In this period, the highest capacity utilization rates were recorded in the manufacture of computers, electronic and optical products and motor vehicles. As opposed to the positive outlook on the aforementioned indicators, the decline in consumer confidence has moved into its third month as of October.

Caj Industrial Production and GDP
(annual change, %)



Leading Indicators
(seasonally adjusted)



Source: Treasury, Turkstat, Datastream, CBRT

Foreign Trade Balance (USD billion)

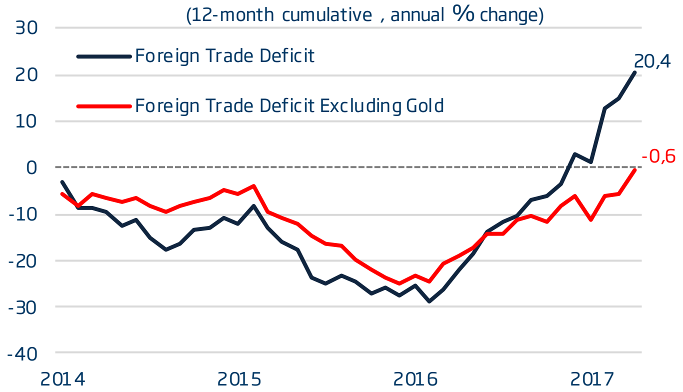
	September 2016	September 2017	Δ (%)	Jan.-Sep. 2016	Jan.-Sep. 2017	Δ (%)
Exports	10.9	11.8	8.7	104.2	115.1	10.5
Imports	15.3	20.0	30.6	146.3	169.0	15.5
Foreign Trade Deficit	**-4.4**	**-8.1**	**85.0**	**-42.1**	**-53.8**	**27.9**
Import Coverage (%)	71.3	59.3	-	71.2	68.1	-

Rapid expansion in foreign trade deficit...

In September, export volume increased by 8.7% yoy to 11.8 billion USD. Import volume rose by 30.6% yoy to 20 billion USD. Thus, foreign trade deficit expanded by 85% yoy, the fastest increase in more than six years.

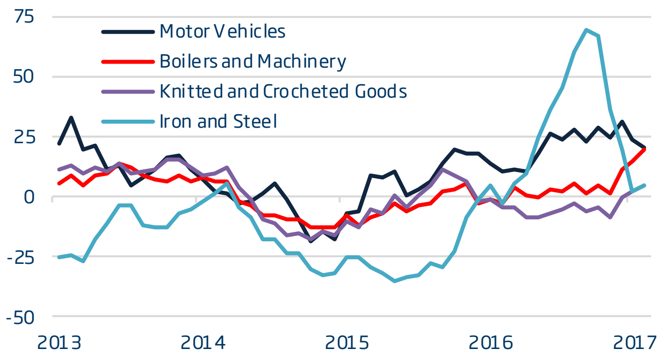
In the first 9 months of the year, exports went up by 10.5% yoy and imports surged by 15.5% yoy. While the annual expansion in foreign trade deficit became 27.9% in this period, import coverage ratio declined to 68.1% from 71.2% a year ago.

Foreign Trade Deficit
(12-month cumulative , annual % change)



As 12-month cumulative data suggested, the role of gold trade in the widening of foreign trade deficit has been noteworthy in the recent period. Indeed, excluding gold trade, the deficit narrowed albeit slightly. In this period, gold trade added 8.7 billion USD to the expansion of the foreign trade deficit.

Main Exporting Items
(3-month moving average, annual % change)



Automotive and machinery exports on a firm footing...

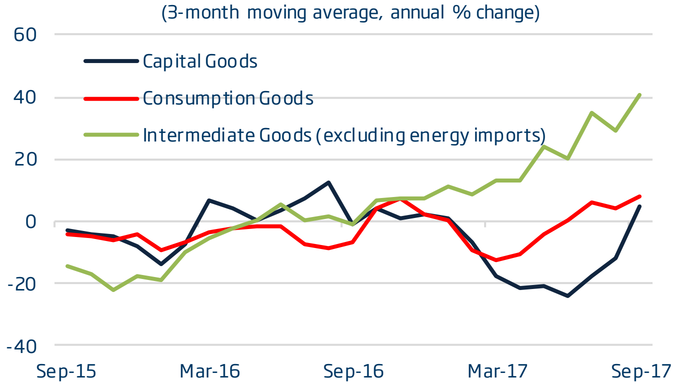
Exports of motor vehicles and boilers and machineries were the main drivers of the growth in exports in September. Considering the top 10 sectors with largest exports volume, only one sector, namely knitted and crocheted goods, posted an annual decline in this period.

Iron and steel exports, which had a strong performance in the first half of the year along with the upturn in commodity prices, lost some steam during the recent months. Increased domestic demand for the iron and steel products might be behind this loss of momentum. Indeed, with the strong demand from the construction sector, imports of iron and steel surged by more than 60% yoy, the most rapid rise since February 2011.

Energy imports continued to soar.

Other than the strong pace of gold imports, energy imports pulled the foreign trade deficit up. Due to the upturn in economic activity and the rise in oil prices, energy imports climbed up by 51% yoy in September, the sharpest increase in six years. The momentum gained in economic activity with the support of exports performance was also mirrored in the imports of intermediate goods. Excluding energy (mineral oils and fuels) imports, intermediate goods imports continued to surge as the 3-month moving average data suggested. Imports of consumer goods, on the other hand, exhibited a moderate performance due partly to the weakness in TRY. However, imports of capital goods remained weak despite the increase recorded in the third quarter.

Imports based on BEC
(3-month moving average, annual % change)



Upside risks to the foreign trade deficit...

As opposed to the recovery in EU economies, the pick up in oil prices and strong domestic economic activity put upward pressure on foreign trade deficit. The trajectory of gold imports also seems to be significant for foreign trade balance in the period ahead. All these indicate that the current account deficit could exceed 40 billion USD at the end of this year.

Source: Datastream, Turkstat

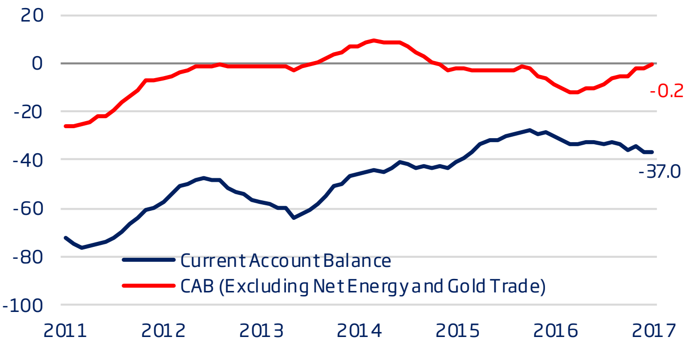
Current account deficit was better than expected in August.

Current account deficit came in below market expectations with 1.2 billion USD in August. The deficit was 1.4 billion USD in the same month of last year. While the expansion in foreign trade deficit pushed the deficit up, the recovery in tourism revenues played an important role in positive performance of the current account balance in August.

In the first eight months of the year, the current account deficit expanded by 19% compared to the same period of the previous year and became 27.2 billion USD. Analyses of 12-month cumulative data reveals that the current account deficit narrowed to 37.0 billion USD in August. When the gold and energy trade are excluded, the improvement in the current account deficit was noteworthy.

Current Account Balance

(12-month cumulative, USD billion)



Gold and energy imports have been the main drivers.

Monthly gold imports, which were at a record-high level with 2.7 billion USD in July, fell to 1.1 billion USD in August, the lowest level since February. Despite this fall, gold imports have increased by 0.7 billion USD compared to the same month of the previous year. This limited the recovery in current account deficit this month. The slight rise in oil prices also has also a negative impact on the current account balance.

Increase in tourism revenues...

The recovery in tourism revenues continued in August. In this period, tourism revenues picked up by 29.2% yoy to 3.4 billion USD, the highest reading in the last two years. Despite the limited increase in tourism spending, net tourism revenues rose to 3 billion USD in August. Net tourism revenues grew by 22.1% yoy in the first 8 months of 2017.

The increase in the contribution of portfolio investments...

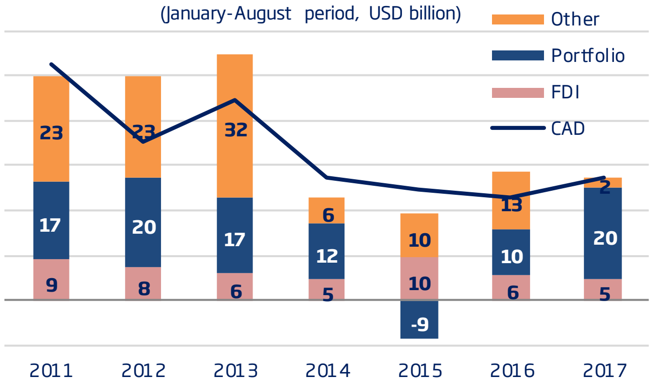
Portfolio investments kept its importance in the financing of the current account. In August, thanks to the positive mood on global markets, portfolio investments posted a net capital inflow of 2.2 billion USD. Bond issuances by general government played a significant role in the performance of portfolio investments.

Foreign direct investments lost momentum in August. In this period, direct investments registered a net capital inflow of 657 million USD. In the first 8 months of the year, net direct investment inflows amounted to 4.9 billion USD.

Other investments also continued to present a weak outlook. In August, there has been a net capital inflow of 133 million USD in other investments. While banks were net credit borrowers in short term with 692 million USD, they

Financing of CAD

(January-August period, USD billion)



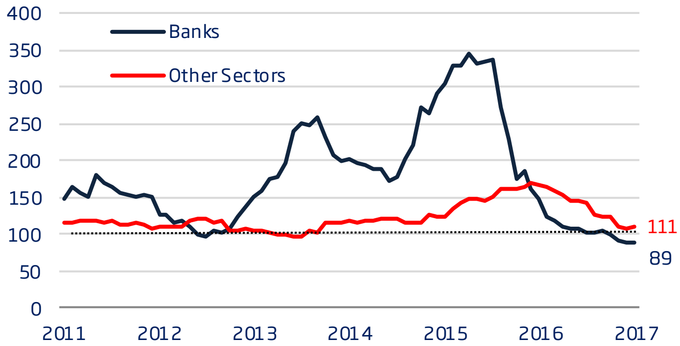
Breakdown of Net Capital Inflows (12-month cumulative, USD million)

	December 2016	August 2017	Breakdown of Net Capital Inflows (%) December 2016	August 2017
Current Account Balance	**-32,634**	**-36,972**	-	-
Total Net Foreign Capital Inflows	**33,447**	**25,925**	**100.0**	**100.0**
-Direct Investments	9,160	8,454	27.4	32.6
-Portfolio Investments	6,300	16,110	18.8	62.1
-Other Investments	6,691	-3,881	20.0	-15.0
-Net Errors and Omissions	11,273	5,225	33.7	20.2
-Other	23	17	0.1	0.1
Reserves(1)	**-813**	**11,047**	-	-

Note: The numbers may not add up to total due to rounding.
(1) (-) sign indicates an increase in reserves while (+)

Source: Datastream, CBRT

made a net loan repayment of 884 million USD in long term. Other sectors were net credit borrowers in both short and long term with 354 million USD and 726 million USD, respectively.



Long-term debt roll-over ratios...

According to 12-month cumulative data, banks' long-term debt roll-over ratio was 89%, the lowest reading in the last 7.5 years. That ratio for other sectors, on the other hand, became 111% in August registering a limited increase .

In August, net errors and omissions recorded a capital inflow of 1.6 billion USD. Showing the fastest rise in one year, CBRT reserves surged by 3.4 billion USD.

Expectations...

According to the provisional foreign trade data, foreign trade deficit widened considerably in September due largely to the rapid increase in the imports of intermediate goods. This situation is likely to have negative repercussions on the current account deficit. The recovery in tourism revenues is expected to continue albeit losing some steam. Against this backdrop, we anticipate that the current account deficit will continue to expand in September.

Balance of Payments (USD million)

	August	January - August		%	12-month
	2017	2016	2017	Change	Cumulative
Current Account Balance	**-1,237**	**-22,887**	**-27,225**	**19.0**	**-36,972**
Foreign Trade Balance	-4,279	-27,685	-34,043	23.0	-47,217
Services Balance	3,511	9,673	12,079	24.9	17,855
Travel (net)	2,997	8,671	10,583	22.1	15,872
Primary Income	-675	-5,912	-6,764	14.4	-9,850
Secondary Income	206	1,037	1,503	44.9	2,240
Capital Account	**5**	**23**	**17**	**-26.1**	**17**
Financial Account	**374**	**-18,394**	**-28,786**	**56.5**	**-31,730**
Direct Investments (net)	-657	-5,623	-4,917	-12.6	-8,454
Portfolio Investments (net)	-2,237	-10,278	-20,088	95.4	-16,110
Net Acquisition of Financial Assets	-273	-357	-1,011	183.2	857
Net Incurrence of Liabilities	1,964	9,921	19,077	92.3	16,967
Equity Securities	520	430	3,211	646.7	3,604
Debt Securities	1,444	9,491	15,866	67.2	13,363
Other Investments (net)	-133	-12,955	-2,383	-81.6	3,881
Currency and Deposits	-349	-4,093	-266	-93.5	5,615
Net Acquisition of Financial Asse	-48	368	1,068	190.2	6,080
Net Incurrence of Liabilities	301	4,461	1,334	-70.1	465
Central Bank	-50	-327	-166	-49.2	-315
Banks	351	4,788	1,500	-68.7	780
Foreign Banks	-376	4,049	143	-96.5	576
Foreign Exchange	164	-298	-349	17.1	131
Turkish Lira	-540	4,347	492	-88.7	445
Non-residents	727	739	1,357	83.6	204
Loans	-639	-6,375	1,031	-	2,140
Net Acquisition of Financial Asse	132	194	-58	-	-23
Net Incurrence of Liabilities	771	6,569	-1,089	-	-2,163
Banking Sector	-192	-1,354	-3,373	149.1	-5,301
Non-bank Sectors	1,080	8,689	2,751	-68.3	3,764
Trade Credit and Advances	868	-2,509	-3,119	24.3	-3,926
Other Assets and Liabilities	-13	22	-29	-	52
Reserve Assets (net)	3,401	10,462	-1,398	-	-11,047
Net Errors and Omissions	**1,606**	**4,470**	**-1,578**	**-**	**5,225**

Source: Datastream, CBRT

Budget gave TRY 6.4 billion deficit.

In September, budget expenditures recorded a limited increase by 2.6% compared to the same month of the previous year while budget revenues climbed by 32.9% yoy. Thus, the central government budget deficit, which was TRY 16.9 billion in September 2016, dropped to TRY 6.4 billion in the same month of this year. Despite the 34.6% increase in interest expenditures, the primary balance ran TRY 2 billion surplus in September thanks to the recovery in budget revenues.

During January-September period, the budget deficit which came in at TRY 12 billion in 2016, reached TRY 31.6 billion in the same period of this year. Budget expenditures expanded by 17.2% annually while budget revenues rose by 12.9% in this period.

Tax revenues gained momentum.

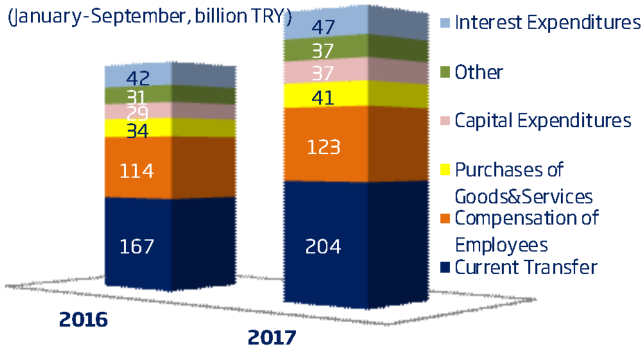
In September, tax revenues increased at an annual pace of 35.5%, the highest reading so far this year. About one-third of this growth came from the surge in SCT revenues. Especially, the 86.2% annual expansion in SCT revenues collected from tobacco products was noteworthy in September. Having surged by 63.7% yoy, VAT on imports contributed 10.4 pp to the growth in tax revenues. In addition, income tax revenues, rising by 30.3%, had a positive impact on budget figures. Domestic VAT, on the other hand, posted slower annual growth rate of 13.8% in September.

In the first nine months of the year, tax revenues went up by 17.1% yoy. While corporate tax revenues and VAT on imports had a strong performance in this period, domestic VAT rose by only 6.5% yoy.

Deceleration in public expenditures...

Budget expenditures recorded a slight increase in September due to the 8.2% annual decrease in current transfers. The lack of the transfers for the social security deficit finance in September dragged down budget expenditures by 7.5 pp. Indeed, TRY 4 billion had been transferred by the Treasury for the social security deficit finance in September 2016. The rapid increase in agricultural subsidy payments together with the considerable shrunk in capital expenditures came to the forefront in September.

Budget Expenditures
(January-September, billion TRY)



In January-September period, the current transfers made the highest contribution to the increase in budget expenditures. Capital expenditures also played an important role in the budget spending growth, particularly the increase in immovable capital produce. Interest expenditures, on the other hand, rose by 11.8% in this period.

Expectations...

In the first three quarters of the year, it was seen that the recovery in economic activity was directly reflected in tax revenues. In fact, inflation adjusted annual increase in tax revenues became 5.3% in this period. Moreover, the rapid pick-up in imports in recent period supported the budget outlook particularly through the revenues collected from VAT on imports. Accordingly, we expect that the revival in budget revenues may continue in the forthcoming period and budget expenditures might continue to expand on the back of the measures taken to support economic activity. In this framework, we anticipate that the budget deficit will be TRY 61.7 billion at the end of this year, as projected in the MTP, and thus the budget deficit to GDP ratio will be around 2% in 2017.

Central Government Budget (TRY billion)

	September		%	January-September		%	2017 Budget	MTP	Real/MTP
	2016	2017	Change	2016	2017	Change	Target	Target	Target (%)
Expenditures	**53.0**	**54.4**	**2.6**	**416.5**	**488.2**	**17.2**	**645.1**	**673.7**	**72.5**
Interest Expenditures	6.2	8.4	34.6	41.7	46.6	11.8	57.5	57.5	81.0
Non-Interest Expenditures	46.7	46.0	-1.6	374.8	441.6	17.8	587.6	616.2	71.7
Revenues	**36.1**	**48.0**	**32.9**	**404.5**	**456.6**	**12.9**	**598.3**	**612.0**	**74.6**
Tax Revenues	30.9	41.8	35.5	329.0	385.3	17.1	511.1	520.5	74.0
Other Revenues	5.2	6.1	17.8	75.5	71.3	-5.6	87.2	91.6	77.8
Budget Balance	**-16.9**	**-6.4**	**-62.0**	**-12.0**	**-31.6**	**162.7**	**-46.9**	**-61.7**	**51.2**
Primary Balance	**-10.7**	**2.0**	**-**	**29.6**	**15.0**	**-49.5**	**10.6**	**-4.2**	**-**

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

Source: Ministry of Finance, Datastream

CPI came in above expectations.

Monthly CPI increase in October was realized as 2.08%, higher than the market anticipations. According to the Reuters' survey CPI was expected to rise by 1.87% in this period. Thus, CPI recorded the highest October inflation since 2011. Increase in Domestic Producer Price Index (D-PPI), on the other hand, was realized as 1.71% in October.

Annual CPI inflation reached 11.9% in October, the highest level in the last nine years. In this period, the annual D-PPI inflation also increased to 17.3%.

October	CPI		D-PPI	
(change %)	2016	2017	2016	2017
Monthly	1.44	2.08	0.84	1.71
Year-to-Date	6.23	9.52	4.66	11.66
Annual	7.16	11.90	2.84	17.28
Annual Average	7.89	10.37	3.83	14.47

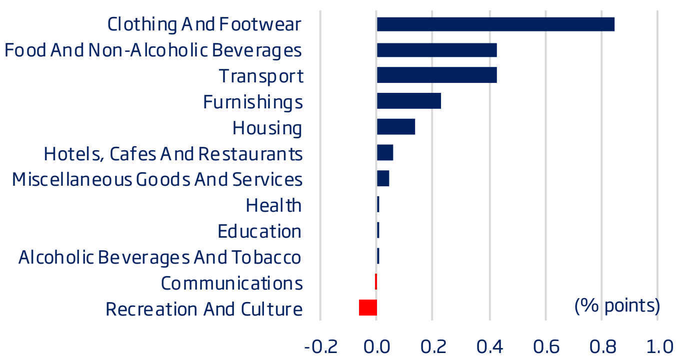
Higher energy prices continue to weigh on CPI.

In October entertainment/culture and communication were the only groups that dragged down CPI. In this period, clothing and footwear group made the highest contribution to CPI increase since seasonal factors play a significant role in this period. Clothing and footwear group, of which the prices increased by 11.5% compared to the previous month, made a contribution of 82 basis points to CPI inflation.

Food prices, which declined on a monthly basis for the last five months, rose nearly 2% in October and made an upward impact of 42 basis points to CPI. Thus, annual inflation in food prices reached 12.7%.

The fact that oil prices have risen above 60 USD/barrel in recent period points to a negative picture in terms of inflation outlook. Indeed, prices in transportation group, which are highly sensitive to energy prices rose by 2.6% on a monthly basis and became the third expenditure group that contributed the most to CPI by 42 basis points. The annual price increase in the said group increased to 16.8%.

Contributions to the Monthly CPI Inflation

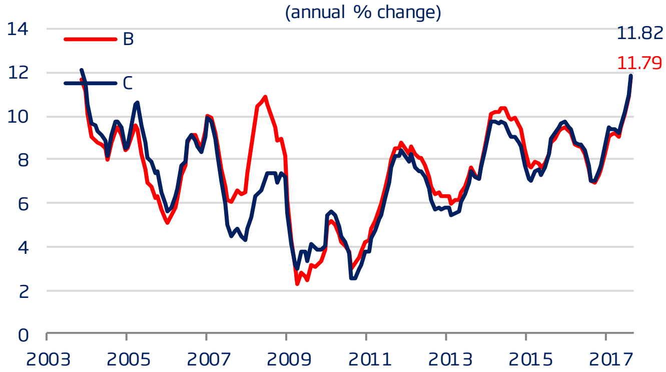


Since the tax cuts in furniture and white goods ended as of September, prices in furnishings group increased by 3% on a monthly basis and pulled up CPI by 22 basis points.

The deterioration in core inflation indicators continued.

The rise in core inflation indicators continued in October. Annual inflation in B index, which is one of the core inflation indicators closely monitored by CBRT, has reached its highest level by 11.79% since the base year of inflation has changed in 2003. Annual inflation in C index also rose to 11.82%, the highest level since January 2004.

Special CPI Aggregates
(annual % change)



B:excluding unporcessed food, energy, alcoholic beverages, tobacco and gold
C:excluding energy, food, non-alcoholic beverages, alcoholic beverages, tobacco and gold

Energy and metal prices pushing D-PPI up.

Increases in base metal and energy prices in October contributed 65 basis points to the overall increase in D-PPI. On the other hand, textile and chemical sectors in this period were the other main drivers of the increase in D-PPI.

The likelihood of CPI completing the year in single-digit level has weakened.

The high level of energy prices compared to the last year indicates that the upward pressure on inflation will continue. It is assessed that the lagged effects of the TRY depreciation in the recent period are negative in terms of the inflation outlook in the medium term. In this framework, we think that despite the strong base effect in December the likelihood of CPI declining to single-digit level at the end of the year has weakened. The upward trend in core inflation indicators also pointed that decline in inflation at the end of the year would be limited. In this context, we believe that CPI could exceed 10.3% at the end of 2017, the upper band of the CBRT's forecast in the latest inflation report.

Source: Datastream, Turkstat

Central banks were at the core of the agenda.

Political developments and central bank decisions were the main items on the global economic agenda recently. Political tensions have elevated following the independence referendum held in the northern Iraq and oil prices have increased due to the concerns over territorial integrity of Iraq, OPEC's second largest producer. On the other hand, the independence referendum held in Catalonia and the subsequent developments have raised concerns about the future of the EU amid an environment of bottlenecks in the Brexit talks.

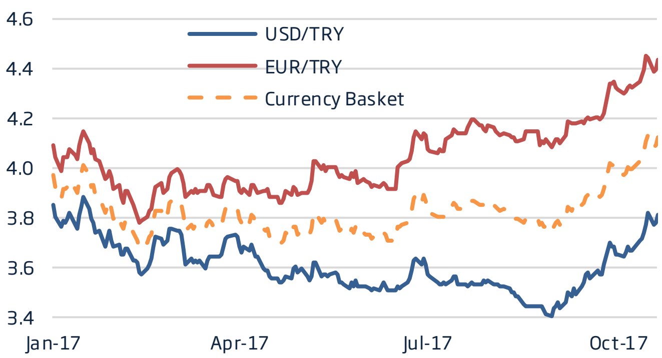
The appointment of the next Fed chair, succeeding Yellen, was closely monitored by the markets as Taylor and Powell that had been considered for the position affected the course of the markets. Euro has depreciated in October since remarks by the ECB after the meeting sounded a dovish tone on monetary policy.

The visa crisis between the United States and Turkey combined with the problems with EU countries in October led to deterioration in risk perception towards the country. This put downward pressure on domestic markets.

Rapid increase in USD/TRY...

USD/TRY, which remained relatively flat in the first week of October, has risen rapidly due to escalated visa tension. In the following period, although TRY pared its losses to some extent, the upward pressure increased again at the end of the month. As of October 31, USD/TRY climbed by 6.4% compared to the end of September to 3.79. EUR/TRY also increased by 4.9% to 4.42 during the same period.

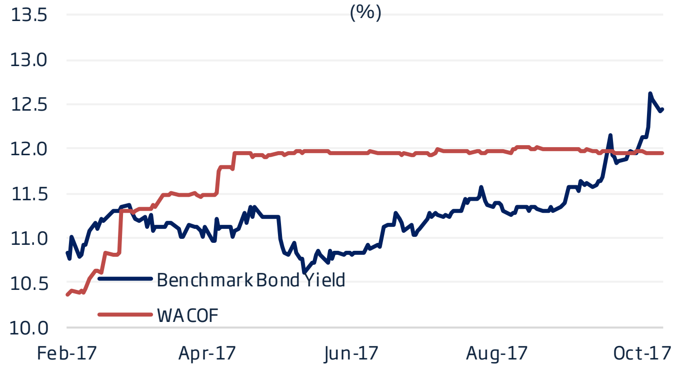
FX Rates



Rise in interest rates...

Interest rates also moved up in October. This became more evident in the face of the rapid depreciation in TRY. The 2-year benchmark bond yield has reached its highest level since June 2009 with 12.8% on October 31.

Benchmark Bond Yield and CBRT WACOF



Volatility in BIST-100 index...

BIST-100 index has fallen below 100,000 points on October 9, for the first time since June. However, in addition to impulse purchases, growing expectations that the issue would be resolved through diplomatic means drove the index up again. As global stock exchange markets hovered around all-time high levels, emerging market equities also affected positively. As of October 31, BIST-100 index increased to 110,143 points, surging by 7% compared to the end of September.

CBRT kept monetary policy unchanged.

CBRT Monetary Policy Committee left interest rates on hold in line with the market expectations at its meeting held on October 26. The statement published after the meeting stressed the high course of inflation. It is said that the tight monetary policy stance decisively would be maintained until a marked improvement in the inflation outlook is observed. The Committee also reiterated that further monetary tightening will be delivered if needed.

At the beginning of November, the CBRT revised the upper limit and the tranches for the FX maintenance facility within the reserve options mechanism. Accordingly, the upper limit for the FX maintenance facility was lowered to 55% from 60% and all tranches was reduced by 5 points. With this revision, approximately 5.3 billion TRY of liquidity will be withdrawn from the market and approximately 1.4 billion USD of liquidity will be provided to banks.

CBRT raised inflation forecasts.

The CBRT revised its inflation forecasts upward according to the fourth inflation report of the year. The CBRT increased inflation forecasts for 2017, 2018 and 2019 by 1.1, 0.6 and 1 percentage points to 9.8%, 7% and 6%, respectively. The key drivers of this updates are the Turkish lira depreciation and the rise in TL-denominated import prices stemmed from the surging oil and other commodity prices.

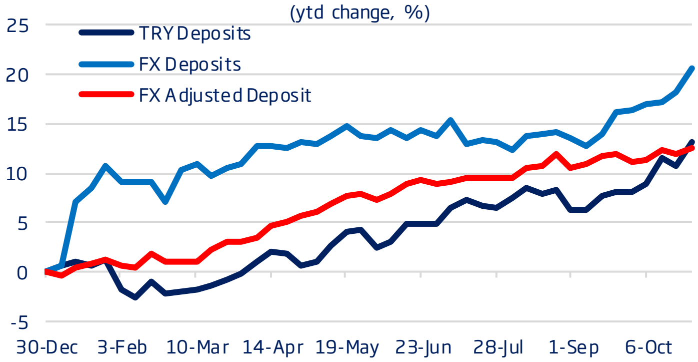
Source: Datastream, Treasury, CBRT

Deposit volume rose by 16.3% ytd.

According to Weekly Bulletin published by BRSA, as of October 27, total deposit volume became TRY 1,793 billion, picking up by 16.3% compared to the end of 2016. The recent upsurge in FX rates led to an acceleration in total deposit growth. Indeed, year-to-date expansion in total deposits was 12.5% according to the exchange rate adjusted figures.

The depreciation in TL led to a shift in demand to FX deposits from TRY deposits since the last week of September. As of October 27, TL deposit volume rose by 13.1% ytd whereas FX deposit volume increased by 20.6% ytd. Growth in FX deposit volume in USD terms was realized as 11.8% in this period.

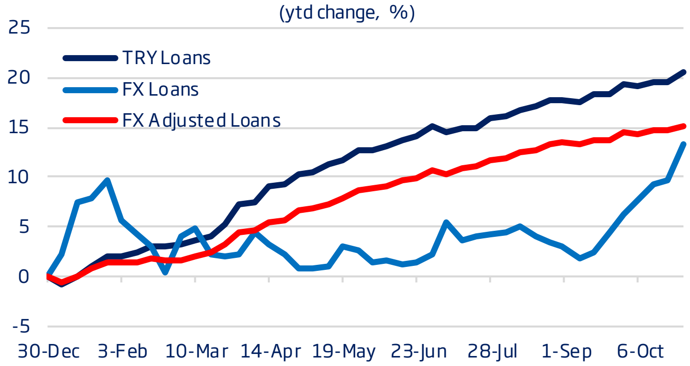
Deposit
(ytd change, %)



TL loan volume continued to increase.

Thanks to the pick-up in loans supported by Credit Guarantee Fund scheme, especially in the first half of the year, TL credit volume posted a rapid increase. Thus, as of October 27, TL loan volume expanded by 20.5% ytd. Having had a weak performance due to the high level of exchange rates, FX loans in USD terms remained broadly flat. As of October 27, total loan volume expanded by 18% ytd.

Loans
(ytd change, %)

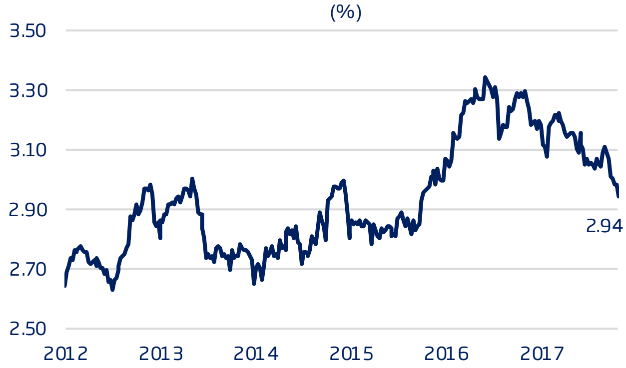


Analysis of annual growth rates showed that deposit volume increased by 24.1% while loan volume expanded by 25.5% as of October 27.

Non-performing loan ratio kept decreasing.

Rapid increase in loan volume in 2017 led to a fall in non-performing loan ratio. Despite the rise in gross non-performing loan by an amount of TRY 4.9 billion ytd as of October 27, non-performing loan ratio decreased to 2.94% from 3.20% in this period. Hence, non-performing loan ratio of the banking sector dropped to the lowest level in more than two years.

NPL Ratio
(%)



Securities portfolio...

As of October 27, securities portfolio of the banking sector grew by 9.6% compared to the year-end. The fall in the securities available for sale became 10.5% in this period. The portfolio of securities held as collateral, which was TRY 60 billion at the end of 2016, reached TRY 154 billion as of October 27.

The portfolio of securities held under custody gained momentum and surged by 17.6% ytd as of October 27. The rise of non-residents' securities portfolio by 24.7% ytd played a big role in this development. Residents' securities portfolio, on the other hand, expanded at a slower pace of 12.6% in the same period.

Net foreign currency position...

As of October 27, banks' on-balance sheet FX position was (-) USD 42,544 million while off-balance sheet FX position was realized as (+) USD 42,610 million. Hence, banking sector's net FX position became (+) USD 66 million.

Source: BRSA Weekly Bulletin

Concluding Remarks

Decisions by the central banks of developed countries and political developments have been high on the agenda of the global economy in recent period. Having launched its balance sheet reduction process in October, the Fed is expected to conduct an additional interest rate hike during the rest of this year. Trump announced Jerome Powell as his nominee for the next chair of the Fed. Powell is expected to adopt a similar stance to Yellen. In Europe, the ECB has decided to cut its bond buying starting from January 2018 while extending quantitative easing until September 2018. The Bank of England increased its policy rate for the first time in 10 years, in line with expectations. In such an environment where developed country central banks have been taking only gradual and cautious steps towards long anticipated normalization of monetary policy, the global risk appetite has remained strong.

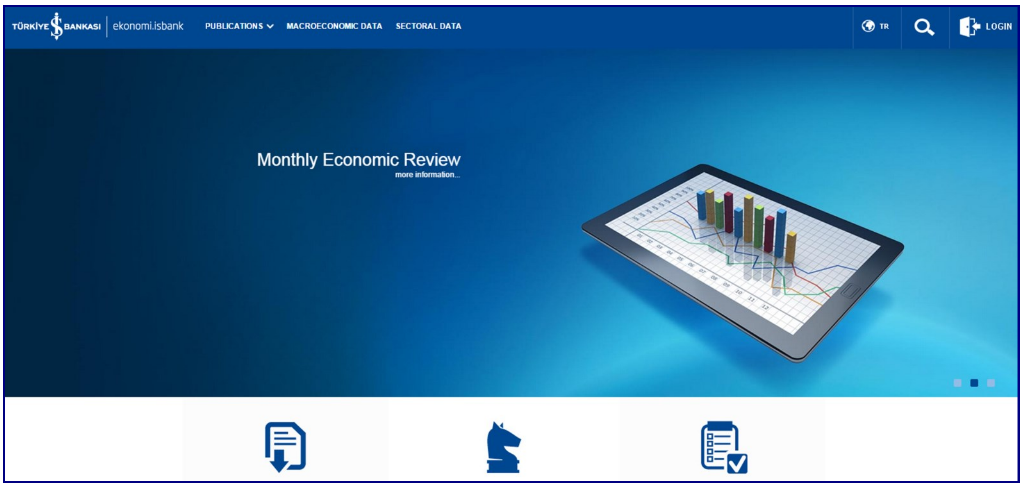
In the political arena, particularly developments in Europe have caused uncertainty. Brexit process has been rendered highly problematic. Political tension has mounted in Spain recently. Beside these, in Germany, tough coalition talks have occasionally triggered a negative mood. Against this backdrop, the relationship between Turkey and the EU appears to be more fragile.

In addition to the geopolitical problems, visa tension with the US has negatively affected the risk perception towards Turkey in October. While TL weakened against dollar and euro, bond rates increased. Nevertheless, the favorable economic outlook prevails thanks to the strong support of public sector and the low base effect. On the other hand, as inflation remains at high levels, further tightening of monetary policy will be on the table.

Forecasts (%)	**2017**	**2018**
Growth	5.0	4.1
CA Deficit/GDP	5.1	5.3
Inflation	10.0	9.0

Year-end forecast for inflation

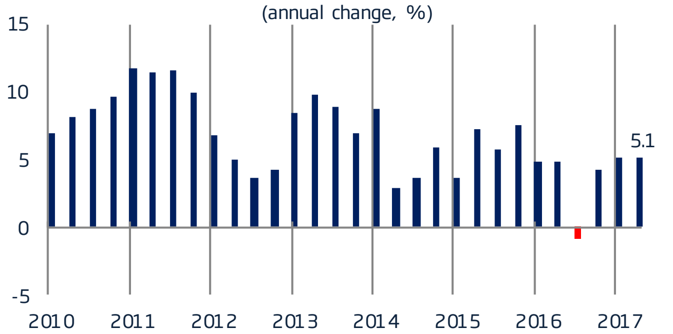
Our reports are available on our website **https://research.isbank.com.tr**



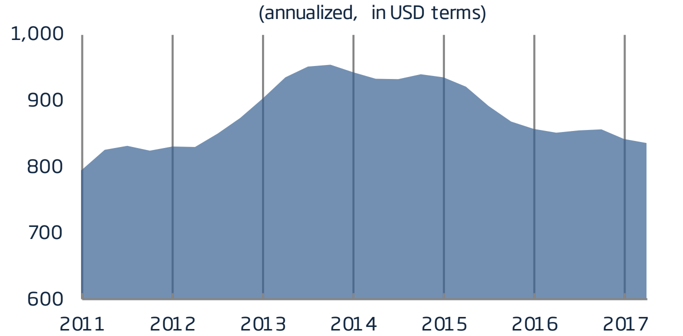
Turkish Economy at a Glance

Growth

GDP Growth
(annual change, %)

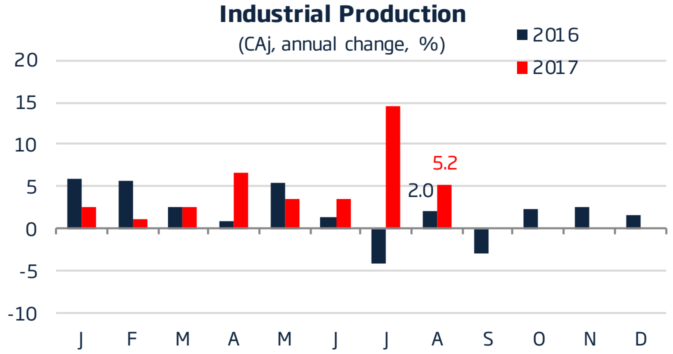


GDP
(annualized, in USD terms)

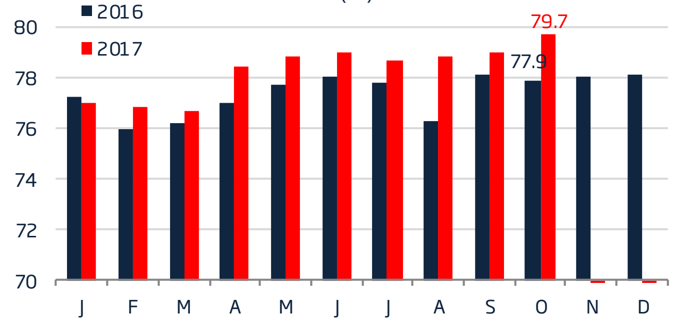


Industrial Production and Capacity Utilization Ratio

Industrial Production
(CAj, annual change, %)

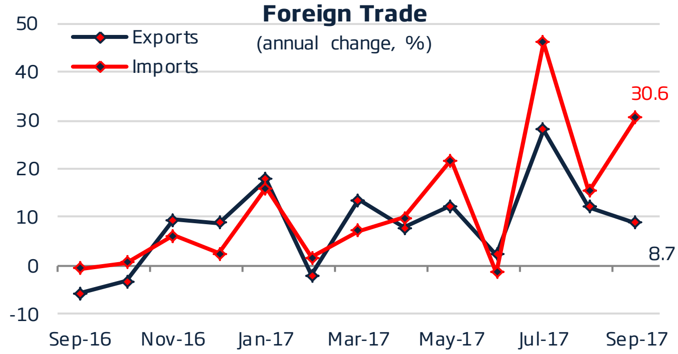


Capacity Utilization Ratio
(%)

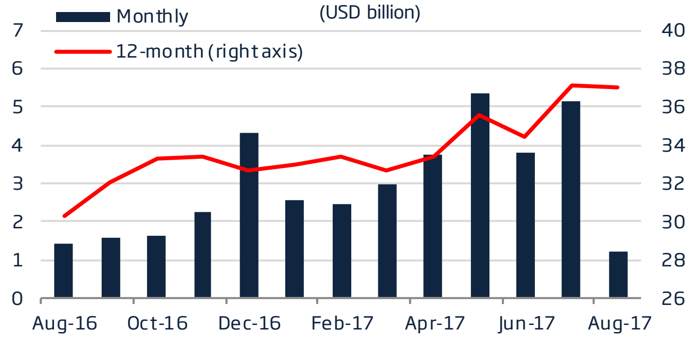


Foreign Trade and Current Account Balance

Foreign Trade
(annual change, %)

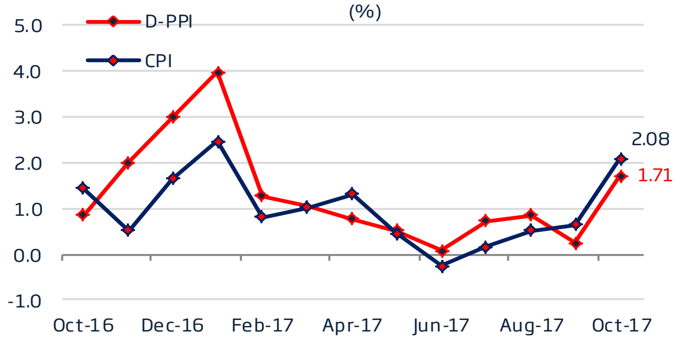


Current Account Deficit
(USD billion)

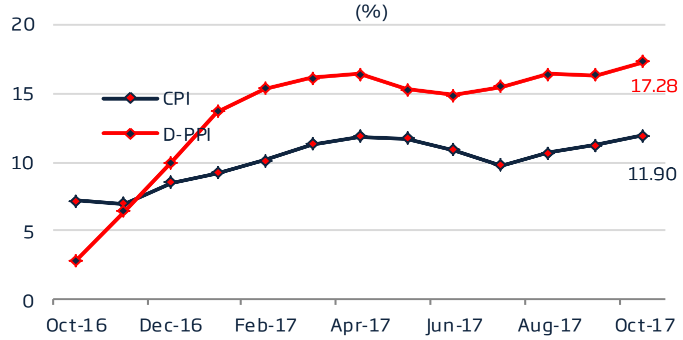


Inflation

Monthly Inflation
(%)



Annual Inflation
(%)



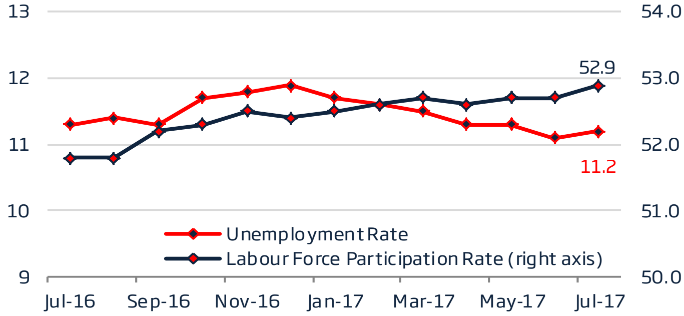
Source: CBRT, Datastream, Turkstat

Turkish Economy at a Glance

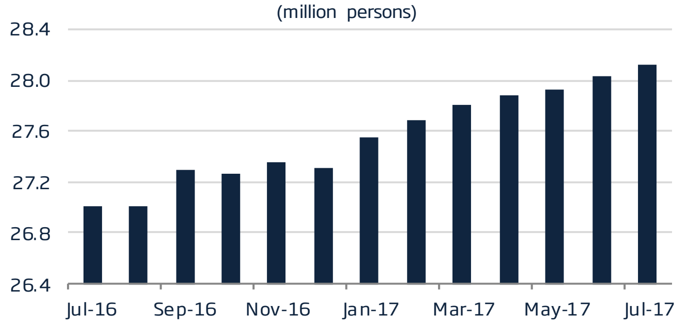
TÜRKİYE İŞ BANKASI

Labor Market

Seasonally Adjusted Labour Force Indicators
(%)

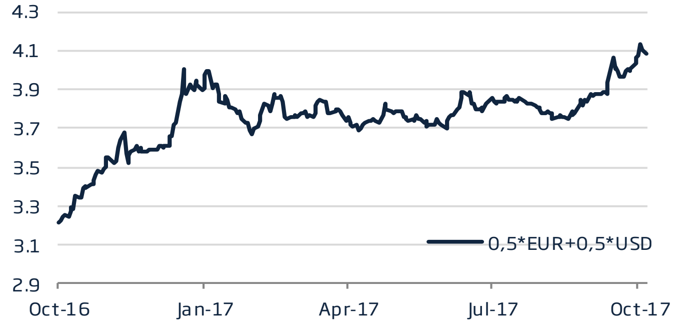


Seasonally Adjusted Employment
(million persons)

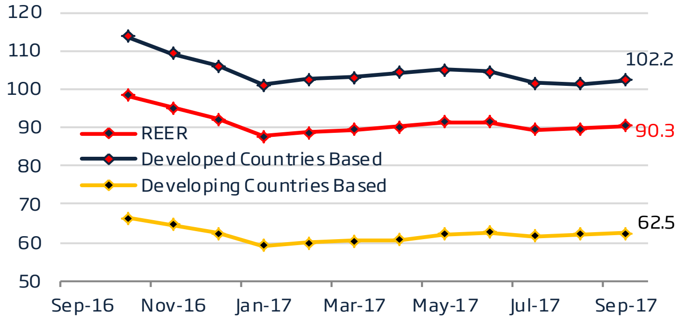


FX Market

Currency Basket

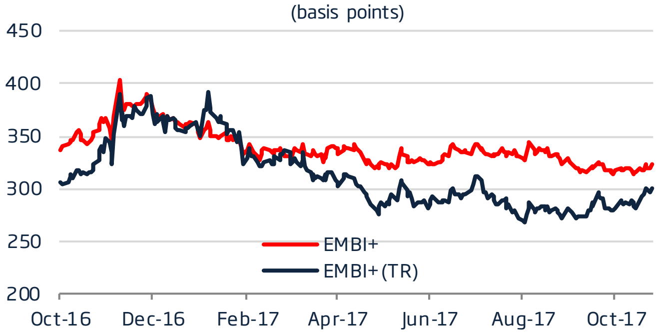


CPI Based Real Effective Exchange Rate

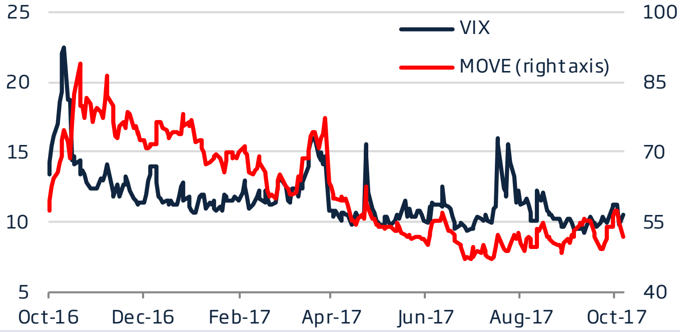


Risk Indicators

Risk Premiums
(basis points)

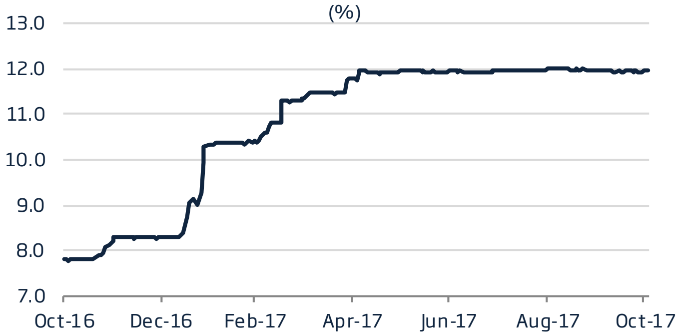


VIX and MOVE Index

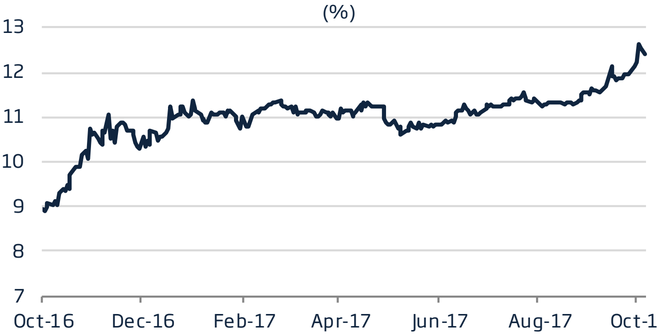


Interest Rates

Weighted Average Cost of CBRT Funding
(%)



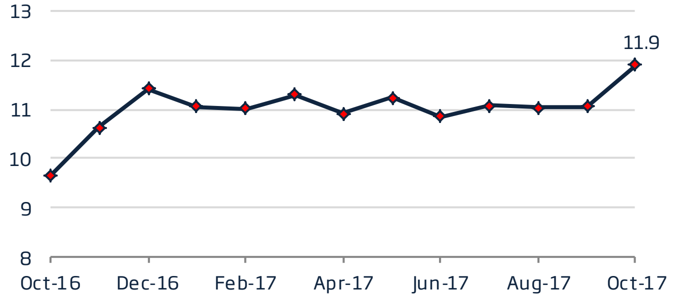
Yield of 2-Year Benchmark Bond
(%)



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

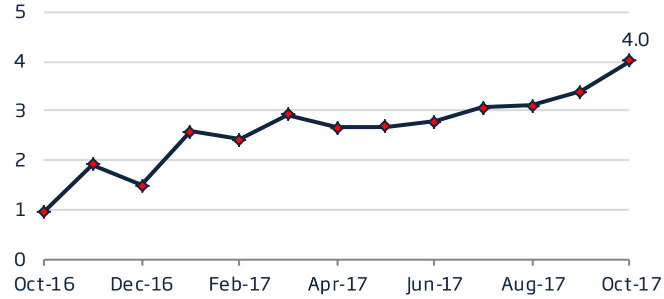
Bond-Bill Market

Average Compound Yields in Treasury Auctions (%)



Expected Real Yield of TRY GDDIs

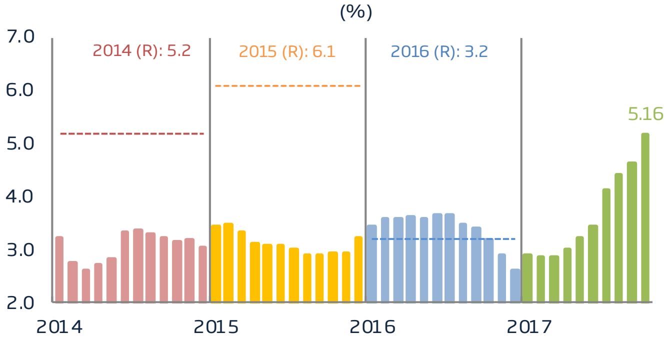
(%)



CBRT's Survey of Expectations and Other Leading Indicators

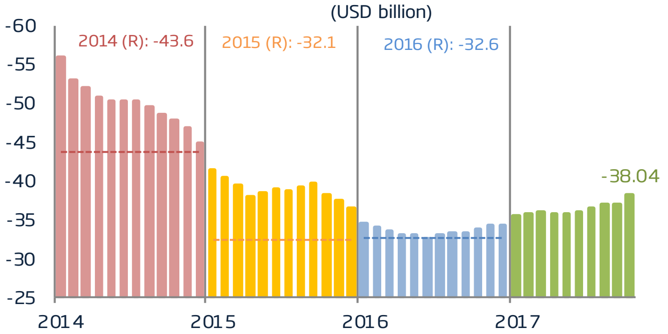
Expected GDP Growth for the Current Year

(%)



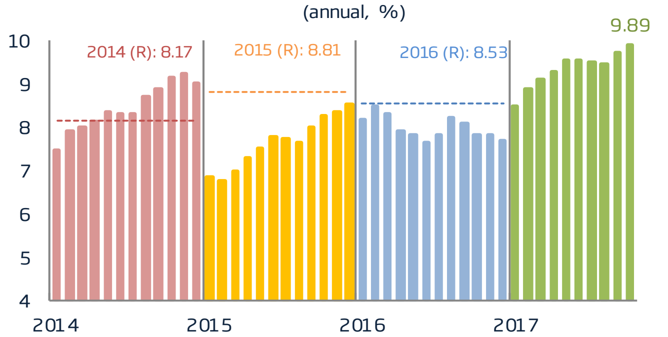
Expected CAD for the Current Year

(USD billion)

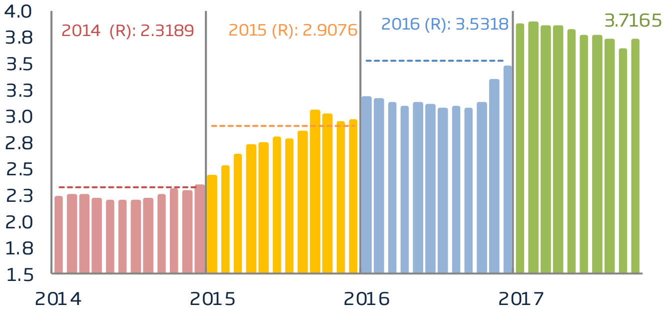


Expected CPI Inflation by the End of the Year

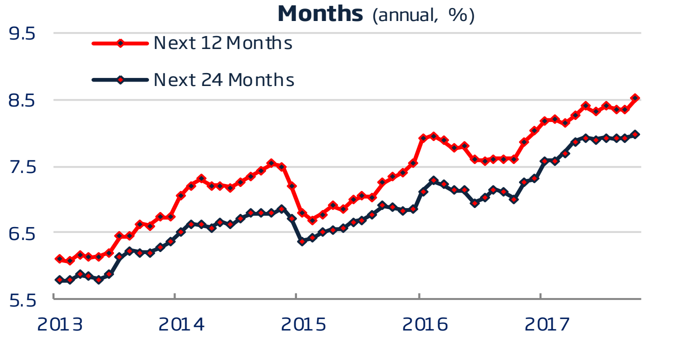
(annual, %)



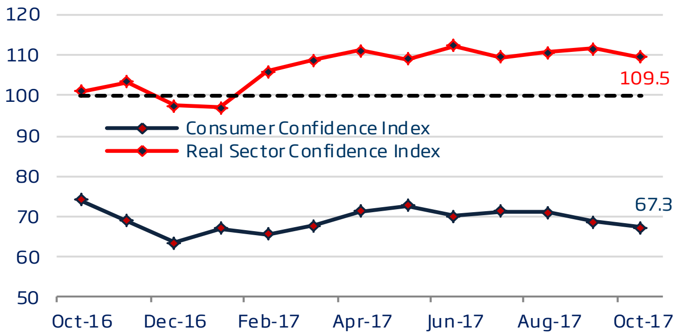
Expected Level of USD/TRY by the End of the Year



Expected CPI Inflation for the next 12 and 24 Months (annual, %)



Confidence Indicators



(R) Realization

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

Turkish Economy at a Glance

TÜRKİYE İŞ BANKASI

Growth	2012	2013	2014	2015	2016	17-Q1	17-Q2	17-Q3
GDP (USD billion)	871	950	935	862	863	175.9	204.8	-
GDP (TRY billion)	1,570	1,810	2,045	2,339	2,609	649.5	734.2	-
GDP Growth Rate (%)	4.8	8.5	5.2	6.1	3.2	5.2	5.1	-
Inflation (%)						**Aug-17**	**Sep-17**	**Oct-17**
CPI (annual)	6.16	7.40	8.17	8.81	8.53	10.68	11.20	11.90
Domestic PPI (annual)	2.45	6.97	6.36	5.71	9.94	16.34	16.28	17.28
Seasonally Adjusted Labor Market Figures						**May-17**	**Jun-17**	**Jul-17**
Unemployment Rate (%)	8.8	9.1	10.3	10.2	11.9	11.3	11.1	11.2
Labor Force Participation Rate (%)	48.5	48.5	51.0	51.7	52.4	52.7	52.7	52.9
FX Rates						**Aug-17**	**Sep-17**	**Oct-17**
CPI Based Real Effective Exchange Rate	110.3	100.3	105.0	97.5	92.0	89.6	90.3	
USD/TRY	1.7847	2.1485	2.3378	2.9189	3.5176	3.4526	3.5561	3.7966
EUR/TRY	2.3530	2.9605	2.8288	3.1708	3.7102	4.1048	4.2040	4.4228
Currency Basket (0.5*EUR+0.5*USD)	2.0688	2.5545	2.5833	3.0448	3.6139	3.7787	3.8801	4.1097
Foreign Trade Balance[1] (USD billion)						**Jul-17**	**Aug-17**	**Sep-17**
Exports	152.5	151.8	157.6	143.8	142.5	151.1	152.6	153.5
Imports	236.5	251.7	242.2	207.2	198.6	214.1	216.6	221.3
Foreign Trade Balance	**-84.1**	**-99.9**	**-84.6**	**-63.4**	**-56.1**	**-63.0**	**-64.1**	**-67.8**
Import Coverage Ratio (%)	64.5	60.3	65.1	69.4	71.8	70.6	70.4	69.4
Balance of Payments[1] (USD billion)						**Jun-17**	**Jul-17**	**Aug-17**
Current Account Balance	**-48.0**	**-63.6**	**-43.6**	**-32.1**	**-32.6**	**-34.4**	**-37.1**	**-37.0**
Capital and Financial Accounts	**-48.9**	**-62.1**	**-41.6**	**-21.9**	**-21.3**	**-29.2**	**-32.8**	**-31.7**
Direct Investments (net)	-9.5	-9.3	-5.8	-12.5	-9.2	-8.6	-9.0	-8.5
Portfolio Investments (net)	-41.0	-24.0	-20.1	15.7	-6.3	-15.2	-14.3	-16.1
Other Investments (net)	-19.2	-38.8	-15.3	-13.4	-6.7	4.7	1.3	3.9
Reserve Assets (net)	20.8	9.9	-0.5	-11.8	0.8	-10.0	-10.8	-11.0
Net Errors and Omissions	**-0.9**	**1.6**	**2.0**	**10.2**	**11.3**	**5.2**	**4.4**	**5.2**
Current Account Balance/GDP (%)	**-5.5**	**-6.7**	**-4.7**	**-3.7**	**-3.8**	-	-	-
Budget[2][3] (TRY billion)						**Jul-17**	**Aug-17**	**Sep-17**
Expenditures	**361.9**	**408.2**	**448.8**	**506.3**	**583.7**	**376.0**	**433.8**	**488.2**
Interest Expenditures	48.4	50.0	49.9	53.0	50.2	32.8	38.2	46.6
Non-interest Expenditures	313.5	358.2	398.8	453.3	533.4	343.2	395.7	441.6
Revenues	**332.5**	**389.7**	**425.4**	**482.8**	**554.4**	**351.7**	**408.7**	**456.6**
Tax Revenues	278.8	326.2	352.5	407.8	458.7	292.1	343.5	385.3
Budget Balance	**-29.4**	**-18.5**	**-23.4**	**-22.6**	**-29.3**	**-24.3**	**-25.2**	**-31.6**
Primary Balance	**19.0**	**31.4**	**26.5**	**30.4**	**21.0**	**8.4**	**13.0**	**15.0**
Budget Balance/GDP (%)	**-1.9**	**-1.0**	**-1.1**	**-1.0**	**-1.1**	-	-	-
Central Government Debt Stock (TRY billion)						**Jul-17**	**Aug-17**	**Sep-17**
Domestic Debt Stock	386.5	403.0	414.6	440.1	468.6	504.6	513.3	523.5
External Debt Stock	145.7	182.8	197.9	238.1	291.0	312.5	307.2	319.0
Total Debt Stock	**532.2**	**585.8**	**612.5**	**678.2**	**759.6**	**817.1**	**820.5**	**842.5**

(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)	2012	2013	2014	2015	2016	Aug.17	Sep.17	Change[1]
TOTAL ASSETS	**1,370.7**	**1,732.4**	**1,994.3**	**2,357.4**	**2,731.0**	**2,989.9**	**3,053.9**	**11.8**
Loans	**794.8**	**1,047.4**	**1,240.7**	**1,485.0**	**1,734.3**	**1,954.1**	**1,993.9**	**15.0**
TRY Loans	588.4	752.7	881.0	1,013.4	1,131.4	1,335.0	1,356.2	19.9
Share (%)	74.0	71.9	71.0	68.2	65.2	68.3	68.0	-
FX Loans	206.4	294.7	359.7	471.5	602.9	619.1	637.7	5.8
Share (%)	26.0	28.1	29.0	31.8	34.8	31.7	32.0	-
Non-performing Loans	23.4	29.6	36.4	47.5	58.2	63.0	62.7	7.8
Non-performing Loan Rate (%)	2.9	2.8	2.9	3.1	3.2	3.1	3.0	-
Securities	**270.0**	**286.7**	**302.3**	**329.7**	**351.6**	**368.5**	**375.7**	**6.9**
TOTAL LIABILITIES	**1,370.7**	**1,732.4**	**1,994.3**	**2,357.4**	**2,731.0**	**2,989.9**	**3,053.9**	**11.8**
Deposits	**772.2**	**945.8**	**1,052.7**	**1,245.4**	**1,453.6**	**1,601.2**	**1,635.3**	**12.5**
TRY Deposits	520.4	594.1	661.3	715.4	845.1	899.3	918.4	8.7
Share (%)	67.4	62.8	62.8	57.4	58.1	56.2	56.2	-
FX Deposits	251.8	351.7	391.4	530.0	608.5	701.9	716.8	17.8
Share (%)	32.6	37.2	37.2	42.6	41.9	43.8	43.8	-
Securities Issued	**37.9**	**60.6**	**89.3**	**97.8**	**116.3**	**129.8**	**134.9**	**16.0**
Payables to Banks	**173.4**	**254.2**	**293.2**	**361.3**	**417.6**	**411.2**	**427.4**	**2.3**
Funds from Repo Transactions	**79.9**	**119.1**	**137.4**	**156.7**	**137.8**	**87.0**	**97.1**	**-29.6**
SHAREHOLDERS' EQUITY	**181.9**	**193.7**	**232.0**	**262.3**	**300.3**	**340.2**	**345.0**	**14.9**
Profit (Loss) of the Period	23.5	24.7	24.6	26.1	37.5	33.3	37.2	-
RATIOS (%)								
Loans/GDP	50.6	57.9	60.7	63.5	66.5	-	-	-
Loans/Assets	58.0	60.5	62.2	63.0	63.5	65.4	65.3	-
Securities/Assets	19.7	16.6	15.2	14.0	12.9	12.3	12.3	-
Deposits/Liabilities	56.3	54.6	52.8	52.8	53.2	53.6	53.5	-
Loans/Deposits	102.9	110.7	117.9	119.2	119.3	122.0	121.9	-
Capital Adequacy (%)	17.9	15.3	16.3	15.6	15.6	17.2	17.2	-

(1) Year-to-date % change

Source: BRSA

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